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42

Sami Yläoutinen

Development and Functioning of Fiscal Frameworks in the Central and Eastern European Countries

JYVÄSKYLÄN YLIOPISTO

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Editors
Tuomo Takala, School of Business and Economics, University of Jyväskylä
Pekka Olsbo, Marja-Leena Tynkkynen
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ABSTRACT

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The focus in this study is on the fiscal institutions and medium term fiscal frameworks in the Central and Eastern European countries, or the CEECs. The purpose of the study is to argue that fiscal commitment has value over fiscal non-commitment, and then to study how the governments of the CEECs use the fiscal institutions to reach fiscal commitment and to improve fiscal discipline. Further, the study draws conclusions on how the underlying political fundamentals have affected the development of fiscal institutions, and finally how the differences in the frameworks have affected the fiscal performance in these countries. The study begins with a formulation of a simple closed-economy model where the monetary policy follows a Taylor-type rule while the government can employ some type of commitment technology or alternatively fiscal policy is discretionary. Credible policy-commitment can steer private sector's expectations in a way which enhances policymaker's chances to reach its objectives. The impulse responses from the model simulations reflect the effect of this expectation-channel. The results from the review of national fiscal institutions confirm that in general, the governments in the CEECs use jointly negotiated agreements to commit themselves to fiscal targets for budget aggregates ("commitment approach"), rather than delegation of significant fiscal powers to the finance minister ("delegation approach"). Some of the important elements of the commitment approach are however still lacking. The evidence presented in this study also lends general support to the notion about interdependency between the political fundamentals and the development of fiscal institutions. A comparison to the EU-15 countries reveals that in general, the EU-15 countries have developed stronger fiscal institutions. The detailed institutional data-set depicted in the study has then been used to form a set of indices which are in turn used as explanatory variables in a statistical analysis in order to identify whether the differences in the procedures have had an impact on the fiscal performance. The differences between the fiscal frameworks are not powerful explanatory variables to the fiscal performance for the 1995-1999 period, possibly due to the lack of stable and reliable fiscal data and the effects of economic transition to public finances. This conclusion is, however, reversed for the latter period (1999-2002) suggesting that countries with more centralised fiscal procedures have enjoyed better fiscal discipline. Looking forward, the theoretical considerations and the experience from the EU-15 suggest that strengthening the commitment-elements of the fiscal institutions, in particular multi-annual plans, provides a promising avenue for promoting fiscal discipline in the CEECs.

Keywords: Fiscal policy, fiscal institutions, national budget, fiscal commitment, transition countries
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Author´s address	Sami Yläoutinen Ministry of Finance P.O Box 28, FIN-00023 Government sami.ylaoutinen@vm.fi
Supervisors	Jaakko Pehkonen, University of Jyväskylä, School of Business and Economics Kari Heimonen, University of Jyväskylä, School of Business and Economics
Reviewers	Jürgen von Hagen, University of Bonn, Center for European Integration Studies Mika Widgrén, Turku School of Economics and Business
Opponent	Mika Widgrén, Turku School of Economics and Business

FOREWORD

Doctoral studies take years of consistent and hard work. Indeed, this has been an educating and exciting period for me, but looking back, it has also been a long, hard slog. I could not imagine successfully completing this project without the help and support I have received throughout the years from various individuals. Therefore, a list of thank yous is in order.

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I would like to express my sincere thanks to the country experts in the Central and Eastern European countries who have provided me with information and patiently answered to my numerous questions. They need to remain anonymous but their help has been invaluable. All the remaining errors are of course mine. Financial support from the Yrjö Jahnsson Foundation is gratefully acknowledged.

I am fortunate to have had my family, relatives and friends – too numerous to single out all of them – to keep my spirits high. For all of you, and in particular for my mother Sirkka and father Kari, thank you.

This dissertation is dedicated to my wife Sanna. Her understanding, love and support seem to know no limits.

In Helsinki, 11 August, 2005

Sami Yläoutinen

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"- Question: But this was mostly talk of economic matters.
- Illarionov: Economic matters above all, of course.
- Question: But political parties are in the field of public politics.
- Illarionov: To quote Lenin, politics is concentrated expression of economics. The main issues in the political process are economic issues. Take any issue at all, and at the bottom of it you'll find money. The question of how money should be distributed: our money, your money, private money, state money. The main issue in politics is always about money. "

An excerpt from the interview of Andrei Illarionov, Economic Advisor to President of the Russian Federation, Vladimir Putin, in Novaya Gazeta, April 15, 2004

1 INTRODUCTION

The amount of attention devoted to the Central and Eastern European countries and their economies has substantially increased, as these countries have pursued economic and political integration with European Union, or the EU. Economic policies, and especially fiscal policies, have been at the centre of this attention.[1]

The focus in this study is on the fiscal institutions and medium term fiscal frameworks in the Central and Eastern European countries, or the CEECs, which together form the overall setup for fiscal policymaking. The purpose of the study is to argue that fiscal commitment has value over fiscal non-commitment, and then to study how the governments of the CEECs use the fiscal institutions to reach fiscal commitment and to improve fiscal discipline. Further, the study draws conclusions on how the underlying political fundamentals have affected the development of fiscal institutions, and finally how the differences in the frameworks have affected the fiscal performance in these countries.

1 The Central and Eastern European countries, or the CEECs, refer to Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, the Slovak Republic and Slovenia.

The motivation for examining these issues is clearly connected with the CEECs' membership in the EU, which represents a giant leap for fiscal policies of the CEECs in terms of the requirements imposed by the EU's macroeconomic framework.[2] These requirements will be intensified even further once the CEECs become part of the euro area, as the policy coordination in E(M)U is related to the idea that the effects of budgetary policies of individual countries may also have significant area wide repercussions.

But irrespective of the convergence towards the EU and the euro, the CEECs will be facing fiscal challenges related to their economic fundamentals that will highlight further the importance of the design and implementation of fiscal policy framework in these countries. The transition process, defined as reallocation of resources from state to private sector, has not been concluded but is nearing completion in many of the CEECs.[3] Looking ahead, incomplete real convergence vis-à-vis current EU countries suggests that reaching sustainable rates of GDP growth will be a key challenge for the CEECs in the years, and even decades to come. This challenge is complicated by the constraints – most notably high degree of volatility in output levels, a high degree of openness and reliance on foreign saving to finance investment needed to advance catching up – many of the CEECs are facing.[4] Also this aspect highlights the importance of prudent fiscal management in the CEECs, and consequently the role of national fiscal institutions.

The task to create sound and stable economy and society has been even greater when one notes that after the fall of communism the economic and political environment – and thus also the foundations for both fiscal management and party and electoral systems – were fundamentally changed. Many systems had to be re-designed from entirely new perspective or even be built from scratch. Therefore, the CEECs provide a unique opportunity for studying what routes this work has taken and indeed if those routes are the ones suggested by the theoretical literature.

The debate on the usefulness and functioning of fiscal rules and targets has gained strength by the creation of the single currency. The institutional framework behind Economic and Monetary Union is by now familiar; single monetary policy is managed by the independent European Central Bank while the governments remain in control of national fiscal policies which are nevertheless subject to coordination procedures.

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2 Bulgaria and Romania are expected to join the EU in 2007.

3 For discussion on economic transition, see e.g. Roland, 2000 and Coricelli, 1997. This definition of transition is also incorporated in several transition models dealing with (optimal) speed of transition, such as in Dewatripont and Roland, 1992, Aghion and Blanchard, 1994, Chadha and Coricelli, 1994 and Castanheira and Roland, 2000. They all view transition as reallocation of resources that take place after price liberalisation and the replacement of central planning by the market as the system for allocation of resources. More informal treatments are provided by Tanzi, 1993 and Dąbrowski, 1997. For a review of how the CEECs have proceeded with transition, see Gros and Suhrcke, 2000 and different editions of Transition Reports by European Bank for Reconstruction and Development.

4 For a discussion on the fiscal policy challenges in the CEECs, see Cristou and Daseking, 2002, and Italianer, 2002.

The economic arguments used to justify the constraints on fiscal policies in EMU have to do with the interdependency of the euro countries. Effects of economic policy actions taken in one member state can be transmitted to the rest of the euro area via close economic linkages (i.e. through trade flows within the euro area, interest rates and exchange rate). Moreover, inappropriate and simultaneous fiscal policies in several countries could have spill-over effects throughout the euro area price developments and could therefore trigger countervailing action by the ECB.[5] In a similar vein, theoretical studies have established a need for fiscal constraints to limit free-rider behaviour and/or the deficit bias stemming from government myopia.[6]

The literature on optimal monetary policy design and central bank independence has a long tradition of considering the virtues of monetary commitment. Seminal work by Kydland and Prescott, 1977 and 1980 stressed the importance of credible policy commitment instead of discretionary optimisation.[7] A policymaker enhances his/her chances to reach the policy objectives, if he/she is successful in steering private agents' expectations about future policy. To achieve this, a policymaker needs to be able to communicate details about how policy will be conducted in the future. The best way to do this is by being explicit about the rules and goals that guide its decision-making, and to establish a reputation that a policymaker abides by the rules.

In the spirit of this discussion, the study begins with a formulation of a simple closed-economy model – presented in chapter two – where the monetary policy follows a Taylor-type rule while the government can, when conducting its fiscal policy, employ some type of commitment technology or alternatively fiscal policy is discretionary. Thus the set-up allows a comparison between fiscal discretion and commitment when monetary policy is committed to a policy rule. The impulse responses from the model simulations show that generally speaking the shocks produce stronger initial response under the discretionary regime but under the fiscal commitment the effects of the shocks are more persistent. These results reflect the effect of the expectation-channel; under commitment-regime the policymaker knows that there is link between the private sector's expectations about its future policies and the current outcomes. In discretionary optimisation, in contrast, expectations play no role.

The goal of this exercise is a simple one: to establish that fiscal commitment does have value over fiscal non-commitment. The model does not, however, take explicit position on the type of commitment technology the govern-

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5 See e.g. the Report by the Ecofin Council to the European Council in Helsinki in December 1999 on economic policy coordination: "*The main reason behind the principle of close co-ordination is the fact that the economies of the Member States are increasingly linked with each other. The completion of the Single Market and the single currency accelerate economic integration in the Community and give rise to more and more spill-over effects. There is thus an intensified common interest among Member States in each other's economic policies, the avoidance of free-rider behaviour, the creation of a level playing field, and in the contribution of each to the EU's overall growth and employment performance.*"

6 Beetsma and Uhlig, 1999, Buti, Franco and Ongena, 1998, Dixit and Lambertini, 2003a and Woodford, 2000.

7 See also Barro and Gordon, 1983, Rogoff, 1985 and Svensson, 1997.

ment utilises. Examples of plausible commitment technologies are constitutional restrictions (for example credible fiscal rules embodied in a legal framework), a delegation of decisions (for example to an independent agency) or reputational mechanisms (establishing a solid credibility for the announced policies).[8]

The feature these arrangements have in common has to do with credibility: a precondition for a successful management of private sector's expectations on future policies – which are, as mentioned above, one of the important determinants of current outcomes – is the ability to implement credible policies. The forthcoming chapters are concerned about how such fiscal commitments can be achieved using national fiscal institutions. The focus of the study stays on the issues of fiscal commitment; how policymakers can enhance public understanding of their policies and indeed encourage themselves to act in a more disciplined way, but the emphasis in this literature will be on the link between national fiscal institutions and fiscal discipline.

There are of course several approaches to study fiscal policy issues. Rising public debts and deficits experienced in the past decades have sparked an extensive amount of debate on the causes for such phenomena. Neoclassical theory of fiscal policy stresses the virtues of tax smoothing: tax rates should be kept stable and leave it to the automatic stabilisers to smooth the economic cycle. [9] Keynesian models, on the other hand, emphasise more active role of fiscal policy: recessions call for expansionary policies and contractionary during expansions. The political economy literature provides different explanations as to why incumbents deviate from these principles.

Chapters three to six of the study take a politico-institutional view of fiscal discipline. As explained in the literature review presented in chapter three, the general idea in theories of political economy is to ask why fiscal policies deviate from the socially optimal benchmark. The general answer provided in these theories has to do with the concept of political constraints which refers to the constraints due to conflict of interest and to the need to make collective choices in the face of these conflicts. Indeed, one of the fundamental observations behind the theories of political economy is that policymakers have other motives behind their policy choices than simply being social welfare maximisers.[10]

A number of political economic models seeking explanations for the behaviour of public deficits and debts have surfaced. One prominent branch of the literature emphasises political fundamentals, such as political polarisation of the electorate (proportional electoral systems, which tend to produce coalition governments, are considered more unstable than pluralist systems) and political instability (the current government is unsure of its possibilities for re-

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8 For a discussion about possible 'solutions' to the time-inconsistency problem, see e.g. Drazen, 2000.

9 See Barro, 1979, 1989 and Lucas, 1986.

10 See Drazen, 2000.

election and it attempts to use debt as a strategic variable). The proponents of this view are sometimes called "electoral institutionalists". [11]

"Fiscal institutionalists", on the other hand, stress the importance of fiscal institutions, broadly defined as the rules and regulations according to which budgets are prepared, approved and implemented. [12] Attention is therefore on the budget process which, in political economy, is viewed as a mechanism through which political interest groups bargain over conflicting goals trying to achieve their objectives. Consequently this branch of literature views national fiscal institutions as important determinants of public deficits and debts. Implicit idea then is that by changing these rules, a country's fiscal performance can be altered in a predictable way. In other words, if policy outcomes are influenced by variables related to institutional characteristics, then one has to intervene at the institutional level to improve policymaking.

According to this view, the underlying reason for excessive spending stems from the common pool resource problem, or the CPR problem, which results from the finding that government spending is often targeted at specific sub-sets of population while being paid by the general population. The implication is that policymakers systematically overestimate the net marginal benefit of increased public spending. This fragmentation of budget process can be overcome by centralising the budget process. More specifically, the existence of fiscal biases stemming from political economy aspects has served as a justification for two ideal ways to promote centralisation of the budget process, and consequently fiscal rigour: *commitment* via set of binding limits or targets on budget aggregates which are negotiated collectively at the beginning of a budgetary process, and *delegation* of significant fiscal powers to "a fiscal entrepreneur" (prime minister or "strong" finance minister).[13]

Both above-mentioned views have their flaws. Policy conclusions from the electoral institutionalists' views are difficult to draw since political fundamentals are deeply rooted in a country's history and tradition and are therefore difficult to change. On the other hand, the view according to which strong fiscal institutions provides "a one-size-fits-all" solution which – regardless of a country's broader constitutional context – is always conducive to fiscal discipline does not seem to offer a complete explanation either. Further, this view does

11 See Tabellini and Alesina, 1990, Persson and Svensson, 1989 and Roubini and Sachs, 1989.

12 Few words on terminology; "Fiscal" and "budgetary" policies are often used as synonyms while strictly speaking this is not the case. The former could be defined as a branch of economic policy encompassing all decisions related to revenue and expenditure in general government finances whereas the latter comprises decisions related to on-budget activities only, and can be thus seen as a part of fiscal policy implemented via the budget. This division could be reflected also in the terms "fiscal" and "budgetary" institutions, which are both used in the literature. While the budget process is in the heart of this approach, such institutions affect more widely the dynamics of decision-making on fiscal policy issues, and thus the influence is not strictly confined only to public spending. Therefore, the term "fiscal institutions" will be used throughout the paper.

13 See von Hagen, 1992, von Hagen and Harden, 1994 and 1996.

not explain why some countries choose to employ a certain type of fiscal institution, and others do not.

But these views are not necessarily contradictory. The literature building on these two above-mentioned approaches argues that the nature of CPR problem depends also on electoral and party systems.[14] Electoral institutions and party systems are important in determining what is the most effective way to achieve centralisation of the budget process.

Fiscal institutions refer to different rules and procedures under which the budget proposal is formed, approved and implemented. A closely related aspect has to do with different fiscal targets and frameworks under which these targets are set and formulated. For the EU member states, there is a special emphasis on the medium-term budgeting which follows from the obligations set out in the Stability and Growth Pact, or the SGP, which establishes the budgetary commitments in the medium term. The EU member states formulate their fiscal policy targets under the stability and convergence programmes which consequently have also a medium term emphasis.

These procedures do not however determine exactly how government should use and implement fiscal targets. Indeed, research on the EU-15 countries[15] have established that there is considerable variation among the member states in the practices of setting fiscal targets and in what is done to achieve them.[16] Fiscal targets themselves – their scope, specificity and status within the annual budget process – can differ too in a number of ways.

The focus in chapters three to six will be on national fiscal institutions and medium term fiscal frameworks in the CEECs which together form the overall setup for fiscal policymaking. Chapter four discusses electoral and party systems in the CEECs, and in particular their role in countries' tendency to adopt a certain type of fiscal institution. This allows one to draw conclusions on how the underlying political fundamentals have affected the development of fiscal institutions. Chapter five, in turn, gathers and reviews an extensive data-set on the institutional details of the fiscal institutions and the multi-annual fiscal frameworks employed by the CEECs. Comparable data from earlier studies[17] permits comparisons between the CEECs and the EU-15. The general purpose of this chapter is to study how the governments of the CEECs use the fiscal institutions and what are the roles of different actors and their relative importance in the budget processes in these countries. [18] The institutional data-set de-

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14 See Hallerberg and von Hagen, 1999.

15 In this study, the pre- (2004) enlargement EU countries are referred to as "the EU-15".

16 See Hallerberg, Strach and von Hagen, 2001 and European Commission, 2003.

17 Hallerberg et al, 2001, European Commission, 2003a, Mattson and Strøm, 1995, Döring, 1995b and Hallerberg, 2000.

18 This type of empirical research can be useful also in providing guidance with a more theoretically oriented work. Persson and Tabellini, 2000 note that "legislative bargaining models entail a detailed set of assumptions about the rules for approving legislation. The details are crucial and changing the extensive form of the game can lead to radically different results. […] Which assumptions are more reasonable and appropriate giving the policy issues and countries involved? […] To be more confident in this approach we need careful empirical and applied research." (191) Alesina and Perotti, 1999 also highlight the significance of different actors in budget processes.

picted in chapter five has then been used to form a set of indices characterising the institutional characteristics of fiscal procedures. The indices are in turn used as explanatory variables in a statistical analysis in chapter six in order to identify whether the differences in the procedures have had an impact on the fiscal performance.

The results from the examination of fiscal frameworks in chapter five confirm that practically all countries have taken steps to develop their national fiscal institutions, even if further challenges in many countries remain. In general, the governments in the CEECs use jointly negotiated agreements to commit themselves to fiscal targets for budget aggregates ("commitment approach"), rather than delegation of significant fiscal powers to the finance minister ("delegation approach"). Indeed, the commitment element especially in the planning and decision-making stage of the budget process is strong in the majority of the CEECs. The finance minister acts as an agenda setter by presenting the fiscal guidelines to the rest of the government. The cabinet however possesses a strong role in setting the targets, negotiating the budgets and resolving the emerging conflicts. The commitment element of the fiscal frameworks is also strengthened – albeit to a varying degree – by an introduction of multi-annual budgeting.

Some of the important elements of the commitment approach are however still lacking. The fiscal targets used in these countries can be, in general, considered as 'weak'. In other words, the targets are based on political commitment and they serve as non-binding or indicative benchmark for budget-making process. The majority of countries do not discuss the deviations between the objectives laid out in the multi-annual plans and the actual outcome thus weakening the credibility of the multi-annual targets (or guidelines). Finally, the CEECs do not typically have clear provisions in place on what should be done in times of economic under- or over-performance.

Due to a small number of countries, the comparisons between the CEECs and the EU-15 are only suggestive. In general, the EU-15 countries have developed somewhat stronger fiscal institutions. For example, the commitment states of the EU-15 have sought to strengthen the joint commitments by utilising the multi-annual plans and the coalition agreements; a practise which as of yet has not taken hold among the CEECs. However, many practises in the CEECs have been introduced very recently and they are still taking shape.

The dominance of commitment approach was expected based on the review of the political fundamentals performed in chapter four. The theory predicts that countries with multi-party governments – as in the vast majority of the CEECs – find it easier and more effective to rely on commitment. Further,

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They note that many of the models have been developed for the US context, and therefore the emphasis has been on the legislature, with fairly little attention to executive. While this emphasis has been justified for the US case, they say, one needs to focus more on the formulation of budget within the government in parliamentary democracies especially in those countries where the legislature's role in amending the executive's budget proposal is limited, and thus intra-governmental negotiations can be very important for the final outcome. (23)

the theory predicts that those countries with volatile political conditions should develop weaker fiscal institutions compared to politically more stable countries. Broadly speaking, the reality matches also with this prediction. The evidence presented in this study therefore lends general support to the notion about interdependency between the political fundamentals and the development of fiscal institutions.

Statistical analysis has then been performed in order to identify whether the differences in the fiscal procedures have had an impact on the fiscal performance. The lack of stable and reliable fiscal data for the 1995-1999 period and the effects of economic transition to public finances hinder the analyses especially for these early years. Indeed, for the first part of the period (1995-1998), the evidence is non-existent. Thus, the differences between the fiscal frameworks are not powerful explanatory variables to the fiscal performance during this period. This conclusion is, however, reversed for the latter period (1999-2002) suggesting that countries with more centralised fiscal procedures have enjoyed better fiscal discipline.

The evidence suggests that especially the planning- and decision-making and implementation and monitoring stages of the budget process have been important in ensuring fiscal rigour. Due to a very short time-period and limitations in the fiscal data, the results should be treated with caution. Looking forward, the theoretical considerations and the experience from the EU-15 suggest that strengthening the commitment-elements of the fiscal institutions, in particular multi-annual plans, provides a promising avenue for promoting fiscal discipline in the CEECs.

This study is organised as follows. After this introduction, the importance of fiscal commitment is studied with a help of a simple new-Keynesian framework. Chapter three reviews briefly theoretical and empirical literature on fiscal institutions. Then in chapter four, the role of electoral and party systems in the choice of fiscal institutions is discussed. This chapter includes also a country-specific discussion on the electoral and party systems in the CEECs, which will allow making predictions about the fiscal institutions these countries should have ideally chosen. Chapter five presents the details of the fiscal frameworks employed by the CEECs, and compares the details of the frameworks to those of the EU-15. This chapter also includes a discussion on how well the reality matches with the prediction that followed from the review of the political fundamentals. In chapter six, a statistical analysis is performed to find out how the differences in the frameworks across the CEECs have affected the fiscal performance in these countries. Finally, chapter seven concludes.

2 FISCAL COMMITMENT VERSUS DISCRETION

The creation of the single currency and the underlying economic policy framework has substantially increased the debate on the usefulness of rules based fiscal and monetary policy. Theoretical studies have established a need for fiscal constraints to limit free-rider behaviour and/or the deficit bias stemming from government myopia.[19] Some other works have reached different conclusions on the desirability of fiscal constraints or policy coordination within a monetary union. Chari and Kehoe, 1998 and Dornbusch, 1997 argue that fiscal restrictions are not needed – and can possibly be even harmful – when the monetary authority can commit its policies. Dixit and Lambertini, 2003b consider a special case where the ideal points of all countries' fiscal authorities and the common central bank coincide (i.e. they have identical output and inflation targets), and find that fiscal constraints may be redundant independently of whether the monetary authority can commit its policies ex-ante. Further, Rogoff, 1985 and Kehoe, 1989 find that lack of cooperation between governments acts as a disciplining device; thus cooperation between the governments may, in fact, reduce welfare when an incentive towards time-inconsistent behaviour is present.[20]

Seminal work by Kydland and Prescott, 1977 and 1980 stressed the importance of credible policy commitment instead of discretionary optimisation. If a policymaker is able to steer private agents' expectation about future policy, he/she enhances his/her chances to reach the policy objectives. To achieve this,

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19 See footnote six of this study for references.

20 While the official EU economic policy framework recognises the need for economic policy coordination between the governments, it's worthwhile to note that no ex-ante coordination between the fiscal authorities and the monetary authority take place. Some have indeed argued that a different institutional framework is needed, where fiscal policies in the euro area would be represented at a more official level. This would enable more institutionalised coordination between monetary and fiscal authorities (for example von Hagen and Mundschenk, 2001, see also Alesina and Tabellini, 1987 who show that when monetary and fiscal policies are not coordinated, a monetary commitment might not improve welfare over discretionary regime if the two authorities have different relative weights assigned to their final objectives). Some others see that far-reaching economic policy coordination as unpractical and even counterproductive (for example Alesina, Blanchard, Gali, Giavazzi and Uhlig, 2001 and Korkman, 2001).

a policymaker needs to be explicit about the rules and goals that guide its decision-making, and to establish a reputation that a policymaker abides by the rules.

This chapter approaches the interaction between fiscal and monetary policies and the importance of fiscal commitment by forming a simple new-Keynesian framework. New-Keynesian literature originated e.g by Svensson, 1986 and Rotemberg, 1987 has been gaining ground in a policy analysis. Walsh, 2003 calls new-Keynesian framework as standard approach today and notes that such framework is consistent with optimising behaviour by private agents and incorporates nominal rigidities, yet is simple enough for use in exploring a number of policy issues. Fiscal commitment has an important role in the framework presented in this chapter. In the spirit of Kydland and Prescott, fiscal commitment in this context means that the government is able to choose its policy once and for all at the start of the game.[21]

The following closed-economy model includes sticky prices and the monetary policy follows a Taylor-type rule. Price stickiness is achieved by assuming that the firm faces costs when it changes prices. The model includes an endogenous supply of labour and income tax as the only form of taxation. Income tax is proportional (instead of a lump sum tax) and it has distortionary effects. The fiscal policy in the model has both supply- and demand-side effects compared to a conventional approach where only the latter effects are present.[22] The government can, when conducting its fiscal policy, employ some type of commitment technology or alternatively fiscal policy is discretionary. Thus the set-up allows a comparison between fiscal commitment and discretion when monetary policy is committed to a policy rule.[23]

The model formulated in this chapter draws on Railavo, 2003 and 2004a. The workhorse model is however modified by letting the government maximise a utility function, too. This allows modelling fiscal commitment and discretion in a sensible fashion.[24]

2.1 The household

The household maximises the utility function drawing utility from real private consumption c_t, real government consumption g_t, real money balances

21 Properties of fiscal commitment has been considered in Dixit and Lambertini, 2003a, Klein and Rios-Rull, 2002 and Velasco, Benhabib and Rustichini, 2001.

22 See Chari and Kehoe, 1999.

23 Note that the term “fiscal commitment” has a slightly different meaning in this chapter compared to third and forthcoming chapters, where “commitment approach” is used to describe a specific model of fiscal governance.

24 Regarding the household and the firm, the model presented here follows closely that of Railavo, 2003 and 2004a. The only difference is that while in Railavo, 2003 and 2004a, the government and private consumptions were assumed to be separable in the household’s utility function, here they are inseparable. This affects the output and real money balance equations, as well as labour supply equation which, in turn, affects the potential output and Phillips curve equations.

$\frac{M_t}{P_t} = m_t$ and leisure L_t. Labour l_t is $l_t = 1 - L_t$. The utility function, which is assumed to be continuous, increasing and concave, is then

$$E_t \sum_{t=0}^{\infty} \delta^t u(c_t, g_t, m_t, l_t) \tag{1}$$

The household faces budget constraint which includes nominal interest bearing bonds B_t and nominal money balances M_t. Nominal interest is R_t, whereas inflation is defined as $\frac{P_t - P_{t-1}}{P_t} = \pi_t$ or $1 - \pi_t = \frac{P_{t-1}}{P_t}$. Nominal and real ($r_t$) interest rates can be written as

$$(1 + R_t)(1 - \pi_{t+1}) = (1 + r_t)\,, \tag{2}$$

where π_{t+1} is the inflation rate at *t+1*. The household also receives nominal net income $P_t w_t l_t (1 - \tau_t)$, where w_t is real gross wage and τ_t is the tax rate and a share of the profits made by firms $P_t \mathrm{X}_t$.

Household's flow budget constraint in nominal terms is

$$P_t c_t + M_t - M_{t-1} + B_t \le (1 + R_{t-1}) B_{t-1} + P_t w_t l_t (1 - \tau_t) + P_t \mathrm{X}_t \tag{3}$$

and in real terms

$$c_t + m_t - (1 - \pi_t) m_{t-1} + b_t \le (1 + r_{t-1}) b_{t-1} + w_t l_t (1 - \tau_t) + \mathrm{X}_t \tag{4}$$

Lagrangian function can now be written as

$$L = E_t \sum_{t=0}^{\infty} \delta_H^t u(c_t, g_t, m_t, l_t) + \lambda_t \begin{pmatrix} (1 + r_{t-1}) b_{t-1} + w_t l_t (1 - \tau_t) + \mathrm{X}_t - c_t - m_t \\ + (1 - \pi_t) m_{t-1} - b_t \end{pmatrix}, \tag{5}$$

where $\delta_H = \frac{1}{1 + \rho_H}, \rho_H > 0$ is the household's discount factor and λ is the Lagrange multiplier. First order conditions for optimality then become

$$u_c(c_t, g_t, m_t, l_t) - \lambda_t = 0 \tag{6}$$

$$u_m(c_t, g_t, m_t, l_t) - \lambda_t + \delta_H E_t \lambda_{t+1} (1 - \pi_{t+1}) = 0 \tag{7}$$

$$u_l(c_t, g_t, m_t, l_t) + \lambda_t w_t (1 - \tau_t) = 0 \tag{8}$$

$$-\lambda_t + \delta_H E_t \lambda_{t+1} (1 + r_t) = 0\,, \tag{9}$$

where subscripts refer to partial derivatives.

Combining equations (6) and (9) yields the Euler condition for optimal intertemporal allocation of consumption

$$\frac{u_c(c_t, g_t, m_t, l_t)}{E_t u_c(c_{t+1}, g_{t+1}, m_{t+1}, l_{t+1})} = (1 + r_t)\delta_H \tag{10}$$

Combining equations (6), (7) and (9), and using (2) yields marginal rate of substitution between money and consumption which equals to the opportunity cost of holding money, which, in turn, is related to nominal interest rate

$$u_m(c_t, g_t, m_t, l_t) = u_c(c_t, g_t, m_t, l_t)\frac{R_t}{1 + R_t} \tag{11}$$

Finally, combining equations (6) and (8) yields marginal rate of substitution between labour supply and consumption which equals the real net wage rate

$$u_l(c_t, g_t, m_t, l_t) = -[u_c(c_t, g_t, m_t, l_t) w_t (1 - \tau_t)] \tag{12}$$

The utility function is assumed to be constant-relative-risk-aversion-type function, or CRRA-function

$$u(c_t, g_t, m_t, l_t) = \frac{(c_t^{\gamma} g_t^{1-\gamma})^{1-\sigma}}{1-\sigma} + \frac{\Gamma m_t^{1-\sigma}}{1-\sigma} - \frac{l_t^{1+\theta}}{1+\theta}\ , \tag{13}$$

where $\sigma \geq 0$ is the coefficient of relative risk aversion[25], Γ is a positive constant, $\theta \geq 0$ is the inverse of labour supply elasticity and γ and $(1-\gamma)$ are the proportions of utility the household draws from private and public consumption, respectively ($0 < \gamma < 1$). Using (13) the equations (10)-(12) can be re-written as

$$(c_t^{\gamma} g_t^{1-\gamma})^{-\sigma} \gamma \left(\frac{c_t}{g_t}\right)^{\gamma-1} = E_t (c_{t+1}^{\gamma} g_{t+1}^{1-\gamma})^{-\sigma} \gamma \left(\frac{c_{t+1}}{g_{t+1}}\right)^{\gamma-1} (1 + r_{t+1})\delta_H \tag{14}$$

$$\Gamma m_t^{-\sigma} = (c_t^{\gamma} g_t^{1-\gamma})^{-\sigma} \gamma \left(\frac{c_t}{g_t}\right)^{\gamma-1} \frac{R_t}{1 + R_t} \tag{15}$$

$$-l_t^{\theta} = -\left[(c_t^{\gamma} g_t^{1-\gamma})^{-\sigma} \gamma \left(\frac{c_t}{g_t}\right)^{\gamma-1} w_t (1 - \tau_t)\right] \tag{16}$$

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25 In the CRRA-function, coefficient σ determines the household's willingness to shift consumption between different periods; the smaller σ is, the more slowly the marginal utility falls as consumption rises and more willing the household is to allow its consumption is vary over time. See e.g. Romer, 1996.

First, equation (16) is re-formulated slightly to yield

$$l_t = (c_t^{\gamma} g_t^{1-\gamma})^{-\frac{\sigma}{\theta}} \gamma^{\frac{1}{\theta}} \left(\frac{c_t}{g_t}\right)^{\frac{\gamma-1}{\theta}} w_t^{\frac{1}{\theta}} (1-\tau_t)^{\frac{1}{\theta}} \tag{17}$$

This is the labour supply function which is needed in the next section. Note that the wage-elasticity of labour supply is $\frac{1}{\theta}$. Then equations (14) and (15) are log-linearised and re-arranged to yield[26]

$$\ln c_t = E_t \ln c_{t+1} + \Omega \ln g_t - \Omega E_t \ln g_{t+1} - \Phi \ln(1+r_t) - \Phi \ln \delta_H , \tag{18}$$

$$\text{where } \Omega \equiv \frac{(1-\sigma)(\gamma-1)}{\gamma(1-\sigma)-1} \text{ and } \Phi \equiv \frac{1}{\gamma(\sigma-1)+1} \tag{19}$$

and

$$\ln m_t = \Psi \ln c_t - \Xi \ln g_t - \Theta \ln\left(1 - \frac{1}{1+R_t}\right) - \Theta \ln \gamma + \Theta \ln \Gamma , \tag{20}$$

$$\text{where } \Psi \equiv \frac{\gamma(\sigma-1)+1}{\sigma} ,\ \Xi \equiv \frac{\gamma(\sigma-1)-\sigma+1}{\sigma} \text{ and } \Theta \equiv \frac{1}{\sigma} \tag{21}$$

Next, the equations (18) and (20) need to be written as deviations from a steady state. Equation (18) holds at steady state with values $\bar{c}_t$, $\bar{c}_{t+1}$, $\bar{g}_t$, $\bar{g}_{t+1}$ and $\bar{r}_t$. Similarly equation (20) holds at steady state with values $\bar{m}_t$, $\bar{c}_t$, $\bar{g}_t$ and $(1+\bar{R}_t)$. Also, let $\hat{c}_t$ denote the logarithmic deviation of c_t from its steady state value $\bar{c}$, or formally: $\hat{c}_t \equiv \log c_t - \log \bar{c}_t$. Using this notation, the steady state values are subtracted from both equations. This gives

$$\begin{aligned} &\ln c_t - \ln \bar{c}_t = E_t(\ln c_{t+1} - \ln \bar{c}_{t+1}) + \Omega(\ln g_t - \ln \bar{g}_t) - \Omega E_t(\ln g_{t+1} - \ln \bar{g}_{t+1}) \\ &- \Phi[\ln(1+r_t) - \ln(1+\bar{r}_t)] - \Phi(\ln \delta_H - \ln \delta_H) \end{aligned} \tag{22}$$

and

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26 The signs and magnitudes of Ω, Φ, Ψ and Ξ are perhaps not immediately obvious. As an example, with parameter values $\sigma = 0.5$ and $0 < \gamma < 1$, their potential values can vary as follows: $0 < \Omega < 0.5$, $1 < \Phi < 2$, $1 < \Psi < 2$ and $0 < \Xi < 1$. Note further that Ω and Ξ get negative values if $\sigma > 1$. Finally, note that if $\gamma = 1$, the equations (18) and (20) collapse to the corresponding equations in Railavo, 2003 and 2004a. This is exactly what should happen given the fact that with $\gamma = 1$ the utility function (13) is the same as in Railavo, 2003 and 2004. The same applies to other relevant equations in this section.

$$\ln m_t - \ln \overline{m}_t = \Psi(\ln c_t - \ln \overline{c}_t) - \Xi(\ln g_t - \ln \overline{g}_t) - \Theta\left[\ln(1+R_t) - \ln(1+\overline{R}_t)\right]$$
$$- \Theta(\ln \gamma - \ln \gamma) + \Theta(\ln \Gamma - \ln \Gamma) \tag{23}$$

Using approximations $\ln(1+r_t) - \ln(1+\overline{r}_t) \approx \hat{r}_t$ and $\ln(1+R_t) - \ln(1+\overline{R}_t) \approx \hat{R}_t$, and the notation introduced in the previous paragraph, equations (22) and (23) can be written as deviations from the steady state

$$\hat{c}_t = E_t \hat{c}_{t+1} + \Omega \hat{g}_t - \Omega E_t \hat{g}_{t+1} - \Phi \hat{r}_t \tag{24}$$

and

$$\hat{m}_t = \Psi \hat{c}_t - \Xi \hat{g}_t - \Theta \hat{R}_t \tag{25}$$

Final output is consumed by household and purchased by the government by the amount of g_t. This gives the economy-wide resource constraint that can be used to eliminate $\hat{c}_t$ from equations (24) and (25)

$$y_t = c_t + g_t \tag{26}$$

Log-linearisation of (26) follows Uhlig, 1999:

$$y_t = \overline{y} e^{\hat{y}_t} \approx \overline{y}(1 + \hat{y}_t) = \overline{y}\hat{y}_t \tag{27}$$

Note that constant drops out since it satisfies steady state relationship. Performing similar log-linearisations for c_t and g_t, one gets

$$\overline{y}\hat{y}_t = \overline{c}\hat{c}_t + \overline{g}\hat{g}_t \text{ or } \hat{y}_t = \frac{\overline{c}}{\overline{y}}\hat{c}_t + \frac{\overline{g}}{\overline{y}}\hat{g}_t \text{ or } \hat{c}_t = \frac{\overline{y}}{\overline{c}}\hat{y}_t - \frac{\overline{g}}{\overline{c}}\hat{g}_t \text{ or}$$
$$E_t\hat{c}_{t+1} = \frac{\overline{y}}{\overline{c}} E_t \hat{y}_{t+1} - \frac{\overline{g}}{\overline{c}} E_t \hat{g}_{t+1} \text{ or } \ln c_t = \ln \overline{c}_t - \frac{\overline{y}_t}{\overline{c}_t}(\ln y_t - \ln \overline{y}_t) - \frac{\overline{g}_t}{\overline{c}_t}(\ln g_t - \ln \overline{g}_t) \tag{28}$$

These different forms of the resource constraint will be needed throughout this and the following sections. Then, using $E_t\hat{c}_{t+1}$ from (28), equation (24) can be written as

$$\hat{y}_t = E_t \hat{y}_{t+1} + \left(\frac{\overline{c}}{\overline{y}}\Omega + \frac{\overline{g}}{\overline{y}}\right)\hat{g}_t - \left(\frac{\overline{c}}{\overline{y}}\Omega + \frac{\overline{g}}{\overline{y}}\right)E_t \hat{g}_{t+1} - \frac{\overline{c}}{\overline{y}}\Phi \hat{r}_t \tag{29}$$

This is the output equation. As mentioned in Railavo, 2003, expectations of the future, not lagged variables, play an important role in aggregate demand.

Next, $\hat{c}_t$ from (28) is again used by plugging it into (25). This yields the real money balance equation

$$\hat{m}_t = \frac{\bar{y}}{\bar{c}}\Psi\hat{y}_t - \left[\frac{\bar{g}}{\bar{c}}\Psi + \Xi\right]\hat{g}_t - \Theta\hat{R}_t \tag{30}$$

2.2 The firm

Mirroring Railavo, 2003 and 2004a, there is a continuum of identical firms operating in a monopolistically competitive market. A representative profit maximising firm uses production technology

$$y_t = Al_t \text{ or } l_t = \frac{y_t}{A}, \tag{31}$$

where $A = \mu e^{\upsilon * time}$ denotes technological development and l_t denotes labour. Production technology is a Cobb-Douglas production function without capital and constant returns to scale. The latter part of (31) determines the labour demand l_t^D. The firm faces a real marginal cost

$$\frac{\partial}{\partial y_t}\left[w_t\left(\frac{y_t}{A}\right)\right] = w_t\frac{1}{A} \equiv mc_t \tag{32}$$

By setting the labour supply equation (17) to equal labour demand, one obtains equilibrium wages w_t

$$w_t = \left[c_t^{\gamma} g_t^{1-\gamma}\right]^{\sigma}\left(\frac{y_t}{A}\right)^{\theta} c_t^{1-\gamma} g_t^{\gamma-1}(1-\tau_t)^{-1}\gamma^{-1} \tag{33}$$

After plugging equilibrium wages into the marginal cost equation (32) and taking natural logarithms, one gets[27]

$$\theta \ln y_t + \Lambda \ln c_t - \Pi \ln g_t - (1+\theta)\ln A - \ln(1-\tau_t) - \ln\gamma = \ln mc_t, \tag{34}$$

where $\Lambda \equiv \gamma\sigma + (1-\gamma), \Pi \equiv (\gamma-1)\sigma - (\gamma-1)$ and $\ln A = \ln\mu_t + \upsilon * time$ (35)

Let's note $z_t \equiv \ln\mu_t$ and assume that the productivity z_t follows the stochastic process $z_t = \rho z_{t-1} + \varepsilon_t$ with $0 \le \rho \le 1$ and the white noise supply shock $\varepsilon_t = i.i.d.(0,\sigma_\varepsilon^2)$. Equation (34) holds also at the steady state. In order to log-

27 With parameter values $\sigma = 0.5$ and $0 < \gamma < 1$, the potential values of Λ and Π can vary as follows: $0.5 < \Lambda < 1$ and $0 < \Pi < 0.5$. Note that Π gets negative values if $\sigma > 1$.

linearise (34), one needs to subtract the steady state values and use the notation from the previous section. This yields

$$\theta\hat{y}_t + \Lambda\hat{c}_t - \Pi\hat{g}_t - (1+\theta)\hat{z}_t + \frac{\bar{\tau}}{1-\bar{\tau}}\hat{\tau}_t = \hat{mc}_t \tag{36}$$

Recall the resource constraint (28) from the previous section. Plugging $\hat{c}_t$ from (28) into (36) permits writing the marginal cost equation as deviations from the steady state:

$$\left(\Lambda\frac{\bar{y}}{\bar{c}} + \theta\right)\hat{y}_t - \left(\Lambda\frac{\bar{g}}{\bar{c}} + \Pi\right)\hat{g}_t - (1+\theta)\hat{z}_t + \frac{\bar{\tau}}{1-\bar{\tau}}\hat{\tau}_t = \hat{mc}_t \tag{37}$$

In a flexible price equilibrium, the nominal marginal cost equals the nominal price and mark-up. In real terms this is $mc_t = \frac{1}{k}$, where k is the mark-up, or in the steady state equilibrium $\ln\overline{mc}_t = \ln\frac{1}{k}$. Now, recall the resource constraint (28) written with respect to $\ln c_t$, plug this into (34) and rearrange. This yields

$$\begin{aligned}&\left(\Lambda\frac{\bar{y}}{\bar{c}} + \theta\right)\ln y_t - \left(\Lambda\frac{\bar{g}}{\bar{c}} + \Pi\right)\ln g_t - (1+\theta)\ln A - \ln(1-\tau_t) - \ln\gamma\\ &= \ln\frac{1}{k} + \Lambda\frac{\bar{y}}{\bar{c}}\ln\bar{y} - \Lambda\ln\bar{c} - \Lambda\ln\frac{\bar{g}}{\bar{c}}\ln\bar{g}\end{aligned} \tag{38}$$

The right hand side of (38) can be assumed to be approximately zero.[28] Solving with respect to $\ln y_t$ gives

$$\ln y_t^* = \frac{\Lambda\frac{\bar{g}}{\bar{c}} + \Pi}{\Lambda\frac{\bar{y}}{\bar{c}} + \theta}\ln g_t + \frac{1+\theta}{\Lambda\frac{\bar{y}}{\bar{c}} + \theta}\ln A + \frac{1}{\Lambda\frac{\bar{y}}{\bar{c}} + \theta}\ln(1-\tau_t) + \frac{1}{\Lambda\frac{\bar{y}}{\bar{c}} + \theta}\ln\gamma \tag{39}$$

or

$$\hat{y}_t^* = \frac{\Lambda\frac{\bar{g}}{\bar{c}} + \Pi}{\Lambda\frac{\bar{y}}{\bar{c}} + \theta}\hat{g}_t - \frac{\frac{\bar{\tau}}{1-\bar{\tau}}}{\Lambda\frac{\bar{y}}{\bar{c}} + \theta}\hat{\tau}_t + \frac{1+\theta}{\Lambda\frac{\bar{y}}{\bar{c}} + \theta}\hat{z}_t \tag{40}$$

28 Alternatively, it could be assumed that the right hand side of (38) equals a 'small' positive constant.

In (40), y_t^* is the flexible price level of output which Railavo, 2003 and 2004a call potential output. As can be seen from the equation, an expansionary fiscal policy (via increased g_t or decreased τ_t) will increase potential out.[29] The same effect is achieved via technology changes.

As regards the pricing equation for the firm, it is assumed that the firm faces costs *a* when it changes prices.[30] Higher *a* is associated with more costly price changes. This introduces price stickiness to the model. As in Railavo, 2003 and 2004a, it is possible to take a quadratic approximation of firm's profit around P^*, which reflects the path of prices the firm would follow if there were no costs associated with price changes. The forward-looking firm sets prices by minimising the quadratic cost function

$$\frac{1}{2}E_t\sum_{j=0}^{\infty}\delta_F^j\left[(\ln P_{t+j}-\ln P_{t+j-1})^2+a(\ln P_{t+j}-\ln P_{t+j}^*)^2\right], \tag{41}$$

where $\delta_F=\dfrac{1}{1+\rho_F}, \rho_F>0$ is the discount factor for the firm. First order condition becomes

$$\ln P_t=\frac{1}{1+a+\delta_F}\ln P_{t-1}+\frac{\delta_F}{1+a+\delta_F}E_t\ln P_{t+1}+\frac{a}{1+a+\delta_F}\ln P_t^* \tag{42}$$

Define inflation as $\pi_t=\ln p_t-\ln p_{t-1}$. Note also that the long-run prices $\ln P^*$ are determined by the marginal cost: $\ln P_t^*-\ln P_t=mc_t$ or after log-linearising $\hat{P}_t^*-\hat{P}_t=\hat{m}\hat{c}_t$. Then, the equation (42) can be re-written as

$$\hat{\pi}_t=\delta_F E_t\hat{\pi}_{t+1}+a(\hat{m}\hat{c}_t) \tag{43}$$

Using the marginal cost equation (37), equation (43) becomes

$$\hat{\pi}_t=\delta_F E_t\hat{\pi}_{t+1}+a\left[\left(\Lambda\frac{\bar{y}}{\bar{c}}+\theta\right)\hat{y}_t-\left(\Lambda\frac{\bar{g}}{\bar{c}}+\Pi\right)\hat{g}_t-(1+\theta)\hat{z}_t+\frac{\bar{\tau}}{1-\bar{\tau}}\hat{\tau}_t\right] \tag{44}$$

The equation expresses the Philips curve as deviations from the steady state. Re-write (44) further by using equation (40) for the potential output. One gets

$$\pi_t=\delta_F E_t\pi_{t+1}+a\left[\left(\Lambda\frac{\bar{y}}{\bar{c}}+\theta\right)\left(y_t-y_t^*\right)\right] \tag{45}$$

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29 Note again that if $\sigma>1$, then Π gets negative values. In other words, increase in g_t may not increase potential output if coefficient σ gets 'large' values.

30 See also Rotemberg, 1987.

This is what Railavo, 2003 and 2004a calls the new Keynesian supply curve where the current inflation depends on future, not past inflation. As can also be seen from the equation, fiscal policy has effects on inflation via potential output.

2.3 The government

The government can commit its fiscal policies, or alternatively it can not. The latter case is referred to as fiscal discretion. The monetary authority, in turn, follows a Taylor-type interest rate rule.

First, define the government's nominal flow budget constraint as

$$B_t + \tau_t Y_t + M_t - M_{t-1} = (1+R_{t-1})B_{t-1} + G_t, \tag{46}$$

where B_t stands for government bonds, $\tau_t Y_t$ for tax revenue, M_t for nominal money balances and G_t for government spending.

Dividing (46) by P_t , using approximation $(1+r_t) = (1+R_t)(1-E_t\pi_{t+1})$ and recalling $1-\pi_t = \dfrac{P_{t-1}}{P_t}$ gives the government's real flow budget constraint

$$b_t + \tau_t y_t + \pi_t m_{t-1} + m_t - m_{t-1} = (1+r_{t-1})b_{t-1} + g_t, \tag{47}$$

which states that the budget is balanced when 'new' debt (b_t), tax revenue ($\tau_t y_t$) and seigniorage revenue ($\pi_t m_{t-1} + m_t - m_{t-1}$) equal payments on 'old' debt ($(1+r_{t-1})b_{t-1}$) and government spending (g_t). The intertemporal budget constraint is

$$(1+r)b_t \le \sum \left(\frac{1}{1+r}\right)^i (\pi_{t+i} m_{t-1+i} + m_{t+i} - m_{t-1+i} + \tau_{t+i} y_{t+i} - g_{t+i}), \tag{48}$$

which states, in turn, that the maximum level of outstanding debt (including the interest payments) is given by the discounted level of seigniorage revenues and by the difference between tax revenue and public spending.

Finally, the government expenditure can be written as

$$g_t = \rho_g g_{t-1} + \varepsilon_t^g, \tag{49}$$

where $0 \le \rho_g \le 1$ and the white noise supply shock $\varepsilon_t^g = i.i.d.(0, \sigma_\varepsilon^2)$.

2.3.1 Fiscal commitment

Fiscal commitment in this context means that the government is able to choose its policy once and for all at the start of the game. Persson and Tabellini, 2000 call this type of policies ex ante optimal policies. Policies are said to be credible in the sense that a government can influence private-sector's expectations. The government's problem is modelled according to Ramsey primal approach.[31] The basic idea is to eliminate taxes and prices from the household's budget constraint by using the first order conditions. The government maximises the household's utility function subject to the constraints that ensure the existences of prices and taxes so the government's allocation is consistent with the optimising behaviour of the household and the firm. Under commitment regime, the government commits to the tax policy as a Stackelberg leader after which the private sector forms its expectations.

First, recall the economy's resource constraint (26). To obtain the resource constraint needed in the Ramsey approach, substitute (26) into the firm's production technology-equation (31). This yields

$$c_t + g_t = Al_t \tag{50}$$

Next, to obtain the second constraint needed in the primal approach, so-called implementability constraint, one needs to replace $(1+r_{t-1})$, $w_t(1-\tau_t)$ and $(1-\pi_t)$ from the household's budget constraint (4). First, recall the Euler condition (10). Slight manipulation gives

$$(1+r_{t-1}) = \frac{u_c(c_{t-1}, g_{t-1}, m_{t-1}, l_{t-1})}{\delta u_c(c_t, g_t, m_t, l_t)} \tag{51}$$

A combination of equations (6), (7) and (9) yields

$$(1-\pi_t) = \frac{u_c(c_{t-1}, g_{t-1}, m_{t-1}, l_{t-1}) - u_m(c_{t-1}, g_{t-1}, m_{t-1}, l_{t-1})}{\delta u_c(c_t, g_t, m_t, l_t)} \tag{52}$$

Finally, a combination of (6) and (8) yields

$$w_t(1-\tau_t) = -\frac{u_l(c_t, g_t, m_t, l_t)}{u_c(c_t, g_t, m_t, l_t)} \tag{53}$$

Then, the government maximises the associated Lagrangian function[32]

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31 Ramsey, 1927. See also Chari and Kehoe, 1999 where the procedure is explained.

32 In order to simplify the notation, $u(c_t, g_t, m_t, l_t)$ is written simply as u^t. As before, the subscripts refer to partial derivatives.

$$L = E_t \sum_{t=0}^{\infty} \begin{array}{l} \delta_G^t u^t + \mu_t^1 \left[\left(\dfrac{u_c^{t-1}}{\delta u_c^t} \right) b_{t-1} - \left(\dfrac{u_l^t}{u_c^t} \right) l_t + \mathrm{X}_t - c_t - m_t + \left(\dfrac{u_c^{t-1} - u_m^{t-1}}{\delta u_c^t} \right) m_{t-1} - b_t \right] \\ + \mu_t^2 (c_t + g_t - Al_t) \end{array} \tag{54}$$

where the part in outer brackets have been obtained by replacing $(1+r_{t-1})$, $w_t(1-\tau_t)$ and $(1-\pi_t)$ from the household's budget constraint (4) by using equations (51)-(53). The government's discount factor is $\delta_G = \dfrac{1}{1+\rho_G}, \rho_G > 0$ and μ^1 and μ^2 are the Lagrange multipliers. Note further that if implementability and resource constraints hold, then the government's intertemporal budget constraint (48) is also satisfied.

First order conditions then become

$$u_c^t + \mu_t^1 \left[\frac{\delta_G^{-1} u_{cc}^t \left[u_m^{t-1} m_{t-1} - u_c^{t-1} m_{t-1} - u_c^{t-1} b_{t-1} \right] + u_{cc}^t u_l^t l_t}{(u_c^t)^2} - 1 \right] + E_t \mu_{t+1}^1 \frac{u_{cc}^t (b_t + m_t)}{\delta_G E_t u_c^{t+1}} + \mu_t^2 = 0 \tag{55}$$

$$u_m^t - \mu_t^1 + E_t \mu_{t+1}^1 \left[\frac{u_c^t - u_{mm}^t m_t - u_m^t}{\delta_G E_t u_c^{t+1}} \right] = 0 \tag{56}$$

$$u_l^t - \mu_t^1 \left[\frac{u_{ll}^t l_t + u_l^t}{u_c^t} \right] - \mu_t^2 A = 0 \tag{57}$$

$$c_t + g_t - Al_t = 0 \tag{58}$$

$$-\mu_t^1 + E_t \mu_{t+1}^1 \frac{u_c^t}{E_t u_c^{t+1}} = 0 \tag{59}$$

The idea is to solve for $\hat{c}_t$ and $\hat{l}_t$, plug them back to the household's first order conditions and finally solve for the "commitment tax rate" τ_t^C . First, use the first order conditions to eliminate the Langrange multipliers and "A" from (55) and (57), respectively. This gives

$$u_c^t + \left[\frac{u_m^t u_c^t - u_m^t u_{mm}^t m_t - \left(u_m^t\right)^2}{u_{mm}^t m_t + u_m^t} + u_m^t\right]$$
$$\left[\frac{\delta_G^{-1} u_{cc}^t \left(u_m^{t-1} m_{t-1} - u_c^{t-1} m_{t-1} - u_c^{t-1} b_{t-1}\right) + u_{cc}^t u_l^t l_t}{\left(u_c^t\right)^2} - \frac{\left(u_{ll}^t l_t + u_l^t\right) l_t}{u_c^t (c_t + g_t)} - 1\right] + \frac{u_m^t u_{cc}^t (b_t + m_t)}{u_{mm}^t m_t + u_m^t} + \frac{u_l^t l_t}{c_t + g_t} = 0 \tag{60}$$

$$u_l^t - \left[\frac{u_m^t u_c^t - u_m^t u_{mm}^t m_t - \left(u_m^t\right)^2}{u_{mm}^t m_t + u_m^t} + u_m^t\right]\frac{u_{ll}^t l_t + u_l^t}{u_c^t}$$
$$+\left(\frac{c_t + g_t}{l_t}\right)\left[\begin{array}{l} u_c^t + \left[\frac{u_m^t u_c^t - u_m^t u_{mm}^t m_t - \left(u_m^t\right)^2}{u_{mm}^t m_t + u_m^t} + u_m^t\right] \\ \left[\left[\frac{\delta_G^{-1} u_{cc}^t \left(u_m^{t-1} m_{t-1} - u_c^{t-1} m_{t-1} - u_c^{t-1} b_{t-1}\right) + u_{cc}^t u_l^t l_t}{\left(u_c^t\right)^2} - 1\right] + \frac{u_m^t u_{cc}^t (b_t + m_t)}{u_{mm}^t m_t + u_m^t}\right] \end{array}\right] = 0 \tag{61}$$

Next steps are to write these equations using the CRRA-function (13), to log-linearise the resulting equations using Uhlig's, 1999 method (see (27) above) and to solve for $\hat{c}_t$ and $\hat{l}_t$, respectively. This yields

$$\hat{c}_t^C = \frac{\mathrm{B}^{Cc}\hat{g}_t - \Delta^{Cc}\hat{l}_t^C - \mathrm{E}^{Cc}\hat{m}_t - \mathrm{H}^{Cc}\hat{b}_t + \mathrm{I}^{Cc}\hat{c}_{t-1}^C + \mathrm{K}^{Cc}\hat{g}_{t-1} - \mathrm{N}^{Cc}\hat{m}_{t-1} + \mathrm{O}^{Cc}\hat{b}_{t-1}}{\mathrm{T}^{Cc}} \tag{62}$$

$$\hat{l}_t^C = \frac{\mathrm{B}^{Cl}\hat{c}_t^C + \Delta^{Cl}\hat{g}_t - \mathrm{E}^{Cl}\hat{m}_t - \mathrm{H}^{Cl}\hat{b}_t + \mathrm{I}^{Cl}\hat{c}_{t-1}^C + \mathrm{K}^{Cl}\hat{g}_{t-1} - \mathrm{N}^{Cl}\hat{m}_{t-1} + \mathrm{O}^{Cl}\hat{b}_{t-1}}{\mathrm{T}^{Cl}}, \tag{63}$$

where the multipliers refer to a set of parameter and steady state values.[33]

Finally, one needs to plug the consumption-labour allocation to the household's first order conditions and solve for the tax-rate. Using the marginal rate of substitution between labour supply and consumption (12), the labour demand (31) and the resource constraint (26) yields

$$\theta \ln l_t = (\gamma - 1 - \sigma\gamma)\ln c_t + (1 - \gamma - \sigma(1-\gamma))\ln g_t + \ln(c_t + g_t) - \ln A + \ln(1 - \tau_t) + \ln\gamma \tag{64}$$

or

[33] For a full forms of the equations, see annex 1. The "C" in the superscripts refers to "fiscal commitment" whereas "c" and "l" refer to "consumption" and "labour", respectively. The same applies to equations (71) and (72) where "D" stands for "fiscal discretion".

$$\frac{\bar{\tau}}{1-\bar{\tau}}\hat{\tau}_t = [(\gamma(1-\sigma)-1)+\bar{c}]\hat{c}_t + [(1-\gamma-\sigma(1-\gamma))+\bar{g}]\hat{g}_t - \theta\hat{l}_t - \hat{z}_t \tag{65}$$

Substituting (62) and (63) and solving for $\hat{\tau}_t^C$ finally gives the "commitment tax rate".[34]

2.3.2 Fiscal discretion

In the previous section the government was able to commit to the tax policy as a Stackelberg leader. If such commitment technology is not available, the policy is chosen sequentially and the government re-optimises in every period.[35] The government thus loses the control of private-sector's expectations. The Lagrangian function becomes

$$L = u^t + \mu_t^1\left[\left(\frac{u_c^{t-1}}{\delta u_c^t}\right)b_{t-1} - \left(\frac{u_l^t}{u_c^t}\right)l_t + X_t - c_t - m_t + \left(\frac{u_c^{t-1}-u_m^{t-1}}{\delta u_c^t}\right)m_{t-1} - b_t\right] \\ + \mu_t^2(c_t + g_t - Al_t) \tag{66}$$

First-order conditions become

$$u_c^t + \mu_t^1\left[\frac{\delta^{-1}u_{cc}^t\left[u_m^{t-1}m_{t-1} - u_c^{t-1}m_{t-1} - u_c^{t-1}b_{t-1}\right] + u_{cc}^t u_l^t l_t}{(u_c^t)^2} - 1\right] + \mu_t^2 = 0 \tag{67}$$

$$u_m^t - \mu_t^1 = 0 \tag{68}$$

$$u_l^t - \mu_t^1\left[\frac{u_{ll}^t l_t + u_l^t}{u_c^t}\right] - \mu_t^2 A = 0 \tag{69}$$

$$c_t + g_t - Al_t = 0 \tag{70}$$

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34 Checking the second order conditions in this and following sections is non-trivial. However, none of the simulations indicate these are violated.

35 Velasco, Benhabib and Rustichini, 2001 consider optimal tax policies without commitment by imposing an incentive constraint on the choice of the government. Under this constraint the government chooses not to deviate from the equilibrium policy and the welfare value of continuing with the announced policy must be higher than the welfare value of deviating from it. The idea is to model explicitly the credibility losses that result when the government chooses to deviate from the announced policies on one hand, and the benefit of the revision of the tax plan, on the other. The additional constraint ensures that the revision of the original tax plan is not desirable. On the use of the incentive constraint, see also Persson and Tabellini, 2000.

As above, use the first order conditions to eliminate the Langrange multipliers and "A". This yields

$$u_c^t + u_m^t \left[\frac{\delta^{-1} u_{cc}^t \left(u_m^{t-1} m_{t-1} - u_c^{t-1} m_{t-1} - u_c^{t-1} b_{t-1} \right) + u_{cc}^t u_l^t l_t}{\left(u_c^t \right)^2} - \frac{\left(u_{ll}^t l_t + u_l^t \right) l_t}{u_c^t \left(c_t + g_t \right)} - 1 \right] + \frac{u_l^t l_t}{c_t + g_t} = 0 \quad (71)$$

$$u_l^t - u_m^t \left(\frac{u_{ll}^t l_t + u_l^t}{u_c^t} \right) + \left(\frac{c_t + g_t}{l_t} \right) \left[u_c^t + u_m^t \left[\frac{\delta^{-1} u_{cc}^t \left(u_m^{t-1} m_{t-1} - u_c^{t-1} m_{t-1} - u_c^{t-1} b_{t-1} \right) + u_{cc}^t u_l^t l_t}{\left(u_c^t \right)^2} - 1 \right] \right] = 0 \quad (72)$$

Again, write the equations using the CRRA-function (13), log-linearise and to solve for $\hat{c}_t$ and $\hat{l}_t$, respectively. This yields

$$\hat{c}_t^D = \frac{\mathrm{B}^{Dc} \hat{g}_t - \Delta^{Dc} \hat{l}_t^D - \mathrm{E}^{Dc} \hat{m}_t + \mathrm{I}^{Dc} \hat{c}_{t-1}^D + \mathrm{K}^{Dc} \hat{g}_{t-1} - \mathrm{N}^{Dc} \hat{m}_{t-1} + \mathrm{O}^{Dc} \hat{b}_{t-1}}{\mathrm{T}^{Dc}} \quad (73)$$

$$\hat{l}_t^D = \frac{\mathrm{B}^{Dl} \hat{c}_t^D - \Delta^{Dl} \hat{g}_t - \mathrm{E}^{Dl} \hat{m}_t + \mathrm{I}^{Dl} \hat{c}_{t-1}^D + \mathrm{K}^{Dl} \hat{g}_{t-1} - \mathrm{N}^{Dl} \hat{m}_{t-1} + \mathrm{O}^{Dl} \hat{b}_{t-1}}{\mathrm{T}^{CC}}, \quad (74)$$

where the multipliers again refer to a set of parameter and steady state values.[36] As above, plugging (73) and (74) into (65) yields the "discretion tax rate", $\hat{\tau}_t^D$.

2.3.3 Monetary authority

Interest rate is set according to Taylor type interest rate rule (see Taylor, 1993)

$$R_t = \pi_t + r^* + \eta_1 (\pi_t - \pi^*) + \eta_2 (\ln y_t - \ln y_t^*), \quad (75)$$

where r*is the long-term real interest rate, $\pi *$ is the inflation target, y* is the potential output (see equation 40) and η_1 and η_2 are the Taylor rule parameters for inflation and out, respectively. Monetary policy is tightened with an increase in these parameters. Note that the rule responds to deviations from the inflation target and potential output.

36 For the full forms of the equations, see annex 1. For the notation, see footnote 31.

2.4 Model simulation

The following table presents the parameter values used in the model simulations.

TABLE 1 Parameter values

Parameter	Parameter value
Risk aversion coefficient, σ	0.5
Adjustment cost parameter, a	0.02
Inverse of the labour supply elasticity, θ	1.55
Proportion of utility between private and public consumption, γ	0.8
Steady state variables	
$\bar{c}$	0.8
$\bar{g}$	0.2
$\bar{y}$	1.00
$\bar{b}$	0.3
$\bar{m}$	0.01
$\bar{l}$	0.5
$\bar{\tau}$	0.5
$\bar{R}$	0.01
Coefficient Γ	0.3
Taylor rule parameter for inflation, η_1	0.5
Taylor rule parameter for output, η_2	0.4
Parameter ρ	0.81
Parameter ρ_G	0.975
The household discount factor, δ_H	1
The firm discount factor, δ_F	1
The government discount factor, δ_G	0.98
Output coefficient in Philips curve, $a\left(\Lambda \frac{\bar{y}}{\bar{c}} + \theta\right)$	0.046
Interest rate coefficient of the output equation, $\Phi \frac{\bar{c}_t}{\bar{y}_t}$	1.34

The values correspond broadly to those used in the related literature.[37] The risk aversion coefficient σ is set to 0.5. It is assumed that the household draws its utility mainly from private consumption and thus parameter γ is set to 0.8. Thus the interest rate coefficient of the output equation $\Phi \frac{\bar{c}_t}{\bar{y}_t}$ becomes 1.34. Adjustment cost parameter a is 0.02 and output coefficient in Philips curve

[37] Rotemberg and Woodford, 1998, Clarida, Galf and Gertler, 2000 and Bullard and Mitra, 2002. See also Railavo 2003.

$a\left(\Lambda\frac{\bar{y}}{\bar{c}}+\theta\right)$ is 0.046. Inverse of the labour supply elasticity θ is 1.55, and therefore the wage elasticity of labour supply $\frac{1}{\theta}$ is 0.65. Note that the Taylor rule parameter for output η_2 is set to 0.4. This is smaller than in the original Taylor, 1993 rule meaning that the monetary authority is less interested in output than in Taylor, 1993. Persistence of the two types of shocks hit by the economy is calibrated in a similar fashion than in Railavo, 2003. In particular, Cooley and Prescott, 1995 find that 95 percent of the shock remains after one quarter, so in annual terms parameter ρ is set to 0.81. Further, Blanchard and Perotti, 2002 find that 95 percent of government consumption shock is present after two years, and thus parameter ρ_G is set to 0.975. As noted in Railavo, 2003, these parameter values reflect the economic structure of a large economy, such as the euro area. Finally, the household and the firm discount factors are set to 1, whereas the government discount factor δ_G is set to 0.98.

The system is given by the output equation (29), the real money balance equation (30), the potential output equation (40), the inflation equation (45), the government budget constraint equation (47), the government spending equation (49), the tax rate equations (65) for commitment and discretion and the interest rate rule equation (75), all which are written as deviations from the steady state.

In order to compare how the economy responds under the two fiscal regimes – fiscal commitment and fiscal discretion – the system is hit by two different types of temporary shocks; a technology shock (1 % increase in technology) and a government spending shock (1 % increase in government spending). The following tables show the impulse responses as deviations from the baseline. The solid line represents reactions under fiscal commitment regime and the dash line under fiscal discretion.

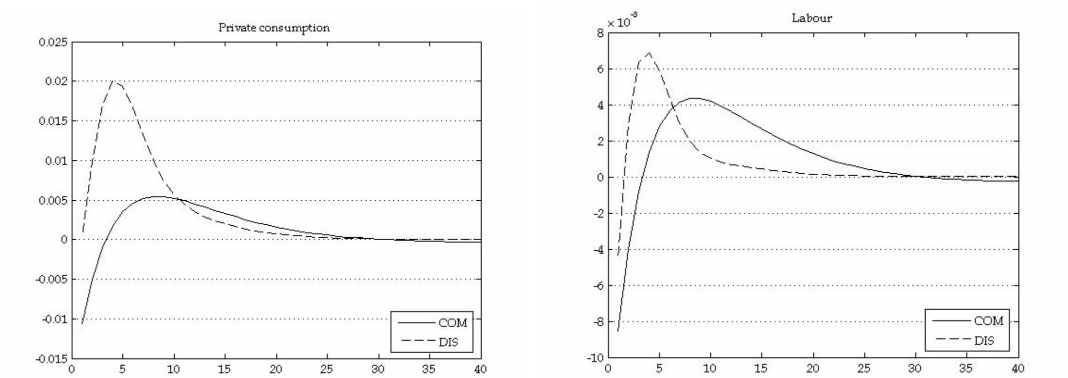

FIGURE 1 Temporary (1 period) 1 % increase in technology (% deviations from baseline) (continues)

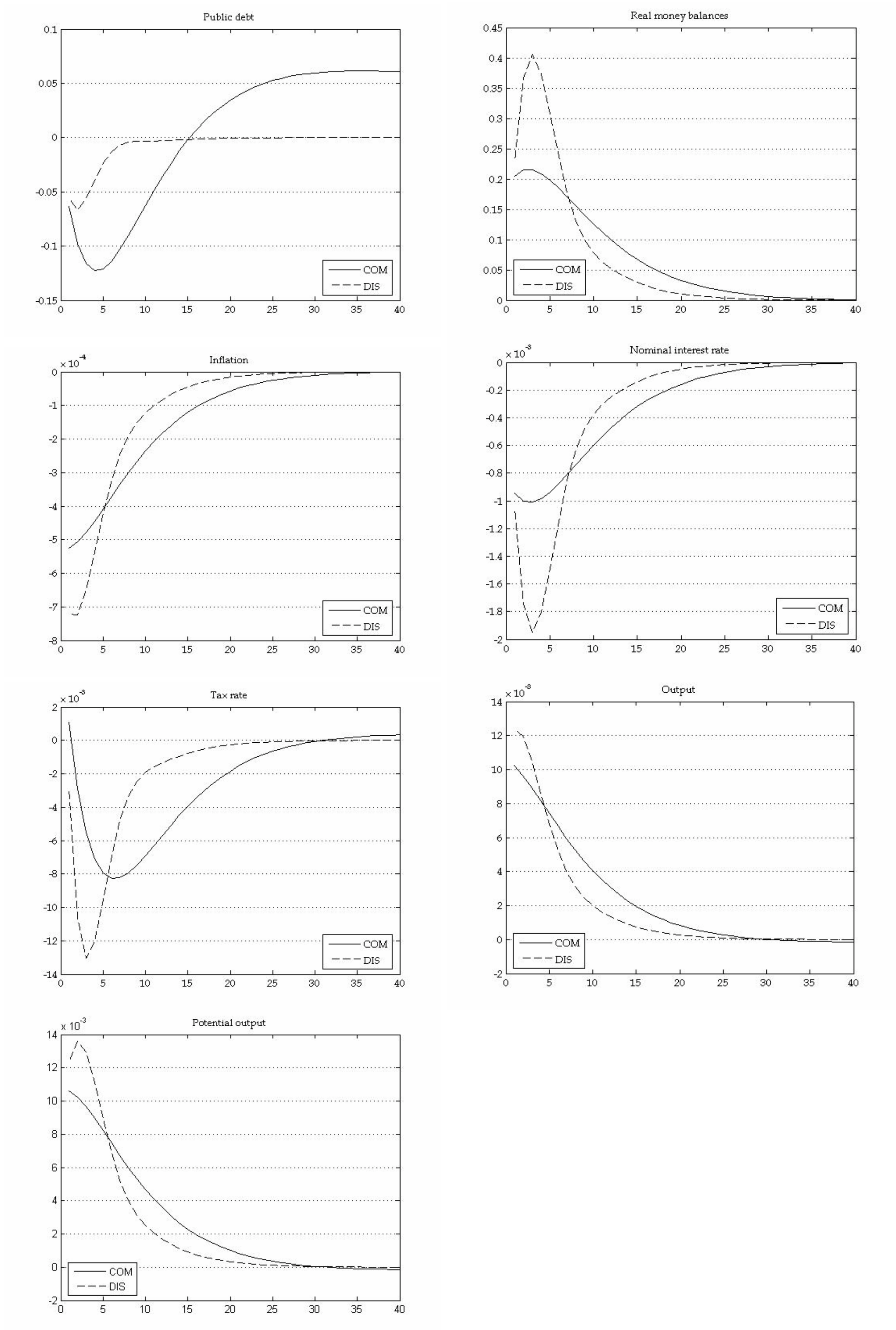

FIGURE 1 Temporary (1 period) 1 % increase in technology (% deviations from baseline) (continued)

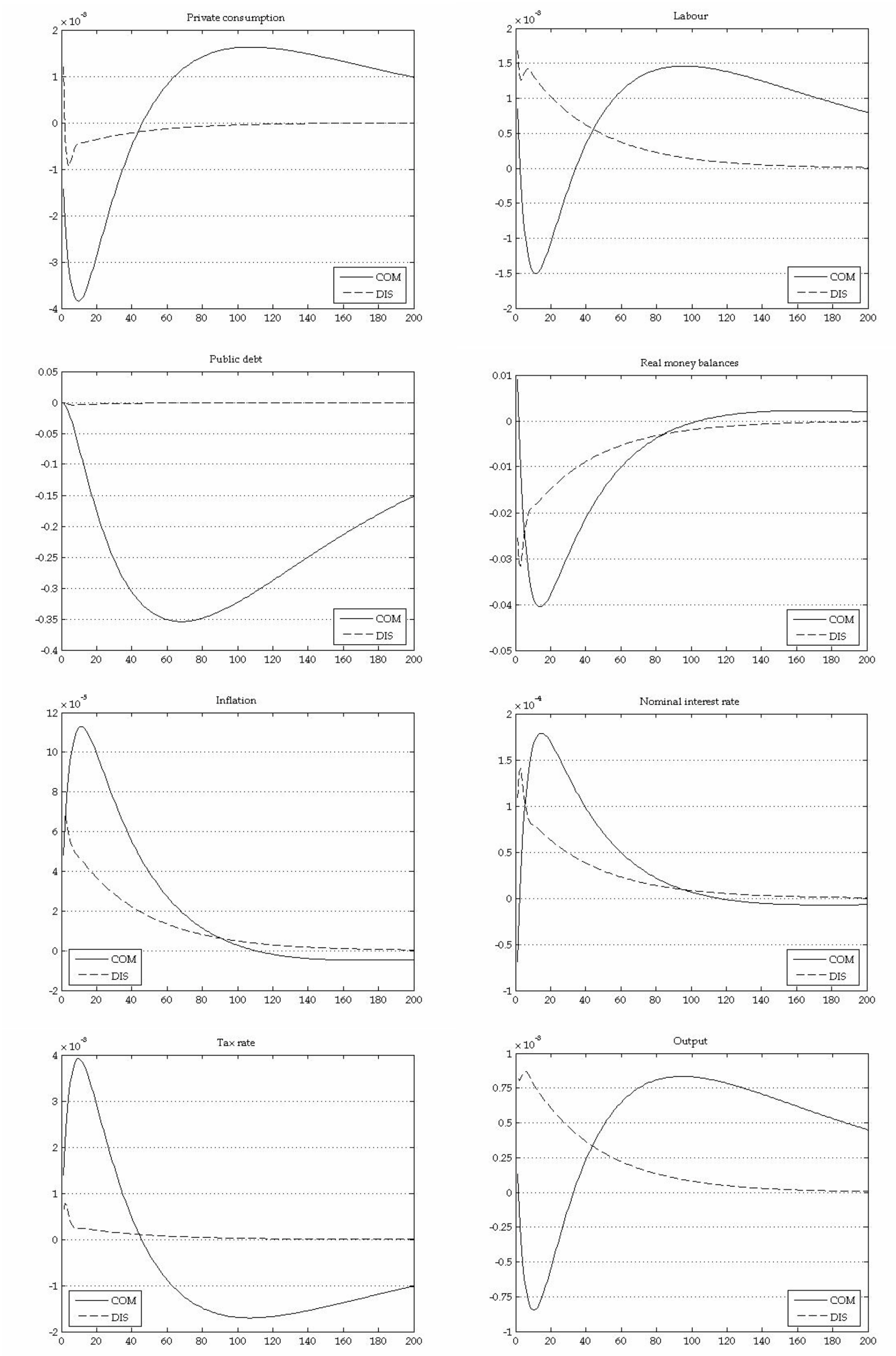

FIGURE 2 Temporary (1 period) 1 % increase in government spending (% deviations from baseline) (continues)

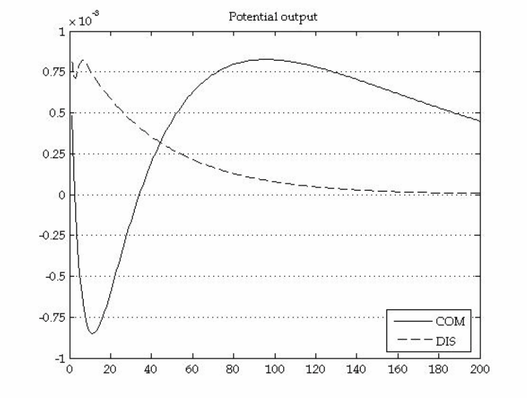

FIGURE 2 Temporary (1 period) 1 % increase in government spending (% deviations from baseline) (continued)

Under the commitment regime, the tax rate reacts negatively to the technology shock. Potential output increases and consequently inflation falls. A fall in tax rate has eventually positive effects on labour[38]. Also private consumption reacts eventually positively. Public debt falls initially but it then increases above the baseline. Overall, the effects are similar under discretion. Public debt reacts negatively even though the tax rate drops. Note that public debt is influenced also by total tax revenue and thus an increase in output (without an increase in public spending) can dominate. Under discretion, the initial reactions are generally stronger and the system returns to its steady state more swiftly.

The public consumption shock increases initially the tax rate under fiscal commitment, and the potential output drops before increasing above the baseline. Recall that in line with the new Keynesian supply curve presented above, fiscal policy has effects on inflation via potential output. Consequently, the drop in potential output causes inflationary effects. Under the discretionary regime the tax rate is increased but only marginally. Thus the increase in public consumption generates an increase in the potential output. Public debt shows a very small reaction. As in the case of technology shock, public consumption shock produces generally larger initial responses under discretion and the convergence towards steady state is faster than under commitment.[39] In the case of the public consumption shock, the convergence towards the steady state is considerably slower under both regimes compared to the technology shock.[40]

Thus generally speaking both shocks produce stronger initial response under the discretionary regime. Under the fiscal commitment the effects of the shocks are more persistent. Note that the results are in line with the results ob-

38 Recall that labour l_t was defined as $l_t = 1 - L_t$, where L_t is leisure.

39 As regards the volatility of the impulse responses, one can note that technology shock produces generally more volatile reaction under discretion than under commitment. This is reversed for the public consumption shock. Regarding volatility of responses in some other studies, Klein and Rios-Rull, 2002 compare commitment and non-commitment fiscal policies in a model with capital and labour. They find that capital income taxes are more, and labour income taxes less volatile under commitment.

40 For a discussion about macroeconomic effects of fiscal policy disturbances, see Barro, 1989 and Baxter and King, 1993.

tained in the literature focussing on monetary commitment and discretion. For example, Walsh, 2003 shows the response of the output gap and inflation to a transitory cost shock. Under monetary commitment regime, the response of both output gap and inflation are more persistent whereas under discretion the system returns quickly to its steady state values. Walsh notes that by keeping output below potential for several periods into the future after a positive cost shock, the central bank is able to lower expectations of future inflation.[41]

Indeed, the literature on optimal monetary policy has stressed the value of policy commitment. As noted by Woodford, 2003, discretionary optimisation does not generally produce optimal outcomes, despite of having some intuitive appeal. One might think that analysing the economy's current state and its possible future paths and then choosing the optimal current action consistent with that analysis is a perfectly sensible procedure. However, as Kydland and Prescott, 1977 and 1980 showed, and as is further illustrated by Woodford, 2003, this is true only to the extent that the economy evolves mechanistically as a function of its past state, exogenous disturbances and the current action of the policymaker. As private sector's expectations about future policies are one of the determinants of current outcomes, discretionary policymaking becomes suboptimal. Credible policy-commitment can therefore steer private sector's expectations in a way which enhances policymaker's chances to reach its objectives.[42]

The impulse responses shown above reflect exactly the effect of this expectation-channel. Under commitment-regime the policymaker knows that private sector's expectations about its future policies affect current outcomes. A policymaker thus takes into account this link. Discretionary optimisation, in contrast, is essentially only a sequence of static optimisation problems and expectations are ignored altogether.

While policy commitments have a pivotal role in the model, this chapter did not take explicit position on the type of commitment technology a government utilises. Such fiscal arrangements can include constitutional restrictions, such as credible fiscal rules embodied in a legal framework or reputational mechanisms, such as establishing a solid credibility for the announced policies. Some have suggested delegation of some aspects of fiscal management to an independent agency.[43]

The purpose of this chapter was to establish that fiscal commitment has value over fiscal non-commitment. Woodford, 2003 notes that policy-commitments serve essentially two purposes: they will make it more likely that policymakers themselves will act appropriately, but crucially, policy-

41 See also Railavo, 2004b which presents a model similar to the one here where monetary policy is conducted under two regimes, commitment and discretion. Under commitment, output persistency is increased compared to discretion.

42 The literature on optimal monetary policy has been emphasised here; it has dominated the research on the benefits of policy commitment and has therefore provided a good parallel for the discussion. Contributions that demonstrate the benefits of fiscal commitment include e.g Dixit and Lambertini, 2003a, Persson and Tabellini, 2000, Klein and Rios-Rull, 2002, Velasco, Benhabib and Rustichini, 2001.

43 Eichengreen, Hausmann and von Hagen, 1999 and Wyplosz, 2001.

commitments can also ensure that the actions taken by the policymakers are correctly understood by the private sector.

The emphasis was therefore on policy-credibility; otherwise the government loses its ability to affect private sector's expectations. The focus in the forthcoming chapters is shifted to study how such credible fiscal commitment can be achieved using national fiscal institutions. Credible fiscal commitments are in the heart of this approach, too but the emphasis in the related literature is on the link between solid national fiscal institutions and fiscal discipline. This literature – which is based on a politico-institutional view of fiscal discipline – will be viewed next.

3 LITERATURE SURVEY: FISCAL INSTITUTIONS AND FISCAL DISCIPLINE

The role of fiscal institutions in promoting fiscal disciple and related research has increased substantially during the past decade. This literature includes both theoretical and empirical contributions, both of which will be reviewed below.

3.1 Theoretical issues

Number of political economic models seeking explanations for the behaviour of public deficits and debts has surfaced. [44] Here the focus will be on models where a common pool resource problem, or CPR problem, plays a central role. This view suggests that fiscal biases are a result of coordination failure at the executive and/or the legislature level. Consequently, the ways to alleviate the fiscal bias has to do with dealing the effects of the fragmentation of budget process.

3.1.1 How fiscal deficit bias arises?

There is increasing consensus that one of the major reasons for persistent public deficits (i.e. the bias towards excess spending) stems from the common pool resource problem, or the CPR problem, which can arise when representatives of geographically based constituencies fail to fully internalise the financing costs of projects that benefit their own constituency, because the costs are borne by

[44] For a closer examination, see Alesina and Perotti, 1995, who divide models dealing with politico-institutional determinants of the government budget into six groups: 1) models based upon opportunistic policy makers and naive voters with "fiscal illusion", 2) models of intergenerational redistributions, 3) models of debt as a strategic variable, linking the current government with the next one, 4) models of coalition governments, 5) models of geographically dispersed interests, and 6) models emphasising the effects of budgetary institutions.

taxpayers as a whole.[45] Weingast, Shepsle and Johnsen, 1981 pioneered this literature when they formally modelled the basic public choice mechanism comprising a representative legislature. The same general idea is often applied to deal with issues related to public spending within a government consisting of ministers with different portfolios. The "spending ministers" fail to internalise the full cost of financing expenditure program that benefit his/her ministry which implies that policymakers systematically overestimate the net marginal benefit of increasing public spending, and as a result, spending increased beyond the level which equates marginal costs and benefits.

Early common pool models explain how budget procedures can have an implicit bias towards overspending, but are silent on budget balance. As Alesina and Perotti, 1999 notes, one needs dynamic models to analyse deficits. Technical difficulty lies in the fact that in a dynamic model each legislative vote determines the state of the world (in particular the level of public debt) inherited by the following legislature, or the following vote by the same legislature. Thus, rational legislators should vote today taking into account the effects of their decision on future voting equilibria, with different levels of debt.

Chari and Cole, 1993, take a step in this direction with their two-period model, where a legislature makes collective decisions about local public goods expenditures and how they are financed. In particular, the legislature makes decisions on how much of the expenditures should be financed by current taxes and how much should be debt financed. In the model by Chari and Cole, there is a free rider problem in that spending by each committee chairman is excessively high.[46] Thus, the legislature unanimously prefers to debt finance as a way of reducing such future spending, even when all legislators are certain to continue in office.[47] In other words, if the legislature could commit to future spending decisions, the equilibrium level of debt is optimal, though the spending levels are not. Legislators prefer to use debt as a way to control excess spending if commitment is not possible.

Hallerberg and von Hagen, 1999 too show that the common property approach is able to generate excess deficits. They propose an extension to two periods of the model of budgeting within government proposed by von Hagen and Harden, 1996. The budgeting decision now involves not only allocating funds among the spending ministers but also setting taxes endogenously in order to meet the intertemporal budget constraint. Again, individual spending

45 For an overview of literature on common pool problem, see the presentations by Ostrom, Gardner and Walker, 1994, von Hagen, 1998, and Poterba and von Hagen, 1999a and contributions therein.

46 Chari and Cole consider the case of US Congress. The authors work is motivated by the arguments in Weingast, Shepsle and Johnsen, 1981, who argue that under traditional practice in the US Congress, members defer to spending requests of individual representatives, particularly committee chairmen, who tend to promote spending requests that benefit their own districts.

47 The results resemble those of Persson and Svensson, 1989 where the result is due to political instability, more specifically, due to the assumption that the policymaker is uncertain whether he or she will continue in office, and therefore fishes to restrain spending decisions by future policymakers that might come from another political group.

minister would disregard the externality arising from their expenditure decision, and hence in a completely decentralised budget process both spending and borrowing (in the first period) would be inefficiently high.

Velasco, 2000 focuses on the dynamic aspects of fragmented fiscal policy-making with his infinite horizon model. He considers a society divided into several influential interest groups, each of which benefits from a particular kind of government spending. The central fiscal authority is assumed to be weak, in that each of the interest groups can influence fiscal authorities to set the net transfers on the group's target item at some desired level. All the interest groups share the same budget constraint, enjoying common access to government resources.[48] Velasco shows that a divided government structure lead rational fiscal authorities to run debts and deficits that are "too high". Two distortions are present if a certain number of agents share the stock of resource. First, each uses the whole stock and "their share" of the stock as the basis for consumption or saving decisions. Second, the return on savings as perceived by one agent is the technological rate of return (the rate of interest) minus what the other agents take out. Therefore, assumed that savings depend positively on the rate of return, each agent under-saves (over-spends in the case of fiscal policy). Deficits are thus incurred and debts accumulated even in contexts where there is no incentive for intertemporal smoothing, so that a central planner would run a balanced budget. A related implication of this model is that long-run levels of public debt are higher than those that would be chosen by a benevolent planner.

Essentially the same results are obtained by Velasco, 1999, a companion paper to Velasco 2000.[49] There the author has analysed whether these dynamic budget inefficiencies can be overcome by allowing the groups within the government to develop 'reputations' for low spending. Velasco shows that reputation may indeed cause groups to moderate spending and stabilise the growth of government debt, but only after a period of time during which debt is built up and government wealth falls. A fiscal stabilisation may not be sustainable from the low levels of debt, but may become sustainable once debt reaches a sufficiently high level. In other words, fiscal stabilisation is delayed.

3.1.2 How fiscal deficit bias can be restrained?

Fiscal deficit bias stemming from the CPR problem results from a failure of spending ministers or interest groups to internalise the true costs associated with increased spending. The solutions to deal with this bias emphasise the importance of fiscal institutions, broadly defined as the rules and regulations according to which budgets are prepared, approved and implemented. Implicit idea then is that by changing these rules, a country's fiscal performance can be

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48 This set-up can be interpreted, for example, as having sectoral ministers with special interest that overwhelm weak finance minister.

49 There are some technical differences between Velasco, 1999 and 2000. The former employs a discrete time model with an equilibrium concept of 'switching equilibrium', not Markovian as in the latter paper.

altered in a predictable way. In other words, if policy outcomes are influenced by variables related to institutional characteristics, then one has to intervene at the institutional level to improve policymaking.

In the literature, three different phases of a budget process is usually identified: the formulation of a budget proposal within the executive, the presentation and approval of the budget in the legislature, and the implementation of the budget by the bureaucracy (see table 2).

Most of the literature has focussed on the first two phases of the budget process. This emphasis seems justifiable since during these phases it is established who have an influence on the final budget outcome and when, as well as what is the size of the budget. These phases also illustrate the different decision-making arenas in a budget process: the executive formulates the budget proposal after which the legislature debates, amends and votes on it.

TABLE 2 Illustrative phases of a budget process

Action
Executive Planning Stage Formulation of budget targets and guidelines Preparation of budget bids Compilation of budget draft Reconciliation Finalisation of budget proposal
Legislative Approval Stage Debate, amendment of and vote on budget proposal Approval by government
Implementation Stage Execution of the budget act In-year changes of the budget
Ex-post Control and Accountability

Source: von Hagen and Harden, 1994

Decision-making within the executive

One major implication of the common-pool models reviewed above is that fiscal institutions that lead participants in the budgeting process to internalise the costs of budget deficits will lead to smaller budget deficits. Von Hagen, 1992, von Hagen and Harden, 1994 and 1996 analyse the bias towards excess public spending in a game theoretic framework where centralisation is introduced by creating a dominant player in the budget process, usually the finance minister, who is vested with strategic prerogatives over the spending ministers. Similarly, this approach involves vesting the executive branch of government with strategic superiority over the legislative branch. The other approach to achieve centralisation is through collective negotiation among relevant policymakers to determine budget targets early in the budget process. Therefore, centralisation of the decision-making in the budgetary process can help overcome fragmentation of the budgetary process by allowing a comprehensive view of the budgetary implications of all measures to be taken into account, and forces participants to the process to recognise the real costs and benefits of each measure.

Indeed, the existence of fiscal biases stemming from political economy aspects has served as a justification for two ways to promote centralisation in different phases of the budget process, and consequently fiscal rigour: *commitment* which brings commitment via set of binding limits or targets on expenditure which are negotiated collectively at the beginning of a budgetary process, and *delegation* of fiscal powers to ″a fiscal entrepreneur″ (prime minister or "strong" finance minister).[50]

Delegation essentially implies a transfer of fiscal powers from the assembly to the executive, and within the executive from the various spending departments to one minister, normally the finance minister. To be effective, entrepreneur of delegation approach must be able to monitor others, have selective incentives at his disposal, and be willing to bear the costs of monitoring. Once the government has approved the budget, the parliament can make only limited amendments to it. Under the commitment approach, the targets are negotiated among the different ministers at the beginning of the budgetary process, often on a multi-year horizon. Agreed targets become binding for all departments and are regularly reviewed to verify compliance. Finance minister's role can be important especially in enforcing the existing contract. The parliament has a strong position in this process especially in monitoring the budget's implementation.

There is also a third approach which Hallerberg et al 2001 refer to as *hybrid*. The hybrid solution is most likely to be found from countries where minority governments are the norm, and this approach draws on features from both delegation and commitment. Within the government, finance minister has an important role in formulating their budget proposals but since the government can not pass the budget without gathering support from the opposition, ideally there should be an understanding, or even a contact, between the government and one or more opposition parties so as to ensure support needed to pass the budget and to prevent last minute bids by the opposition to extort further concessions from the government.

Finally, countries that have decentralised budget processes and that have thus done little to address the CPR problem are referred to as *fiefdom* governments. Spending ministers consider their spheres as their own fiefdoms are there are no mechanisms in place to encourage taking a global view on the budget process.

The proponents of this view, according to which strong fiscal institutions provide the route for greater fiscal discipline, are often called "fiscal institutionalists". "Electoral institutionalists", on the other hand, emphasise the role of

50 See von Hagen, 1992, von Hagen and Harden, 1994 and 1996. Alesina and Perotti, 1999 use somewhat different terminology. They call institutions that attribute strong powers to prime minister or finance minister as *hierarchical*, and institutions that emphasise prerogatives of spending ministers (and jointly negotiated targets) as *collegial*.

political fundamentals.[51] The dynamics in the latter models stem from political instability and the focus is on the conflict and ideological polarisation between parties. The current government is unsure of its possibilities for re-election and it attempts to use debt as a strategic variable. As a coalition government consists of number of different parties, this implies that coalition governments are less able to deal effectively with negative shocks compared to single party governments. Electoral systems have, in turn, major impact on the government formation.[52] As proportional representation systems, or PR-systems, tend to produce coalition governments (whereas plurality-majoritarian systems produce single-party governments), this implies that PR-systems are conducive to greater public deficits.

Both of these approaches have received criticism. Political fundamentals are deeply rooted in countries' history and tradition and are therefore difficult to change. If these political factors are seen as the underlying reason for poor fiscal performance, policy conclusions are difficult to draw. On the other hand, it is perhaps not plausible to think that one can disregard a country's political tradition altogether and argue that a certain type of fiscal institution provides "one-size-fits-all" solution. Further, this view does not seek to explain why some countries employ a certain type of fiscal institution and others do not.

Hallerberg and von Hagen, 1999 establish a connection between the design of the budget process and a country's electoral system. They show that the distinction between one-party and multiparty governments affects which fiscal institution (i.e. delegation or commitment) a country will (should) use to promote fiscal discipline. In states with plurality systems where one-party governments are the norm, centralisation can be achieved effectively by delegating strong agenda-setting powers to a finance minister, whereas in states with systems of proportional representation, and where multiparty coalitions are the common form of government, the CPR problem is solved by a commitment to fiscal targets negotiated among the coalition partners.

The reason why one-party governments can be expected to opt for delegation approach follows from the expectation that members of the same political party are likely to hold similar views. The players therefore share the same views regarding the distribution of funds and conflicts of interest arise only from the common-pool problem. In a coalition government, in contrast, cabinet members are more likely to have different views regarding the distribution of transfers. Agreement of the budget therefore involves a compromise between the coalition partners. Delegating agenda-setting powers to the finance minister creates a problem because he is a member of one of the coalition parties himself, and a delegation creates a principal agent problem. The problem does not arise in the case of commitment, since fiscal targets are negotiated collectively.

The second distinction between delegation and commitment approaches follows from the scope and strength of the punishments and rewards a finance

51 See Tabellini and Alesina, 1990, Persson and Svensson, 1989 and Roubini and Sachs, 1989.

52 The role of electoral systems will be discussed in greater detain in chapter 4.

minister can use to assure the adoption of his proposal. During the budget negotiations, the finance minister's power must be backed by the prime minister and since the prime minister in one-party government is the strongest cabinet member, his backing gives the finance minister considerable fiscal powers over spending ministers in a single-party government.

Finally, the scope of punishments for defecting from an agreed budget forms the third distinction. In a one-party government, the ultimate punishment for a single cabinet member who overspends is dismissal from the government. Since consequences from such punishment are mild for the government as a whole, it is fairly easy for a prime minister to enforce. The threat that the coalition breaks up if a spending minister overlooks the contract agreed collectively forms more effective punishment mechanism in the case of coalition governments.

Decision-making within the legislature

Once the executive has formulated the budget proposal, it is the legislature which debates, amends and votes on it after which it is finally approved by the executive.

A considerable body of literature has examined decision-making within legislatures, and the relative powers between the executive and legislature. It has focussed on functioning of parliamentary committees in general, and on procedural rules which determine how the legislature can alter the executive's budget proposal.[53] Indeed, assuming that the legislature can propose changes – but not without restrictions – the issue is what procedural rules mitigate or aggravate the problem of oversupply of pork barrel projects[54]. The voting and the amendment rules are in the heart of this discussion.[55]

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53 Hallerberg and Marier, 2004 have considered to what extent it is desirable in the first place to increase the executive's powers relative to the legislature. They argue that the level of the CPR problem in the parliament depends on the type of electoral system. In other words, the differences across electoral systems lead to systematic differences in the level of fragmentation within parliament. In particular, the more candidate-centered the electoral system is, the higher is the level of fragmentation. Consequently, the need to increase the executive's fiscal powers over the legislature is larger, the higher the level of fragmentation is. Therefore, it is not necessarily the case that stronger executive improves fiscal rigour. Following Carey and Shugart, 1995 and based on the details of the electoral systems, they create an index for the incentives of personal vote which reflects the degree of fragmentation within the legislature, and using a data set for the Latin American and Caribbean countries they find evidence to support the notion that strengthening of the executive's position is most effective when the personal vote is high. No such exercise has been performed for EU-15 or for the CEECs. Hallerberg, 2001 uses personal vote index for the EU-15 to consider whether parliament committees in states with high personal vote have in practise more restrictive procedures in place compared to states with low personal vote. The evidence generally follows the expectation.

54 When a collectively financed program whose benefits are concentrated in a small group is thought to have social costs that exceed the social benefits, it is commonly referred to as a "pork barrel spending". See e.g. Drazen, 2000.

55 The models developed initially for the analysis of the legislature, especially US Congress, could be used, after some changes, to analyse in abstract terms the dynamics of

Parliamentary procedures' impact on political outcomes has been subject to a long debate.[56] Doubts have been expressed as to whether parliaments have in general an important role to play anymore in legislative processes, or have they become a mere "rubber stamp" approving the executives' proposals. Recent neo-institutional literature has made a contribution to this discussion by applying the rational choice theories to examine to what extent policy outcomes are affected by the institutions, including parliaments, in which they are processed.[57] The role of parliamentary committees has especially been emphasised. As Mattson and Strøm, 1995 note, "as anyone who has observed such bodies [parliaments] in action will have noted, much of the real deliberations take place away from the plenary arena in much smaller groups of legislators such as legislative committees" (249).[58]

Much of this literature on parliamentary committees has been motivated by the committee structure of the US Congress. It has focussed especially on two functions that parliamentary committees serve. Distributive perspective sees legislators as involved in collective choice situations where members with heterogeneous preferences try to obtain favourable projects – pork barrel projects – through cooperation and deal-making. Such projects, while being favourable to individual members, are however inefficient collectively.[59] The rationale for legislative committees, according to this view, is that members are enabled to make credible commitment because the committees assign "property rights" over specific policy areas to subgroup of legislators and thus distribute spending across different policy areas.

The distributive perspective has been challenged by authors who stress informational aspects of the legislative process. This informational perspective relies on the majoritarian postulate, which asserts that legislative choices, including committee assignments and powers, are ultimately under majority control. Therefore, there is no reason to think that legislative majority would put up with committees which produce budget busting legislation most representatives would oppose. Secondly, informational perspective draws on the uncertainty premise: legislators do not know precisely the relationship between the policy instruments and the policy outcomes. Due to this random component, any given legislation can have an unanticipated outcome. But legislators can mitigate some of these effects through policy specialisation by allowing committees to specialise in particular policy areas. Thus through specialisation committee members can gain private information about the consequences of various policy instruments and provide information to the legislature at large.[60]

Hallerberg, 2000 brings together the literature on parliament committees and the theory on fiscal institutions. His arguments do not establish an unam-

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decision-making also within the executive. In this study the models dealing with executive and legislature, respectively, are nevertheless presented separately.

56 For this discussion, see Döring, 1995a and contributions therein.

57 See Strøm, 1995 and references therein.

58 For a review on how the institutionalisation process of parliamentary committees has evolved, see Longley and Davidson, 1998.

59 See Shepsle and Weingast, 1994.

60 See e.g. Krehbiel, 1991.

biguous direction of causality but he argues that the way the committees are organised can have an effect on the effectiveness of fiscal institutions. More specifically, the expectation is that delegation states should develop weak committees which do not have power to change government bills nor to collect information on individual ministers' actions. These powers would undermine the fiscal powers of finance minister and consequently weaken the effectiveness of delegation approach. Fiefdom states should have equally weak parliaments. Ministers want to have autonomy over the policy decisions in their ministries and they do not want the parliament to challenge that autonomy. Commitment states, on the other hand, should have parliament committees with power to collect information and inform coalition partners from possible defections from jointly negotiated targets.

Similarly to the literature on parliamentary committees, also the literature on the voting rules has been motivated by the US Congress and state legislatures. After the Budget act of 1974, Congress was required to enact a budget resolution that set overall spending levels and then instructed authorisations and appropriations committees to keep within those levels when writing their separate bills, instead of considering appropriations requests one at a time and letting the overall level of spending be determined residually. The idea was to enforce an ex ante fiscal discipline on the legislature by fixing the overall size of the budget rather than letting it to be determined by the accumulation of bills.

Ferejohn and Krehbiel, 1987, study theoretically the determination of the size of the budget under two alternative voting procedures: a budget process and an appropriations process. The former resembles the post-1974 period when decision-making involved deciding first on the size of the budget and then on the levels of individual appropriations. The latter then have resemblance to pre-1974 budgeting. The authors assume that the budget can be allocated to two projects, and different legislators have different preferences for the relative preferences of these two projects. The two processes are modelled as sequential two-stage games where the vote of a legislator in the first stage in each of the two processes is influenced by the known preferences of other legislators and by the known consequences of a vote at the second stage.

The conclusion is that it is not always the case that the size of the budget is smaller when the legislatures vote first on the total size of the budget and then on the composition (top-down approach), relative to the case in which the overall budget size is determined as a residual (bottom-up). While the size of the budget is in general not independent of the order of votes, the relative size of the budget with different orders of votes depends on the distribution of legislatures' preferences of budget composition. Thus the effect of sequencing budget decisions on the size of the budget can not be determined independently from the distribution of the policy makers' preferences for spending over various policy dimensions.[61]

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61 This result depends crucially on rationality of budget voters. This is an empirical issue but it is very difficult to observe these preferences in real-life situations. To address this, Ehrhart et al, 2000 conduct a series of controlled laboratory experiments with a series of independent trials of voting over budgets.

The intuition of this result is that regional legislators should be forward looking: when voting on the first item on the budget, they will calculate how their first vote will affect the final outcome both in terms of size and the composition. Conversely, when voting on the size first, rational legislators can compute how a certain size will then lead to a certain composition in the following vote.[62]

Chari and Cole, 1995, attempt to show how voting rules can eliminate pork barrel spending. They consider a model in which a central government provides local public goods financed by uniform taxation. The amounts of these goods are determined by majority voting in legislature. The authors allow legislators to make payments to other legislators. These payments are affected by the legislators' voting-behaviour. One interpretation for this set up can be that the interest groups, which a particular legislator represents, make campaign contributions. They show that in such an environment, an inefficiently high level of local public good is provided. They also allow legislators to make payments to bill proposers contingent on the nature of the bills that are proposed. The authors show that when such payments are allowed there is a free rider problem, so that inefficiently high level of fiscal expenditure results if the legislature has a large number of members and if other legislators are uncertain about proposer's preferences. This inefficiency regarding local public goods disappears with unanimous consent rules, but such a rule works badly for global public goods leading to inefficiency with unanimity. In other words, a one type of voting rule can not achieve desirable outcomes for both local and global public goods.

Turning to literature on the amendment rules, Baron, 1989, 1991 and Baron and Ferejohn, 1989 consider in a series of papers the effect that different amendment rules have on the legislators' choice of how benefits are allocated and on the efficiency of fiscal policies.

This line of research emphasises a distinction between closed and open rules in amendments. In a closed rule procedure, a proposal made by a legislator is immediately approved or voted down. If the proposal fails, a new legislator is called upon in the next session to submit a proposal. An open rule procedure allows members to call for a vote on the original proposal or to put forward an amendment. In the latter case, the proposal and the amendment are put up to a vote, and the winner becomes the new proposal on the floor in the next session.

Baron, 1991, based on the approach pioneered by Baron, 1989 Baron and Ferejohn, 1989, focuses on the sequential nature of legislative action as structured by the rules related to proposal making, amending and voting. He considers a repeated non-cooperative bargaining game where voting is governed by majority rule. In each session randomly selected member of legislature

62 The model by Ferejohn and Krehbiel has been criticised for not considering two problems that top-down budgeting is intended to solve: policymakers who value a large budget as a goal in itself, and policymakers who do not consider fully the costs of the spending programmes they support. An attempt to cover these shortcomings has been made by Hallerberg and von Hagen, 1997.

makes a proposal for the distribution of the benefits among the legislative districts. Distributive programs are characterised by ratio between the aggregate benefits it provides and by the tax cost requited to supply it. More specifically, a concept used in determining the approval or rejection of a proposal is the "critical benefit-cost ratio" which is a function of the size of the legislature and a parameter of the preferences of the members. Any program that has a benefit-cost ratio that exceeds this critical ratio would be proposed and approved by the legislature regardless of whether it is efficient or not. Once the proposal is made, two amendment rules are considered; an open and closed rule.

In the setting of the model, the majoritarian incentive to distribute benefits among a minimal number of districts is strong and can result in the adoption of inefficient distributive programs, that is, programs that has costs exceeding the benefits. The equilibrium proposal will distribute the benefits to a minimal majority of districts required for the proposal to be approved. The ineffectiveness of those programs depends on the procedures employed by the legislature. The possibility of an amendment provided by an open rule can prevent some pork barrel programs from being adopted. This is because members who were not selected to make a proposal can offer an amendment and this increases the cost of attracting his or her vote. That is, more benefits have to be offered to other members and as a result the proposal power of the selected member to exploit other members is reduced. An open rule may however result in delay in adoption of the program which can be regarded of a cost associated with an open rule. When the number of amendments permitted per session is high, the cost of delay is small and an open rule will be preferred to a closed rule when both efficient and inefficient programs exist.[63]

In actual legislatures the agenda setter in the budget process is the government. Thus, closed rules attribute more power to the government and less to the legislature, and are therefore – using the language by Alesina and Perotti, 1999 – more hierarchical. The implication is that with closed rules budgets are approved more rapidly and typically reflect more closely the preference of the government. Thus, a closed rule generally leads to the approval of more inefficient budgets, to the allocation of benefits to a minimum winning coalition, and to a strong "first-mover" advantage to the player who proposed the budget. An open rule yields a more egalitarian distribution of resources and may result in delayed approval of the budget.

Alesina and Perotti, 1999 note that two implications on the choice of rules follow. First, a closed rule is preferable if avoiding delays is an important con-

63 In the context of a parliamentary committee system, the model by Baron predicts that a legislature would assign a closed rule to committee proposals that are believed to have a set of feasible programs for which the benefit-cost ratio is at least one (i.e. efficient proposals). This is due to desire to avoiding the delays in the decision-making that can be associated with an open rule. But importantly if the committee had better information about the cost-benefit ratio than the legislature, the latter may prefer to grant a restrictive amendment procedure to the committee's proposal with a view of creating an incentive for expertise. The role of information in legislative decision-making under uncertainty has been addressed for example by Gilligan and Krehbiel, 1989 and Krehbiel, 1991.

sideration. This is likely to be the case in high-debt countries or in periods of macroeconomic instability. On the other hand, in countries and periods of low debt and fiscal stability, considerations of allocative efficiency and fairness may be predominant, leading to adoption of an open rule. (20)

Strauch, 1999 extends the framework of Baron, 1989, 1991 and Baron and Ferejohn, 1989 to a bargaining process between leaders, such as the governor and the legislative leadership, and members. The two types of agent bargain about the size of the budget because the leaders take the social costs of the entire budget into account while the members focus on special constituencies and, therefore, demand higher spending. In addition, Strauch, 1999 considers the ex post veto power of the executive. The model yields two main results: first, endowing the leadership with strong proposal and particularly ex post veto authority offers a powerful tool for curtailing the budget. Second, the constellation of rules matters. While the open rule procedure with veto authority of the leader produces lower budgets than would a simple open rule without the executive veto option, a closed procedure may yield lower expenditures than an open procedure with veto authority. In other words, the entire constellation of institutional rules is important when explaining the final budget outcome.

As a summary of the vast theoretical literature discussed above, the models seeking to explain the fiscal deficit bias emphasised the role of the coordination failure at the executive and legislature level. In the reviewed models, the playing field consisted either of the representatives of geographically based constituencies, a government consisting of ministers with different portfolios or simply of a society divided into several influential interest groups each of which benefits from a particular kind of government spending. The general idea in the CPR models is that the players share an access to a common pool of tax resources. Each player considers the benefits of his/her increased spending but as a result the socially optimal spending level which equates marginal costs and benefits is exceeded, even if the individual spending projects are rational from the individual player's point of view. The literature that has focused on the ways to alleviate this spending bias argued that the excess spending stemming from this fragmentation can be restrained by forcing the players to take the global view into account. In the context of the budget process, which is the main focus of this paper, this meant either investing one minister within the cabinet with significant fiscal powers over other ministers or jointly negotiating binding fiscal targets. The relationship between the executive and the legislature is not without significance, either. The legislature's powers vis-à-vis the executive are defined by the type of voting and amendment rules in the plenary and more generally by the overall characteristics of its parliamentary committees.

3.2 Empirical evidence

Empirical work has been numerous, but as noted by Poterba and von Hagen, 1999b, they suffer from the fact that institutional environments of national fiscal policy are complex and therefore difficult to characterise empirically. Existing empirical work have developed number of ways of characterising budget rules, political institutions and other factors that may affect fiscal policy.

One branch of literature has developed numerical indices summarising key aspects of relevant institutional features with a view to gather wide range of information about the different phases and aspects of the budgetary process. This can include the government preparation of the budget, the legislative phase, the implementation phase, the degree of transparency of the budget and the existence of numerical targets.

This approach has been used in regression analysis but it is subject to some obvious deficiencies. Indeed, it is difficult to construct indices that could capture the complex reality of budget making. Furthermore, following Alesina and Perotti, 1999, an objection for this research strategy is that institutions are themselves endogenous. Institutions may be changed as a result of unsatisfactory fiscal performance and the choice of different institutions may be a function of other socio-political-historical variables that may influence both the institutional choice and fiscal outcome. This would seem to make institutions a poor explanatory variable. However, as is also noted by Alesina and Perotti, institutions are fairly difficult to change and as a result there is a strong status-quo bias in institutional reform. Therefore, at least to a point one can use institutional features as explanatory variables.

The other approach often employed is case studies which can be richer in details but lacks statistical features. Nevertheless, it is worthwhile to note that different approaches have lead to similar conclusions regarding the role of fiscal institutions. It would seem that these different empirical treatments can be employed to cover each other's shortcomings.

Based on analysis of budgetary processes, von Hagen, 1992 – and subsequently von Hagen and Harden, 1994 and 1996 – construct indices which rank the budgetary procedures according to institutional characteristics that should promote coordinated and cohesive decision-making and thus should be conducive to fiscal discipline. The authors group these characteristics under five items: the structure of negotiations within the government, the structure of the parliamentary process, the informativeness of the budget draft, the flexibility of the budget execution and the long term planning constraint. Using non-parametric tests and regression analysis they use the indices to test their two main hypothesis, that is, "long-term constraint hypothesis" according to which a tight link between budgetary decisions and multi-period fiscal program should be conducive to fiscal discipline, and "structural hypothesis" which states that fiscal discipline is enhanced if budgeting procedures give strong prerogatives to prime or finance minister, limit parliamentary amendments and facilitate strict execution of the budget law.

Their data set consists of fiscal data over the period of 1980-1990 from then-European Community member countries. They find strong support for the structural hypothesis but only weak support for the long-term constraint hypothesis. The authors' interpretation is that a long-term constraint alone is insufficient to overcome the problems of fiscal discipline especially if a country concerned has structural weaknesses in her budgeting procedures.

Following similar method, Alesina et al, 1996 create an index with 10 different components which refer to different stages of budgetary process for 20 Latin American and Caribbean countries. The budget institutions are characterised by "hierarchical-collegial" dimension.[64] Based on the empirical analysis for the period 1980-92, the authors conclude that hierarchical institutions have been associated with more fiscal discipline. Also Stein, Talvi and Grisanti, 1999 focus on Latin American countries. They study both the impact of electoral institutions as well as budgetary procedures on fiscal performance. As regards the latter, the authors follow Alesina et al, 1996 in formulating an index of budgetary institutions. Their analysis covers the years 1990-95. Also their conclusion is that more hierarchical elements in the budget processes produce greater fiscal discipline. Further, they find that countries with large district magnitude, or large degree of proportionality, have larger deficits.[65] However, they do not find evidence that centralised budgetary institutions can compensate the potentially adverse fiscal consequences of proportional representation on fiscal deficits and debt.

Above, Hallerberg and von Hagen, 1999 argued that for countries with one-party governments, delegation to a strong finance minister is effective, whereas countries with multiparty coalitions should use fiscal targets negotiated among the coalition partners. The former are called delegation-states, and the latter commitment-states. The empirical part of their paper lends support to this notion. In particular, they review briefly the electoral systems of the EU-15, and based on this discussion, form predictions about the forms of fiscal management countries should ideally choose. They find that the reality generally follows the expectation, even though some exceptions also exist. The regressions, which cover the years 1981-1994, include dummy variables for the commitment and delegation states. The variables for both fiscal institutions are significant and have a correct sign.

Following similar framework, Hallerberg, Strauch and von Hagen, 2001 perform a comprehensive review of the multi-annual fiscal frameworks and fiscal institutions employed by the EU-15. The motivation for studying multi-annual frameworks stems from the fact that EU countries formulate their fiscal policies under the EU procedures which in turn have a medium-term orientation. The authors find that there is considerable variation in the ways that fiscal

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64 See footnote 50 of this study for the explanation of this terminology.

65 District magnitude measures the average number of representatives elected per district and it is used to characterise differences across electoral systems. See chapter 4.

targets are being set and what is done in practice to achieve those targets. They also find that the link between the fiscal targets and fiscal performance is not particularly strong. However, the empirical evidence indicates that once the distinction between different forms of fiscal management – delegation and commitment – is taken into account, the design of fiscal rules does have considerable importance for fiscal performance.[66] That is, fiscal rules matter, but the way in which they matter depends critically on the broader institutional design of the budgetary process.

The authors also study the relationship between the national budget procedures and the stability and convergence programs. This approach follows from obligation of the EU member states to formulate their budget targets under stability or convergence programs. More specifically, the authors investigate the way these programs are connected to annual budget process. As the authors also note, there has been discussion about how to improve the integration of programs into domestic budget-making. One suggestion has been to require parliaments to pass the stability or convergence programmes as legislation.[67] The reason given is that such involvement would enhance the credibility of the programs both at the EU level and at the national level. According to findings in Hallerberg et al, 2001, this suggestion is misguided. The authors argue that the real disconnect is at the governmental level, not in parliament. They note – in a similar fashion than von Hagen et al, 2002 (see footnote 66) – that the timing of the programs is clearly an issue. Most countries have already drafted budgets for the upcoming year by the time they submit the updates to their programs. If the programs are to have more relevance in the annual budget process, the authors suggest that they be drafted earlier in parallel with the drafting (or conception) of the budget plan.

Very little work has been done on the CEECs. Gleich, 2002 is to date the only published comprehensive study on fiscal institutions and their impact on fiscal performance in these countries over the period of 1994-1998. He follows the method originating from von Hagen, 1992 and constructs indices which measure the degree of centralisation in different phases of budgetary process.

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66 These results could have potentially important implications not only on how countries choose to design their fiscal institutions, but also on EU level coordination procedures. Stability and Growth Pact, or SGP, is an example of a commitment solution which therefore might not be effective in delegation states. On this point, see von Hagen, Hughes Hallett and Strauch, 2002. They provide some preliminary evidence that SGP have worked better in states where the budget process operates under commitment approach. The authors conclude that the procedures under the SGP should be linked more closely to the national budgetary procedures, for example by setting both processes on the same calendar. Further, Hallerberg, Strauch and von Hagen, 2004 argue that since the 'big states' are all delegation states, this line of reasoning provides an additional, institutional explanation of why particularly the large countries have had problems meeting the Maastricht fiscal criteria. Also International Monetary Fund, 2004 argue that the SGP works in the spirit of the commitment approach and thus the Pact is more suitable to commitment countries. It also finds that the fiscal governance approach can explain the weak fiscal performers under the SGP.

67 A similar but not quite as explicit suggestion was included in the report on economic policy coordination by the Council of Economic and Finance Ministers in 1999: "*Moreover, they [national governments] might consider how to improve national parliaments' support for their stability and convergence programmes.*". See para 40 of the Report.

According to his results, countries having more centralised budget institutions have enjoyed higher fiscal discipline.[68] He does not, however, consider the differences between commitment and delegation approaches nor how the political factors have affected the choice and effectiveness of fiscal institutions.[69]

Turning to empirical work on parliamentary committees, Mattson and Strøm, 1995 have utilised the division between distributive and information perspective in analysing the role of parliamentary committees in Western European legislatures. They rely on institutional data-set on the parliamentary committees and use the inter-correlations between different features of the committees to reach more specific and detailed comparisons and analysis on committees' powers – which the authors sub-divide into two dimensions: drafting authority and agenda control – in different countries.

More specifically, if the distributive perspective is correct, then strong legislative committees should be correlated with a system of enforced property rights and should have well-established rights and powers within well-defined jurisdictions. This committee structure should coexist with a structure in which the plenary for a grant committee deference and practice various forms of universalistic behaviour. Finally, the authors expect strong committees coexist with relatively weak political parties unable to crack committee dominance.

The informational perspective, on the other hand, relies more on the notion that committee powers should be a matter of delegation, rather than property rights. There should also be a clear evidence of committee dedication to expertise and information collection, and efforts to strengthen information collection. Those kinds of committees should also those capable of exerting power vis-à-vis the floor.

The authors' findings are associated with both of the competing themes in the literature on legislative organisation. The informational perspective is confirmed by the finding that those features that are associated with the committees' ability to effectively transmit information to the floor foster the type of committee authority that the authors call agenda control. But they also find that drafting authority and committee specialisation go hand in hand. The authors note that while this finding is in no way incompatible with the informational

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68 Gleich uses debt-to-GDP ratio as one of dependent variables in his study. In the case of the CEECs, the use of debt-ratio could be problematic and lead to wrong conclusions. For example, Gleich calculates a spearman rank correlation between the indices formed based on his study and average debt-ratios. The expectation is that strong fiscal institutions (high index values) are associated with lower average debt-ratio. The correlation coefficient confirms this expectation. However, this result is affected by the fact that the two countries with lowest debt levels are Estonia and Latvia. These countries were left with a very small debt burden as Russia inherited the ex-Soviet Union debts. Incidentally, these countries have also very high index values. More generally, debt levels reflect cumulative effects of fiscal management over time and should be interpreted with caution especially in the case of relatively short time periods.

69 Other geographical areas have been covered as well. Empirical work on the US has focused less on budgetary procedures and more on what impact different budget laws have on fiscal positions in different states. See Bayoumi and Eichengreen, 1995 and Poterba 1996. For further empirical studies that have been applied to different regions, see contributions in Poterba and Von Hagen, 1999a.

perspective, it may even more strongly suggest a distributive perspective in which "property rights" to various policy areas are a cornerstone.

Building upon Mattson and Strøm, 1995, Hallerberg, 2000, studies the role of parliamentary committees in the budgetary process within the EU countries and seeks to explain why differences in parliamentary committees' powers across European parliaments exist. Due to small number of cases his conclusions are without statistical significance and thus only suggestive but the author nevertheless finds evidence that committee powers in EU have evolved according to the expectations that followed from the theoretical considerations: according to the formal powers, the parliamentary committees in the delegation states are on average weaker information providers than the parliamentary committees in the commitment states.[70]

70 However, the categorisation of states into commitment and delegation states used in Hallerberg, 2000 – which follows Hallerberg and von Hagen 1999 – differs from the categorisation made in Hallerberg et al, 2001. In fact, in one divides the states according to the latter source, hardly any differences in formal powers between different categories of states exist. This could be due to the fact that parliamentary procedures evolve slowly whereas many states have experienced changes in their fiscal institutions in recent years which have also led to changes in their categorisation. Also, the data on parliamentary committees stem from 1995. One would need comparative data on committees for 2000 in order to make the comparisons more accurate. Finally, Mattson and Strøm, 1995 and Hallerberg, 2000 considered only formal powers of parliamentary committees. Hallerberg, 2001 makes a similar comparison based on the "Study of the Parliamentary Passage of Legislation"-database which includes information on how the formal powers have been implemented in practise. Conclusions are somewhat different for commitment and fiefdom states. The former group of countries have not in practise often exercised their right to collect information. Parliamentary committees in fiefdom states, on the other hand, have been most active in collecting information.

4 THE ROLE OF ELECTORAL AND PARTY SYSTEMS IN THE CHOICE OF FISCAL INSTITUTIONS

The Central and Eastern European countries are often characterised as transition economies. Besides economic transition, these countries have obviously been subject to political transition, too. Indeed, political transformation was an inseparable part of the whole transition process as the communistic system collapsed and other forms of government were sought for. The role of government had to be re-defined and the system of governance rebuilt.[71]

The significance of political fundamentals in relation to fiscal institutions has to do with different modes of fiscal governance outlined above, namely delegation, commitment, fiefdom and hybrid. In states where one-party governments are the norm, centralisation of the budget process can be achieved effectively by delegating budgetary powers to a strong finance minister, whereas in states where multiparty majority governments are the common form of government, the common pool resource problem is solved by a commitment to fiscal targets negotiated among the coalition partners. The hybrid solution draws on both of these approaches. Finally, if a country has developed a decentralised budget process, it is referred to as fiefdom government.

This branch of literature states that while fiscal institutions do have an important role in providing fiscal rigour, such institutions can not be examined in isolation from broader political context. In other words, as fiscal institutions are designed to affect the behaviour of political actors, such as political parties, individual ministers or parliament members, a consideration of such arrangements have to take into account underlying political fundamentals which undoubtedly have an effect on the behaviour of political actors.[72]

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71 Notable exceptions from this pattern are China and Vietnam where economic transition has started without significant modifications in their political systems.

72 See also Poterba and von Hagen, 1999b who note that "[…] the work […] suggests an intimate connection between the design of the budget process and other dimensions of a country's constitution […]. Budgetary institutions that work in one constitutional context may fail to work in others, because they do not provide the proper incentives and constraints to promote and enforce agreement on efficient levels of spending and deficits." (11)

The first part of this chapter discusses what role electoral and political systems have in countries' tendency to adopt a certain type of fiscal institution. In addition to simple multi-party vs. single-party comparison, additional features of the party systems that affect the incentives for a government to centralise the budget process need to be analysed before such conclusions can be drawn. These include such factors as the degree of ideological differences between government parties and the overall stability of electoral and party systems. Since many of these factors are difficult to quantify exactly and because the CEECs do not constitute a homogenous group, there is a need for a country-specific discussion. This is done in the second part of the chapter.

4.1 What explains the choice of fiscal institutions?

The theory predicts that a government type is one of the crucial factors determining what form of fiscal governance a country is likely to employ.[73] This is because the number of players within the government and their mutual dynamics affect greatly the willingness of the players to centralise the budget process and the effectiveness of fiscal institutions.

Electoral systems and their effect on party formation have received a fair share of attention in the literature. Duverger, 1951 was the first one to describe how electoral rules shape a nation's political party system. His main idea was that high thresholds favour large parties against small ones, and consequently electoral systems with majoritarian elements – as we will shortly see – are conducive to two-party system.

Duverger's views have been criticised for having the direction of causality backwards; electoral systems are themselves endogenous since parties can, and often do, shape electoral systems; it is thus the party system that shape electoral institutions, not the other way around. Duverger and his descendants have also been accused of having overlooked the importance of social cleavages for the party formation.[74]

The proponents of this alternative approach emphasise the role of social cleavages in the society, such as ethnic, religious or language issues or socio-economic differences, in party formation; if a country has only one cleavage, say left-right cleavage, it is more likely that this country has only two main party blocks each promoting ideology that mirrors this cleavage.[75] If a country simply does not have an ethnic minority, for example, there would not be much demand for a party who would be a champion for ethnic issues.

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73 Government type refers here to a distinction between multi-party and single party governments, and between minority and majority governments.

74 For a review of this discussion, see Cox, 1997.

75 Lipson 1964, Lipset and Rokkan, 1967. The latter presented the famous "freezing hypothesis" according to which the party systems in Western Europe had frozen during the 1950s and 1960s along the cleavage structures.

It is likely that both of these views have an effect on party formation. Neto and Cox, 1997, argue, among others, that these approaches are not mutually exclusive as cleavages and electoral systems do interact. Therefore, the number of parties is a product of both of these factors.

Putting the question about the direction of causality aside, the link between features of electoral systems and number of parties is well established.[76] Electoral systems can be thus expected to have a major impact on the government type. This follows from their influence on the likelihood of one party winning the majority of seats in the parliament, and therefore having an ability to form a one-party majority government.

While there is a large number of details within different election systems, two main categories can be distinguished. *Plurality-majority systems* almost always use single-member districts, meaning that the candidate who receives most votes in an electoral district gets elected. On the other hand, *proportional representation systems*, or PR systems, attempt to reduce the disparity between a party's share of the national vote and its share of the parliamentary seats. If a "large" party wins 30 percent of the votes, it should gain approximately 30 percent of the seats, and a "small" party winning five percent of the votes should consequently gain five percent of the total seats in the parliament.

Under majoritarian systems, a party needs to win majorities to get its candidates elected, and thus these systems do not encourage multipartism. Indeed, plurality-majority systems tend to produce two-party systems, and consequently single-party governments, whereas the PR systems yield multi-party systems and therefore multiparty governments. In other words, systems which operate under lower proportionality favour larger parties, and the fewer parties there are in the parliament, the easier it becomes for a single party to form a government.[77]

Indeed, number of parties is clearly an important element in government formation. If a country has only few parties, it is more likely that one party can gain enough seats to form a majority on its own. At the extreme, if a country only has one party, there is not much uncertainty as to what will be its government type. The "effective number of parliamentary parties" describes relative power parties have in the parliament. If there are, say, four equally strong parties, the number of effective parties is four. But if two of these parties hold 40

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76 In addition to references made above to Duverger's work, see Taagepera and Shugart, 1993.

77 One can also make a distinction between minimal winning coalitions – which do not include parties that are not necessary to reach majority in a parliament, oversized cabinets – which contain more parties than are necessary for majority support, and minority cabinets. Lijphart, 1999, 90-96, includes a discussion on different coalition theories that predict which type of coalitions is the most likely one if no single party can form a majority government on its own. In a nutshell, these theories range from the ones which consider the number of parties as the most crucial factor (parties want to exclude unnecessary partners from cabinet to maximise their share of cabinet posts and power) to theories which emphasise the role of policy preferences (parties with similar policy preferences form and maintain coalitions more easily). Lijphart notes that the latter have been able to predict the actual cabinet coalitions better than the former.

percent of the seats and the other two only 10 percent each, the number of effective parties is reduced to 2.9.[78] Therefore, as the number of effective parties diminishes, we witness a parliament dominated by fewer parties. Put in another way, PR systems are likely to have larger number of effective parties than plurality-majority systems.[79] Consequently, the former systems should be conducive to multiparty governments.

The effective number of parties is linked with a district magnitude, which is one of the most crucial characteristics of any electoral system. In PR systems, proportionality is generally increased with district magnitude.[80] The systems which aim to achieve larger proportionality will utilise large districts, because such districts are able to ensure that also small parties can gain representation in the parliament. Thus, countries with smaller district magnitudes are likely to have fewer effective parties.

Effective threshold provides yet another measure for proportionality. This measure refers to minimum level of support that a party needs to win seats in a parliament: high thresholds imply low proportionality. Consequently, high thresholds are associated with low district magnitudes. But proportionality can also be affected by a legal threshold which many of the CEECs have decided to employ. For example, Slovakia has an assembly with 150 members and a single district. District magnitude is therefore very large, 150, and mechanistically calculated effective threshold would be small, only 0.5 percent implying that a party that receives mere 0.5 percent of the total vote could expect to gain representation in the parliament. However, electoral law of Slovakia establishes a legal threshold of 5 percent which prevents candidates from very small parties from getting elected.[81]

Therefore, based on this discussion one would expect majority-plurality systems (or PR systems with low district magnitudes and high threshold) to be conducive to one-party governments, and PR systems with high district magnitudes and lower thresholds to be associated with majority multi-party governments.

As noted above, the number of parties is not only a product of electoral systems, but also cleavage structures play a role; the number of cleavages in a society can have an effect on party formation. Cleavage structures also mirror the ideological polarisation of a society, which too can have an important role in the choice of fiscal institutions. One should note that strictly speaking the num-

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78 See annex 2 for the exact formulas for different measures mentioned in this section.

79 This link has been confirmed by empirical studies; see Lijphart, 1984 and 1994, and Taagepera and Shugart, 1993.

80 In majoritarian systems district magnitudes greater than 1 would increase disproportional outcomes. As Lijphart, 1994 explains, at the extreme, a single nation-wide district would give all seats to a party winning majority, assuming strict party-line voting. Therefore, single-member districts in majoritarian systems limit the degree of disproportionality. (20)

81 A further feature of electoral systems that is not considered here, but that affects proportionality, is mathematical methods for converting votes into seats under PR systems. Shvetsova, 1999 presents a survey of these formulas, and other features of electoral systems, employed in the CEECs. The country-specific text below in chapter 4.2.2 will pay attention to these formulas when considered appropriate.

ber of parties is crucial for the choice of fiscal institutions only to the extent that it reflects ideological differences between the players within the government. The theory stated that one of the reasons why one-party governments can be expected to opt for delegation approach follows from expectation that members of the same political party are likely to hold similar views, whereas in a multi-party government cabinet members are more likely to have different views regarding the distribution of transfers.

Therefore, the number of parties is not *per se* the crucial factor; what matters is the ideological difference between the government parties. Multi-party governments that are formed as a rule between parties with few ideological differences may find it easier to delegate fiscal powers to finance minister. This set-up would be conducive to delegation approach, even if multi-party governments were the norm.[82]

One should not however interpret this point too strictly, as it is quite probable that parties seeking to form a coalition are likely to prefer partners that hold similar views to their own. Therefore, one would expect that parties within the coalition have fewer ideological differences that they do with the opposition parties. What is crucial is whether those parties are political rivals in the elections or if they run for assembly as a block or alliance. If they compete for votes, they are more unlikely to give fiscal powers to their rivals.[83]

In sum, a review of electoral systems and cleavage structures are both needed to come to a conclusion on what type of fiscal institution a country is likely to develop. If a country has a simple cleavage space, or if it employs an electoral system with majoritarian elements, it is likely that two main parties, or party blocks with similar ideologies, compete in elections. Government is formed around one of these parties which implies that, considering the lack ideological differences, the delegation approach is employed. Consequently, more diffused cleavage structure with a PR system is conducive to coalition governments with different ideological views. This set-up favours commitment approach.

It is also possible that under certain conditions, a government is more likely to develop a decentralised budget process, named above as fiefdom approach. The stability of the electoral and party systems is important. If the po-

82 This argument has a resemblance to the veto-player literature. "Veto-player" refers to actors that have to agree to the proposed change in policies or legislative status quo. Tsebelis, 1999 and 2002 argue that the ideological distances between the veto-players are crucial, not their absolute number.

83 Similarly these two factors are most likely highly correlated; parties that run as a one block are probably ideologically close to one another. Lijphart, 1999 also proposes four different criteria which he uses to judge whether closely allied parties should be considered as two parties or as one party. The first criterion has to do with electoral cooperation; separate political parties normally compete in elections. The second criterion revolves around the degree of cooperation between the parties in parliament, and more specifically, whether the two parties form a single parliamentary party group and caucus together. The third criterion asks, do the parties behave like separate parties in cabinet formations. In other words, are the two parties as a rule together in the government and opposition. Fourth, Lijphart notes that it makes sense to consider two parties as a single party only if their cooperation is long-standing. If alliances are ad-hoc, temporary and shifting, this criterion is not satisfied. (70-71)

litical system is undergoing constant changes, and importantly, if these changes transform into instability also in government types it is unlikely that stable fiscal institutions can develop in such conditions. Further, if party system is so unstable that the party discipline in the legislature is as a rule undermined, credible fiscal commitments – which are the essence of commitment approach – can not be enforced. The political parties within executive would not find it meaningful to make commitments that are likely to be compromised by disobedient voting behaviour of the coalition partners' parliament members at the legislative stage. Thus, one would expect to find fiefdom-type institutions from countries with no stable patterns in their government types. Countries with undisciplined voting behaviour are unlikely to go for commitment approach.[84]

Based on this discussion, one can make the following predictions[85]:

- *Commitment approach*: Countries with multi-party majority governments (most likely to be found from countries that have proportional elements in their electoral systems and/or diffused cleavage structures, not likely to be found from countries with undisciplined voting behaviour.).
- *Delegation approach*: Countries with single-party majority governments (most likely to be found from countries that have majoritarian elements in their electoral systems and/or simple cleavage structure), or multi-party majority governments with scant ideological differences.
- *Hybrid approach*: Countries with minority governments.
- *Fiefdom approach*: Countries with unstable party systems and no stable patterns in their government types.

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84 Hallerberg, 2004 proposes one further condition under which a government is more likely to develop a decentralised budget process, namely the degree of uncertainty a government parties have concerning their re-election. If a political system has low degree of party competition, in other words, if a same party is constantly in the government, there is little incentive for it to centralise the budget process. Idea behind this proposition is that a party which is very dominant does not have to worry about mismanagement of the economy, which would 'normally' be punished by the electorate. With low party competition this is less of a threat. It is worth noting that the degree of party competition and stability, or volatility, of a party system can be interlinked. If a party system has "very" low stability, in other words, if changes over successive elections in the balance of party support are substantial and new political formations commonly emerge, a country has high degree of party competition and probability that dominant parties will be developed is lower. The opposite is not necessarily true. Even if party system has stabilised, and has, say, three equally strong parties with stable electoral support, the degree of competition can nevertheless be high. Practically all of the CEECs have had low party system stability, which implies that uncompetitive party systems are unlikely to be found from these countries. Therefore, this criterion is not considered here. Slovenia is a potential exception and its case is considered in the country specific discussion below. Finally, it is, of course, difficult to determine the "optimal" degree of party competition, or volatility. Very high instability of a party system can be detrimental to democratic consolidation, whereas some degree of variation in partisan support may be taken as evidence that the party system is responsive to changing preferences of voters. (Birch, 2001, 1-2). See also footnote 121 of this study.

85 See also Hallerberg, 2004 for a similar summary.

4.2 Electoral and party systems and the choice of fiscal institutions in the CEECs

In this section, details of electoral systems and available evidence on cleavage structures and party volatility are presented. The latter part of the section considers in greater detail the country-specific considerations which then allow making predictions on which modes of fiscal governance can be expected to be found from the CEECs.

4.2.1 Electoral and party systems in the CEECs

Table 3 presents the details of electoral systems in the CEECs. As regards the election systems (i.e. PR versus plurality-majority systems), one can see that the vast majority of the CEECs rely on PR systems, even though more variation can be found from the details of these systems.[86] Only Hungary and Lithuania employ a mixed system which both incorporates some elements of majoritarian systems. The correlation between effective number of parties and effective threshold has a correct sign (-0.29).[87] Bulgaria has the lowest district magnitude among one-tier systems, the lowest effective number of parties and consequently highest effective threshold. Romania has the second-largest threshold. In many cases the legal threshold is higher than mechanistically calculated one thus determining the effective threshold, and also limiting proportionality. Finally, one also notes that changes in electoral systems in the CEECs have not been uncommon.[88]

Therefore, based on the dominance of the PR systems – and their conduciveness to multi-party governments – one is tempted to conclude that commitment approach can be expected to be the norm in the fiscal institution of the CEECs.

But as mentioned above, also cleavage structures matter for the party formation. They also reveal something about the ideological polarisation between the government parties which, in turn, affects their willingness to delegate fiscal powers to a single actor within the government.

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86 This dominance of PR systems is a common feature throughout the world. According to Lijphart's, 1994 calculations, 52 out of 70 systems fall in to this category.

87 If one ignores the legal thresholds and uses only mechanistically calculated effective thresholds, the correlation is increased, but only marginally to -0.31.

88 Benoit, 2002 and 2003 has examined the evolution of electoral laws in Eastern Europe using a model which attempts to describe how and why electoral institutions are shaped by political parties. His theory predicts that electoral laws will change when each party in the coalition expects to gain more seats under an alternative electoral institution, and when this coalition has sufficient power to implement such a reform.

TABLE 3 Comparison of electoral systems in the CEECs

	Years of elections included	Election system	Assembly size	Number of districts	District magnitude, average	Effective number of parliamentary parties, average	Legal national threshold, %	Effective threshold, %
Bulgaria	-91, -94, -97, -01	PR, closed list	240	31	7.7	2.64	4	8.9
Czech Republic	-92, -96, -98	PR, open list (mv) (1)	200	8	25.0	4.22	5 (higher for coalitions)	5
Czech Republic	-02			14	14.3	3.67		5.0
Estonia	-92, -95, -99	PR, open list	101	11,3 (2)	8.9	5.18	5	7.8
Hungary	-90, -94, -98, -02	mixed, 3-tier	386	176/20 /1	1/7.6/58	3.08	5	5
Latvia	-93, -95, -98, -02	PR, open list (mv)	100	5	20.0	5.79	5 (higher for coalitions)	5
Lithuania	-92, -96, -00	mixed, 2-tier (mv) (3)	141	71/1	1/70	3.59	5 (higher for coalitions)	5
Poland	-91	PR, 2-tier	460	37/1	10.6/69	10.76	5 (4)	5
Poland	-93, -97			52/1	7.5/69	3.43	5 (higher for coalitions)	7
Poland	-01	PR, open list		41	11.2	3.60	5 (higher for coalitions)	6.3
Romania (5)	-90, -92, -96, -00	PR, closed list	355.8	41.8	8.5	3.67	5 (higher for coalitions)	8.3
Slovakia	-92, -94	PR, open list (mv)	150	4	37.5	3.80	5	5
Slovakia	-98, -02			1	150	4.58		
Slovenia (6)	-92, -96, -00	PR, open list	90	8	11	5.65	4	6.3

Notes: Own calculations. PR=proportional representation-system, mv=multiple votes. For data sources and further explanations, see annex 2.

Cleavage structures, which reflect more abstract ideological construction of a country, are more difficult classify and present in a numerical form than institutional features of electoral systems. Nevertheless, party systems' ideological positions have been mapped. Lijphart, 1999 characterises different dimensions of party systems of 36 countries, but none of those countries include the CEECs. Another way to present the ideological distances in a numerical form would be to rely on veto-player literature which treats the number of parties in a government as “veto players”. More veto players a government includes, more difficult it becomes to pass laws or to act in a ‘flexible’ manner. Tsebelis, 1999 and 2002 present a somewhat more subtle argument stating that the ideological distances between the veto players are crucial, not their absolute number. The latter also presents coding rules, which can be used to measure left-right division between parties. Again, his data does not include the CEECs.[89]

Some attempts have been made also with the CEECs. Kitschelt, 1995 studies the early years of post communist party formation in Bulgaria, the Czech Republic, Hungary and Poland. He finds that even during these early years and despite of electoral volatility, a clear party structuring had been taking place in the Czech Republic, Hungary and Poland, and also in Bulgaria this process was underway. His study also suggests that the parties have started to group around three relevant cleavages: liberal camp that champions free markets, national and Christian camp that invokes religious values and is less concerned about the economic reforms and post-socialist camp that is most hesitant to accept market liberalisation.

TABLE 4 Comparison of cleavage structures in the CEECs

	BUL	*CZ*	*EST*	*HUN*	*LAT*	*LIT*	*POL*	*ROM*	*SLK*	*SLN*
Historical										
Core population vs. ethno-linguistic minorities	+		+		+			+	+	
Religious vs. secular		(+)	+	+		+	+		+	+
Urban vs. rural	(+)		+	+	+		+	+		+
Workers vs. owners	(+)	+		+	(+)	+	+	+	+	+
Social democrats vs. communists	+	+		+	+	+	(+)	+		+
Contemporary										
National vs. cosmopolitan	+	+		+	+			+	+	+
Protectionist vs. free market	+	+		+	+	+		+	+	+
Generational				+						+
Transitional										
Apparatus vs. forums/fronts	+	+	+			+	+	+		+
No of cleavages	6	5.5	4	7	5.5	5	4.5	7	5	8

Notes: source: Hellén, Berglund and Aarebrot, 1998. “+” marks a salient cleavage, “(+)” marks marginal salience relevant to the criteria. For further explanations, see annex 2.

A more comprehensive treatment have been done by Hellén, Berglund and Aarebrot, 1998 who have formed, based on the contributions in their edited volume, patterns of post-communist cleavage types in all of the CEECs (see table 4). The authors have classified the cleavages into three different categories. Historical cleavages reflect of classification used already by Lipset and Rokkan, 1967 in their study on Western European parties, and it includes cleavages

89 Hallerberg, 2004 has used this data in mapping the ideological distances of parties of EU-15.

stemming from long-running process of national and industrial revolution. Thus these divisions can originate from social conflicts already present in the inter-war period. Contemporary cleavages, in contrast, include cleavages that were not present during the inter-war period, but have been surfaced later. Finally, transitional cleavage tries to capture cleavages related to fall of communism.[90]

Naturally, this division is done at a rather high level of abstraction. Also, one should note that cleavage types do not automatically translate into equal number of parties. The table nevertheless demonstrates that all of the countries have multi-dimensional cleavage space which, together with the dominance of PR systems, suggests diverse party systems. Country-specific text below will discuss the cleavage structures more carefully, but as a general observation one can detect a North (Baltic countries and Poland) and South (the rest) dichotomy, the former having a more simple cleavage structure.

Berglund, Hellén and Aarebrot, 1998b argue in the same volume that strong cleavages do exist in the CEECs, and those parties that have been enjoying stable electoral support, have often achieved it by exploiting these cleavages. Nevertheless, due to volatile electoral behaviour and still changing party structure, the CEECs have not yet established a stable link between the cleavage structure and the emerging party systems. Cleavage structures have not yet "frozen" either. Further, Hellén, et al. 1998 note that to a degree these weaknesses have been offset by constraining proportionality of their electoral systems, most notably via high thresholds which have mitigated volatility. All of the CEECs, they conclude, are on the road towards democratic consolidation. Romania, Bulgaria and Slovakia lag behind the rest but even they have achieved considerably more progress than, for example, majority of the CIS states. (375)

Considering the massive change that took place just over a decade ago, it is not a surprise to see that the party systems in the CEECs are still to some extent in turmoil. This can be a product of both rapid socio-economic changes which have resulted to changes in cleavages, as well as of changes in electoral systems in some of the CEECs. Indeed, several studies have established that party system volatility is higher in these countries compared, for example, to their Western-European counterparts.[91]

90 For a more detailed explanation of these individual cleavages, see annex 2.

91 Tóka, 1997, 1998, Olson, 1998, Lewis, 2001a. See also Birch, 2001 and Lewis, 2001b for a discussion about the party stability in the CEECs.

TABLE 5 Comparison of government types in the CEECs

	Multi-party %	(of which) majority %	(of which) minority %	Single party %	(of which) majority %	(of which) minority %	Care-taker/non-party, %	Stability of government types	No of govts
Bulgaria									
91-02	34.5	100	0	45.6	80.8	19.2	19.9	0.30	7
91-97	37.4	100	0	19.1	0	100	43.5	0.37	5
97-02	32.1	100	-	67.9	100	0	0	0.56	2
Czech Republic									
92-02	59.8	66.8	33.2	40.2	0	100	0	0.52	5
92-98	100	64.0	36.0	0	-	-		0.54	3
98-02	10.4	100	0	89.6	0	100		0.81	2
Estonia									
92-02	93.4	77.9	22.1	2.4	0	100	4.1	0.59	8
92-95	82.6	100	0	0	-	-	17.4	0.71	2
95-02	96.8	72.0	28.0	3.2	0	100	0	0.58	6
Hungary									
90-02	100	100	0	0	-	-	0	1	5
90-98	100	100	0					1	3
98-02	100	100	0					1	2
Latvia									
93-02	100	75.0	25.0	0	-	-	0	0.63	10
93-98	100	55.5	44.5					0.51	6
98-02	100	100	0					1	4
Lithuania									
92-02	60.4	89.4	10.6	36.6	100	0	3.0	0.43	8
92-96	0	-	-	93.2	100	0	6.8	0.87	3
96-02	99.4	89.4	10.6	0	-	-	0.6	0.80	5
Poland									
91-02	86.3	90.7	9.3	13.7	0	100	0	0.66	8
91-97	100	83.4	16.6	0	0	0		0.72	5
97-02	73.5	100	0	26.5	0	100		0.61	3
Romania									
90-02	60.9	67.3	32.7	39.1	27.6	72.4	0	0.41	9
90-96	55.4	30.5	69.5	44.6	46.7	53.3		0.46	5
96-02	66.8	100	0	33.2	0	100		0.55	4
Slovakia									
92-02	100	89.4	10.6					0.80	6
92-98	100	82.0	18.0	0	-	-	0	0.70	4
98-02	100	100	0					1	2
Slovenia									
92-02	100	90.0	10.0	0	-	-	0	0.82	7
92-97	100	77.8	22.2					0.66	3
97-02	100	100	0					1	4

Notes: Own calculations. Government type refers to a distinction between multi-party and single party governments, and between minority and majority governments. For data sources and further explanations, see annex 2.

Lewis, 2001b notes that despite of volatile politics, most of the CEECs have developed quite stable patterns of democratic government. In many countries two major parties or electoral unions have merged with one or more second-rank parties which have been able to gain enough parliamentary strength to present themselves as viable coalition partners for the formation of reasonable stable governments. Indeed, the extent to which party system volatility has been transformed into volatility in government formations, which is our primary concern, is less obvious.[92]

Table 5 sheds some light on this issue by presenting a comparison of government types in the CEECs. Also, the second-last column of the table presents a Herfindahl index which is often used to describe industry concentration. Here, the index is a sum of squared time-proportions a certain government type has been in office. It thus reveals to what extent a country has had only one government type: an index value of one means that a country in question has only had one government type whereas a low value means that a country has had number of different government types, and therefore the governments have in this sense been unstable.

At a first glance, it would seem that only few countries have enjoyed stable government types. Only Hungary has had exclusively majority multi-party governments, and in Estonia, Latvia, Poland, Slovak Republic and Slovenia multi-party governments have clearly been dominant. Bulgaria, Czech Republic, Lithuania and Romania seem to present no stable patters.

However, breakdown of the post-communist period into earlier and later periods reveal some important patters. Partly these patters reflect the fact that the degree of political stability in these countries has increased as time has passed. One clear sign of this is that the portion of caretaker or non-party governments, which can be regarded as temporary solutions employed in times of political restlessness, are virtually non-existent in the latter part of 1990s. Also the index values in the second-last column have generally increased.

Considering for the purposes of this paper, the latter period is particularly interesting because the fiscal data used later does not cover the very beginning of the 1990s. Politically unstable countries would seem to include Bulgaria, Estonia and Romania, possibly also Poland. Lithuania's case is interesting; during the first half of the period it had no multiparty governments at all, whereas the second half they became clearly dominant. Bulgaria has had large proportion of

92 Tsebelis, 2002 includes a review of literature dealing with causes for government (in)stability. Broadly speaking two approaches have emerged: the first focuses on the parliamentary features (political polarisation and fragmentation within and between the parties in the parliament) and the second on government features (in government). (210-214). Laver and Shepsle, 1996 is one example of the former approach while Tsebelis himself argues in favour of the latter. Further, as Tsebelis, 2002 also notes, government stability is not an unambiguous concept. In this study, the term "government stability" refers to stability in "government types", in other words, whether a country has had consistently multi-party or single party governments, and whether those governments have been minority or majority governments. The primary concern in this study is not what causes unstable governments. Rather, the goal is to say something about what the government types in the CEECs have been and will be in the future.

majority single party governments whereas Czech Republic has had almost exclusively single party governments but it is important to note that they have all been minority governments. Rest of the CEECs (Hungary, Latvia, Slovakia and Slovenia) have had almost entirely majority multi-party governments during the latter part of the 1990s.

Some words of caution are in order. In particular, the figures in the table 5 do not make a distinction between party blocks and more uniform parties. Similarly, the figures do not reveal what is the degree of cooperation between the government parties. These points are relevant especially in the case of Bulgaria and Hungary, and they are refined further in the country-specific discussion below.

Indeed, the discussion above gives already some guidance on the underlying political fundamentals and their role in the choice of fiscal institutions. However, before drawing any final conclusions, a more detailed country-specific treatment is called for. This is done next. [93]

4.2.2 Political developments and predicted fiscal institutions in the CEECs

Bulgaria

Post-communist Bulgaria saw the emergence of two main political blocks; A coalition of parties called Union of Democratic Forces, or SDS, was an advocate of radical reforms which was also motivated by the removal from power of the former communists, grouped around Bulgarian Communist Party, renamed as the Socialist Party. Strmiska, 2000 notes that the Bulgarian party system has been most often classified as a limited multipartism or as a ”two and a half” party system.

Bulgaria is often mentioned as one of the countries were the party consolidation has lagged behind some of the other CEECs. The lack of political stability especially during the early years of post-communist period is mirrored in the frequency of caretaker governments during the first half of 1990s. The 1994 elections paved the way for the emergence of new political formations, reflected also in a steady, albeit small increase in the effective number of parliamentary parties, but the Socialists and the SDS remained by far the most powerful parties. Government formations were consequently also formed around one of these groups. After 1994 elections the Socialists formed a coalition with smaller parties. Before the 1997 elections, the parties that formed the SDS decided to merge into a single party, and together with People’s Union – an alliance formed by the Democratic Party and the Agrarians – it ran under the umbrella of United Democratic Forces. This move from a coalition of parties to a single party did seem to stabilise its organisational structure and increased its effectiveness as a governing party. The alliance gained an absolute majority in the

[93] A thorough discussion on post-communist politics in the CEECs is beyond the scope of this paper. For such a review, see contributions in Berglund, Hellén and Aarebrot, 1998a and in Lewis, 2001a. Note also that the text does not take into account the post-2003 events.

parliament and formed the government. The same heterogeneity applied also to Socialists where different factions have been competing against each other.[94] This was one of the major reasons why the party experienced partial disintegration after the defeat in 1997 elections. (Karasimeonov, 1998, 354)

In addition to this internal disaccord within party blocks, another typical feature in Bulgarian politics has been the attitudes towards communist past which has been a persistence cleavage. Parties under SDS coalition, notes Karasimeonov, 1998, were united by very one-dimensional ideology which stemmed from motivation to remove the former communists from power. Karasimeonov, 1996 notes further that especially during the first part of the 1990s the distrust between the ex-communists (the Socialists) and anti-communists (SDS) camps was so great that this "warlike" relationship prevented any meaningful dialogue between the two. As neither had a clear majority in the parliament, this strong polarisation hindered greatly political stability. (50)

The 2001 elections shook up the bi-polar nature of the Bulgarian party system as the National Movement Simeon II, a party formed just two months before the elections around its central figure former king Simeon II, took a landslide victory leaving the SDS and the Socialists in opposition. The National Movement Simeon II formed a government together with Movement for Rights and Freedom. National Movement Simeon II is however the dominant party in the government with 11 ministers, while Movement for Rights and Freedom holds two posts. One minister originates from the Socialists. Also National Movement Simeon II has suffered from internal disputes and several parliament members have defected to other parties.

While the party system formation has not matured, Bulgaria has had a very stable electoral system during the post-communist period. It employs a PR system, but it is a country with most majoritarian features among the CEECs if one considers district magnitude, effective number of parties and effective threshold. Bulgaria's politics have been dominated throughout the 1990s by small number of relevant parties or party alliances. According to the table 5, it does seem that Bulgarian government types have not yet established clear patterns.

It is also important to note that all of the governments that in table 5 have been coded as "single-party governments" have actually been formed by loose and internally incoherent electoral coalitions, not uniform parties. Olson, 1998 notes that continuation of broad fronts in Bulgaria has separated it from the other countries of Central Europe. [95] Indeed, electoral alliances have been a dominant feature of Bulgarian politics. Strmiska, 2000 argues that the extensive practice of electoral alliance and political bloc formation has been a natural ob-

94 Strmiska, 2000 calls SDS and Socialists as "ideologically and programmatically underdeveloped and incoherent formations with a number of rather negative features from the point of view of establishing and developing a pluralist democratic system" (3). Kitschelt, 1995 states that "within a matter of less than five years, Bulgarian politics has manoeuvred itself into a stalemate situation in which no single party is characterised by an internally agreed upon program and operational strategy to realise that program" (79).

95 According to Olson, 1998, the same applies to Romania.

stacle to the identification of the actual number of independently operating relevant parties and alliances with a clearly defined identity, legitimacy and mobilisation sources. (1)

Based on this discussion it seems that due to the political volatility – in other words frequent shifts between minority, non-party and majority multi-party governments – Bulgaria is a candidate for a fiefdom approach. After non-party acting government in 1997, Bulgaria has been governed by governments formed by electoral coalitions or multi-party governments. It remains to be seen if the majoritarian features in its electoral system will contribute to convergence toward two-party system in the future and if the parties will become more united. Continuation of this trend would suggest delegation approach for Bulgaria in the future.

The Czech Republic

One of the notable features of the post-communistic politics in the Czech Republic is the recurrence of minority governments. The country became independent in 1993, and the composition of its first government was determined based on elections held in June 1992. This multi-party government had a majority in the parliament and it served the full election term. But minority governments became the norm ever since. Nomination of a minority multi-party government after the 1996 elections was preceded by negotiations between the Civil Democratic Party, or the ODS, a ruling party in the government and the opposition party, the Social Democrats, or the CSSD. Brokl and Mansfeldová, 1997 note that negotiations on the government programme called for concessions on the part of the coalition partners as well as the CSSD. (346)

After the 1998 pre-term elections, which resulted from growing economic problems, tension among the coalition and finally from a political scandal about party finances of the ODS, the Czech Republic got its first single-party government when the CSSD won the elections. Again, this was a minority government and thus the CSSD was forced to strike an "Opposition Agreement" with the ODS.[96] Benoit, 2002 describes the agreement as essentially a cartel arrangement imposing various mutual conditions on these two parties. The ODS would tolerate a CSSD minority government in exchange for not supporting votes of no confidence, and was promised chairmanship of both houses of parliament and leadership of essential parliamentary commissions. (31). This contract was supplemented in 2000 with additional elements.[97]

A discontent with the proportional electoral system began to emerge in the late 1990s, and especially among the largest parties, the CSSD and the ODS,

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96 Benoit, 2002 notes that "the proportional Czech electoral system had once again resulted in a minority government that lacked coalition potential […] (31).

97 This "Toleration Act" included following issues: State budget for the year 2000 and the budget outlook, basic parameters of changes in the electoral system, preparation for the EU entry, determination of relevant terms and conditions for tolerating minority cabinet, and communication of the clubs of deputies and senators for the two parties. See Mansfeldová and Brokl, 2001, 278-279.

there was a clear strive for a more majoritarian system. This was also one of the elements in their opposition contract. The discussion of the proposal for a new electoral law, which included an increase of electoral district from 8 to 35, stressed the formation of large parties and a functional cabinet.[98] The law passed both chambers but President Václav Havel refused to sign it citing the constitution which stipulates that elections are to take place under a system of proportional representation. Amid continued pressure from the parliament, President was forced to appeal to the Constitutional Court on the issue. Finally, the electoral law was reformed for 2002 elections by increasing the electoral districts to 14. As the assembly size remained unchanged, the average district magnitude was, by definition, reduced, and thus system became more majoritarian, but not as much as in the original proposal.

The Czech Republic has seen a consistent decrease in the number of parliamentary parties during its independence. In 1992 elections, the number of parliamentary parties soared to 9 while the effective number of parliamentary parties was 4.8. In 1996 elections no new parties were able to gain seats while few of the old ones were not able to re-new their representation. In the June 1998 elections only five parties exceeded the 5% threshold and gained representation in the parliament and in 2002 elections, effective number of parliamentary parties was reduced further.

On of the reasons cited for this development has been the legal threshold. Brokl and Mansfeldová, 1997 point out that ever since the 1992 elections the legal threshold began to have a psychological effect, and voters were reluctant to cast votes for minor parties who were perceived as having little chances for getting elected. The same observation is made by Mansfeldová, 1998.[99]

Recent election reform could add momentum for this development. One of the reasons given for the reform was encourage two-party system and increase majority governments. The 2002 elections are the only elections held under the new system, and as a result, a two-party government was formed with a narrowest majority in the assembly.[100] It is of course too early to observe how the political system will develop in the future. Looking back, the Czech Republic has had the largest portion of minority governments among the CEECs and political deals between government and opposition parties have thus been com-

98 Benoit, 2002 notes that the ODS and CSSD had enough seat in the parliament to change the electoral law and even the constitution towards a more restrictive electoral law which would encourage a two-party system and make majority governments more likely. Both parties performed explicit calculations estimating that such rules would enhance their seat shares under a variety of scenarios, even though they would be political opponents. (31). See also Benoit 2003.

99 For smaller parties this has been a cause for concern. Office for Democratic Institutions and Human Rights observed in its final report for 1998 elections: "a number of complaints were made […] by some parties regarding […] the 5% national threshold, claiming [it is] too high and limit the chances for smaller parties to compete in the election and gain representation in Parliament. […] During discussions with a range of Czech politicians, it was pointed out that the 5% threshold on a national level is designed to produce a parliament made up of a limited number of nationally-based parties rather than a parliament consisting of a larger number of smaller parties." (4-5)

100 It has 101 seats in 200 seat parliament.

mon. This suggests that one could expect to find hybrid elements from the Czech Republic's fiscal institutions. On the other hand the shifts from one-party to coalition governments have continued right up until the end of the period which suggests fiefdom approach. Looking ahead, if the two-party system takes hold along with the reform of Czech electoral system which limited proportionality, prediction is – similarly to Bulgaria – that Czech Republic could develop features from delegation approach. Otherwise it will be a candidate for commitment.

Estonia

Estonia has had almost exclusively multi-party governments. It has also had fairly stable electoral system. Number of parties rose very quickly after Estonia regained its independence in 1991. As was the case with the Czech Republic, also Estonia implemented a five percent threshold which caused numerous parties to reorganise into electoral alliances. Lagerspetz and Vogt, 1998 note that while many of these alliances later became parties, the party system remained long relatively fragmented. This fragmentation has somewhat diminished over the course of the 1990s. In 1999 elections electoral coalitions were forbidden which gave additional momentum for this consolidation as party coalitions were forced to merge into parties in order to exceed the five percent threshold.

The fragmentation of the party system does not, in the case of Estonia, seem to mean ideological fragmentation. While clear ideological differences between different movements existed in the beginning of transition process, the ideological differences later diminished. "Ideological vagueness" is quoted by Lagerspetz and Vogt, 1998 as one of the fundamental problems in Estonian politics.[101] (68-72). They present also evidence according to which voters have traditionally made their electoral choices on individual, rather than on party grounds. (58-59).

Estonia has had eight governments during the period examined (see table 5). These pre-term changes did not however result from disputes over political issues as such, but political scandals involving charges of mishandlings in political and personal affairs by respective prime ministers. Lagerspetz and Vogt, 1998 identify this as one reason why voter activity has traditionally been low in Estonia. Nevertheless, excluding a minority government which was formed after series of political scandals which forced Coalition Party's Prime-Minister Tiit Vähi to step down, proportional election system has consistently produced majority multi-party governments.[102] Despite of the suggestion that ideological differences have been scarce also regarding economic policy issues, fairly consistent coalition governments indicates commitment approach.

101 According to Lagerspetz and Vogt, 1998, this consensus is extended also to economic issues. They note that there has been almost no opposition at all to the cornerstones of the economic policies, including economic integration towards west and the need for balanced budgets. (75)

102 The reign of this minority government is the reason why Estonia's Herfindahl index decreased during the latter period. Note that a majority multiparty government was formed also after the 2003 parliamentary elections.

Hungary

Hungary's electoral system has been described as one of the most complicated in the world but it has served the country well since it has been one of the most stable ones among the CEECs. As Tóka, 1998 notes, political stability has been a distinct feature of Hungarian politics.[103] Nevertheless, the complexity of the system makes it difficult to classify. Consequently, the different measures included table 3 for Romania should be interpreted with caution.[104]

The post-communist party-scene was dominated by the Hungarian Socialist Party, or the MSZP, a successor of the Hungarian Socialist Workers' Party, and several "new" parties. Of all these new groups, the Democratic Forum, or the MDF, was the most efficient in building up a nation-wide party organisation, and it received over 40 percent of the seats in the parliament in the 1990 elections, and a three-party MDF-led majority government was formed.

The Democratic Forum as well the coalition government suffered from internal disaccord. Meanwhile, the opposition was preparing for the 1994 elections, and in early 1993 the Free Democrats, or the SZDSZ, and the Young Democrats, or the Fidesz, signed an agreement with the attempt to facilitate their cooperation and to evaluate based on mutual understanding the ruling coalition and the Socialists. This agreement had little effect as the Fidesz, after suffering from some internal disorder, re-evaluated its political strategy and turned away from the leftist side towards national conservatism and Democratic Forum as potential partner. (Ilonszki and Kurtán, 1994, 324)

As a result, the popularity of the Fidesz decreased dramatically, and the 1994 elections brought a landslide victory for the Socialists. The results reflect the majoritarian bias in the Hungarian electoral system; the Socialists received absolute majority in the parliament with only 33 percent of the party list votes. Consequently it could have formed a single party majority government but opinion polls indicated that the public was largely against an exclusive Socialist government and favoured coalition. The Socialists formed a coalition with the Free Democrats. The principles of coordination and policy goals of the coalition partners were included in a 144-page document, first of its kind. (Ilonszki and Kurtán, 1995, 364)

The political agenda after the elections was dominated, among other things, by unsatisfactory economic performance. This caused tensions within the government as well as between the government and opposition. An exam-

103 This stability has not however been all-inclusive as internal government reshuffles have not been uncommon. For instance in 1995, six ministers out of total 15 left the cabinet. Three of these resignations were related to the economic package introduced by Minister of Finance. In 1996, five ministers resigned, or were replaced. (Ilonszki and Kurtán, 1996 and 1997) In the subsequent years the reshuffles did not cease altogether but they were less frequent.

104 Hungary's election system combines three essentially distinct systems to elect parliament: voting for single candidates from single member districts, list voting for parties in larger territorial districts using proportional rules to award seats from party lists, and proportionally allocated compensation seats from national compensation lists. See Benoit, 2001a for the analysis of the Hungarian system.

ple of this was an economic package announced the Minister of Finance (member of the Socialist party) in March 1995. The content of the package was not discussed in advance in the cabinet and while the package passed the parliament, the two government parties – and especially the Socialists – were divided on major elements of the package. Working relations between the coalition partners stabilised later that year. Ilonszki and Kurtán, 1996 note that the Free Democrats agreed with the new economic programme but "as a minor, and numerically an 'unnecessary' partner in the coalition they could not have much influence in other policy areas". (363)

Also opposition was prone to internal crises. However, the Fidesz, renamed as the Fidesz-MPP (Alliance of Young Democrats-Hungarian Civic Party), remained united and was seeking to challenge the government in the 1998 elections. The Fidesz-MPP succeeded in this and gained 148 seats compared to 134 seats for the Socialists. Consequently they were not able to establish a majority government without forming a coalition with smaller parties. Democratic Forum was considered to be a natural partner for the Fidesz-MPP. Even these two parties did not have enough seats to form a majority themselves as thus Independent Smallholders Party, or the FKGP, was taken on board after they gave up its original radicalism to become more acceptable for government posts.[105] (Ilonszki and Kurtán, 1997, 1998 and 1999)

Ilonszki and Kurtán, 1999 note that the 1998 elections held the features of consolidation, and the party system became less fragmented. Centre-left (the Socialists) and centre-right (the Fidesz-MPP) dominated. (413) These elections were also significant because in contrast to previous elections, parties coordinated their electoral strategies. Benoit, 2001b notes that this was the case especially with Fidesz-MPP and Democratic Forum who had joint candidates in 78 electoral districts. Further, Fidesz-MPP and Democratic Forum, and the Socialists and Free Democrats in a few cases, stroked agreements not to compete against one another in several single member districts in the first round and urged voters of non-represented parties to support the allied party's candidate instead. (7)

This consolidation continued since. Benoit, 2001b argues that despite the expectation that the PR component of Hungary's mixed system would be able to sustain multipartism, its party system has been steadily converging towards two parties. (15-16). Indeed, effective number of parties has been on a decreasing path[106], and after the 2002 elections only three parties entered the parliament, the Socialists and the Fidesz-MPP being again the dominant parties. Just like after the 1994 elections, the Socialists – having obtained over 46 percent of the seats – formed a coalition with Free Democrats.

In the light of the table 3 Hungary is not the most likely candidate for having multi-party governments while according to the table 5, Hungary has only had multi-party coalition governments, which all have served full election terms. Nevertheless, majoritarian influence in the Hungarian electoral system

105 The Fidesz-MPP had 12 portfolios, while the FKGP had 4 and the MDF one.
106 After the 1990 elections 3.8, and after the 2002 elections 2.2.

has manifested itself in the fact that all of the governments have included only two or three parties ("large party" supplemented with few portfolios for "minor parties").

It is also useful to note that the governments have consistently included the same cluster of parties reflecting at least partially left-right cleavage. The Socialists formed a "leftist" coalition with Free Democrats after the 1994 and 2002 elections, while Democratic Forum and the FKGP have been in the same government after 1990 and 1998 elections. By the 1998 elections, Fidesz-MPP had already overtaken a role as the main opposition party to the Socialists from Democratic Forum.

It is also important to note that these blocks have pursued electoral cooperation. As mentioned above, in the 1998 elections the Fidesz-MPP and Democratic Forum who ended up being coalition partners after the elections and the Socialists and Free Democrats who ended up in the opposition coordinated their electoral strategies. After 2002 elections, bipolar nature of the Hungarian system was crystallised even further with the Socialists and Free Democrats forming the government and the Fidesz-MPP being the sole opposition party. This bipolarity has been a consistent theme for Hungarian politics throughout the 1990s, and it suggests that – unlike in the rest of the CEECs – fiscal institutions in Hungary can be expected to include features from a delegation approach. Kitschelt, 1995, and Tóka, 1998 also note that the party polarisation has been more substantial on non-economic than on economic issues. This made it easier to enter to government alliances and it also could have facilitated delegation of fiscal powers to a single player within the government.

Latvia

As is the case with many other CEECs, also in Latvia the legal threshold of five percent has encouraged parties to form electoral alliances. In Latvia's case these coalitions have often been unstable, especially during the first half of the 1990s. Smith-Sivertsen, 1998 note that this instability has contributed to the fact that political parties in Latvia have traditionally not had stable basis for electoral support. Consequently, fluid political system has encouraged parties to be formed around charismatic leaders.[107]

Davies and Ozolins, 2001 note that shifting, collapsing and re-structuring of electoral alliances in Latvian politics make it difficult to assess how the political viewpoints, or popularity, of different parties have developed overtime. Indeed, every election has brought major changes to the parliament composition. Based on the evidence of the 1998 elections, Davies and Ozolins, 2001 see some signs that the Latvian political system is stabilising. However, the 2002 elections witnessed again the emergence of new party coalitions while some of the old

107 Electoral system also encourages for this; Latvian voters can indicate their approval for a preferred candidate, or disapproval for a disliked candidate. Since party hopefuls can be named as candidates in more than one district, leading party figures in particular tend to be listed in all districts in order to capitalise their name recognition. See Davies and Ozolins, 2001 and table 3 of this paper.

ones were dismantled. Latvia has also had several government reshuffles. Many of these changes have been related to mergers of different parties, or resignations of individual parties.

This volatility makes it a challenging task to evaluate the link between the cleavage structures and party formation. Smith-Sivertsen, 1998 find ethnic, rural/urban and historic, in particular pro/contra-independence, cleavages to be most apparent. Davies and Ozolins, 2001 argue that in broad terms the Latvian parties can be arranged also along the left-right spectrum. "Rightist" parties include For Fatherland and Freedom, the People's Party and the Alliance 'Latvia's Way', while "leftist" side include the Social Democratic Alliance and the National Harmony Party. Ahead of the 2002 elections, the two latter parties formed a coalition For Human Rights in United Latvia which makes use of ethnic cleavage but is much divided over economic issues.

Smith-Sivertsen, 1998 argues that in the 1993 and 1995 elections the socio-economic issues became more dominant while ethnic issues were downplayed. Nevertheless, strong presence of other salient cleavages has affected the government formation and governments have not necessary been formed around left-right cleavage. In fact, Smith-Sivertsen, 1998 codes each post-communist government as "centre" in left-right spectrum. Also after the 1998 election, the government included For Fatherland and Freedom ("right"), the Alliance Latvia's Way ("centre-right") and the Social Democratic Alliance ("centre-left"). After the 2002 elections, leftist For Human Rights in United Latvia was left to opposition as the centre-right parties formed the coalition government. Latvia's Way failed to exceed the 5 per cent hurdle and it disappeared from the party scene while the New Era, a new centrist party led by a former Central Bank Governor, gained a leading role in the new government.

Latvia has one of the largest district magnitudes and effective number of parties in the sample which would suggest frequent multi-party governments. Indeed, excluding the very beginning of the 1990s, and despite of volatile party system, the government types have been stable, and excluding the two fairly brief minority coalitions during the early 1990s, Latvia has only had majority multi-party governments. This implies a commitment approach.

Lithuania

In contrast to Latvia, its southern neighbour Lithuania has enjoyed much higher degree of party system stability. Lithuania is the only country in the sample alongside with Hungary that combines elements from proportional and majoritarian system. Žeruolis, 1998 notes that this majoritarian bias has served an effective obstacle for new political entrepreneurs and has been conducive to the maintenance of a two-block system. (123)

The dominance of the two main parties has not been absolute. Since 1992 elections there are five main parties which have had representatives regularly in the parliament. Out of these, the Homeland Union, or the TS(LK), and the ex-communist Lithuanian Democratic Labour Party, of the LDDP, have traditionally been the leading parties.

Similarly to Bulgaria and Hungary, the Lithuanian governments have, especially during the latter part of the period, included "a leading party" supplemented with few portfolios for "minor parties". Between the 1992 and 1996 elections the LDDP-led single-party government was in power, while the latter part of the decade, the TS(LK)-led government was complemented with the Christian Democrats and the Centre Union. Both of these governments had several prime-ministers. Indeed, a distinctive feature in Lithuanian politics has also been constant changes in the government, involving mostly only prime-ministers. Usually the party composition and even composition of ministers have remained fairly constant.

The 2000 elections changed this bi-polarity by introducing new players – the Liberal Union and the New Union – into the parliament. In contrast to previous governments, the resulting multi-party government included two fairly equal parties instead of having one clearly dominant party. Liberal Union and New Union formed a minority coalition government which ruled less than a year and was dissolved after New Union broke coalition ties with the liberals and signed a coalition agreement with the Social Democratic coalition.

The majoritarian bias in the Lithuanian electoral system and fairly stable party system has interestingly not produced stable governments. During 1992-2002 (i.e. three election terms) Lithuania has had eight governments.[108] Bi-polarity was evident especially during the first part of the decade when Lithuania only had majority single-party governments. In principle this would suggest delegation for this period. The government formed after 1996 included one major party, TS(LK), with 10 portfolios and two minor parties with 5 portfolios combined. Thus, despite of the bipolarity this government already could be classified as coalition government. After 2000 elections, the stream of multi-party majority governments continued, with the exception of one brief minority government. Thus Lithuania should be tilted towards commitment approach, especially towards the end of the period.

Poland

Poland has had a very unstable electoral system. Benoit and Hayden, 2004 also note that the Polish party system is the most complicated and the most dynamic in Eastern Europe. (11).

In the 1991 elections close to 30 parties gained parliamentary seats.[109] This followed from very proportional electoral systems which did not include any threshold for the district level.[110] The cabinet formation was considerably hampered by the large fragmentation in the parliament as there simply was no self

108 This figure excludes three acting governments which served only from few days to two weeks at most. Two of these acting governments were in office in 1999, and one in 2001.

109 This is also reflected in the very high effective number of parties (10.76).

110 It also included a very proportional Hare-Niemayer method as a formula for converting votes into seats at a district level. On the national list, the seats were allocated according to modified Saint-Lague formula.

evident base for a majority. Thus after the 1991 elections there was a widespread view especially among the largest parties that the highly proportional electoral rules were impeding the consolidation of the party system and making the formation of stable coalitions impossible. (Grzybowski, 1998, 167, Benoit and Hayden, 2004, 21)

This was one of the main motivations for election reform which reduced the proportionality for the 1993 elections by introducing a 5 percent nationwide threshold for districts and 7 percent threshold for national list.[111] Number of electoral districts was also increased. Indeed, after the 1993 effective number of parties was reduced to 3.91. The subsequent elections in 1997 reduced it even further to 2.95.

But equilibrium was yet to be achieved. Parties that had been losing seats due to less proportional electoral law wanted to increase proportionality again. Several proposals from different parties were tabled and eventually in 2001 the law was changed.[112] The changes included increasing the district magnitudes, changing the d'Hondt formula to Modified Saint-Lague and abolishing the national list. (Benoit and Hayden, 2004, 26-29)

Benoit and Hayden, 2004 conclude their analysis on the evolution of Polish electoral system by arguing that because of the rapidly changing support for the parties, coupled with the simple majority rule required to amend the electoral law, the equilibrium condition where the electoral institutions stabilize has yet to be reached in Poland, and parties are likely to continue to shape the electoral law. (32)

It is perhaps not surprising that these changes have left its mark also to government types which have not developed any stable patters during the post-communist period. During the first post-communist years, Poland had fairly unstable minority coalition governments but after the 1993 elections Democratic Left Alliance, or SLD, and Polish Peasant Party, or PSL, both post-communist parties, formed a PSL-led two party majority coalition.[113] Jasiewicz, 1994 argues that the new electoral law was the major reason for their success. Indeed, Grzybowski, 1998 notes that PSL obtained twice as many seats under the new law compared to the old one. (172)

The coalition was not particularly harmonious, and it suffered from many disputes. Some ministers, including the Minister of Finance (and Deputy Prime Minister) from SLD resigned in 1994 after disagreements with the Prime Minister. Nevertheless, 1994 was the first year after 1987 without change in government. This stability was short-lived as in 1995 the disagreements between the Prime Minister and the President surfaced. The government received a vote of no confidence and SLD-led majority coalition was formed. (Jasiewicz, 1995, 1996)

After the 1997 elections, Electoral Action Solidarity, or the AWS, and Freedom Union, or the UW formed a coalition government. Jasiewicz and

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111 D'Hondt allocation formula was also applied.

112 There was an attempt to introduce less proportional electoral law already in 1997, but it narrowly failed the parliament vote (182 to 181).

113 The government was supported also by the Union of Labour until June 1994.

Jasiewicz-Betkiewicz, 2001 note that the coalition was born out of necessity, as it was the only viable majority coalition in the parliament. These two parties both had their roots in Solidarity movement but they never really trusted each other.[114]

This distrust manifested itself especially in issues of economic policy where the agreement was difficult to achieve throughout the lifetime of the coalition. Even when the party leaders struck a deal and imposed formal party discipline, it was never certain that it would be accepted by all members of the AWS. Jasiewicz and Jasiewicz-Betkiewicz, 2001 note that in particular a group of 21 parliament members, commonly referred to as "the Blackjack", became a de facto opposition to the government economic policies. In January 2001 they even submitted a formal motion for a vote of no confidence in the Minister of Treasury. The motion failed by just two votes, but another no confidence motion was submitted in August. This time the Prime Minister had to dismiss the Minister. (386-387)

Finally the coalition broke up when the Freedom Union decided to leave the government, but continued to support the government in important votes. The AWS continued as a minority government[115] until the next elections in 2001 after which a majority multi-party government was formed between SLD and PSL.[116]

Poland has had unstable government formations. During the beginning of the 1990s it had minority governments followed by number of majority multiparty governments, a period of minority government, and again multiparty government which too then collapsed. There is also some strong evidence that especially after 1997 elections the party discipline was undermined particularly on economic issues.[117] Despite having a fairly long period of multiparty government at the time, this distrust makes it difficult to agree on binding and credible common goals which are the essence of the commitment approach.

114 The AWS was a loose block of several parties which, according to Jasiewicz and Jasiewicz-Betkiewicz, 2001 occupied a firm place on the right of the political spectrum as far as cultural (religious values) and ideological (condemnation of Communism) cleavages are concerned. On issues of economic and social policy, however, it has often opted for populist and interventionist solutions, while in principle supporting market reforms. The Freedom Union was less concerned with other ideological issues, but it has been the most consistent proponent of free market economy on the Polish political scene. (387)

115 As mentioned already, the table 5 does not make a distinction between party blocks and more uniform parties, and thus the AWS has been coded as a single-party. Due to its fairly short and volatile existence, the AWS should probably not be considered as a single party according to Lijphart's criteria mentioned in footnote 81 of this paper.

116 This government also collapsed following internal disputes in the beginning of 2003. See e.g. "Poland's ruling coalition collapses", Financial Times, March 2, 2003.

117 For more evidence of the undisciplined voting, see section 5.3.1 of this paper. Further, a certain degree of instability was evident also earlier. A member of Bureau of Research from Polish Sejm writes: "[During the early years of 1990s] the presence of a multitude of political parties and a wide range of diversity of interests in the Polish Sejm […] manifested itself in its entirety during the work on the central budget. Deputies frequently identified their own individual or group interests with the public interest. Inexperienced experts of the Bureau [of Research] were under constant fire from "dissatisfied" deputies." (Staskiewicz, 2002, 2).

Commitment approach would be the predicted institutional solution for Poland but because of this instability, Poland is a candidate for fiefdom approach.

Romania

As can be seen from the table 3, Romania has the second-largest effective threshold in the sample. Romania has also gradually limited the proportionality of its electoral system by implementing reforms that have reduced the district magnitude and applying legal threshold ahead of 1992 elections. Legal threshold was increased further ahead of 1996 elections. These changes are also reflected in a steady decrease in effective number of parliamentary parties.[118]

Crowther, 1998 argues that excluding Albania, Romania was probably least prepared for democratic rule among the Eastern European countries. The hard-line Ceaușescu regime systematically fostered political alienation and fractured society along class and ethnic lines. (297) The fall of the dictatorship in 1989 left the political field wide open.

The provisional power was quickly assumed by National Salvation Front, which changed its name in 1993 to Party of Romanian Social Democracy, or the PDSR, after uniting with three smaller parties, and it consequently dominated both the 1990 and 1996 elections. Crowther, 1998 calls the first election campaign an unequal contest at best, pitting a cohesive successor communist party with near monopolistic access to state resources against the fragmented opposition. The PDSR also formed the backbone for the governments formed after these elections. Minority governments were the norm during the first half of the 1990s.

The 1996 elections marked a change in the Romanian political scene as the PDSR was left second after the Democratic Convention of Romania, or the SDR, an alliance of rightist parties claiming victory. The PDSR's popularity was eroded by the political and economic stagnation. A SDR-led majority coalition was formed but the coalition was prone to internal disputes and it underwent several changes.

The 2000 elections were won again by the PDSR and ultra-nationalist Greater Romania Party experienced a surprise-surge in its support and came second. The PDSR, renamed as Social Democratic Party, or the PSD, formed a single-party minority government which was supported by centrist parties, especially the Hungarian Democratic Union. At least partly their motivation not to seek to overturn the minority government has to do with their dislike towards Greater Romania Party and its anti-Hungarian and anti-Semitic politics.

Table 5 suggests that Romania was not developed stable government formations, a proposition supported by the discussion above. Romanian politics has been characterised by regular changes from single-party to multi-party, and from minority to majority governments. Thus, fiefdom approach is the expectation for Romania. Proportional elements in its electoral system combined with

118 This decrease started after 1992, when the effective number of parties was 4.75. After 2000 elections it was 3.42.

diffused cleavage structure suggest commitment approach for Romania in the future when political conditions are stabilised.

Slovakia

The most powerful of Slovak post-communist parties has been the Movement of Democratic Slovakia, or the HZDS, a leftist descendant of a broad based citizens' movement called the Public Against Violence. Remarkably, the HZDS has been the biggest parliamentary party after every election since 1992 but this position has not however guaranteed it a leading role – or even a post – in every government. After the birth of independent Slovakia, a HZDS-led minority two-party government was formed, but several parliament members left the HZDS in the beginning of 1994, as a row over the market reforms, privatisation in particular, culminated. A broad based 'right-center-left'-minority coalition led by Democratic Union was formed ahead of the 1994 preterm elections. (Mansfeldová, 1998, 212-213, Malova, 1995, 468)

The elections restored the HZDS's position as a leading government party. First, there was an attempt to form a broad based HZDS-led coalition with Christian Democratic Movement and Party of Democratic Left but both parties withdraw from the negotiations. Finally, the HZDS (12 cabinet posts) was able to form a majority coalition with the nationalist or rightist Slovak National Party, or the SNS (2 posts) and populist left-oriented Association of Workers in Slovakia, or the ZRS (4 posts). Out of these partners, the HZDS and the SNS had most common ground especially regarding the nationalist aspects of their programmes but also they were divided by some other areas, especially foreign policy. The ZRS's agreement to participate to the coalition was considered as a somewhat of a surprise, and their demands concerning the distribution of the cabinet posts delayed the government's inauguration. (Mansfeldová, 1998, 213, Malova, 1995, 470, Malova, 1996, 455)

Malova, 1996 points out that 1995 was the first year since the collapse of communist rule in 1989 without a change in government. Ruling parties had been internally incoherent and party discipline generally weak. Now political situation however stabilised as during the year not even one change of minister occurred and voting behaviour was disciplined. (454) The voting discipline was weakened during the course of 1997 when several bills failed to pass the parliamentary vote. The government's privatisation policy was particularly controversial topic. For example, the National Property Fund, controlled by members of the board where the HZDS had a majority was accused of selling many profitable companies to ruling parties' supporters. (Malova, 1997, 484)

Meanwhile, the opposition reached agreement on pre-electoral co-operation. As a result the Slovak Democratic Coalition, or the SDK, was born which was an alliance comprising the centre-right Christian Democratic Movement and the Democratic Party, the centrist Democratic Union, and two minor centre-left parties, the Social Democratic Party of Slovakia and the Slovak Green Party. While the alliance was ideologically diverse, its main motivation was to challenge the incumbent regime. The HZDS in particular was accused of unconstitutional legislation and other violations of the rule of law. (Malova and Učeň, 1998, 521)

Slovakia's electoral law was changed after the 1994 elections as the number of districts was reduced from four to one; territory of the Slovak Republic forms now one election district. This was seen as an attempt by the HZDS to capitalise the nationwide recognition enjoyed by its leader and Prime Minister Mečiar. (Malova and Učeň, 1999, 501-502) Despite of these efforts the 1998 elections marked an end to the reign of the HZDS. It remained marginally the largest party gaining 43 seats against 42 seats of the SDK. The SDK led majority coalition government was formed. The SDK was joined by Party of Democratic Left, or the SDL, Party of Civic Understanding, or the SOP and Party of Hungarian Coalition, or the SMK. The HZDS was left to opposition. Its controversial politics left it in political isolation with the SNS as the only potential coalition partner.

The SDK did not prove to be sustainable alliance. Several factions departed from it in 2000 and as a result it shrank from its original 42 to 29. The government maintained however the majority in the parliament as these factions continued to support the government. Učeň, 2001 notes that there were many attempts by individual parties to promote their position at the expense of their coalition partners. Practically all coalition members were connected to various economic pressure groups. Especially the SDL was opposing the SDK even joining the HZDS a vote of no confidence in April 2000. The rest of the coalition partners rejected the SDL's position. (404-408)

The SKD finally disintegrated in 2000 as the problems culminated. The party lacked an efficient internal decision-making mechanism and different factions had different visions about the alliance's future: some believed that non-socialist forces should unite in a large and ideologically looser party organisation while others preferred a coalition of ideologically and organisationally distinct programmatic parties. The Slovak Democratic and Christian Union, or the SDKU, was born on the ruins of the SDK. Democratic Union merged into SDKU while opponents created the Liberal Democratic Union. (Učeň, 2001, 410)

This prepared the basic set up for the 2002 elections. Also this time, the HZDS was the biggest party and the SDKU came second. The HZDS was however again unable to form a coalition and it was left to opposition. A SKDU-led majority government was formed with the Christian Democratic Movement, the Hungarian Coalition Party and the Alliance of the New Citizen.

Slovakia has had politically a very eventful port-communist period. The first part of the period was marked by the dominance of the HZDS which resulted to accusations of authoritarian rule and have consequently left the HZDS to opposition. During the latter part of the 1990s, there has been consistent stream of majority coalition governments. This would suggest commitment approach, even if political conditions have at times been rather volatile.

Slovenia

While the right-left cleavage is present in Slovenia and corresponding rightist and leftist parties can be distinguished for the Slovene party scene, this division has been curtailed by the existence of a strong political centre. Given this pattern, explains Zajc, 1998, Slovene political parties have been prepared to choose from a wide variety of political partners.[119] As a result, all of the post-independence governments have been centre-oriented and the Liberal Democratic Party, or the LDS has been dominating the Slovene politics. (280)

Similarly to Slovakia's Public Against the Violence movement, the first Slovenian post-communist coalition was a broad based alliance, called Demos which included most of the newly established democratic parties. For the first post-independence elections the Damos coalition was replaced by a temporary 'small coalition' including Liberal Democratic Party, or the LDS, Social Democratic Party, or the SDSS, the Greens, or the ZS, Slovene Socialist Party, or the SSS and Slovene Democrats, or the DS. During the first election term Slovenia was ruled by oversized coalition led by the LDS. Zajc, 1998 notes that these coalitions had little understanding for the role of opposition and the opposition parties were not able to present viable alternatives to the ruling coalition. Conflicts were handled in negotiations between the coalition partners, not in the parliament. The government found it politically practical to avoid debate and discussions in the important economic policy issues. (284-285)

The 1996 elections normalised the situation somewhat. Zajc, 1998 refers to the majority LDS-led coalition government that followed the elections as more balanced and more pragmatic. (285) This government, formed in addition to the LDS by Slovene People's Party, or the SLS and Democratic Party of Slovenian Pensioners, or the DeSUS, was the longest serving government in Slovene post-independent history. It was dissolved in 2000 following the SLS's decision to unite with the opposition's Christian Democrats, or the SKD to form the SLS+SKD, Slovene People's Party.

A SLS+SKD-led government was formed which served a very short term as the 2000 elections were on the way. After the 2000 elections, Slovenia got once again a LDS-led majority four-party coalition government.

The Slovene politics has been relatively stable. While there has been several government reshuffles during the election terms, the governing coalitions have been generally stable and the country has not had any single-party governments. This would seem to make Slovenia a candidate for commitment approach.

There are however two features in Slovenian politics which suggest that making such conclusion could be more complicated. First, as will be seen from the data presented in chapter 5, the number of defecting parliament members in budget votes – in other words, members who vote against the government de-

119 This is also reflected in Slovenia's effective number of parliamentary parties in table 3 which is highest in the sample (excluding the Poland's corresponding figure following their 1991 atypical elections).

spite being a member of governing coalition – has typically been rather large. Given that the governments in Slovenia have not enjoyed large majorities the parliament, this might have not encouraged relying on common commitments in planning stage that could be broken in legislative stage.[120]

Secondly, the LDS have been very dominant in Slovenian politics as it has had the largest number of MPs in every post-communist parliament and consequently it has been represented in every post-communist government. Above, Hallerberg, 2004 proposed that the degree of uncertainty a government parties have concerning their re-election has an effect of the development of fiscal institutions. If a political system has low degree of party competition, in other words, if a same party is constantly in the government, there is little incentive for it to centralise the budget process. Idea behind this proposition is that a party which is very dominant does not have to worry about mismanagement of the economy, which would 'normally' be punished by the electorate. With low party competition this is less of a threat.[121] This discussion would suggest that Slovenia has developed features of fiefdom approach.

Summary

Above, it was argued that commitment approach is most likely to be found from countries that have proportional elements in their electoral systems and/or diffused cleavage structures, delegation approach from countries that have majoritarian elements in their electoral systems and/or simple cleavage structure, and finally fiefdom approach from countries with unstable government types or undisciplined voting behaviour in budget votes.

The dominance of PR election systems in the CEECs would suggest that the majority of countries should ideally be commitment states. The discussion

120 However, the country authorities indicated that this has not been regarded as a problem in Slovenian policy-making. See chapter 5.3.1 of this paper.

121 A variation in the degree of party competition has somewhat different effects on government's fiscal behaviour in different political economy models. According to Hallerberg, 2004, a low party competition does not provide incentive for the government to centralise the budget process and overspending follows since a party who can be fairly sure of re-election does not have to fear punishment from the electorate even if it mismanages the economy. However, in some other political economy models overspending arises from the uncertainty about policymaker's prospects of being retained in the office which in turn has effects on his behavior: he may choose policies in a way that he thinks will maximize his changes to be re-elected, or if he knows that he could be replaced by someone with different preferences, he may choose policies in a way which hampers his successors policy-alternatives. For example, in Alesina and Tabellini, 1990 uncertainly of re-election – or "high party competition" – have different effects on government's fiscal behaviour than in Hallerberg, 2004. The party in power will always issue debt if it believes there is some probability he will be turned out of the office, and the policymaker is better off consuming according to his own preferences than transferring resources to an unknown future. At extreme, if he/she knows for sure that he/she will not be in the next government, there is no reason *not* to overspend. In other words, a policymaker overspends not because it does not fear punishment from the electorate, but because it wants to hamper its successors (which has different preferences) policy-alternatives.

above largely confirms this expectation, but the story is somewhat more nuanced.

Table 6 attempts to bring together much of the discussion presented above on the party and electoral systems in the CEECs.[122] The collapse of communism led rather unsurprisingly to certain political turmoil. Bulgaria, Czech Republic and Romania have experienced frequent shifts in their government types. Czech Republic could be on its way towards a two-party system if the electoral reform will work to this effect. The same could apply also to Bulgaria as its electoral system also limits proportionality and the effective number of parliamentary parties lowest among the CEECs. This is largely due to dominance of electoral alliances. Poland would be a candidate for a commitment approach as coalition governments have been dominant but it has experienced rather volatile political conditions. Its Herfindahl index has in fact decreased during the latter half of the period indicating decreased stability. On the other hand, voting behaviour appears to have become more disciplined during the parliamentary term that started from 2001. Romania's stability has increased but only modestly. Estonia's Herfindahl index decreased during the latter period but this was due to one minority government. Otherwise it has had consistent majority coalitions.

Lithuania has had a fairly high degree of stability. Interestingly, the government types were concentrated on single party governments during the first part of the period, while it has had a consistent stream of coalition governments during the latter part. Slovenia would be a candidate for commitment approach but undisciplined voting behaviour combined with signs of low degree of party competition led to a conclusion that it has developed features from fiefdom approach. Finally, the rest of the countries have had more or less consistently majority coalition governments.

The following chapter will reveal, among other things, if the reality follows these expectations.

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122 It is useful to note that government formation is a complex process and any attempt to explain why a country has chosen a particular form of government using just a few numerical indicators is bound to remain incomplete. This was the reason why a country specific discussion was called for. Further, as can be seen from the table, the link between the number of cleavages and party systems (and consequently fiscal institutions) is perhaps not obvious. Recall from chapter 4.2.1 that due to changing party structures many of the CEECs have not yet established a stable link between cleavage structure and party systems.

TABLE 6 Summary: predicted fiscal institutions in the CEECs

	Stability	**Electoral system proportionality**	**No of cleavages**	**Degree of party discipline in budget votes**	**Fiscal institutions: a prediction**
Bulgaria	0.37 (91-97) 0.56 (97-02)	proportional	6	Defecting MPs not common	fiefdom (91-03); commitment/delegation (future)
Czech Republic	0.54 (92-98) 0.81 (98-02)	proportional	5.5	Defecting MPs not common	fiefdom (92-03); commitment/delegation (future)
Estonia	0.71 (92-95) 0.58 (95-02)	proportional	4	Defecting MPs not common	commitment (92-03)
Hungary	1	mixed	7	Defecting MPs not common	delegation (90-03)
Latvia	0.51 (93-98) 1 (98-02)	proportional	5.5	Defecting MPs not common	commitment (93-03)
Lithuania	0.87 (92-96) 0.80 (96-02)	mixed	5	Defecting MPs in general not common (3-4 MPs/budget vote)	delegation (92-96); commitment (96-03)
Poland	0.72 (91-97) 0.61 (97-02)	proportional	4.5	- In the 1993 - 1997 term: about 3 MPs/vote - In the 1997 - 2001 term: about 10 MPs - present term: no such cases	fiefdom (91-03); commitment (future)
Romania	0.46 (90-96) 0.55 (96-02)	proportional	7	Defecting MPs common but the number is usually small	fiefdom (90-03); commitment (future)
Slovakia	0.70 (92-98) 1 (98-02)	proportional	5	Defecting MPs not common	commitment (92-03)
Slovenia	0.66 (92-97) 1 (97-02)	proportional	8	Defecting MPs common but the number is usually small (1-5 /budget vote)	fiefdom (92-03); commitment (future)

Notes: The data on the degree of party discipline comes from chapter 5 of this study.

5 FISCAL FRAMEWORKS IN THE CEECs: A DESCRIPTION

The first part of the chapter explains how the institutional data has been obtained. This will be followed by a description of the data on fiscal frameworks. The data is presented according the different phases of the budget process, beginning from the executive planning and legislative approval stages ending to the implementation and monitoring stages. This is followed by a comparison to the EU-15. Final section presents a summary of the institutional data.

5.1 About the institutional data

Data on institutional details of fiscal frameworks is not readily available. The data presented below has been obtained primarily by constructing two separate questionnaires.[123] The first one focussed mainly on fiscal institutions and it was sent to authorities of Finance Ministries, Central Banks and Parliaments' Budget Committees[124] of the CEECs. The reason for approaching several authorities in a single country had to do with an attempt to increase the data reliability; the larger number of respondents makes it easier to detect if somebody has understood the questions in a different way, or if somebody has provided – intentionally or unintentionally – otherwise incorrect answers. For example, a person working at the Parliament's Budget Committee might exaggerate the Parliament's influence in the budget process, or an official from a Finance Ministry might feel tempted to present the actions and processes of his/her ministry in a better light than they really are.

123 Both questionnaires can be found from annex 3.

124 For Czech Republic the Parliamentary Institute provided the reply.

The questionnaire was formed partially based on the study by Hallerberg et al, 2001 which focussed on fiscal frameworks in the EU-15.[125] The reason for drawing on this study was that this allows re-producing similar institutional data for the CEECs. This data can then, in turn, be used in comparisons with the EU-15 which comprise the most important reference group for the CEECs.

Every Finance Ministry and Central Bank sent their reply to the survey.[126] In addition, six out of ten Parliament's sent their reply. After receiving and studying the replies for the initial questionnaire, follow-up questions were sent to at least one authority – usually to the Finance Ministry – in each country to address any inconsistencies and shortcomings in the initial replies.[127] Still outstanding issues where clarified in a subsequent communication with the countries' authorities. Further, available budgetary legislation, individual country studies by OECD, IMF and the European Commission and the study by Gleich, 2002 were used to cross-check the data for those areas where it was possible.[128] However, since many of the specifics of fiscal frameworks are not cemented into a law but are rather controlled by informal norms, it was possible to rely on legal texts and other material only to a certain extent. Consequently, the communication with the country authorities was necessary to gain better insight into the fiscal practices. Finally, an attempt has been made to track the changes in fiscal practises that have occurred during post-communist period. This has been done especially regarding the information that later will be used in a statistical analysis.[129]

The second questionnaire dealt with the role of parliamentary committees and it was sent to experts in every parliament, and they all replied. This questionnaire was based on the study by Mattson and Strøm, 1995 which too focussed on western European countries.

125 The questionnaire used by the Hallerberg et al, 2001 was not available when constructing the questionnaire for this study, but the published report which presented the details of fiscal frameworks in the EU-15 allowed drawing up the survey in such a way that comparable data was obtained were needed.

126 Some Central Banks announced that due to the fact that fiscal issues fall into the Finance Ministries' domain, they did not feel comfortable providing replies to the questions. In those cases, the replies received from Finance Ministries were sent to the Central Banks which then examined the replies and gave their observations.

127 Because every follow-up questionnaire was individually designed to address country-specific issues, it is not possible to reproduce a representative example of these follow-up questionnaires.

128 See the end of annex 4 for a more detailed list of sources used.

129 In some cases this was a difficult task due to large number of amendments in the organic budget and other laws. All of the amendments were not available in foreign languages. In those cases more emphasis has been put on country authorities' expertise in pointing out most significant changes. No doubt the fiscal frameworks will continue evolving in the future, too. The data presented in this study dates from 2003.

5.2 The executive planning stage

The planning stage refers to the phase when the budget draft is being discussed and formulated within the executive. Depending on a country, the Finance Ministry[130] can have a varying role in planning and formulating the executive's budget proposal. In every country in our set, this process is also guided by a multi-annual fiscal framework, albeit to a varying degree.

5.2.1 The multi-annual fiscal frameworks and annual budget targets

The fiscal challenges faced by the CEECs have a strong medium-term focus which consequently emphasises the role of medium term fiscal frameworks. Fiscal policies need to reconcile challenges that arise from the final stages of economic transition and the reforms needed to advance catching up and from the liberalisation effects that EU membership will entail.

Table 4a.1 of annex 4 present the content of the multi-annual fiscal frameworks in the CEECs. One can see that the implementation of such frameworks has started only recently practically in every country. In many of the CEECs this coincides with the start of Pre-Accession Fiscal Surveillance Procedure which started in the beginning of the millennium. Part of this Procedure is the annual submission of Pre-Accession Programmes, or PEPs, which in turn were the successors to the Joint-Assessment of Medium-term Economic Policy Priorities that were jointly prepared by the Commission and national authorities. The purpose of the Joint Assessments as well as the PEPs has been to develop the capacities of the CEECs to engage medium-term macroeconomic planning. The Joint Assessments were signed by the Commissioner ("for the Commission") and in most cases by the Finance Minister ("for the government"). Therefore, the Joint Assessments already did enjoy some authority but they were often not very explicit in terms of fiscal policy measures nor they were very closely tied into domestic budget-making. Almost every country has introduced later more rigorous multi-annual approach.

In every country the multi-annual framework has a legal base which does not automatically guarantee rigorous multi-annual budgeting. Indeed, the Czech Republic employs only informative multi-annual budget outlook.[131] Both

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130 For the sake of clarity, in the following the term "Finance Ministry" will be used even though in some countries the ministry responsible for fiscal and budgetary issues has a different name.

131 International Monetary Fund's Staff Visit Concluding Statement (preliminary) dated to November 2002 states that "The [Czech] government's four-year fiscal plan with binding limits on spending by individual budgetary chapters (to be formulated and published by mid-December) will be a key tool for setting the agenda for the current government's term and for convincing markets of its commitment to sustainable deficit reduction." (para 8). The same message is conveyed in the Czech 2002 PEP. This information was however premature and the reform was postponed after a change of government and subsequent coalition negotiations. According to the authorities, the reform should be implemented during 2004. The new medium term framework

Romania and Slovakia had initially only informative multi-annual frameworks, and a more formal framework was introduced in both countries only very recently. Hungary has since 1997 presented medium-term fiscal analysis as a part of the budget documentation but that did not include any substantive fiscal targeting. A more formal approach was introduced in 2001 but the new government elected in 2002 removed the framework from the budget law. Currently, the PEP has taken over the role of medium-term framework in Hungary.

Majority of the CEECs' frameworks cover either two or three years in excess of the budget year. Two countries have frameworks covering four years in excess of the budget year. All countries report having rolling frameworks which are updated annually to include one additional year of projections. There is also considerable uniformity regarding where the programmes are being drafted. In almost every country a budget department with the Finance Ministry is responsible for drafting of the programmes.

More variation can be found from the scope of the programmes. Bulgaria, Hungary, Poland, Romania, Slovakia and Slovenia consider general government while Lithuania covers central government without social funds. Estonia, Latvia and the Czech Republic cover central government including all social funds.

The respondents were also asked whether their country has any extra-budgetary funds, and if they do, whether these funds are included in the multi-annual plans. Indeed, some concerns have been expressed that public finances in the CEECs have evolved in a dualistic manner during the course of economic transition. Alongside with the formal system of state budgeting extra-budgetary funds and off-balance sheet have evolved. This may hinder the transparency of public finances making it more unpredictable.[132] Therefore, these funds should ideally be a part of a multi-annual fiscal framework.

Only Estonia states that it does not have such funds. Seven countries (Bulgaria, Hungary, Latvia, Lithuania, Poland, Romania and Slovakia) state that the extra-budgetary funds are included in the multi-annual programme whereas two countries (the Czech Republic and Slovenia) announce the opposite.[133]

One of the most important issues related to any multi-annual programme has to do with fiscal targets or rules it includes. It is perhaps worth pointing out that there is no unequivocal definition for fiscal rules. According to Kopits and Symansky, 1998, a fiscal rule is a permanent constraint on fiscal policy which is

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should cover 2 years (in excess of the budget year) with a binding limit for expenditures covering expenditures of state budget and state extra-budgetary funds. See also the Czech 2003 PEP.

132 See The World Bank, 2001.

133 While the data here indicates that some steps have been taken to address the issue, the data is not sufficiently extensive so as to be able to judge whether the inclusion of these funds by some countries is sufficiently comprehensive or not. The results from the International Monetary Fund's Code of Good Practices on Fiscal Transparency exercise indicate that these steps are indeed inadequate. The coverage of the general government sector in the budget presentation is not complete in the most of the CEECs and government activities are not clearly defined. Also quasi-fiscal activities continue in some of the countries. See also Allan and Parry, 2003 who provide a summary of the progress achieved so far.

intended to be employed by successive governments, and which can be expressed as an indicator. Hallerberg et al, 2001 use less strict definition. They define a fiscal rule as "a combination of a fiscal target with a set of prescriptions of what governments are supposed to do to achieve this target" (2). The latter definition is closer to multi-annual fiscal frameworks and fiscal targets formulated under such framework which can impose fiscal constraints only for the duration of current government.[134]

Ideally, fiscal rules should be operationally simple, flexible, transparent, consistent with other macroeconomic policies and effectively enforceable. A rule which sets the maximum level of the budget deficit is perhaps the simplest fiscal rule. However, relying solely on deficit rule may prove to be insufficient as the government could raise taxes to finance higher expenditure while still complying with the deficit rule.

Maximum level of expenditure growth is another often used fiscal goal. A general consensus exists that policymakers should target expenditures rather then tax receipts as the latter are much more sensitive to cyclical fluctuations. For the same reason expenditure targets should exclude volatile items, such as unemployment-related expenditure and interest payments. Multi-annual, rather than annual targets make it more difficult to water down the targets for example by transferring expenditure from the current to the beginning of the following fiscal year. To avoid pro-cyclicality, expenditure targets could also include provisions on what should be done in times of economic under- or over-performance. Finally, credibility of fiscal rules is also enhanced if it has a legal basis and there exists some ex-ante defined rules on how to proceed in case of non-compliance.[135] When it comes to setting the actual fiscal targets in the CEECs, further complications arise from the demands imposed by the transition to market economies and the process of real convergence that these economies are, and will be, engaged in.[136]

While almost none of the CEECs employ fiscal rules in a strict sense of the term, all of them do use some type of multi-annual targets – or guidelines – to guide their budget-making.[137]

The specificity of the targets is relatively uniform across countries (see table 4a.2). Most of the countries employ multi-annual targets either at the level of individual ministries (Hungary, Lithuania, Romania) and/or sub-ministerial (priority areas or spending categories) level (Bulgaria, Estonia, Hungary, Latvia, Romania, Slovakia and Slovenia). Poland does not have specific multi-annual expenditure targets. Also higher level of aggregation in fiscal targets is used:

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134 Such fiscal targets are sometimes labelled as "fiscal guidelines", see part II of the European Commission, 2001.

135 See Kopits and Symansky, 1998, Kopits, 2001, Brunila 2002 and part V of European Commission, 2003a. Most of these issues will be addressed under this heading, and the section 5.4 includes a discussion on the existence of rules to deal with unanticipated events.

136 Assessments included in Christou and Daseking, 2002 suggest that for the reasons of economic fundamentals, medium-term fiscal positions need to be kept to a small deficit or near balance in many of these countries.

137 Estonia, Poland and Slovenia have fiscal rules on public borrowing in place.

total expenditure (the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Slovakia, Slovenia), budget balance (all countries) and debt (Hungary, Latvia, Lithuania, Poland, Slovakia) are the most widely used multi-annual targets. Regarding the future financial obligations, all countries state that ministries must present cost estimates for future years.

Every country uses some kind of annual budget targets.[138] Bulgaria, Lithuania and Poland have introduced annual targets only recently. Further, in Romania the initial budget circular did not include numerical fiscal targets. This was changed since 2003. Interestingly Bulgaria, Poland and Romania were identified in chapter 4 as being potential candidates for fiefdom approach and Lithuania too has experienced variation in its government types.

Practically every country prepares expenditure targets for individual spending ministries. However, some differences exist regarding at what phase of the budget process the targets are set. This issue will be discussed in the section 5.2.3 which deals with the finance minister's role in the planning and decision-making stage.

The degree of commitment to the multi-annual and annual targets is very uniform: practically all of the countries assess that the multi-annual frameworks provide a non-binding or indicative benchmark for annual budget-making. Only Bulgaria reports that the multi-annual targets are legally binding, but still no ex-ante measures are specified in the case of non-compliance.[139] In this sense, the targets for later years resemble often more broad guidelines than binding targets. Similarly, the annual fiscal targets set in the beginning of the budget process are typically not strictly binding targets which the spending ministers' budget bids can not exceed, but they provide a framework under which the annual budget drafting is carried out.[140] Further, non-compliance results only to reputational losses as every country reports that no ex-ante sanctions are in place.

One further detail has to do with the adjustment mechanism when the actual inflation differ form expected. If there is no adjustment mechanism, then higher (lower) than expected inflation would lead to the real amount spent is lower (higher) than was targeted. As it turns out, as a rule, no adjustment mechanisms are in place.

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138 Here, annual targets refer to targets used in the beginning of the annual budget process to guide the annual budget-making.

139 Further, the Romanian 2002 budget Law states that budget bids prepared by spending ministers "must be within the limits established according to the framework letter" which is circulated before detailed budget drafting starts. This indicates that the annual targets are legally binding. Due to lack of history it is difficult to assess if the limits will prove to be binding also in practise. Indeed, the law also recognises that some overruns might occur by stating that the government will make a decision in case finance ministry and spending ministries have different views about the bids.

140 This does not mean that such targets are without meaning, nor does it mean that higher bids will automatically get approved. The section 5.2.3 on finance minister's role in decision-making phase provides more information about the sequence of decision-making process including what is done in the case of disagreements between the finance and spending ministers. Further, in all countries the annual expenditure ceilings finally approved in the budget are legally binding.

The respondents were also asked if the multi-annual targets are included in a coalition agreement between government parties (see table 4a.5). In fact, all of the countries report that this is not the practise. All of the CEECs publish different kind of government declarations or agreements with a varying status. In general their role in the fiscal policy-making seems to be modest. Typically, the agreements and programmes include only vague verbal policy-intentions which hardly provide much political commitment as fulfilment of such verbal goals is difficult to monitor.[141]

5.2.2 The relationship of the multi-annual fiscal frameworks and PEPs with the annual budgets

The basic purpose of the multi-annual framework is to steer the annual budget-making. Table 4a.3 includes some further evidence that can be considered when assessing the relationship between the multi-annual framework and annual budget. All countries except the Czech Republic and Slovenia report that they use the macroeconomic forecasts included in the multi-annual programme as a basis when the annual budget is being prepared. In these two countries the multi-annual forecasts are used too but the status is only indicative. However, only four countries (Bulgaria, Hungary, Lithuania and Romania) discuss the objectives laid out in the multi-annual plans and the deviations experienced later in the annual budget or in a separate report.[142] Accounting rules and conceptuality of budget targets between the multi-annual and annual budgets is in general the same. According to the authorities, the calendar for preparing the two is also in general well connected.

Another issue has to do with the relationship between the PEPs and the annual budget. The main purpose of the PEPs is not to coordinate the fiscal policies of the CEECs; they will be subject to the more binding macroeconomic

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141 In some countries the government programmes do however include some numerical fiscal goals. In Latvia the 1999 and 2000 government declarations included an intention to avoid fiscal deficits that exceed one percent of GDP. Some countries have anticipated future EU-related obligations in their coalition agreements. Latvia's 2002 declaration included a provision to ensure compliance with Maastricht deficit criteria and medium term intention of non-deficit budgets. Slovakia's 2002 statement included a goal for meeting the Maastricht criteria by 2006 and an aim to reduce public debt. Similarly, Hungary's 2002 government programme included an aim to reach public deficit of 2,5 % in GDP by 2006. Slovenia's government programme is quite vague but the 2000 coalition agreement includes a goal to stabilise share of public finance revenue and expenditure at the 42% level of GDP, a goal to achieve a surplus in public finances and a goal to keep public debt between 35 and 40 % of GDP.

142 This information can be complemented by the results from the IMF's Code of Good Practices on Fiscal Transparency exercise. A summary of the results is provided by Allan and Parry, 2003. They note that while the medium-term framework does guide the annual budget process in most of the CEECs, the guidance provided by the medium-term estimates in annual budget submissions is generally poor. The exceptions are Hungary, Romania and Slovakia. Allan and Parry also note that the countries have not, in general, established clear reporting mechanisms to address the changes from previous year's forward estimates which hamper the credibility of the degree of commitment by the governments to the forward estimates.

policy framework only after their EU accession. Nevertheless, since none of the CEECs foresee any major changes in the practises of preparing the subsequent convergence programmes from the practices currently employed with the PEPs – excluding some necessary changes in the accounting rules – one can use the data in table 4a.4 in assessing what kind of practises the CEECs will use when preparing the convergence programmes.

In all countries both documents are prepared in the same ministry, but not necessarily in the same department. The budget targets are conceptually the same in every country while the accounting rules still differ. Calendar is only somewhat connected or different in Czech Republic, Latvia, Poland, Romania and Slovakia. [143] The table 4a.4 also includes "a similarity index" based on the replies.[144] Based on the index it seems that Poland and Slovenia have closest connection between its PEP and annual budget. Hungary and Romania are not far behind.[145]

5.2.3 The role of the Finance Minister in decision-making

This section and the table 4a.5 consider the role of finance minister in the planning and decision-making stage focussing especially on his/her fiscal powers relative to spending ministers. As mentioned above, a government can achieve the centralisation of the budget process by relying on jointly negotiated fiscal targets or on a strong finance minister. The previous sections indicated that there is fairly small variation in the specificity and the degree of commitment to fiscal targets among the CEECs. More variation can be found from the finance ministers' powers.

Regarding the government's involvement in setting the multi-annual targets, one can notice that in every country the programme is –after being formulated in the finance ministry – discussed and approved by the whole cabinet. In Czech Republic the informal outlook is approved together with the budget proposal, while in the rest of the CEECs the initial multi-annual targets are approved by the cabinet before detailed budgeting starts. However, Latvia's authorities indicated that no determined procedure for considering the multi-annual targets have yet taken shape.

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143 Further, Alain and Perry, 2003 note that in the most of the CEECs the medium-term projections made in the context of PEPs do not have a formal role in guiding the forward estimates included in the budget submissions.

144 All of the indices (excluding the indices on parliamentary committees) in this study are largely formed based on the coding rules from Hallerberg et al 2001. PEP similarity-index is formed by taking into account the following characteristics (max 8 points): Are PEPs produced in the same department, similarity of accounting rules, connectedness of calendar and similarity of the budget targets (2 points for replies "same", "connected", "closely connected", full point for replies "similar", "somewhat connected", and 0 points for replies "different", "disconnected").

145 One should note that the replies to the questions in this section required more subjective judgement from the respondents than most of the other questions included in the questionnaire. This can potentially weaken the reliability of the information.

Another related question has to do with the decision-making sequence regarding the annual targets. As mentioned earlier, while practically every country prepares annual expenditure targets for individual spending ministries, differences exist regarding at what phase of the budget process the targets are set. Earlier in process the finance minister suggests or sets the targets, the larger his/her influence in steering the budget process probably is.

Three main categories of practises can be identified. Some countries did not – in the past – include any numerical targets in the budget circular. This was the case with Bulgaria (until 1998), Lithuania (until 1999) and Poland (until 1999). In some countries – Lithuania (since 1999), Poland (since 1999) and Romania (until 2003) – the fiscal targets are proposed by the finance minister and decided by the cabinet on the basis of the budget bids by the spending ministers. In Hungary and Slovakia the finance minister proposes the targets after discussions with the spending ministers.[146] Finally, in Bulgaria (since 1998), the Czech Republic, Estonia, Latvia, Romania (since 2003) and Slovenia the finance minister proposes the targets and the cabinet makes the decision. Only after this, the spending ministers prepare their budget bids.[147]

Once the spending ministers have formulated their budget bids, it is the finance minister who then formulates the budget proposal for the government. According to table 4a.5, in every country the finance minister proposes the budget. What happens after this varies. The level of discussions in the cabinet involves total levels of spending in all of the countries. In some countries the discussions are more specific and focus on the ministry level spending, or more general budget guidelines are addressed.

An important question concerns the cabinet's involvement in the budget negotiations. The assumption is that if bilateral budget negotiations between finance minister and spending ministers serve as a main arena in the negotiations, the finance minister's influence is increased compared to a practise where the entire cabinet is involved. In majority of countries the cabinet-level as well as bilateral budget negotiations between the finance ministers and spending ministers are held. Hungary and Slovenia are the only two countries where bilateral negotiations have the dominant role, even though Hungarian finance

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146 In Hungary, the parliament was formally involved in setting the fiscal targets included in 2000-2002 budgetary guidelines. This was done however only once "on an experimental basis" and no continuation for this practise is foreseen. The guidelines proposed by the government and approved by the parliament included the following indicators and targets for three years: GDP growth, inflation, government sector deficit excluding privatisation proceeds, average wage increase in the government sector, government revenues/GDP, government expenditure/GDP. There was no change in any of these targets compared to the proposal submitted by the government to the parliament.

147 As it turns out, in none of countries the Finance Minister sets the annual targets without seeking the approval of the whole cabinet. Czech Republic perhaps comes closest. There, the cabinet first makes the decision on the targets on the deficit, the aggregate revenues and spending and sets the spending priorities. After this, the Finance Ministry divides these aggregates into spending limits for the spending ministries without seeking specific approval by the full cabinet. As indicated by the country experts, this resembles more a mathematical exercise and does not amount to setting the targets independently.

minister does provide information about the negotiations also to the political parties that form the government.[148] Latvia (outside the cabinet between political parties), Lithuania (since 1999 the cabinet committee) and Slovakia (state secretaries and Economic Council) use regularly also other arenas for budget negotiations.

In every country individual spending minister can ask a cabinet decision on his budget bid, and that in every country the cabinet can in principle overrule the finance minister. However, a half of the countries – Estonia, Hungary, Lithuania, Poland and Slovenia – state that in practise their finance ministers have a veto power to prevent significant changes in the budget proposal from taking place. In all countries an initial attempt to solve the disagreements is made in bilateral discussions in the budget negotiations and in case no agreement is reached, then the whole cabinet is involved. However, in Hungary, Latvia, Poland and Slovenia the prime minister will finally resolve disputes. This should enhance finance minister's position compared to involvement of the entire cabinet. Lithuania (since 1999) and Poland use also cabinet committee for resolving disputes and in Slovakia, disputes are discussed in the level of state secretaries before the whole cabinet.

The CEECs were also asked whether the opposition has any role already in this stage of the negotiations. This question was motivated by the Czech Republic and its frequent minority governments. As mentioned above, since a minority government can not pass the budget without gathering support from the opposition, ideally there should be an understanding, or even a contact, between the government and one or more opposition parties so as to ensure support needed to pass the budget and to prevent last minute bids by the opposition to extort further concessions from the government. As expected, Czech Republic was the only country to state that opposition parties have a role, but only in case of a minority government.

Table 4a.5 also includes an index which measures the finance ministers' strength in the planning and decision-making stage.[149] Hungary and Slovenia

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148 An important clarification is in order in the Hungarian case. During 1998-2002 the primary responsibility of macroeconomic policy was shifted from the finance minister to the minister of economic and financial affairs. Indeed, the country authorities indicate that during this time the finance minister was "relatively weak" and that much of the decisions that were previously taken by the finance minister were now taken by the full cabinet. Regarding the reasons for such change, one respondent explained that the government wanted to have "strong minister of economic affairs to stimulate the investments, employment, national enterprises, small and medium size business even with the help of the budget, and a relatively weak finance minister to finance it". The text presented in this chapter refers to the situation prevailing before and after this period. Indeed, the authorities insisted that after 2002, the finance minister regained her fiscal powers. The lack of history prevents verification of this statement and thus it remains to be seen if this really is the case.

149 Finance Minister index is formed by the following criteria (max 24 points): bilateral negotiations between the MoF and spending ministers exist: three points if that is the only (main) arena, fractions if not, individual ministers can not ask cabinet decisions (three points), MoF has proposal power over fiscal targets (three points if MoF *sets* the targets, two points if MoF *proposes* the targets *before* initial budget bids are made, full point if MoF *proposes* the targets *after* initial budget bids are made , 0 if no targets), MoF has budgetary powers – agenda setter, veto power, MoF must approve all

have clearly the highest index among the CEECs.[150] Almost half of the countries – Bulgaria, Lithuania, Poland and Romania – have taken measures to increase the centralisation of the budget process during the reviewed period. In all of these cases, the strengthening resulted from changes in a way annual fiscal targets were set.

5.3 The legislative approval stage

After the executive have formulated the budget proposal, the legislative debates on it, amends it and finally votes on it. The data presented in this section describes the legislatures' role in the budget process.[151] In this connection also presidents' roles are briefly assessed. Finally, the role of parliamentary committees is discussed.

5.3.1 The role of the Parliament in the legislative stage

Table 4b.1 compares the relative power of parliaments in budget processes. No parliament can propose the budget independently from the government but every country can propose amendments to the executive's budget proposal.

More differences can be found however in how exactly the parliaments can alter the governments' proposals.[152] In two countries – Bulgaria and Slovakia – parliamentary amendments are not limited whereas in the rest the opposite applies. Poland and Romania have introduced changes in this regard: amendments were not limited in Poland until 1998 and in Romania until 2003. Most common restriction is that parliaments can only give amendments that do not increase the deficit.

Questions on the estimation of the typical size of parliamentary amendments produced fairly uniform replies. In almost every country the size was

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changes to targets (three points for each), disputes are not resolved finally by full cabinet (three points), MoF can not be overruled by full cabinet (three points). The main difference to the coding rules to Hallerberg et al, 2001 has to do with the inclusion of the planning stage (the Finance Minister index in Hallerberg et al, 2001 is formed by the following criteria: negotiations take place bilaterally (fractions if other arenas also used), minister can not ask for cabinet decisions, there are bilateral discussions at all, MoF has special powers (1 each), full cabinet does not resolve disputes, full cabinet can not override MoF).

150 Again, please note that for Hungary this is true only regarding the time period excluding 1998-2002. As can be seen from the table 4a.5, the index value dropped significantly during these four years.

151 The Czech Republic, Poland, Romania and Slovenia have a bicameral system. Since the budgetary powers of the higher champers are limited in all of these countries, the following discussion is restricted to lower champers only.

152 Recall that the literature survey above discussed theoretical aspects of voting amendment rules. Following Baron, 1989, 1991 and Baron and Ferejohn, 1989, a closed rule restricts the legislature's possibilities to propose amendments to the government's proposal and thus gave the government a first mover advantage, whereas open rule allowed more amendment power to the legislature.

small, below half percentage-point of GDP. As also noted by Hallerberg et al, 2001, one should avoid putting too much weight in these figures. One can speculate that a government with a strong parliament anticipates the parliament's preferences and as a result the need for the parliament to amend the government's budget proposal is small.

A related aspect has to do with the consequences of losing the budget vote, and government's ability to call a vote of confidence in a budget vote. Von Hagen, 1992 notes that the more serious the consequences of losing the budget vote are, the more likely it is that the government takes the parliament's views into account. On the other hand, Alesina and Perotti, 1999 note that the parties supporting the government may refrain from defeating the budget proposal for fear for creating a political crisis. They also argue that if the government can choose what is at stake in a budget vote, it achieves a strategic advantage. The government can then effectively change the budget vote into a vote for or against the government.

As it turns out, most of the countries (Bulgaria, Czech Republic, Estonia since 2003, Latvia, Poland, Romania, Slovakia and Slovenia) indicate that the government can call the vote of confidence (which could consequently lead to a fall of government) but all of these countries also report that this happens rarely or never.[153] Only Latvia, Slovakia and Slovenia report that in principle parliamentary amendments could cause the fall of the government but this has never happened.

The respondents were also asked to evaluate how common the defecting parliament members, in other words members from the ruling party who vote against the government, are in budget votes. This is especially relevant in countries which rely on collectively negotiated fiscal targets. Credibility and effectiveness of such targets are considerably hampered if the coalition partners expect that parliament members will not respect them in budget votes.

Without four exceptions every country reports that defecting parliament members are not common. These four exceptions were Lithuania, Poland, Romania and Slovenia. In Lithuania the number has typically been small (3-4 MPs in a budget vote). It is worth pointing out that in Lithuania, the coalition governments have typically enjoyed a fairly strong majority so this small number of defectors has not threatened cabinets' commitments. Respondents from Romania report that the amount of defecting MPs is typically very small. In Slovenia, the number of defectors has typically been somewhat larger and the governments have often had a narrow majority in the parliament. This would suggest that credible jointly negotiated targets might not be effective way to address fragmentation of the budget process in Slovenia. However, the country authorities communicated that this has not been a problem in Slovenian policy-making.[154] The situation has been more serious in Poland where the number of

153 This does not have to mean however that the governments in these countries have never threatened the parliaments with this disciplinary tool.

154 One respondent assured that "this problem was not serious at all […] the Parliament approved what the Cabinet proposed".

defectors especially in 1997-2001 term was large, about 10 MPs in a budget vote. [155]

Above, Ferejohn and Krehbiel, 1987 made the distinction between top-down budgeting (the legislatures vote first on the total size of the budget and then on the composition) and bottom-up approach (the overall budget size is determined as a residual). Bulgaria and the Czech Republic are the only countries among the CEECs which follows the top-down approach. This gives their governments considerable fiscal powers relative to the parliament.[156] In all countries, the expenditures and revenues are treated simultaneously.

Another factor restricting a parliament's possibilities to affect the budget has to do with the existence of a time limit and consequences of failing to adopt the budget in due time. If time limit does not exist, parliament can potentially blackmail concessions from the government by delaying the budget procedure. Czech Republic and Latvia are the only countries that do not have a time limit. Respondents from the Czech Republic indicate that an informal time limit exists.

If the budget is not adopted in due time, the parliament can be dissolved in Estonia and Poland whereas Bulgaria and Lithuania report that government must accept parliament's amendments. Most of the countries report that this happens rarely or never. There are two countries where the budget has not, as a rule, been passed in due time. In both Poland and Romania it has been common for the budget to miss the deadline and in both of these countries this has been due to the governments' failure to respect the deadlines. In Slovenia the 1997 budget was delayed.

In the Czech Republic (until 2001), Poland and Slovakia the government's budget proposal to the parliament is used in case a budget agreement is delayed. This strengthens the government's proposal-making power over the parliament because the government does not 'loose' anything even if the budget fails the deadline. In Hungary the organic budget law prescribes a temporary authorisation by Parliament for Government for collecting budget revenues and spending. In rest of the countries 1/12 of previous year's budget is used until agreement is reached.[157]

Table 4b.1 includes also an index which describes the parliaments' influence in the legislative stage.[158] Latvia and Slovakia have the highest index-

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155 On the other hand, it is useful to note that Polish Sejm has 460 MPs against 90 MPs in Slovenia.

156 This does not of course have to mean that the budgets of countries with the bottom-up approach are determined as a sum of individual bids in legislature as there are other ways to limit parliament's amendment powers.

157 Romania introduced in its 2002 budget law an amendment according to which the size of budget provisions determine which budget is used: 1/12 of the previous year's budget is used if its budget provisions are smaller than in the budget proposal, and vice versa. In Latvia, the budget proposal is used during election years.

158 Parliament index is formed by adding one for each of the following criteria (max 8 points): P can propose separate budget, amendments allowed, amendments not limited, amendments do not have to be offsetting, amendments can cause fall of govt, vote on budget totals at the end of proceedings, no time limit in place, budget proposal not used if agreement delayed. The difference to Hallerberg et al, 2001 stems

values. Czech Republic, Poland and Romania have introduced changes during the period which have, in the case of Poland and Romania reduced considerably their index values.[159]

Finally, as can be seen from table 4b.2, the presidents of the CEECs – excluding Slovenia – have a right to veto the budget.[160] More importantly, none of the presidents has ever used this right. It is, of course, difficult to assess if the presidents' have used their influence via more informal routes. Nevertheless, it seems that the presidents are not crucial players in the budget processes of these countries.

5.3.2 The role of parliamentary committees

The previous sector discussed the legislatures' role in the budget processes. The relationship between the executive and legislature has also implications to public finances that go beyond the annual budget process. As explained above in chapter 3.1.2, the literature on parliamentary procedures' impact on political outcomes has emphasised the role of parliamentary committees. Therefore, the view obtained in the previous section can be complemented by focussing on the roles of the parliamentary committees.

The literature has focussed especially on two functions that parliamentary committees serve, that is, distributive and informational roles. If a legislature is able to alter significantly executive's proposals, or if it possesses initiative powers, it enables the MPs to obtain projects which can be favourable to individual members, but are inefficient collectively. But also committees' ability to effectively transmit information to the floor, as emphasised by the supporters of informational view, can be significant from a fiscal perspective. Following Mattson and Strøm, 1995, the information on parliamentary committees below is divided below into committee structures, procedures and powers. Finally, the role of budgetary committees is considered.

First, related to the committee structures, Mattson and Strøm, 1995 present several reasons why the number and size of committees can be significant. According to distributive perspective, political parties should not be able to crack committee dominance which implies in turn that committees should be independent of the party leadership. Thus the expectation is, the smaller the number of committees, the easier it is for the party leaders to control the committees.

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from the inclusion of additional features to the indices (the timing of the vote on budget totals and procedure with provisional budgets).

159 In the case of the Czech Republic, the index value was increased slightly due to the reform included in the 2000 budget law which finished the practise of operating under the budget proposal in case agreement is delayed. International Monetary Fund criticised the Czech Republic in its 2000 report on Observance of Standard and Codes for the flexibility granted to the central government to ignore the budget appropriated by Parliament. Consequently it welcomed the reforms included in the 2000 budget law that reduced government's discretion.

160 Since 1997 the Polish president can made reference to the Constitution Tribunal for adjudication upon the conformity to the Constitution to the Budget. Before 1997, the president had a veto-right.

Small committees, on the other hand, increase incentives to specialise as smaller committees make it easier to monopolise expertise. In other words, smaller committees should be linked with informational perspective.

Further, longer tenures – in other words, the use of permanent committees instead of ad-hoc committees – facilitate MPs to acquire policy expertise from a particular field which is in conformity with informational perspective. Mattson and Strøm, 1995 argue that similarly well-defined committee jurisdictions work to the same effect. Oversight is facilitated is jurisdictions follow those of the government. Further, if MPs serve only in very limited number of committees, their expertise can be expected to be higher. Therefore, also membership restrictions are relevant feature of the committee systems.

Table 4b.3 presents the structure of parliamentary committees in the CEECs. The typology follows Mattson and Strøm, 1995. They separate ad-hoc committees which are set up on an ad-hoc basis to deal with some specific task and then dissolved and permanent committees. The latter group is divided further into committees that are legislative by function (i.e. committees that are not specialised by policy-area but prepare also legislation), specialised committees (i.e. committees that deal with legislation and other matters of a particular policy area), non-law making committees and joint committees in bicameral parliaments.

The number of permanent committees range from 10 (Estonia) to 25 (Hungary and Poland). Typically, the number of permanent committees is around 15. Slovenia and Poland have the smallest and largest committees, respectively.[161] The size of the committees is discretionary is all countries, but in Lithuania minimum and maximum size, and in Romania maximum size, is regulated. In practise, the committee memberships are allocated proportionally among parties in all countries. Vast majority of the CEECs rely mostly on specialised committees as the number of ad-hoc committees and committees that are legislative by function is generally very small with the exception of Hungary which has nine ad-hoc committees.

In general the permanent committees' jurisdictions correspond with those of the ministries. The two exceptions are the Czech Republic and Slovenia.[162]

161 These numbers are clearly correlated with the size of the parliament: Poland has the largest number of MPs (460), Hungary second-largest (386), Estonia third-fewest (101) and Slovenia fewest (90) among the CEECs.

162 The respondent from the Czech Republic assessed that for the most part, the committees do not correspond to the Czech ministries. Some overlapping however clearly exists. The names of the committees are: Economic committee, Mandate and Immunity committee, Organizational committee, Petition committee, Budgetary committee, Constitutional law committee, Elections committee, European integration committee, Security and defence committee, Social policy and healthcare committee, Public administration, regional development and environmental affairs committee, Science, education, culture, youth and physical education committee, Foreign affairs committee, Agricultural committee. Regarding Slovenia, its parliament has two types of working bodies: committees and commissions. The committees are responsible mainly for the areas covered by ministries. During 1996-2000 parliamentary term, 12 committees were set up, whereas in the following term, the parliament had 10 committees. The commissions, on the other hand, are responsible for certain individual issues which in general do not correspond with those of ministries. They nevertheless

Hungary, Slovakia and Slovenia do not have formal restrictions in the number of committees a single MP may serve, and in practise it is common that MPs in these countries serve in more than one committee. In all other countries such restrictions exist, and typically MPs are allowed to serve in one or two committees.

Mattson and Strøm, 1995 consider also the use of subcommittees. The distributive and informational perspectives interpret the significance of subcommittees somewhat differently. Following the distributive perspective, the frequent use of subcommittees could pose a risk that the subcommittees deviate even more from the preferences of the parliament as a whole than their parent committees and as a result, particular interests would be emphasised. Informational perspective, on the other hand, sees subcommittees as an effective way to achieve specialisation.

Every country, except Estonia, allows sub-committees. A respondent from the Estonian parliament reports that in Estonia subcommittees are not formally allowed but informal working groups can be set up. Information in Olson, 2002 confirms that the parliaments in many of the CEECs also actively use these possibilities. He notes that the structure, composition and function of subcommittees are much more variable than those of permanent committees.

The second broad set of committee features has to do with committee procedures. More specifically, committee membership and chair allocation, procedures in the case of party changes, committee openness to public, minority reports and committee stage are considered. Such committee features determine the overall operation framework under which committees organise themselves and do their work. Mattson and Strøm, 1995 note that according to the distributive perspective, the committees are equipped with such procedural status which will facilitate the members to enforce gains from trade.[163] Informational perspective, on the other hand, states that procedural rules are in place to facilitate specialisation and distribution of information.

As can be seen from table 4b.4, committee membership seems to be allocated proportionally in all of the CEECs. In this sense, minority rights are well protected.[164] More variation can be however found from committee chair allocation. In most countries, the committee itself selects its chairman. In Hungary and Slovakia, the house makes the formal selection whereas in Slovenia it is the Bureau of the President of the National Assembly. However, the available evidence suggests that in practise the parties themselves negotiate the chair alloca-

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also deal with legislative matters. The 1993 rules of procedure specify four standing commissions. During 1996-2000 parliamentary term, nine other commissions were also set up. In the following term, the parliament had all together nine commissions, five of which specified by the 2002 rules of procedure.

163 See also Shepsle and Weingast, 1987.

164 Especially during the early years of post-communist legislatures the principle of proportional allocation was not necessarily followed strictly. This was due to shifting party structures which made it impossible to allocate committee memberships proportionally. On this point, see Olson et al, 1998. Furthermore, even if parties are guaranteed a proportional representation when all committees are added up, it still can be the case that some parties are over(under)represented in individual committees.

tion. Six countries report that committee chairs are allocated proportionally between parties. In Estonia, Hungary, Latvia and Lithuania all or most chair belong to the government parties giving government majority considerable upper hand over minority. This was also the case in the Czech Republic during the 1990s but the practise has been changed since towards proportionality.

Chapter 4 of this paper confirmed that many, if not all, of the CEECs have suffered from a certain degree of political instability. One element of this instability in some countries has been frequent changes in party memberships. Therefore, it is relevant to know what happens if a MP changes his/her party. If a committee seat is personal, frequent party changes can lead to significant changes in the balance of power within the committees. Perhaps recognising this danger, all countries, except the Czech Republic, Latvia and Poland report that committee seats belong to a party. In Czech Republic the committee seat is personal. Respondents from Latvia indicate that in practise some ad-hoc discretion is exercised when party changes occur, whereas in Poland MPs who change their parties usually remain in the committee and parties appoint new members to the "party" seat. As a result, the size of a committee is increased.

Notable uniformity exists when minority rights, publicity and committee stage are considered. All countries allow minority reports. In all countries except Estonia and Romania, the committee deliberations are, as a rule, public. Mattson and Strøm, 1995 argue that public meetings dissipate some of the informational advantage of the committee members. Party leaders are able to monitor committee members more effectively and thus party discipline is easier to enforce. Final column of table 4b.4 reviews the committee stage in deliberation. As noted by Döring, 1995b, if a bill is considered first by the plenary, and then sent to committees with a strict terms of reference, committees possibilities to determining the outcome is considerably reduced, and consequently the proposer's – usually the government's – agenda setting powers are strengthened. As it turns out, in almost all of the CEECs committee deliberations precede plenary stage. Lithuania is the only country which reports that committee stage is after plenary stage.[165] Some variation in the practises exists but based on the replies and relevant legislation, the plenary does not typically seek to impose significant restrictions to the committees' subsequent work in the early stage of the legislative process.

Next set of committee features that should be considered has to do with the actual powers the committees possess. Committee's right to initiate legislation, committee's powers to re-write legislative bills, to compel witnesses to hearings, to demand documents from the government and the degree of openness of the hearings are discussed next. Initiative and re-drafting powers are

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165 In Lithuania after the draft act is submitted, it is sent to the Chairman of the Seimas, committees, parliamentary groups, government, office of the President of the Republic, and when necessary to appropriate local authorities. The initiator of the act presents the draft and whatever conclusions have been received (incl. conclusions from committees) to the Seimas. Received proposals are then put to the vote. If the Seimas decides to commence the procedure of consideration of the draft, a principal committee is decided upon, and the deliberations of draft act continue in the committee.

associated with distributive perspective while the rest of the features mirror informational perspective.

As can be seen from table 4b.5, a majority of the CEECs allow in principle its committees to initiate legislation.[166] Only the Czech Republic reports that its committees do not have a right to initiate legislation nor to consolidate or split legislative bills.[167] Committees in Estonia, Latvia, Poland and Romania have both powers whereas in the rest the committees can either consolidate or split legislative bills (Bulgaria and Slovenia), or initiate legislation (Hungary, Lithuania, Slovakia).

Döring, 1995b considers different practises committees typically employ in altering government's legislative proposals. The key difference is whether the committees are allowed to replace the original text of the bill with their own text, or only allowed to include its amendments in a separate report and leave the original text intact. If committees have a right to alter government's text beyond recognition, and if the vote in the house is then taken on the committee's version, government agenda-setting powers are clearly compromised.

A half of the countries allow amendments to be presented in a committee report or annex. Bulgaria, Estonia, Latvia, Lithuania, Poland and Romania allow its committees to re-draft the original text. A respondent from Poland report that in practise the committees use their power to re-write the original text "very rarely". In Slovenia, Committees' amendments were included in a separate report until 2002 when new Rules of Procedure was adopted. Under the new rules, the Committees can redraft the original bill.[168]

As regards the informational powers, a considerable uniformity exists. All of the countries excluding Latvia and Poland allow the committees to compel witnesses to hearings and all countries allow the committees to demand docu-

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166 How actively the committees in practise exercise this right is to some extent an open question. Hungarian respondent replied that this happens only couple times during a parliamentary term. In Latvia, a total of 420 draft bills presented in 2002 of which 62 was proposed by committees against 252 bills proposed by the government. In Poland, 10 % of the enacted bills were proposed by the committees during 1993-1997 term (Olson et al, 1998). Several respondents indicated that committees in their countries used this power in practise rather rarely.

167 In many countries individual MPs can propose legislation. While it is quite possible that these powers are used more actively, it does not mean that bills proposed by MPs are finally adopted. For example in Slovenia – one of the three countries among the CEECs which does not allow its committees to initiate bills – a total of 631 acts were adopted during the parliamentary term of 1996-2000, and 570 of these were proposed by the Government. (Report on National Assembly's Work in the Parliamentary Term 1996 – 2000). In Polish Sejm, the MPs have been more active. During the 1993-1997 term, almost 40 % of the enacted bills were proposed by individual members whereas over 66 % of the enacted bills were proposed by the government. (Some bills have multiple sources. Olson et al, 1998). As Olson et al, 1998 notes, government bills are typically better prepared and thus more likely to be successful in a legislative process. Bills prepared by individual MPs are on the other hand poorly drafted and they suffer from lack of legal expertise. (115-117)

168 As for the reasons behind the change, one respondent from Slovenia mentioned a desire to strengthen the committees' powers and to shorten the legislative procedure in the plenary stage.

ments from the government when preparing legislation.[169] Most of the countries also report that as a rule the hearings are public. The two exceptions are Estonia and Romania. Typically, only the hearings of committees whose tasks are related to national security are non-public, or if the discussions can be otherwise – for example due to commercial secrets – regarded as confidential. The committees have discretion in deciding whether or not to hold non-public hearings, but available information indicates that the hearings are rarely non-public. The last column of table 4b.5 presents information about the existence of a special budget research organisation within the legislature. Most of the parliaments do not have a special budget research organisation within the legislature – excluding the committee staff. The only country where such unit exists is Poland.[170] Estonia reports that its analysis department performs also budgetary research.

Tables 4b.5 and 4b.6 also present indices that describe the distributional and informational attributes of parliamentary committees in the CEECs.[171] The committees in Estonia, Latvia, Poland and Romania have the most distributional attributes whereas the committees in Bulgaria, Romania and Slovakia have the most informational attributes.

Finally, table 4b.7 presents information about the role of budgetary committees and standing committees when the budget proposal is being scrutinised.[172] In Estonia, Poland and Slovakia the standing committees review all parts of the budget and can propose amendments to all parts of the draft budget (in Estonia as a rule to the part of their own jurisdiction). In the rest of the countries, they only review those parts that fall into their jurisdiction. Hungary, Latvia and Lithuania report that, even though as a rule the standing committees review only those parts of the budget that fall into their jurisdiction, the committees can nevertheless in principle propose amendments to all parts

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169 Strictly speaking, there is a difference between a power to invite and a power to compel witnesses. The respondents that gave an affirmative answer to this question indicated that the committees are in practise able to hear the witnesses that they choose whether or not the committees have a formal power to do so.

170 The unit was founded already in 1991. A research unit devoted to budget issues was seen as a way to increase expertise in budgetary issues but also as a way to strengthen the parliament's position against the government. A member of Bureau of Research from Polish Sejm explains: "The democratic transformation […] highlighted the issue of seeking greater impact of the Parliament and deputies on the central budget. […] Only they [budget analysis services and independent experts] can provide the deputies with the knowledge and expertise on central budget issues, verify information furnished by the Government and supply necessary information and evaluations, thereby enabling the deputies to deal skilfully with central budget issues." (Staskiewicz, 2002, 2-3).

171 Distributional attributes- index is formed by adding one for each of the following criteria (max 4 points): PCs can initiate legislation, PCs can consolidate/split legislation, PCs can amend legislation and amendments are included in a report/recommendation (1 point), PCs can re-write original government bill (2 points). Informational attributes- index is formed by adding one for each of the following criteria (max 4 points): PCs' jurisdiction corresponds with those of ministries, committee chairs are allocated proportionally, PCs can compel witnesses and demand documents.

172 The term "budgetary committee" is used here and it refers to the standing committee which has the primary responsibility for dealing with the state budget. In some countries this committee has a different name.

of the budget. In the rest of the countries, the committees are allowed to propose amendments only to those parts of the budget that fall into their jurisdiction. The Czech Republic, Estonia, Lithuania, Poland and Romania report that representatives of the standing committees typically attend the budgetary committee meetings when expenditures in their jurisdiction are being death with.

Budgetary committee is typically responsible for coordination the legislative budget procedure and it collects and summarises the amendment proposals submitted by the other standing committees before the budget proposal goes to the plenary. Bulgaria, Estonia, Lithuania and Poland report that in practise the budgetary committee can reject the amendments made by other standing committees, while in rest of the countries this is not the case. But even in the countries without this power the budgetary committee's attitude towards the amendments tabled by other standing committees is not insignificant since it typically presents the budget proposal to the plenary. In all countries the budgetary committee itself can also make amendment proposals to the budget.

Final column of table 4b.7 presents information about who typically participates in the hearings of the committees when they are dealing with the budget proposal. Hungary and Lithuania are the only two countries who report that finance minister does not typically attend, even though civil servants from the finance ministry are present. All countries report that ministers from other ministries typically are present.

5.4 The monitoring and implementation stage

Table 4c.1 presents information on how the CEECs monitor their budget implementation. All countries the Finance Ministry bears the primary responsibility within the government. Level of specificity in monitoring spending and revue is fairly uniform. The former is monitored in individual ministry level in all countries whereas the latter is monitored according to source. In general, the lag between cash flows and reporting is short, usually days, for central government and months for local governments.

Transparency of the budget has been identified as a one element of a "good" budget-making.[173] One related issue is existence of public reports of public outcomes. In every country such reports exists. Some minor differences can be found from the reporting frequency; every country except Slovakia (quarterly) publishes reports at least monthly.

In all countries except Bulgaria, the parliament is informed automatically on the implementation of the budget. In Bulgaria, parliament is informed only if it requests information or in case of deviations from the budget. Central Bank does not typically have a role in monitoring. The exception is Latvia where the

173 See Alesina and Perotti, 1999 who also note that budget transparency can be hindered by keeping various items off budget and deliberately manipulating forecasts which makes it difficult to detect the true state of affairs.

president of the Bank of Latvia may participate in the cabinet meetings and has a consultative role on the fiscal matters; in case of disagreements on fiscal policy, the president of the Bank of Latvia can make a public statement.

Table 4c.2 presents information about the finance ministry's role in implementation of the budget. Some variation among countries exists. Finance Ministers in Bulgaria, Latvia, Poland and Slovakia can in practise block in-year expenditures; in rest of the countries the whole cabinet has a more substantial role in deciding the issue. The finance minister must also approve disbursement of funds in Bulgaria, Estonia, Lithuania, Poland and Romania. Further, finance minister can impose cash limits in most of the countries (Bulgaria, the Czech Republic, Estonia, Poland, Slovakia and Slovenia). In these countries – excluding Estonia – the cash limits are also department specific.

In every country the transfers between budget chapters are in principle allowed. Several limitations however apply in the case with almost every country. In Bulgaria, Poland (until 1998), Romania and Slovakia these transfers require finance ministry's approval. Finally, in all countries except Hungary and Slovenia changes in budget law are allowed during budget execution and in all countries except Bulgaria, Lithuania (until 2000) and Romania unused funds can be carried over into following year but only with several restrictions.

Finally, table 4c.2 includes an index which measures finance minister's role in the implementation stage of the budget.[174] Bulgaria and Poland (until 1999) have the highest index values whereas Hungary has the lowest.

Table 4c.3 includes data about ex-ante rules to deal with positive or negative shocks to their budget balance. The former includes situations where revenues are higher, or expenditures are lower than projected in the budget (and vice-versa for the latter scenario). For example, Christou and Daseking, 2002 have argued that there should be a clear understanding how to respond in times of fiscal over-performance or adverse developments, also given the possibility of some tensions in the face of prioritising between different spending categories. Ad-hoc cuts in investment, for example, could be then avoided. Further, as noted by Brunila and Kinnunen, 2002, a strict adherence to expenditure limits is not appropriate in all situations. If such limits do not pay any attention to cyclically-induced changes, this could result to a pro-cyclical fiscal policy.

In general the CEECs do not have clear ex-ante rules, and in many countries where any rules exist, they have introduced quite recently. Rules to deal with negative shocks are more common: the Czech Republic, Hungary and Latvia report having such rules in place. Bulgaria, Lithuania and Slovakia have some legal provisions in place for negative shocks but it is unclear whether these rules establish in practise an obligation to act in a certain way or if they merely present a possibility to do so and the decision is taken in an ad hoc basis. Finally, Estonia, Poland, Romania and Slovenia do not have any ex-ante

174 Finance Minister in implementation- index is formed by adding one for each of the following criteria (max 4 points): MoF can block expenditure in-year, MoF must approve disbursement of funds, MoF can impose cash limits, MoF must approve transfers of funds between chapters.

formal rules in place. In practise, these countries commonly use supplementary budgets or the governments simply let overall budget balance to adjust.

Finally, table 4c.4 presents information about the relationship between national government and sub-national governments. This issue is not without significance since the SGP requires the general government to have a medium-term budget balance of "close to balance or in surplus". Indeed, this obligation applies to the general government and thus it is a concern of all levels of government, and not just the central or federal government. As noted by European Commission, 2001, the role of all national budgetary players (the central government, Parliament, and local and regional governments) in preparing the stability or convergence programme warrants consideration.[175]

In every CEEC various arrangements between the national government and sub-national governments are in place either to ensure that budgetary targets for general government are met, or to restrict lower levels of government borrowing. However, in several countries the arrangements have been introduced, or completely reformed, very recently.

5.5 A comparison to the EU-15

As already mentioned in chapter 3.2, fiscal institutions are not often easy to change; as a result there is a strong status-quo bias in institutional reform. In the case of the CEECs, this notion is probably less true as these countries have seek to develop their fiscal management throughout the 1990s. Nevertheless, just after a decade – and also taking into account the political volatility in many countries – one would expect that their fiscal institutions are not as developed as for example in their Western European counterparts.

Indeed, some differences do emerge in a comparison between the CEECs and the EU-15. In the planning stage, this applies to some aspects of the multi-annual frameworks. According to European Commission, 2003a, the fiscal targets used in the EU-15 do not possess many of the characteristics given above for 'ideal' fiscal targets either. But interestingly, according to the data presented in Hallerberg et al 2001, the EU-15 countries classified as commitment states include the multi-annual targets in their coalition agreements thus raising the profile of such targets. As a rule, this is not the case in the CEECs.

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175 Also von Hagen et al 2002, discuss to what extent national governments can effectively commit their countries to compliance with the obligations of the SGP. In countries where the national government controls most of the public finances the answer depends largely on its budget process. But in countries where sub-national governments control a large part of the public finances, the answer is more difficult. Von Hagen et al note that 'internal stability pacts' between the central and sub-national governments have been implemented to solve this problem in the EU-15 countries.

TABLE 7 Comparison of the index values between the CEECs and the EU-15: relationship between the EU processes and annual budgets[176]

rank	Country	index value
1	Poland, Slovenia, *UK*	7
4	Hungary, Romania, *Ireland, Luxemburg, Netherlands*	6
9	Bulgaria, Lithuania	5
11	Estonia, Latvia, Slovakia, *Belgium*	4
15	Czech Republic, *Austria, France, Germany, Italy, Spain, Sweden*	3
22	*Finland*	2
23	*Greece, Portugal*	1
25	*Denmark*	0

means (index-values):	CEECs	EU-15	t-test for equality of the means
all states	5.1	3.4	t-value: 2.28, p: 0.03
delegation-states	6.5	3.3	t-value: 2.38, p: 0.05
commitment-states	4.8	4.8	-

Regarding the relationship between annual budgets and EU-procedures, two clear differences stand out between the CEECs and the EU-15 (see table 7). First, the connectedness is generally higher in the CEECs, and secondly, the two delegation states in the CEECs have the highest index value. In the EU-15, the delegation states have on average low connectedness.[177] The former difference could explained by the fact that the EU procedures, including Joint-Assessment of Medium-term Economic Policy Priorities that were jointly prepared by the Commission and national authorities, introduced medium-term budgeting to many of the CEECs. Further, the national procedures have been in general in a state of change. Therefore, these procedures could have had a greater influence in shaping the fiscal processes in the CEECs compared to EU-15 where the national traditions have perhaps been more firmly rooted.

The table 8 presents the indices on the finance ministers' influence in the decision-making stage.[178] The differences are not statistically significant but the results suggest that the EU-15 states have somewhat stronger finance ministers than the CEECs. Delegation states have equal index values in the CEECs and the EU-15.

A comparison to EU-15 reveals that while the differences are not statistically significant, the parliaments are somewhat weaker in the CEECs compared

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176 Notes for tables presented in this section: "EU-processes" in table 7 refer to convergence or stability programmes for the EU-15, and to PEPs for the CEECs. EU-15 countries marked in *italics*. Source for the EU-15: Hallerberg et al 2001 (tables 10 and 11 Mattson and Strøm, 1995, Döring, 1995b, Hallerberg, 2000). CEECs delegation states: HUN, SNA; CEECs commitment states: BUL, CZE, EST, LAT, LIT, POL, ROM, SKA; EU-15 delegation states: AUS, FRA, GER, GRE, ITA, SP, UK; EU-15 commitment states: BEL, FIN, IRL, LUX, NL; (note: DEN, PT and SWE fall into the "hybrid" category). The indices for the CEECs are formed based on 2003 data unless otherwise noted.

177 On the other hand, UK – a delegation state – has the highest index value among the EU-15.

178 The index-values for the CEECs in tables 8 and 9 are different from the ones presented in tables 4a.5 and 4b.1 of the annex 4, respectively. This is due to minor differences in the coding rules as explained above in this chapter (see footnotes 149 and 158). In order to produce comparable values, the indices for the CEECs in tables 8 and 9 are calculated according to the coding rules used in Hallerberg et al, 2001.

to EU-15 in the legislative stage of the budget process (see table 9). This is especially true for commitment states. Tables 10 and 11 present a comparison regarding informational and distributional attributes, respectively. It seems that while the CEECs have a somewhat weaker parliaments in the legislative stage of the budget process, their parliament committees do in fact possess more formal powers than the parliament committees in the EU-15.

TABLE 8 Comparison of the index values between the CEECs and the EU-15: the role of finance minister in decision-making stage

rank	Country	index value
1	*Austria, Italy*	8
3	Hungary (excl. 98-02), *France, UK*	7
6	*Denmark*	6.3
7	Slovenia, *Greece, Spain*	6
10	Poland, *Belgium*	5.5
12	Estonia, *Germany, Ireland*	4.5
15	Lithuania	4.3
16	*Sweden*	4
17	Hungary (98-02), Romania, *Finland, Netherlands*	3.5
21	Latvia	3.3
22	*Luxemburg*	3
23	Bulgaria, Czech Republic	2.5
25	Slovakia	2.3
26	*Portugal*	2

means (index-values):	**CEECs**	**EU-15**	**t-test for equality of the means**
all states	4.1	5.3	t-value: 1.55 , p: 0.14
delegation-states	6.5	6.6	t-value: 0.15 , p: 0.88
commitment-states	3.6	4.0	t-value: 0.72, p: 0.48

TABLE 9 Comparison of the index values between the CEECs and the EU-15: the role of parliament in legislative stage

rank	Country	index value
1	*Belgium, Luxembourg, Netherlands*	5
4	Slovakia, *Austria, Portugal, Sweden*	4
8	Bulgaria, Latvia, Poland (pre-97), Romania (pre-02), *Denmark, Germany, Italy, Spain*	3
17	Czech Republic, Hungary, Slovenia, *Finland*	2
20	Estonia, Lithuania, Poland (post-97), Romania (post-02), *France*	1
27	*Greece, UK, Ireland*	0

means (index values):	**CEECs**	**EU-15**	**t-test for equality of the means**
all states	2.0 (pre-98: 2.4)	2.8	t-value: 1.25 , p: 0.22
delegation-states	2,0	2.0	-
commitment-states	2.0 (pre -98: 2.5)	3.4	t-value: 1.46 , p: 0.17

TABLE 10 Comparison of the index values between the CEECs and the EU-15: informational attributes of the parliamentary committees

rank	Country	index value
1	Bulgaria, Romania, Slovakia, *Spain*	4
5	Czech Republic (post-02), Estonia, Hungary, Lithuania, Poland, Slovenia, *Austria*, *Denmark*, *Luxembourg*, *Portugal*, *Sweden*	3
16	Czech Republic (pre-02), Latvia, *France*, *Germany*, *Belgium*, *Finland*, *Netherlands*	2
23	*Italy*	1
24	*Greece*, *Ireland*, *UK*	0

means (index-values):	CEECs	EU-15	t-test for equality of the means
all states	3.2 (pre-02: 3.1)	2.0	t-value: 2.79, p: 0.01
delegation-states	3.0	1.7	t-value: 1.16, p: 0.28
commitment-states	3.3	1.8	t-value: 2.93, p: 0.01

TABLE 11 Comparison of the index values between the CEECs and the EU-15: distributional attributes of the parliamentary committees

rank	Country	index value
1	Estonia, Latvia, Poland, Romania, *Austria*, *Sweden*	4
7	Bulgaria, Lithuania, Slovenia (post-02), *Belgium*, *Finland*, *Germany*, *Italy*, *Luxembourg*, *Spain*	3
16	Hungary, Slovakia, Slovenia (pre-02), *Greece*, *Portugal*	2
21	Czech Republic, *Denmark*, *France*, *Ireland*, *Netherlands*, *UK*	1

means (index-values):	CEECs	EU-15	t-test for equality of the means
all states	3.0 (pre-02: 2.9)	2.3	t-value: 1.50 , p: 0.15
delegation-states	2.5	2.4	t-value: 0.08, p: 0.94
commitment-states	3.1	2.2	t-value: 1.46, p: 0.17

TABLE 12 Comparison of the index values between the CEECs and the EU-15: the role of finance minister in implementation stage

rank	Country	index value
1	Bulgaria, Poland (pre-99), *Austria*, *France*, *Greece*, *UK*	4
7	Poland (post-99), Slovakia, *Italy*, *Spain*, *Ireland*	3
12	Estonia, Romania, *Germany*, *Denmark*, *Portugal*, *Luxembourg*	2
18	Czech Republic, Latvia, Lithuania, Slovenia, *Belgium*, *Finland*, *Netherlands*	1
25	Hungary, *Sweden*	0

means (index-values):	CEECs	EU-15	t-test for equality of the means
all states	1.8 (pre-99: 2)	2.4	t-value: 1.16, p: 0.26
delegation-states	0.5	3.4	t-value: 4.71, p: 0.002
commitment-states	2.1	1.6	t-value: 0.88, p: 0.40

Finally, regarding the implementation stage, the comparison to the EU-15 reveals (see table 12) that the CEECs have on average lower index values. This implies that the finance ministers in the EU-15 have stronger role in the implementation stage compared to their colleagues in the CEECs.

Therefore it seems that some differences can be found between the EU-15 and the CEECs. In short, the multi-annual plans in the EU-15 are generally developed further than in the CEECs. However, the connection of the EU procedures and the annual budget process seems to be closer in the CEECs. The EU-15 has somewhat stronger finance ministers whereas the evidence on the parliaments' role was somewhat mixed: the EU-15 states have stronger parliaments in the legislative stage in the budget process whereas the parliamentary committees in the CEECs possess more formal powers the committees in the EU-15.

What then could be the practical implication of this information? The EU-15 countries have more powerful ministers, but there are some reasons to believe that having a strong finance minister would be more important for the CEECs than for the EU-15. As mentioned above, the fiscal targets employed by the EU-15 do not generally include features given for ideal fiscal targets. However, as just mentioned the EU-15 – and particularly the commitment countries – have developed the commitment elements, in particular their multi-annual frameworks, further than the CEECs. The CEECs are still in a process of developing similar practises and a strong finance minister who helps to ensure fiscal rigour could therefore be more necessary. On the other hand, the closer connection of the EU procedures and the annual budget process could be good news for the CEECs. [179] One of the suggestions included in Hallerberg et al, 2001 was to ensure a tighter connection between the stability and convergence programmes and the annual budget in the EU-15 countries. Especially different timing was a cause for concern. These issues are re-visited shortly in chapter five.

5.6 Summary

Table 13 brings together the discussion about the predicted fiscal institutions from chapter 4 with the discussion above about the actual fiscal institutions.[180] The connection between the theory's predictions and the reality is especially strong regarding the executive stage. Almost all countries have strengthened the commitment element recently by establishing multi-annual frameworks. The two countries with the most powerful finance ministers – Hungary and Slovenia – are classified here as "weak" delegation countries due to the fact that the finance ministers' powers do not cover implementation stage.[181] Further, a

[179] However, further work remains to be done also in the CEECs; see footnote 142 in chapter 5.2.2.

[180] The institutional data from the early post-communist years is not very reliable due to the lack of translated budget legislation from those years. Thus the very beginning of the 1990s is omitted from the last column. Von Hagen, 1998 and Hallerberg and von Hagen, 1999 have performed similar comparisons between predicted and actual fiscal institutions for the EU-15.

[181] One should also note that especially Slovenia's fiscal institutions include many features from commitment approach, too. In this sense, the classification for Slovenia is less pronounced. Also for Hungary this applies only to the period excluding years 1998-2002 with the caveats mentioned in footnote 148 of this study.

general connection between political instability and de-centralised budget processes have existed. Therefore, the important conclusion is that this discussion does lend general support to the interdependency between the political fundamentals and the development of fiscal institutions.

TABLE 13 Predicted and actual fiscal institutions in the CEECs

	Stability	Electoral system proportionality	No of cleavages	Degree of party discipline in budget votes	Fiscal institutions	
					Prediction	Reality
Bulgaria	0.37 (91-97) 0.56 (97-02)	proportional	6	Defecting MPs not common	fiefdom (91-03); commitment/ delegation (future)	fiefdom (94-98); commitment (98-)
Czech Republic	0.54 (92-98) 0.81 (98-02)	proportional	5.5	Defecting MPs not common	fiefdom (92-03); commitment/ delegation (future)	commitment (94-)
Estonia	0.71 (92-95) 0.58 (95-02)	proportional	4	Defecting MPs not common	commitment (92-03)	commitment (94-); strengthened (01)
Hungary	1	mixed	7	Defecting MPs not common	delegation (90-03)	(weak) delegation (94-98; 02-); fiefdom (98-02)
Latvia	0.51 (93-98) 1 (98-02)	proportional	5.5	Defecting MPs not common	commitment (93-03)	commitment (94-); strengthened (01)
Lithuania	0.87 (92-96) 0.80 (96-02)	mixed	5	Defecting MPs in general not common (3-4 MPs/budget vote)	delegation (92-96); commitment (96-03)	fiefdom (94-99); commitment (99-); strengthened (00)
Poland	0.72 (91-97) 0.61 (97-02)	proportional	4.5	- In the 1993 - 1997 term: about 3 MPs/vote - In the 1997 - 2001 term: about 10 MPs - present term: no such cases	fiefdom (91-03); commitment (future)	fiefdom (94-99); commitment (99-)
Romania	0.46 (90-96) 0.55 (96-02)	proportional	7	Defecting MPs common but the number is usually small	fiefdom (90-03); commitment (future)	(weak) commitment (94-03); strengthened (03)
Slovakia	0.70 (92-98) 1 (98-02)	proportional	5	Defecting MPs not common	commitment (92-03)	commitment (94-); strengthened (00)
Slovenia	0.66 (92-97) 1 (97-02)	proportional	8	Defecting MPs common but the number is usually small (1-5 /budget vote)	fiefdom (92-03); commitment (future)	(weak) delegation (94-)

Indeed, the reality in the planning and decision-making stage broadly speaking corresponds with the expectation that followed from theoretical arguments formed in the previous chapters. As expected, the commitment element in the planning and decision-making stage is strong in the majority of the CEECs. The cabinet possesses a strong role in setting the targets, negotiating the budgets and resolving the emerging conflicts. The commitment element of the fiscal frameworks is also strengthened – albeit to a varying degree – by an introduction of multi-annual budgeting. Some of the important elements of the commitment approach are however lacking as these processes are still taking shape.

Based on the information about the executive stage, one can judge that fiscal targets are in general 'weak'. In other words, the targets are based on political commitment and they serve as non-binding or indicative benchmark for budget-making process. The majority of countries do not discuss the deviations between the objectives laid out in the multi-annual plans and the actual outcome thus undoubtedly weakening the credibility of such targets – or guidelines. Typically, the CEECs do not have clear provisions in place on what should be done in times of economic under- or over-performance. Further, in all countries the multi-annual targets are agreed within the cabinet but none of the countries include the agreed commitments in the coalition agreements. Therefore, the defection from jointly negotiated targets is easier as monitoring of the compliance becomes more difficult and political costs from defection are smaller. Nevertheless, it is worth noting that many countries are still in a process of developing their multi-annual frameworks.

According to the index values, the two countries that have clearly most powerful finance ministers in the decision- and planning stage are Hungary and Slovenia. For the Hungarian case this was expected based on the discussion in the previous chapter. Slovenia, on the other hand, has had consistently coalition governments, but the prediction was that the undisciplined voting behaviour and a certain degree of dominance by one party – namely Liberal Democratic Party – might have not encouraged the development of a commitment approach.[182] In both countries the bilateral budget negotiations has a more prominent role, the finance minister has in practise a veto right to prevent significant changes in the budget proposal from taking place and the prime minister – not the full cabinet – finally resolves the disputes.

Further, most of the countries that were identified as being candidates for a fiefdom approach did in fact have rather decentralised budget processes in the beginning of the 1990s. Bulgaria, Poland and Lithuania[183] did not seek to

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182 Interestingly, Poland, another country with undisciplined voting behaviour has a third-strongest finance minister in the planning and decision-making stage according to the index values.

183 Lithuania was not identified as a candidate for a fiefdom approach but a change in its form of governance during the period was predicted. Further, Poland does, in fact, have a fairly strong finance minister according to the index values. It has nevertheless been coded as a fiefdom state for the pre-1998 period. The reason is the absence of numerical fiscal targets during this time and to a lesser extent the volatile political environment. In particular, the relationship between prime minister and finance minister has been quarrelsome leading to finance minister's frequent resignations. As

gain from jointly negotiated annual fiscal targets nor did they have strong finance ministers imposing strategic powers over spending ministers. To some extent this applied also to Romania. All of these countries have, however, strengthened their budget processes towards commitment approach by employing both annual and multi-annual fiscal targets negotiated among the cabinet.[184]

The evidence on the legislative stage is somewhat mixed. Delegation states do not have weaker parliaments in the legislative stage of the budget process compared to the commitment states as the theory expects. The countries have sought to employ different ways to limit the parliamentary amendments, and as a result, the legislature's possibilities to alter the executive's budget proposal are, in general, limited. More generally, the parliamentary committees possess formal distributive powers, such as powers to initiate legislation and to amend legislative bills. However, there is some evidence – albeit mostly anecdotal – that the committees do not use their formal powers to the full.[185] The theory expected that commitment states should have parliament committees with power to collect information so as to inform coalition partners from possible defections from jointly negotiated targets – or from aspirations to do so. The results above largely confirm that the committees in the CEECs possess these powers. Further, the delegation states do in fact have somewhat weaker parliament committees both in terms of distributional and informational attributes. Due to small number of cases, the differences are not statistically significant. Overall, the parliamentary committee systems in the CEECs are organised in a very similar fashion than in the Western Europe.

Final stage concerned the monitoring and implementation of the budget. All countries publish regularly public reports about the outcomes in public finances.[186] Also parliament is well informed. In the implementation stage, the government's role is generally strong as the finance minister in most countries has to seek the full cabinet's approval to carry out different measures. In the

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mentioned in section 3.1.2, one crucial element of delegation approach is the scope and strength of the punishments and rewards a finance minister can use to assure the adoption of his proposal. During the budget negotiations, the finance minister's power must be backed by the prime minister, and since the prime minister is the strongest cabinet member, his backing gives the finance minister considerable fiscal powers over spending ministers. In Poland, this has not been the case. Indeed, it is worth noting that the index values do not automatically translate into different modes of fiscal governance.

184 Both Lithuania and Poland have introduced changes also to other stages of the budget process.

185 This concerns mostly power to initiate legislation. See also Zajc, 1997 who reviews the parliamentary committees in some of the countries of East Central Europe. He concludes by stating that "formal powers are considered an important basis of the strength of committees in the West European parliaments, but formal powers can not reveal the whole picture in the newly democratic [East Central European] countries – committees may be well equipped with formal rights but ill prepared to use them. […] We conclude that the formal powers of parliamentary committees in the [East Central European] countries in general represent the range of possibilities which might be developed over time, although there are many internal and external factors inherently limiting the overall strength of these parliamentary committees." (498)

186 The data here is not sufficient to assess the content and quality of the public reports.

monitoring and implementation stages the theory expects the delegation states to have powerful finance ministers. In the case of the CEECs, this is clearly not the case. In fact, Hungary and Slovenia have the lowest index values in the group.

TABLE 14 Correlation matrix of indices

	Finance minister, planning and decision-making stage (MFD)	Parliament, legislative stage (PL)	Parliament, distributive attributes (PD)	Parliament, informational attributes (PI)	Finance minister, implementation stage (MFI)
Finance minister, planning and decision-making stage	1				
Parliament, legislative stage	-0.38	1			
Parliament, distributive attributes	0.28	-0.17	1		
Parliament, informational attributes	-0.25	0.10	0.01	1	
Finance minister, implementation stage	-0.42	0.08	0.35	0.70**	1

Notes: Entries are spearman rank correlations. Calculations based on 2003 data. Significance levels: < 0.01 = ***, 0.01-0.05 = **, 0.05-0.10 = *.

Indeed, table 14 presents the spearman rank correlation matrix of the different indices, and it becomes immediately clear that no clear patterns can be discovered as the correlations are not statistically significant.

6 FISCAL FRAMEWORKS AND FISCAL PERFORMANCE

The previous sections established that several differences in the fiscal frameworks of the CEECs exist. The interesting question then is how these differences have affected the fiscal performance of these countries.

6.1 About the fiscal data

There are two main reasons why it is difficult to produce an unambiguous answer to the above-mentioned question. These caveats concern especially the earlier years.

First, there are some serious doubts about the stability and reliability of public finances data for these years. The time-series include structural breaks as definitional adjustments have not often been applied retroactively. This means that the fiscal data for the early years of the period provides at best only an approximate indicator of the underlying budgetary situation.[187]

Further, the ongoing transition process and related policy measures have had a significant impact on the behaviour of fiscal indicators. Indeed, transition economies engaged with structural reform process suffer often from persistent fiscal deficits. Theoretical and more informal treatments on transition and fiscal deficits have sought to explain how public expenditure and deficits are affected in the process.[188]

Two basic results seem to stand out from this discussion: first, budget deficits can be expected to occur particularly in the beginning of the (successful) transition and especially in fast reforming countries, and secondly, overly tight fiscal constraints may slow down the transition process. As transition advances one can expect fiscal positions to gradually improve following reforms in tax

187 See also European Commission, 2002 and 2003b.

188 For references, see footnote 3 of this paper. For a review, see Pirttilä, 2000.

systems and enhanced efficiency in the economy in general (other things being equal). This is subject to what strategy with respect to reforms is adopted. Slow reformers have tended to preserve the level of fiscal subsidies while fast reformers have cut subsidies more aggressively but had to increase social expenditures to compensate those affected by market reforms. As European Commission, 2002 also note, a high fiscal deficit may in fact be an inevitable by-product of a successful transition, rather than necessarily an indicator of irresponsible fiscal policy. This would suggest that the differences between the fiscal frameworks might not be powerful explanatory variables to the behaviour of public finances during the transition period. A contrasting view is presented by Gleich, 2002 who finds that fast-reforming countries did not suffer from larger budget deficits during the 1990s, and that the differences in fiscal institutions can in fact explain the fiscal performance for these years.[189]

However, the story is somewhat different for the latter period. The CEECs have participated in a voluntary pre-accession fiscal surveillance procedure which aims to enable the CEECs to participate in EU multilateral fiscal surveillance procedures – take part in the excessive deficit procedure and produce convergence programmes – after EU accession. To this end, the CEECs have submitted annual notifications of public deficits and debt levels, and Pre-accession Economic Programmes, or PEPs each year. In the context of the notifications the CEECs are asked to report general government deficits and debts in the same format as is done by existing member states. A key task is to ensure accuracy of government accounts and their compliance with European System of Accounts, or ESA 95, which forms a basis for budgetary surveillance. The CEECs have also been involved with the work done in the context of International Monetary Fund's Code of Good Practices on Fiscal Transparency, adopted in 1998, and related reports on the observance of standards and codes. One element of this exercise has been accounting practises.[190]

The ESA 95 -based public finances data produced in the context of the fiscal notifications exercise can be considered as consistent, even if the data in-

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189 Pirttilä, 2000, has also found some evidence that contrary to the theory, number of the CEECs have faced smaller fiscal pressure despite rapid reforms while fiscal deficits have been larger in slow reform countries, particularly in several former countries of Soviet Union. Fischer and Sahay, 2000 offer alternative explanation by suggesting that deficits in fast reformers may look worse that they actually are as compared to other countries simply because accounting practises are better in fast reformers.

190 To improve the quality of fiscal data, the IMF has produced Government Financial Statistics Manuals, or GFSMs, which have provided a conceptual and accounting framework. Two editions of this manual have been published. The first one is referred to as GFSM 1986, and the second as GFSM 2001. The idea behind the GFS-manuals has been to build first cash-basis accounting (i.e. government transactions are recorded when transactions are carried out and the financial balance is the result of all transactions made during a fiscal year), and then progressively advance to accrual basis accounting (i.e. government transactions are recorded when economic values are created or transformed regardless of when the actual transaction is completed and the total balance is registered as net borrowing or net lending of the government sector). ESA 95 is based on the latter approach.

cludes only general government balance and debt.[191] The coverage of the fiscal notifications begins from 1999. Further, while the economic transition is not completed, it is nearing completion in many of the CEECs. As a result, its effects on the public finances are gradually dissipating.[192]

6.2 The analysis

For the reasons given above, the analysis below is performed separately for two periods: 1995-1998 and 1999-2002.[193] The very early years of the 1990s are excluded because the coverage of the information on fiscal institutions does not extend to the very beginning of the 1990s. The fiscal data for the earlier period is taken from EBRD, 2001 and 2003. The fiscal data for the latter period is – unless noted otherwise – taken from European Commission's statistical annex of European Economy (Autumn 2004). The fiscal data refers to general government.[194]

TABLE 15 Public finances data 1995-2002: an overview

Year	Mean budget balance	Standard deviation	Range (min/max)
1995	-2.9	2.3	from -6.7 (HUN) to 0.4 (SKA)
1996	-3.4	2.9	from -10.3 (BUL) to -0.2 (SNA)
1997	-2.3	2.3	from -5.2 (SKA) to 2.2 (EST)
1998	-2.7	2.4	from -5.8 (LIT) to 1.3 (BUL)
1999	-3.8	2.2	from -7.1 (SKA) to 0.4 (BUL)
2000	-3.4	3.4	from -12.3 (SKA) to -0.5 (BUL)
2001	-3.0	2.2	from -6.0 (SKA) to 0.3 (EST)
2002	-3.3	3.1	from -9.2 (HUN) to 1.4 (EST)
Year	**Mean Δ public expenditure**	**Standard deviation**	**Range (min/max)**
1995	-1.0	2.5	from -6.1 (HUN) to 1.2 (CZE)
1996	-1.1	1.6	from -3.8 (HUN) to 1.8 (SKA)
1997	-1.2	3.1	from -9.3 (BUL) to 1.5 (LAT)
1998	1.2	2.5	from -2.6 (SKA) to 5.7 (BUL)
1999	0.5	2.5	from -5.6 (HUN) to 3.3 (LIT)
2000	-0.8	3.1	from -7.3 (LIT) to 2.3 (HUN)
2001	1.0	4.8	from -4.4 (LAT) to 13.4 (HUN)
2002	0.9	2.6	from -2.4 (LIT) to 6.8 (HUN)

191 The general government debt is not used here as a dependent variable as there are not enough years to calculate the annual change in the debt-to-GDP ratio and using the level of debt would be problematic (see footnote 68 of this paper).

192 This is not to say that transition-related effects have completely faded away. For example, debt-ratios in many countries are still being affected by privatisation proceeds and other related measures. See European Commission, 2003b.

193 A further reason to divide the period into two follows from the fact that many countries have introduced reforms to their fiscal institutions around 1998-1999 which have changed the index-values used as explanatory variables in the regressions. Two periods permit the use of time-invariant explanatory variables.

194 Since the fiscal frameworks covered in this study are designed to affect the central government behaviour, one should ideally use central government figures, instead of general government. The figures for general government are however used due to better availability.

TABLE 16 Public finances data 1995-2002: country specific figures

budget balance	BUL	CZE	EST	HUN	LAT	LIT	POL	ROM	SKA	SNA
1995	-5.7	-1.1	-1.3	-6.7	-4.0	-4.4	-3.1	-2.5	0.4	-0.3
1996	-10.3	-1.7	-1.5	-5.0	-1.8	-4.5	-3.3	-3.9	-1.3	-0.2
1997	-2	-2.1	2.2	-4.8	0.3	-1.8	-3.1	-4.6	-5.2	-1.7
1998	1.3	-2.4	-0.3	-4.8	-0.8	-5.8	-3.2	-5.0	-5.0	-1.4
1999	0.4	-3.6	-3.7	-5.6	-4.9	-5.6	-1.4	-4.5	-7.1	-2.2
2000	-0.5	-3.7	-0.6	-3.0	-2.8	-2.5	-0.7	-4.4	-12.3	-3.5
2001	0.2	-5.9	0.3	-4.4	-2.1	-2.0	-3.8	-3.5	-6.0	-2.8
2002	-0.8	-6.8	1.4	-9.2	-2.7	-1.5	-3.6	-2.0	-5.7	-2.4
Δ public exp.	**BUL**	**CZE**	**EST**	**HUN**	**LAT**	**LIT**	**POL**	**ROM**	**SKA**	**SNA**
1995	-4.4	1.2	0.7	-6.1	1.0	-1.6	-1.3	0.8	-0.3	-0.2
1996	0.7	-0.8	-1.0	-3.8	-2.0	-1.6	-2.8	-0.9	1.8	-0.5
1997	-9.3	-0.5	-2.9	0.7	1.5	-0.7	-0.6	0.2	-1.5	0.9
1998	5.7	-0.8	2.0	0.9	2.3	4.1	-1.2	0.7	-2.6	0.6
1999	2.2	1.0	3.1	-5.6	0.8	3.3	-0.7	0.5	0.4	0.1
2000	1.4	1.8	-4.1	2.3	-2.1	-7.3	-1.3	-0.2	2.1	-0.4
2001	-1.4	1.0	-0.8	13.4	-4.4	-1.9	2.6	-0.6	2.3	0.2
2002	-0.7	3.1	1.5	6.8	-0.1	-2.4	0.5	-0.8	2.3	-0.8

Notes: Note that the data for budget balance comes from two different sources thus resulting to a structural break. Data for budget balance for 1995-1998 and data for Δ public expenditure from EBRD 2001 and 2003. Data for budget balance for 1999-2002 from European Commission's statistical annex of European Economy (Autumn 2004). All figures refer to general government.

Tables 15 and 16 present simple descriptive statistics about the general government balance-to-GDP ratio and the annual change in the public expenditure-to GDP ratio. It becomes immediately clear that large differences exist across the CEECs. The question is then, is it possible to explain these differences by the differences in the fiscal frameworks.

One often used method to test whether the differences in the fiscal frameworks have had any impact on the fiscal performance is to construct indices which describe the institutional characteristics of the budget procedures in a given set of countries. Typically, the indices measure the finance minister's strength over spending ministers in the planning and decision-making and implementation stages, and the executive's strength over the legislature in the legislative stage of the budget process. These indices are then used as explanatory variables to different measures of fiscal performance. This is the approach taken in this study, too.

However, while the indices describe the overall characteristics of budget procedures, they do not make any distinction between different forms of fiscal institutions discussed in earlier chapters; commitment, delegation and fiefdom. The theoretical considerations suggested that countries with de-centralised fiscal institutions – named as fiefdom countries – are more likely to suffer from a lack of fiscal discipline compared to countries with commitment and delegation approaches.[195] For the earlier period, the mean budget balance-to-GDP ratio of the fiefdom countries (-3.8 %) is indeed larger compared to the rest (-2.2 %).

195 This is, strictly speaking, different from simply using the index values in the analysis since the index values do not automatically translate into different forms of fiscal institutions.

Particularly striking the difference is to the commitment countries (-1.6 %).[196] However, one should avoid placing too much emphasis on these figures for the reasons explained in the first part of the chapter.

In the latter half of the period, only one country – Hungary – was coded as a fiefdom country. As anecdotal evidence, one can note that after a change in its form of fiscal management from delegation to fiefdom around 1998, Hungary's budget balance-to-GDP ratio deteriorated nearly four percentage points, from -5.6 % in 1999 to -9.2 % in 2002.[197]

The theory suggested further that commitment states rely more on jointly negotiated fiscal targets than on a strong finance minister. Therefore, it can be questioned if an index which puts emphasis on finance minister's dominance should be used in the case of the commitment states.[198] The majority of the CEECs do have a strong commitment element in their fiscal institutions in the sense that the cabinet makes most of the fiscal decisions, not the finance minister. However, based on the discussion in chapter 5, there are some reasons to believe that the commitment element has not in the past been sufficiently strong in these countries to guarantee fiscal discipline.

In the commitment countries of the EU-15 there might indeed be less need for a strong finance minister as the agreed multi-annual plans are cemented in the coalition agreements which help to ensure fiscal discipline. For example, Hallerberg et al, 2001 finds that stronger finance ministers in formulating the multi-annual plans have been effective only in non-commitment (delegation and hybrid) countries. This result was driven by the fact that commitment countries write their budget plans in the coalition agreements and finance minister's influence is thus smaller. In the CEECs, the finance ministers' influence is likely to be more significant in this sense as the use of coalition agreements as a tool for enhancing the fiscal discipline is not widespread. The commitment element has been strengthened by the introduction of the multi-annual frameworks, but this has not happened until very recently. Thus the practises are still taking shape, and their impact can not yet be analysed.

Therefore, it can be argued that a strong finance minister has been necessary to complement the jointly negotiated targets. Consequently, those countries that have decided to invest their finance ministers with more fiscal powers should have enjoyed from better fiscal discipline. This expectation can be tested

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196 The differences of the means between the fiefdom and the rest (t-value 2.33, p=0.02), and between the fiefdom and the commitment countries (t-value 3.29, p=0.002) are statistically significant. Here, Romania is included in the fiefdom category for the earlier period.

197 One can also note high annual increases in the public expenditure-to GDP ratio (see table 16). International Monetary Fund's staff report for the 2003 article IV consultation cites significant expenditure increases on wages, pensions, health-related spending, social benefits and subsidies as the main reasons behind the increased deficit.

198 For example, Hallerberg, Strauch and von Hagen, 2004 form separate indices for commitment and delegation states. The index for commitment states emphasises the fiscal targets and the multi-annual frameworks (and the implementation stage of the budget process is not considered at all). The index for delegation states, in turn, describes the relative powers between the finance minister and spending ministers during decision-making and implementation stages of the budget process.

with the indices that describe the relationship between the finance minister and the spending ministers.[199]

Indices formed in previous sections cover different phases of the budget process measuring the strength of the institution in question: Finance minister index in the planning- and decision-making stage (*MFD*), Parliament index in the legislative stage (*PL*) and Finance minister index in the implementation stage (*MFI*). Regressions for the latter period also include an index (*PEP*) which measures the connection between the pre-accession economic programmes and annual budgets. All of the indices used in this chapter are calibrated so that the potential range of the indices runs from 0 to 8. An increase in an index-value means that the strength of the institution in question is strengthened, unless noted otherwise.[200]

The ordinary least squared regressions from a panel data set have the following basic form:

$$X_{it} = \beta_0 + \beta_1 X_{it-1} + \beta_2 MFD_{it} + \beta_3 PL_{it} + \beta_4 MFI_{it} + \beta_5 PEP_{it} + \beta_6 GDP_{it} + \beta_7 UNE_{it} + \varepsilon_{it}$$

where X denotes the dependent variable (the budget balance-to-GDP ratio or annual change in the public expenditure-to-GDP ratio, depending on a regression) in country i, β_0 is a common intercept for all pool members, X_{it-1} is a lagged dependent variable to correct autocorrelation[201], *GDP* is an annual real growth rate and *UNE* an unemployment rate in a country concerned, and they both are added to capture the effects of economic fluctuations. *MDF*, *PL*, *MFI* and *PEP* refer to different indices as explained above. Finally, ε refers to an error term. In the regressions below, the indices are entered in the regressions first together to test the combined effect and then separately to test their effect independently of each other. Control variables (*GDP* and *UNE*) are included in all regressions.

When budget balance is used as a dependent variable the expectation is that β_2, β_4 > 0 (a less de-centralised budget procedure should be conducive to stronger budget balance), β_3 < 0 (the theory expects that parliaments with powers to significantly alter the executives' budget proposal weaken the fiscal discipline), β_5 > 0 (better connection of the PEPs with the annual budget process should enhance fiscal performance), β_6 > 0 (economic growth should strengthen

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199 Another more practical reason for not forming separate indices for commitment and delegation states is simply that there would not be much variation especially in the commitment index. The coverage and degree of commitment of fiscal targets are rather uniform across countries and the multi-annual frameworks could not be considered due to lack of years. Further limitation comes from the fact that only one country is coded as delegation state for the latter period.

200 In the chapter 5, indices which described more generally parliament's informational and distributional attributes were also formed. These indices are not considered in this section as it is unlikely that these general attributes have noticeable fiscal impact in such a short period of time.

201 See Beck and Katz, 1996. Including a lagged dependent variable to address the problem of serial correlation is commonly used in similar studies (see Hallerberg et al, 1999, de Haan, Moessen and Volkerink, 1999 and Gleich, 2002).

the budget balance) and $\beta_7 < 0$ (higher unemployment should be conducive to weaker budget balance). When the annual change in public expenditure is as a dependent variable, the expected signs are the exact opposite to the ones just presented. In other words, a negative value of a correlation coefficient is associated with a decrease in public expenditure. This should be the case when the degree of centralisation of the budget process is increased.

TABLE 17 Ordinary least squares: 1995-1998

	dependent variable	
	budget balance	**Δ public expenditure**
constant	-1.40*	0.63
	(0.82)	(1.00)
lagged dep. var.	0.40*	-0.48*
	(0.20)	(0.27)
MFD	-0.15	-0.50*
	(0.18)	(0.25)
PL	-0.01	0.75**
	(0.32)	(0.36)
MFI	-0.03	-0.36*
	(0.14)	(0.18)
GDP	0.17	0.18
	(0.12)	(0.12)
UNE	-0.02	-0.17*
	(0.08)	(0.08)
R^2	0.40	0.30
N	40	40

	dependent variable					
	budget balance			**Δ public expenditure**		
	(1)	(2)	(3)	(1)	(2)	(3)
constant	-1.58*	-2.06**	-2.11***	0.95	-1.75	-0.10
	(0.87)	(0.96)	(0.74)	(1.09)	(1.29)	(0.10)
lagged dep. var.	0.40**	0.43**	0.43**	-0.36	-0.38	-0.39
	(0.19)	(0.18)	(0.18)	(0.23)	(0.26)	(0.29)
MFD	-0.13			-0.29		
	(0.21)			(0.27)		
PL		-0.02			0.54	
		(0.29)			(0.34)	
MFI			0.00			-0.15
			(0.14)			(0.20)
GDP	0.17	0.15	0.16	0.18	0.16	0.14
	(0.12)	(0.12)	(0.11)	(0.13)	(0.12)	(0.12)
UNE	-0.02	0.00	-0.00	-0.12	-0.15	-0.06
	(0.06)	(0.08)	(0.07)	(0.07)	(0.09)	(0.07)
R^2	0.40	0.40	0.40	0.18	0.19	0.17
N	40	40	40	40	40	40

Notes: Significance levels: < 0.01 = ***, 0.01-0.05 = **, 0.05-0.10 = *. White heteroskedasticity consistent standard errors in parentheses. Data on public finances from EBRD, 2000 and EBRD, 2003. Data on GDP and unemployment from EBRD, 2000, EBRD, 2003 and individual PEPs. MFD = Finance minister index (planning and decision-making stage), PL = Parliament index (legislative stage), MFI = Finance minister index (implementation stage), GDP = change in annual real GDP, UNE = unemployment rate

TABLE 18 Ordinary least squares: 1999-2002

	dependent variable budget balance
constant	-4.9** (2.17)
lagged dep. var.	0.43** (0.16)
MFD	0.45** (0.22)
PL	-0.30 (0.25)
MFI	0.77** (0.28)
GDP	0.54*** (0.11)
UNE	-0.07 (0.07)
R^2	0.63
N	40

	dependent variable budget balance			
	(1)	(2)	(3)	(4)
constant	-5.79*** (1.84)	-2.84 (1.69)	-3.51*** (1.29)	-5.08*** (1.84)
lagged dep. var.	0.54*** (0.17)	0.59*** (0.17)	0.55*** (0.18)	0.60*** (0.17)
MFD	0.46** (0.22)			
PL		-0.30 (0.27)		
MFI			0.30* (0.17)	
PEP				0.24 (0.23)
GDP	0.47*** (0.10)	0.51*** (0.11)	0.50*** (0.10)	0.49*** (0.10)
UNE	0.07 (0.08)	0.04 (0.08)	-0.09 (0.08)	0.05 (0.08)
R^2	0.59	0.57	0.58	0.57
N	40	40	40	40

Notes: Significance levels: < 0.01 = ***, 0.01-0.05 = **, 0.05-0.10 = *. White heteroskedasticity consistent standard errors in parentheses. Data on public finances from European Commission's statistical annex of European Economy (Autumn 2004). Data on GDP and unemployment from EBRD, 2000, EBRD, 2003 and individual PEPs. MFD = Finance minister index (planning and decision-making stage), PL = Parliament index (legislative stage), MFI = Finance minister index (implementation stage), PEP = Pre-accession programme index, GDP = change in annual real GDP, UNE = unemployment rate

Table 17 present the ordinary least squares for the first period. Overall, the results indicate that the indices can not explain the differences in the fiscal performance in the CEECs.[202] When budget balance is used as a dependent variable, correlation coefficients are not significant and close to zero. Coefficient for

[202] *PEP* is not included here as the pre-accession programmes were not drafted during this period.

MFD even has a wrong sign. When a narrower indicator Δ public expenditure is used as a dependent variable, the index coefficients have correct signs but the significance of the results is generally poor. When indices are included in the regression simultaneously, the index-coefficients do have statistical significance. Nevertheless, overall the evidence from the first period cannot be regarded as conclusive.

Table 18 presents results for the latter period. The results are different compared to the earlier period. The coefficients have correct signs and they are statistically significant. This excludes *PL*; its coefficient has a correct sign but statistical significance is poor.

The results in the lower part of table 18 are obtained by including the indices separately into the regressions. Here, the regressions also include *PEP*. Overall, the results no not change. All coefficients for the indices are statistically significant and they have a correct sign, excluding *PL* and *PEP* for which the coefficients do have a correct signs but the results lack statistical significance.[203]

Overall, these results lend support to the notion that countries with more centralised fiscal institutions have enjoyed from better fiscal discipline. In other words, it seems that strong finance ministers have enhanced fiscal rigour thus complementing the commitments imposed by jointly negotiated targets. Both planning- and decision-making and implementation stages have been important. These results apply to the latter period only as the evidence for the earlier period was inconclusive. Due to a small number of years and lack of extensive fiscal data, the results should be treated with caution. The index measuring Parliaments' influence did not produce unequivocal results. The same was the case with the index measuring the connection between the pre-accession economic programmes and annual budgets. In chapter 5 it was noted that the parliaments' in these countries do in fact possess formal distributive powers, such as powers to initiate legislation and to amend legislative bills, but that they do not use their formal powers to the full. One can speculate that this could be an explanation for the results.[204] Regarding the role of PEPs, it can be noted that PEPs are not designed to coordinate the fiscal policies of the CEECs; they are be subject to a more binding macroeconomic policy framework only as EU members. Therefore, the result for *PEP*-index is not perhaps a surprise.

The results in table 17 suggested that the indices could not explain the differences in the fiscal performance in the CEECs during the first part of the period. As explained in the first part of the chapter, this could be due to lack of

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203 The regressions in tables 18 were also performed using budget balance and Δ public expenditure from EBRD 2000 and 2003 as dependent variables (and including a lagged dependent variable). The results were mixed. In a simultaneous regression with budget balance as a dependent variable, only the coefficient for *MFI* (0.44) was weakly significant. *MFI* was the only index to have a weakly significant coefficient (0.45) also in the separate regressions. When Δ public expenditure was a dependent variable, *MFD* was the only index to have weakly significant coefficients both in the simultaneous (-0.68) and separate (-0.59) regressions.

204 On the other hand, using the institutional data from this study and the indices formed by using the coding rules from Hallerberg et al, 2001, also the coefficient for *PL* index is significant. See table 19 below.

data reliability and/or the transition process which had a significant impact on the behaviour of public finances in the CEECs. In any case, the results for the earlier period are in a striking contrast to the results in Gleich, 2002 which found that the fiscal institutions did have a significant effect on fiscal performance in the CEECs during 1994-1998.

Therefore, it is interesting to compare how well different indices fare when the latter period is analysed. This is done in table 19 which puts together the results from the lower part of table 18 (column A) with regression results obtained by using alternative indices as explanatory variables. The figures in column (B) have been obtained by using the institutional data from this study but the indices are formed by using the coding rules from Hallerberg et al, 2001. The coding rules used in this study do not differ substantially from Hallerberg et al, 2001 and therefore there should not be major differences between the results.[205] Finally, column (C) includes results obtained by using indices from Gleich, 2002.[206]

TABLE 19 Ordinary least squares: a comparison of different indices

	dependent variable budget balance								
	(A)			(B)			(C)		
	(1)	(2)	(3)	(1)	(2)	(3)	(1)	(2)	(3)
constant	-5.79***	-2.84	-3.51***	-5.76***	-2.93*	-3.51***	-3.52*	-3.51**	-5.56***
	(1.84)	(1.69)	(1.29)	(1.86)	(1.46)	(1.29)	(1.95)	(1.60)	(1.91)
lagged dep var	0.54***	0.59***	0.55***	0.56***	0.53***	0.55***	0.62***	0.62***	0.57***
	(0.17)	(0.17)	(0.18)	(0.17)	(0.16)	(0.18)	(0.17)	(0.17)	(0.16)
MFD	0.46**			0.42**			-0.01		
	(0.22)			(0.21)			(0.25)		
PL		-0.30			-0.46**			-0.01	
		(0.27)			(0.22)			(0.16)	
MFI			0.30*			0.30*			0.38
			(0.17)			(0.17)			(0.23)
GDP	0.47***	0.51***	0.50***	0.48***	0.49***	0.50***	0.48***	0.48***	0.44***
	(0.10)	(0.11)	(0.10)	(0.10)	(0.11)	(0.10)	(0.10)	(0.10)	(0.09)
UNE	0.07	0.04	-0.09	0.06	0.06	-0.09	0.03	0.03	0.01
	(0.08)	(0.08)	(0.08)	(0.08)	(0.08)	(0.08)	(0.08)	(0.08)	(0.08)
R^2	0.59	0.57	0.58	0.58	0.60	0.58	0.55	0.55	0.57
N	40	40	40	40	40	40	40	40	40

Notes: Significance levels: < 0.01 = ***, 0.01-0.05 = **, 0.05-0.10 = *. White heteroskedasticity consistent standard errors in parentheses. Data on public finances from European Commission's statistical annex of European Economy (Autumn 2004). Period: 1999-2002. Figures in (A) obtained by using indices and coding rules from this study, figures in (B) obtained by using indices formed based on institutional data from this study and coding rules from Hallerberg et al. 2001, figures in (C) obtained by using indices from Gleich, 2002. MFD = Finance minister index (planning and decision-making stage), PL = Parliament index (legislative stage), MFI = Finance minister index (implementation stage)

As expected, the results between (A) and (B) are very similar. The coefficient for *PL* has statistical significance in (B). Interestingly, none of the coefficients in (C)

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205 Note that the *MFI*-index is the same between (A) and (B).

206 Gleich's study did include index values also for the latter period but at the time there were not enough years to test them. Note also that in Gleich's study, increase in the *PL*-index means that the parliament's power relative to the government is decreased.

are statistically significant, and the coefficients for *MFD* and *PL* are almost zero. The coefficient for *MFI* has a correct sign.

The main difference between the indices formed in this study and the indices in Gleich, 2002 stems from the coding rules. In other words, many of the features of fiscal institutions used to form the index in this study have not been considered in Gleich's study (and vice versa). Some features of the fiscal institutions are included in the both set of indices but the information itself obtained in this study is, in some cases, different from Gleich, 2002. The results in table 19 suggest that a great deal of care should be exercised when this research strategy is adopted as the final outcomes are clearly sensitive to the way the indices are formed. This concern both the decision on what features of the fiscal institutions are the most relevant ones and should be thus included in the indices, but also the quality of the institutional data.[207] The analysis undoubtedly also suffers from lack of history and fiscal data. Only time will remedy this problem.

207 The institutional data in these types of studies are often for the most parts based on questionnaires filled by country authorities. The inherent difficulty with this approach is that it is difficult to verify the correctness of the replies (despite of the best efforts to do so: see section 5.1 of this paper).

7 CONCLUSIONS

The CEECs have been in transition from centrally planned to market economies. While the transition process has advanced considerably during the past decade, many challenges still remain, including reaching sustainable rates of GDP growth which will enable these countries to advance with real convergence for example vis-à-vis the EU-15 countries. This aspect highlights the role of fiscal management. The EU as well as the euro membership and related obligations also impose demands to the fiscal management, and economic policies more generally. However, the EU procedures do not define how member states should arrange their national fiscal institutions to meet these demands.

The purpose of the study is to argue that fiscal commitment has value over fiscal non-commitment, and then to study how the governments of the CEECs use the fiscal institutions to reach fiscal commitment and to improve fiscal discipline. Further, the study drew conclusions on how the underlying political fundamentals have affected the development of fiscal institutions, and finally how the differences in the frameworks have affected the fiscal performance in these countries.

The study began with a formulation of a simple closed-economy model where the monetary policy follows a Taylor-type rule while the government can, when conducting its fiscal policy, employ some type of commitment technology or alternatively fiscal policy is discretionary. Thus the set-up allowed a comparison between fiscal discretion and commitment when monetary policy is committed to a policy rule. The impulse responses from the model simulations show that generally speaking the shocks produce stronger initial response under the discretionary regime but under the fiscal commitment the effects of the shocks are more persistent. These results reflect the effect of the expectation-channel; under commitment-regime the policymaker knows that there is link between the private sector's expectations about its future policies and the current outcomes. In discretionary optimisation, in contrast, expectations play no role. Successful management of private sector's expectations is important because credible policy-commitment can steer private sector's expectations in a way which enhances policymaker's chances to reach its policy-objectives.

The model did not take explicit position on the type of commitment technology the government utilises. The rest of the study was concerned about how such fiscal commitments can be achieved using national fiscal institutions. The focus of the study stayed on the issues of fiscal commitment; how policymakers can enhance public understanding of their policies and indeed encourage themselves to act in a more disciplined way, but the emphasis in this literature was on the link between national fiscal institutions and fiscal discipline.

In order to perform this analysis, an extensive data set on the institutional details of the multi-annual fiscal frameworks and different phases of the budgetary processes employed by the CEECs was gathered and reviewed. Comparable data from earlier studies permitted comparisons between the CEECs and the EU-15. Finally, electoral and party systems in the CEECs, and in particular their role in countries' tendency to adopt a certain type of fiscal institution, was also discussed.

The theory has recognised two ideal ways to promote centralisation of the budget process, and consequently fiscal rigour: commitment via set of binding limits or targets on budget aggregates which are negotiated collectively at the beginning of a budgetary process, and delegation of significant fiscal powers to one player within the government, typically to a finance minister. The results in this paper confirm that practically all countries have taken steps to develop their national fiscal institutions, even if further challenges in many countries remain. In general, the governments in the CEECs use jointly negotiated agreements to commit themselves to fiscal targets, rather than delegation of significant fiscal powers to the finance minister. The commitment element in the planning and decision-making stage is therefore strong in the majority of the CEECs. The cabinet possesses a strong role in setting the targets, negotiating the budgets and resolving the emerging conflicts. The commitment element of the fiscal frameworks is also strengthened – albeit to a varying degree – by an introduction of multi-annual budgeting. Some of the important elements of the commitment approach are however lacking as these processes are still taking shape.

The fiscal targets used in these countries can be, in general, considered as 'weak'. In other words, the targets are based on political commitment and they serve as non-binding or indicative benchmark for budget-making process. The majority of countries do not discuss the deviations between the objectives laid out in the multi-annual plans and the actual outcome thus weakening the credibility of the multi-annual targets.

Regarding legislative stage, the countries also have sought to employ different ways to limit the parliamentary amendments, and as a result, the legislature's possibilities to alter the executive's budget proposal are, in general, limited. The theory expected that commitment states should have parliament committees with power to collect information so as to inform coalition partners from possible defections from jointly negotiated targets – or from aspirations to do so. The results above largely confirm that the committees in the CEECs possess these powers. Overall, the parliamentary committee systems in the CEECs are organised in a very similar fashion than in the Western Europe.

Final stage concerned the monitoring and implementation of the budget. All countries publish regularly public reports about the outcomes in public finances and also the parliaments are well informed. Also in the implementation stage, the government's role is generally strong as the finance minister in most countries has to seek the full cabinet's approval to carry out different measures. Finally, the CEECs do not typically have clear provisions in place on what should be done in times of economic under- or over-performance – a feature often given for "ideal" fiscal targets.

The comparison to the EU-15 countries suggested that the CEECs are lagging behind in some aspects. This concern especially the multi-annual frameworks where the practises in the CEECs are still taking shape. For example, the commitment states of the EU-15 have sought to strengthen the joint commitments by utilising the multi-annual plans and coalition agreements. As of yet, this practise has not taken hold among the CEECs.

The dominance of commitment approach was expected based on the review of the political fundamentals. Further, the evidence also suggested that political instability have effected adversely the development of fiscal institutions. This finding was also in line with the theoretical arguments. The study therefore indicates that the ways the fiscal institutions have evolved are not random. No direct causal relationship can be established, but the results suggest that the development of fiscal institutions in the CEECs has in general followed the expectations that stemmed from the review of the political fundamentals.

The statistical analysis suggests that countries with more centralised fiscal procedures have enjoyed better fiscal discipline. The evidence was the most solid regarding planning- and decision-making and implementation and monitoring stages. These results must be however interpreted with caution due to a short time-period and limitations in the fiscal data.

Looking forward, the theoretical considerations and the experience from the EU-15 indicate that strengthening the commitment-elements of the fiscal institutions, in particular multi-annual plans, provides a promising avenue for promoting fiscal discipline.[208] The experience of the commitment states of the EU-15 suggest that increasing the fiscal powers of finance ministers generates only limited value added.[209] This could be the case also in the majority of the CEECs once the commitment-elements have been strengthened to a sufficient degree.

The results also point to a more general lesson involving this line of research strategy. The formulation of different indices characterising institutional details of a country's fiscal management is a useful and illustrative way to describe fiscal procedures and making comparison across countries. However, results from a statistical analysis are sensitive to the way the indices are formed.

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208 Many fiscal challenges faced by the CEECs have a strong medium-term focus which also emphasise the importance of multi-annual fiscal plans.

209 Hallerberg et al, 2001 and 2004. However, this does not mean that finance minister's powers are without meaning in the commitment countries, where finance minister's role is important for example in enforcing the existing fiscal contract.

This concern both the decision on what features of the fiscal institutions are the most relevant ones and should be thus included in the indices, but also the quality of the institutional data. To be more confident about the conclusions, it is thus useful if a statistical analysis in such studies is accompanied with a more qualitative description about fiscal frameworks.

There is every reason to believe that the fiscal institutions will continue to evolve in the future, too. In the coming years we are likely to witness vigorous efforts by the CEECs to qualify for the single currency affecting further the behaviour of public finances. Further, as party and electoral systems are yet to be stabilised in some countries, fiscal institutions could also be affected in the process. The analysis performed in this study should thus be seen as a preliminary first step. Consequently, the research on the fiscal institutions in the CEECs remains a relevant topic for years to come.

YHTEENVETO (SUMMARY)

FINANSSIPOLITIIKAN KEHIKKOJEN KEHITTYMINEN JA TOIMINTA KESKI- JA ITÄ-EUROOPAN MAISSA

Tutkimus keskittyy Keski- ja Itä-Euroopan maissa (KIE-maat) käytössä oleviin finanssipolitiikan säännöstöihin ja kehikkoihin, joiden puitteissa kyseiset maat suunnittelevat ja toteuttavat finanssipolitiikkaansa. Tutkimuksen tavoitteena on osoittaa, että sääntöihin ja/tai tavoitteisiin perustuvalla finanssipolitiikalla on hyötyjä täysin harkinnanvaraiseen finanssipolitiikkaan verrattuna. Lisäksi tarkoituksena on tutkia, miten KIE-maat käyttävät kansallisia finanssipoltiikan instituutioita, miten poliittiset tekijät ovat vaikuttaneet niiden kehittymiseen ja mikä on eri toimijoiden suhteellinen rooli kyseisten maiden budjettiprosessissa. Lopuksi tarkastellaan ovatko kehikkojen väliset erot johtaneet myös käytännössä eroihin finanssipolitiikan kurinalaisuudessa. Katsaus perustuu laajaan KIE-maiden finanssipolitiikan instituutioista kerättyyn aineistoon. Aineisto on vertailukelpoista aikaisempien EU-15- maita käsitelleiden vastaavista teemoista tehtyjen tutkimusten kanssa, mikä myös mahdollistaa vertailun KIE- ja EU-15-maiden instituutioiden välillä.

Tutkimuksen alussa muodostetaan makromalli, jonka avulla vertaillaan sääntöihin ja/tai tavoitteisiin perustuvaa finassipolitiikkaa sekä täysin harkinnanvaraista finanssipolitiikkaa. Rahapolitiikka puolestaan perustuu keskuspankin noudattamaan ns. Taylor-periaatteeseen, jossa keskuspankki reagoi poikkeamiin inflaatiotavoitteesta ja potentiaalisesta tuotannosta. Työn tarjonta määräytyy endogeenisesti ja verotuksen vääristävät vaikutukset on otettu huomioon. Talouden kehitykseen vaikuttavat häiriöt julkisessa kulutuksessa ja tuottavuudessa. Tulokset mallisimuloinneista osoittavat, että sääntöön perustuvan finanssipolitiikan tapauksessa shokkien vaikutukset kestävät kauemmin, kun taas päätösperäisen finanssipolitiikan regiimissä talous palaa nopeasti tasapainoon. Tulos on identtinen optimaalista rahapolitiikkaa käsittelevän kirjallisuuden kanssa. Häiriöiden persistenssi heijastelee sitä, että hallitus ottaa yksityisen sektorin odotukset huomioon ja pyrkii vaikuttamaan niihin uskottavien sääntöjen avulla. Päätösperäinen optimointi olisi optimaalista vain siinä tapauksessa, jos talous kehittyisi mekanistisesti menneen kehityksen, eksogeenisten häiriöiden ja hallituksen nykyisen politiikan seurauksena. Heti kun yksityisen sektorin odotukset (jotka vaikuttavat tänään tehtävien politiikkapäätösten vaikutuksiin) otetaan huomioon, päätösperäinen optimointi ei tuota parasta tulosta. Tällöin on olennaista, että hallitus pyrkii uskottavilla säännöillä ja/tai tavoitteilla ohjaamaan yksityisen sektorin odotuksia.

Finanssipolitiikan instituutioiden roolia korostava kirjallisuus puolestaan perustuu nk. *common pool resource*-ongelmaan (jatkossa CPR-ongelma). CPR-ongelmaa käsittelevä kirjallisuus lähestyi aihetta alun perin kansanedustuslaitoksen toiminnan kautta. Kansanedustajat pyrkivät saamaan julkisia varoja oman vaalipiirinsä hyväksi, mutta kustannukset tulevat koko populaation mak-

settavaksi. Samaa ideaa on sittemmin sovellettu hallituksen toimintaan, jossa hallituksen eri ministerit pyrkivät lisäämään oman hallinnonalansa määrärahoja. Samalla ministerit yliarvioivat systemaattisesti suuremmasta julkisesta kulutuksesta koituvan nettorajahyödyn ja julkinen kulutus kasvaa yli sen tason, jolla sosiaaliset rajahyödyt ja –kustannukset olisivat yhtä suuret. Myöhemmät dynaamiset mallit ovat osoittaneet, että CPR-ongelma voi johtaa myös kasvaviin alijäämiin.

CPR-ongelmaa ja finanssipolitiikkaan liittyviä instituutiota korostava kirjallisuus pohtii miten finanssipolitiikan valmistelua, päätöksentekoa ja toteutumista ohjaavat käytännöt ja säännöstöt vaikuttavat itse finanssipolitiikkaan ja sen kurinalaisuuteen. Huomio siis keskittyy suurelta osin budjettiprosessiin, joka tässä kirjallisuudenhaarassa nähdään mekanismina, jonka puitteissa erilaiset poliittiset intressiryhmittymät pyrkivät saavuttamaan omaa ideologiaansa vastaavat tavoitteet. Jos siis halutaan parantaa esimerkiksi finanssipolitiikan kurinalaisuutta, on puututtava niihin säännöstöihin, joiden puitteissa finanssipolitiikkaa suunnitellaan ja toteutetaan.

Kaikille maille sopivia ”yhden koon” finanssipolitiikan säännöstöjä ei kuitenkaan ole olemassa, vaan säännöstöjen luomat kannustimet – ja sitä kautta niiden tehokkuus – riippuvat maan poliittisista tekijöistä. Vaikutus finanssipolitiikan instituutioiden valintaan on riippuvainen hallitusmuodosta: nk. *delegation*-lähestymistavassa finanssipoliittinen valta on keskitetty yhdelle hallituksen toimijalle, tyypillisesti valtiovarainministerille. Tämä on tehokas keino CPR-ongelman ratkaisemiseksi erityisesti maissa, joissa yksipuoluehallitukset ovat vallitsevia. Koalitiohallitusten yleisyys taas puoltaa hallituksen jäsenten yhteisesti sopimia tavoitteita (nk. *commitment*-lähestymistapa).

Jos maassa ei poliittisen epävakauden vuoksi ole tietty hallitustyyppi ollut hallitseva, kumpikaan finanssipolitiikan instituutio-tyyppi ei ole todennäköisesti saanut hallitsevaa asemaa eikä CPR-ongelmaa ole pyritty ratkaisemaan millään tavalla. Tällaista maata on kirjallisuudessa kutsuttu termillä *fiefdom*.

Jos siis halutaan tietää, mitkä finanssipolitiikan instituutioiden muodot olisivat jollekin maajoukolle yllä esitetyn teoriakehikon mukaan perusteltuja, tulee huomio kiinnittää maiden hallitustyyppeihin. Maan hallitustyyppi taas määräytyy politiikan teorioiden mukaan maan käytössä olevan vaalijärjestelmän sekä maan yhteiskunnallisen rakenteen (engl. cleavage structure) perusteella: Suhteellinen vaalitapa johtaa enemmistövaalitapoja todennäköisemmin koalitiohallituksiin. Mitä monitahoisempi yhteiskunnan rakenne taas maassa on, sitä enemmän muodostuu puolueita, jotka pyrkivät hyödyntämään kyseisiä eroavaisuuksia.

KIE-maiden ylivoimaiden enemmistö käyttää suhteellista vaalitapaa, joskin vaalijärjestelmien suhteellisuuden asteissa on eroja. KIE-maiden poliittisia tekijöitä käsittelevien tutkimusten perusteella voidaan todeta, että maat ovat yhteiskunnalliselta rakenteiltaan ”monitahoisia”. Tätä ovat omalta osaltaan edistäneet suuret yhteiskunnalliset muutokset. Suurimmassa osassa maita koalitiohallitukset ovatkin olleet yleisiä ja siksi odotus on, että *commitment*-lähestymistapa on KIE-maissa hallitseva. Yhteiskunnallisista muutoksista ja vaalijärjestelmiin tehdyistä jatkuvista uudistuksista johtuen on tuskin yllätys, että useat maat ovat olleet poliittisesti verraten epävakaita. Vaihtelu eri hallitusmuotojen välillä on ollut erityisen suurta Bulgariassa, Tšekissä, Liettuassa, Puolassa ja Romaniassa. Teoriakehikon perusteella on syytä olettaa näiden maiden olleen nk. *fiefdom*-maita ainakin 1990-luvulla, jolloin poliittinen epävakaus oli suurinta. Poikkeuksen muihin KIE-maihin muodostaa Unkari, jossa on muita kaksinapaisempi poliittinen kenttä. Tämän tulisi muodostaa suotuisat olosuhteet *delegation*-lähestymistavalle.

Tutkimuksessa esitetyn aineiston mukaan käytännössä kaikki KIE-maat ovat vahvistaneet finanssipolitiikan säännöstöjään ja käytäntöjään, olkoonkin, että työ on vielä kesken. Tutkimuksessa kerättyä aineistoa on käytetty finanssipolitiikan instituutioita kuvaavien indeksien muodostamiseksi, joita on puolestaan käytetty selittävinä muuttujina regressio-analyysissä. Vuosien 1995-1999 osalta analyysiä haittaavat epäluotettavat julkisen talouden tunnusluvut ja/tai taloudellinen siirtymäprosessi ja sen vaikutukset julkisen talouden käyttäytymiseen. Tälle periodille tehtyjen laskelmien mukaan finanssipolitiikan instituutioiden eroilla ei ollut vaikutusta julkisen talouden käyttäytymiseen. Sen sijaan myöhempien vuosien (1999-2002) osalta tulokset antavat tukea väitteelle, jonka mukaan budjettiprosessin keskittymistä lisäävät elementit edistävät kurinalaista finanssipolitiikkaa. Erityisesti budjetin suunnittelu- ja päätöksenteko- sekä toimeenpanovaiheilla on ollut merkitystä budjettikurin kannalta. Poliittisesti muita epävakaammilla mailla on ollut yleisesti ottaen heikot finanssipoliittiset instituutiot. Unkarin, jossa todettiin olevan muita KIE-maita kaksinapaisempi poliittinen kenttä, finanssipolitiikan instituutioilla on puolestaan piirteitä *delegation*-lähestymistavasta. Kuten odotettua, suurin osa KIE-maista turvautuu *commitment*-lähestymistapaan. Tämänkaltainen tutkimus ei voi todistaa suoraa syy-seuraus suhdetta, mutta tutkimus antaa tukea väitteelle, jonka mukaan poliittisia tekijöitä ei ole syytä ylenkatsoa tarkasteltaessa finanssipolitiikan valmisteluun ja toteuttamiseen liittyviä säännöstöjä ja käytäntöjä.

Tilastollinen analyysi antoi siis viitteitä siitä, että ”vahvemmat” tai ”keskitetymmät” finanssipolitiikan instituutiot ovat myös käytännössä edistäneet kurinalaista finanssipolitiikkaa. Teoreettisten näkökohtien ja EU-15 maista saadun kokemuksen perusteella voidaan todeta, että nk. *commitment*-elementtien, erityisesti keskipitkän aikavälin budjettikehikkojen, edelleenkehittäminen on suositeltavaa KIE-maissa. Keskipitkän aikavälin suunnittelua korostaa myös se seikka, että KIE-maiden julkisen talouden haasteilla on voimakas keskipitkän aikavälin fokus. EU-15 maita koskevan tutkimuksen mukaan valtiovarainministerin finanssipoliittisen vallan lisääminen *commitment*-maissa ei ole useimmissa tapauksissa realistista ja se tuo finanssikuria edistävässä mielessä vain vähän lisäarvoa. Tämä ei kuitenkaan tarkoita sitä, ettei valtiovarainministerin valtaoikeuksilla olisi *commitment*-maissa merkitystä; valtiovarainministerillä tulee mm. olla mahdollisuus varmistaa, että asetettuja tavoitteita noudatetaan. Hallituksen yhteisesti sopimat finanssipolitiikkaa koskevat pitävät ja uskottavat tavoitteet ovat julkisen talouden kurinalaisuuden ja kestävyyden edistämisen kannalta tehokkaampi keino.

KIE-maiden finanssipolitiikan instituutiot tulevat kehittymään jatkossa edelleen. EU:n ja euroalueen jäsenyydet tulevat vaikuttamaan tähän omalta osaltaan. Lisäksi useiden maiden puolue- ja vaalijärjestelmät eivät ole vielä vakiintuneet. Tästä usein seuraava poliittinen epävakaus voi vaikuttaa myös finanssipoliittisten instituutioiden kehittymiseen. Siksi KIE-maiden finanssipolitiikan instituutioita koskeva tutkimus tulee säilymään relevanttina aiheena vielä pitkään.

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ANNEXES

Annex 1 Full forms of equations (62), (63), (73) and (74), written as deviations from the steady state.

$$
\hat{c}_t^C = \frac{\begin{array}{l}
\left[\frac{\bar{l}^{\theta+1}\bar{g}(\sigma+\theta)}{(\bar{c}+\bar{g})^2} - \gamma(1-\gamma-\sigma(1-\gamma))\bar{c}^{\gamma(1-\sigma)-1}\bar{g}^{1-\gamma-\sigma(1-\gamma)}\left((1-\sigma)+\frac{(\gamma(1-\sigma)-1)(\bar{m}+\bar{b})}{\bar{c}}-1\right)\right]\hat{g}_t - \left[\frac{(\theta+1)\bar{l}^{\theta+1}(\sigma+\theta)}{\bar{c}+\bar{g}} - \frac{(\gamma(1-\sigma)-1)(\theta+1)\bar{l}^{\theta+1}}{\bar{c}}\right]\hat{l}_t \\
-\gamma(\gamma(1-\sigma)-1)\bar{c}^{\gamma(1-\sigma)-2}\bar{g}^{1-\gamma-\sigma(1-\gamma)}\left(\bar{m}\hat{m}_t+\bar{b}\hat{b}_t\right) + \frac{\gamma(\gamma(1-\sigma)-1)^2\bar{c}^{\gamma(1-\sigma)-2}\bar{g}^{1-\gamma-\sigma(1-\gamma)}\left(\bar{m}+\bar{b}\right)}{\delta_G}\hat{c}_{t-1} + \frac{\gamma(\gamma(1-\sigma)-1)(1-\gamma-\sigma(1-\gamma))\bar{c}^{\gamma(1-\sigma)-2}\bar{g}^{1-\gamma-\sigma(1-\gamma)}\left(\bar{m}+\bar{b}\right)}{\delta_G}\hat{g}_{t-1} \\
-\frac{(\gamma(1-\sigma)-1)\bar{c}^{-1}\bar{m}}{\delta_G}\left((1-\sigma)\Gamma\bar{m}^{-\sigma} - \gamma\bar{c}^{\gamma(1-\sigma)-1}\bar{g}^{1-\gamma-\sigma(1-\gamma)}\right)\hat{m}_{t-1} + \frac{\gamma(\gamma(1-\sigma)-1)\bar{c}^{\gamma(1-\sigma)-2}\bar{g}^{1-\gamma-\sigma(1-\gamma)}\bar{b}}{\delta_G}\hat{b}_{t-1}
\end{array}}{\gamma(\gamma(1-\sigma)-1)\bar{c}^{\gamma(1-\sigma)-1}\bar{g}^{1-\gamma-\sigma(1-\gamma)}\left((1-\sigma)+\frac{\bar{m}+\bar{b}}{\delta\bar{c}}+\frac{(\gamma(1-\sigma)-2)(\bar{m}+\bar{b})}{\bar{c}}-1\right)+\frac{(\gamma(1-\sigma)-1)}{\bar{c}}\left(\bar{l}^{\theta+1}-\frac{\Gamma\bar{m}^{1-\sigma}}{\delta}\right)-\frac{\bar{l}^{\theta+1}\bar{c}(\sigma+\theta)}{(\bar{c}+\bar{g})^2}}
\tag{62}
$$

$$
\hat{l}_t^C = \frac{\begin{array}{l}
\left[\begin{array}{l}
\frac{1}{\bar{l}}\bar{c}^{\gamma(1-\sigma)}\bar{g}^{1-\gamma-\sigma(1-\gamma)}\sigma\gamma\left(\gamma(1-\sigma)+\frac{\bar{g}}{\bar{c}}(\gamma(1-\sigma)-1)\right)-\frac{1}{\bar{l}}\gamma(\gamma(1-\sigma)-1)\bar{c}^{\gamma(1-\sigma)-1}\bar{g}^{1-\gamma-\sigma(1-\gamma)}(\bar{m}+\bar{b})\left((\gamma(1-\sigma)-1)+\frac{\bar{g}}{\bar{c}}(\gamma(1-\sigma)-2)+\frac{\bar{g}}{\bar{c}\delta_G}\right) \\
+\frac{\bar{g}}{\bar{c}\bar{l}\delta_G}(\gamma(1-\sigma)-1)\Gamma\bar{m}^{1-\sigma}-\frac{\bar{g}}{\bar{c}}(\gamma(1-\sigma)-1)\bar{l}^{\theta}
\end{array}\right]\hat{c}_t \\
+\left[\begin{array}{l}
\frac{1}{\bar{l}}\bar{c}^{\gamma(1-\sigma)}\bar{g}^{1-\gamma-\sigma(1-\gamma)}\sigma\gamma\left((1-\gamma-\sigma(1-\gamma))+\frac{\bar{g}}{\bar{c}}(2-\gamma-\sigma(1-\gamma))\right)-\frac{1}{\bar{l}}\gamma(\gamma(1-\sigma)-1)\bar{c}^{\gamma(1-\sigma)-1}\bar{g}^{1-\gamma-\sigma(1-\gamma)}(\bar{m}+\bar{b})\left((1-\gamma-\sigma(1-\gamma))+\frac{\bar{g}}{\bar{c}}(2-\gamma-\sigma(1-\gamma))-\frac{\bar{g}}{\bar{c}\delta}\right) \\
-\frac{\bar{g}}{\bar{c}\bar{l}\delta_G}(\gamma(1-\sigma)-1)\Gamma\bar{m}^{1-\sigma}+\frac{\bar{g}}{\bar{c}}(\gamma(1-\sigma)-1)\bar{l}^{\theta}
\end{array}\right]\hat{g}_t \\
-\left[\frac{1}{\bar{l}}\gamma(\gamma(1-\sigma)-1)\bar{c}^{\gamma(1-\sigma)-1}\bar{g}^{1-\gamma-\sigma(1-\gamma)}\left(1+\frac{\bar{g}}{\bar{c}}\right)\right](\bar{m}\hat{m}_t+\bar{b}\hat{b}_t)+\frac{1}{\bar{l}\delta_G}\gamma(\gamma(1-\sigma)-1)^2\bar{c}^{\gamma(1-\sigma)-1}\bar{g}^{1-\gamma-\sigma(1-\gamma)}(\bar{m}+\bar{b})\left(1+\frac{\bar{g}}{\bar{c}}\right)\hat{c}_{t-1} \\
+\frac{1}{\bar{l}\delta_G}\gamma(\gamma(1-\sigma)-1)(1-\gamma-\sigma(1-\gamma))\bar{c}^{\gamma(1-\sigma)-1}\bar{g}^{1-\gamma-\sigma(1-\gamma)}(\bar{m}+\bar{b})\left(1+\frac{\bar{g}}{\bar{c}}\right)\hat{g}_{t-1} \\
-\left[\frac{1}{\bar{l}\delta_G}(\gamma(1-\sigma)-1)\bar{m}\left(1+\frac{\bar{g}}{\bar{c}}\right)\left((1-\sigma)\Gamma\bar{m}^{-\sigma}-\gamma\bar{c}^{\gamma(1-\sigma)-1}\bar{g}^{1-\gamma-\sigma(1-\gamma)}\right)\right]\hat{m}_{t-1}+\frac{1}{\bar{l}\delta_G}\gamma(\gamma(1-\sigma)-1)\bar{c}^{\gamma(1-\sigma)-1}\bar{g}^{1-\gamma-\sigma(1-\gamma)}\bar{b}\left(1+\frac{\bar{g}}{\bar{c}}\right)\hat{b}_{t-1}
\end{array}}{\begin{array}{c}
\bar{l}^{\theta}\theta(\theta+\sigma)-\frac{\Gamma\bar{m}^{1-\sigma}}{\bar{l}\delta_G}(\gamma(1-\sigma)-1)\left(\frac{\bar{g}}{\bar{c}}+1\right)+\frac{1}{\bar{l}}\bar{c}^{\gamma(1-\sigma)}\bar{g}^{1-\gamma-\sigma(1-\gamma)}\sigma\gamma\left(1+\frac{\bar{g}}{\bar{c}}\right) \\
+\frac{1}{\bar{l}}\gamma(\gamma(1-\sigma)-1)\bar{c}^{\gamma(1-\sigma)-1}\bar{g}^{1-\gamma-\sigma(1-\gamma)}(\bar{m}+\bar{b})\left(\frac{\bar{g}}{\bar{c}}\left(\frac{1}{\delta_G}-1\right)+\frac{1}{\delta_G}-1\right)-\bar{l}^{\theta}\theta(\gamma(1-\sigma)-1)\left(1+\frac{\bar{g}}{\bar{c}}\right)
\end{array}}
$$

(63)

$$
\hat{c}_t^D = \frac{\begin{array}{l}
\left[\begin{array}{l}
\dfrac{\bar{l}^{\theta+1}(\theta+1)\bar{c}^{\gamma(\sigma-1)+1}\bar{g}^{\gamma+\sigma(1-\gamma)}}{(\bar{c}+\bar{g})^2\gamma}\left(\dfrac{\bar{c}}{\bar{g}}(1-\gamma-\sigma(1-\gamma))+(2-\gamma-\sigma(1-\gamma))\right)-\dfrac{(\gamma(1-\sigma)-1)(1-\gamma-\sigma(1-\gamma))\bar{c}^{\gamma(\sigma-1)}\bar{g}^{-1+\gamma+\sigma(1-\gamma)}}{\gamma}\left(\bar{l}^{\theta+1}-\dfrac{\Gamma\bar{m}^{1-\sigma}}{\delta}\right) \\
-\dfrac{\gamma(1-\gamma-\sigma(1-\gamma))}{\Gamma\bar{m}^{-\sigma}}\bar{c}^{\gamma(1-\sigma)-1}\bar{g}^{1-\gamma-\sigma(1-\gamma)} \\
-\dfrac{\bar{l}^{\theta+1}\bar{g}}{\Gamma\bar{m}^{-\sigma}(\bar{c}+\bar{g})^2}-\dfrac{(\gamma(1-\sigma)-1)(1-\gamma-\sigma(1-\gamma))}{\delta_G}\left(\dfrac{\bar{m}+\bar{b}}{\bar{c}}\right)
\end{array}\right]\hat{g}_t \\
-\left[\begin{array}{l}
\dfrac{(\gamma(1-\sigma)-1)\sigma\bar{c}^{\gamma(\sigma-1)}\bar{g}^{-1+\gamma+\sigma(1-\gamma)}}{\gamma}\left(\bar{l}^{\theta+1}-\dfrac{\Gamma\bar{m}^{1-\sigma}}{\delta_G}\right)+\sigma-\dfrac{\bar{l}^{\theta+1}(\theta+1)\sigma\bar{c}^{\gamma(\sigma-1)+1}\bar{g}^{-1+\gamma+\sigma(1-\gamma)}}{(\bar{c}+\bar{g})\gamma} \\
+\dfrac{(\gamma(1-\sigma)-1)\sigma}{\delta_G}\left(\dfrac{\bar{m}+\bar{b}}{\bar{c}}\right)
\end{array}\right]\hat{m}_t \\
-\left[\dfrac{\bar{l}^{\theta+1}(\theta+1)\bar{c}^{\gamma(\sigma-1)}\bar{g}^{-1+\gamma+\sigma(1-\gamma)}}{\gamma}\left(\dfrac{(\theta+1)\bar{c}}{\bar{c}+\bar{g}}-(\gamma(1-\sigma)-1)\right)-\dfrac{\bar{l}^{\theta+1}(\theta+1)}{\Gamma\bar{m}^{-\sigma}(\bar{c}+\bar{g})}\right]\hat{l}_t+\left[\dfrac{(\gamma(1-\sigma)-1)^2}{\delta_G}\left(\dfrac{\bar{m}+\bar{b}}{\bar{c}}\right)\right]\hat{c}_{t-1} \\
+\left[\dfrac{(\gamma(1-\sigma)-1)(1-\gamma-\sigma(1-\gamma))}{\delta_G}\left(\dfrac{\bar{m}+\bar{b}}{\bar{c}}\right)\right]\hat{g}_{t-1}-\dfrac{\bar{m}(\gamma(1-\sigma)-1)}{\delta_G}\left[\dfrac{\Gamma\bar{m}^{-\sigma}(1-\sigma)\bar{c}^{\gamma(\sigma-1)}\bar{g}^{-1+\gamma+\sigma(1-\gamma)}}{\gamma}-\dfrac{1}{\bar{c}}\right]\hat{m}_{t-1}+\dfrac{(\gamma(1-\sigma)-1)}{\delta_G}\dfrac{\bar{b}}{\bar{c}}\hat{b}_{t-1}
\end{array}}{\begin{array}{l}
(\gamma(1-\sigma)-1)(1-\sigma)\bar{c}^{\gamma(\sigma-1)}\bar{g}^{-1+\gamma+\sigma(1-\gamma)}\left(\bar{l}^{\theta+1}-\dfrac{\Gamma\bar{m}^{1-\sigma}}{\delta_G}\right)+\dfrac{\gamma(\gamma(1-\sigma)-1)}{\Gamma\bar{m}^{-\sigma}}\bar{c}^{\gamma(1-\sigma)-1}\bar{g}^{1-\gamma-\sigma(1-\gamma)} \\
+\dfrac{\bar{l}^{\theta+1}\bar{c}}{\Gamma\bar{m}^{-\sigma}(\bar{c}+\bar{g})^2}+\dfrac{(\gamma(1-\sigma)-1)(\gamma(1-\sigma))}{\delta_G}\left(\dfrac{\bar{m}+\bar{b}}{\bar{c}}\right)-\dfrac{\bar{l}^{\theta+1}(\theta+1)\bar{c}^{\gamma(\sigma-1)+1}\bar{g}^{\gamma+\sigma(1-\gamma)}}{(\bar{c}+\bar{g})^2\gamma}\left(\gamma(1-\sigma)\dfrac{\bar{c}}{\bar{g}}+(\gamma(1-\sigma)-1)\right)
\end{array}}
\tag{73}
$$

$$
\hat{l}_t^D = \frac{
\begin{array}{l}
\left[\begin{array}{l}
-\dfrac{\left(\gamma(1-\sigma)-1\right)}{\delta_G}\left[\begin{array}{l}
\bar{c}^{\gamma(\sigma-1)}\bar{g}^{\gamma+\sigma(1-\gamma)}\left[\left(\dfrac{\bar{c}}{\bar{g}\gamma}\left(\gamma(\sigma-1)+1\right)+(\sigma-1)\right)\left(\dfrac{\Gamma\bar{m}^{1-\sigma}}{\bar{l}}-\bar{l}^{\theta}\right)\right] \\
-\left[\left(\left(\gamma(\sigma-1)+1\right)+\dfrac{\bar{g}}{\bar{c}}\left(\gamma(\sigma-1)\right)\right)\dfrac{\bar{m}+\bar{b}}{\bar{l}}\right]
\end{array}\right]+\dfrac{\bar{l}^{\theta}\bar{c}^{\gamma(\sigma-1)+1}\bar{g}^{-1+\gamma+\sigma(1-\gamma)}\left(\gamma(1-\sigma)-1\right)}{\gamma}(\theta+1) \\
-\dfrac{\bar{c}^{\gamma(1-\sigma)}\bar{g}^{1-\gamma-\sigma(1-\gamma)}}{\Gamma\bar{m}^{-\sigma}\bar{l}}\gamma\left(\left(\gamma(1-\sigma)\right)+\dfrac{\bar{g}}{\bar{c}}\left(\gamma(1-\sigma)-1\right)\right)-\dfrac{\bar{c}}{\bar{l}}
\end{array}\right]\hat{c}_t \\
-\left[\begin{array}{l}
\dfrac{\left(\gamma(1-\sigma)-1\right)}{\delta_G}\left[\begin{array}{l}
\dfrac{\bar{c}^{\gamma(\sigma-1)}\bar{g}^{\gamma+\sigma(1-\gamma)}}{\gamma}\left[\left(\dfrac{\bar{c}}{\bar{g}}\left(-1+\gamma+\sigma(1-\gamma)\right)+\left(\gamma+\sigma(1-\gamma)\right)\right)\left(\dfrac{\Gamma\bar{m}^{1-\sigma}}{\bar{l}}-\bar{l}^{\theta}\right)\right] \\
-\left[\left(\left(-1+\gamma+\sigma(1-\gamma)\right)+\dfrac{\bar{g}}{\bar{c}}\left(\gamma+\sigma(1-\gamma)\right)\right)\dfrac{\bar{m}+\bar{b}}{\bar{l}}\right]
\end{array}\right]-\dfrac{\bar{l}^{\theta}\bar{c}^{\gamma(\sigma-1)+1}\bar{g}^{-1+\gamma+\sigma(1-\gamma)}\left(1-\gamma-\sigma(1-\gamma)\right)}{\gamma}(\theta+1) \\
+\dfrac{\bar{c}^{\gamma(1-\sigma)}\bar{g}^{1-\gamma-\sigma(1-\gamma)}}{\Gamma\bar{m}^{-\sigma}\bar{l}}\gamma\left(\left(1-\gamma-\sigma(1-\gamma)\right)+\dfrac{\bar{g}}{\bar{c}}\left(2-\gamma-\sigma(1-\gamma)\right)\right)-\dfrac{\bar{g}}{\bar{l}}
\end{array}\right]\hat{g}_t \\
-\left[\dfrac{\left(\gamma(1-\sigma)-1\right)\sigma}{\delta_G}\left[\begin{array}{l}
\dfrac{\bar{c}^{\gamma(\sigma-1)}\bar{g}^{\gamma+\sigma(1-\gamma)}}{\gamma}\left[\left(1+\dfrac{\bar{c}}{\bar{g}}\right)\left(\bar{l}^{\theta}-\dfrac{\Gamma\bar{m}^{1-\sigma}}{\bar{l}}\right)\right] \\
+\left[\left(1+\dfrac{\bar{g}}{\bar{c}}\right)\dfrac{\bar{m}+\bar{b}}{\bar{l}}\right]
\end{array}\right]-\dfrac{\bar{l}^{\theta}\bar{c}^{\gamma(\sigma-1)+1}\bar{g}^{-1+\gamma+\sigma(1-\gamma)}\sigma}{\gamma}(\theta+1)+\dfrac{\sigma}{\bar{l}}\left(\bar{c}+\bar{g}\right)\right]\hat{m}_t \\
+\dfrac{\left(\gamma(1-\sigma)-1\right)^2}{\delta_G}\left[\left(1+\dfrac{\bar{g}}{\bar{c}}\right)\dfrac{\bar{m}+\bar{b}}{\bar{l}}\right]\hat{c}_{t-1}+\dfrac{\left(\gamma(1-\sigma)-1\right)\left(1-\gamma-\sigma(1-\gamma)\right)}{\delta_G}\left[\left(1+\dfrac{\bar{g}}{\bar{c}}\right)\dfrac{\bar{m}+\bar{b}}{\bar{l}}\right]\hat{g}_{t-1} \\
-\left[\dfrac{\Gamma\bar{m}^{1-\sigma}\left(\gamma(1-\sigma)-1\right)\bar{c}^{\gamma(\sigma-1)}\bar{g}^{\gamma+\sigma(1-\gamma)}(1-\sigma)}{\gamma\delta_G\bar{l}}\left(1+\dfrac{\bar{c}}{\bar{g}}\right)-\dfrac{\bar{m}\left(\gamma(1-\sigma)-1\right)}{\delta_G\bar{l}}\left(1+\dfrac{\bar{g}}{\bar{c}}\right)\right]\hat{m}_{t-1}+\dfrac{\left(\gamma(1-\sigma)-1\right)\bar{b}}{\delta_G\bar{l}}\left(1+\dfrac{\bar{g}}{\bar{c}}\right)\hat{b}_{t-1}
\end{array}
}{
\dfrac{\bar{l}^{\theta}\theta\bar{c}^{\gamma(\sigma-1)+1}\bar{g}^{-1+\gamma+\sigma(1-\gamma)}}{\gamma}(\theta+1)-\dfrac{\left(\gamma(1-\sigma)-1\right)}{\delta_G}\left[\begin{array}{l}
\dfrac{\bar{c}^{\gamma(\sigma-1)}\bar{g}^{\gamma+\sigma(1-\gamma)}}{\gamma}\left[\left(1+\dfrac{\bar{c}}{\bar{g}}\right)\left(\dfrac{\Gamma\bar{m}^{1-\sigma}}{\bar{l}}+\theta\bar{l}^{\theta}\right)\right] \\
-\left[\left(1+\dfrac{\bar{g}}{\bar{c}}\right)\dfrac{\bar{m}+\bar{b}}{\bar{l}}\right]
\end{array}\right]-\dfrac{\bar{c}^{\gamma(1-\sigma)}\bar{g}^{1-\gamma-\sigma(1-\gamma)}}{\Gamma\bar{m}^{-\sigma}\bar{l}}\gamma\left(1+\dfrac{\bar{g}}{\bar{c}}\right)+\dfrac{1}{\bar{l}}\left(\bar{c}+\bar{g}\right)-\dfrac{\bar{l}^{\theta}}{\Gamma\bar{m}^{-\sigma}}
}
\tag{74}
$$

Annex 2 Notes for tables 3, 4 and 5

TABLE 3 Comparison of electoral systems in the CEECs

Following Lijphart, 1994, an electoral system is defined as a set of essentially unchanged rules under which one or more successive elections are conducted. New electoral system is defined if new electoral formula is being employed, or if there is 20 % or greater change in district magnitude or assembly size. Lijphart defines new system also if there is a change in legal threshold. In this table this criterion is omitted (minor changes in legal thresholds have been common in the CEECs, and three countries (Poland, Romania and Slovenia) have experienced a 20 % or more increase in legal threshold during the period examined). If a figure is expressed as integer, it refers to exact number, not to average. The table does not make a distinction between electoral alliances and more uniform parties. Thus electoral alliances are as a rule treated as a single party.

[1] Czech Republic has modified also its election system for -92, -96 and -02 elections. The modifications had to do with the way the preferential votes (ie. multiple votes) were calculated. In all of the elections the mandates have been distributed among candidates nominated by the political parties in the order of priority of the list of candidates, but the preferred votes can disturb the list. For -92 elections, the mandate in the first turn is given to that candidate who gained more than half of the votes of those voters, who used their rights of preferential election of candidates. For -96 elections, the candidate who received the number of preferential votes which equals or exceeds ten per cent of the total vote obtained in the electoral region by the political party or coalition the candidate represents shall be awarded a seat first. Finally, for -02 elections candidates who receive a number of preference votes which is at least 7% of valid votes for their party have priority in obtaining a mandate. Therefore, while the system has been ‘open list’ during the whole period, the ‘openness’ of the election system has increased as a result of these successive reforms.

[2] For 1992 elections, the number of districts was 12, and for successive elections 11.

[3] Lithuania has employed mixed 2-tier system the entire period but has introduced some reforms. In 1992 elections, “in a single-candidate electoral area, the voters shall mark the surname of the candidate for whom they are voting, whereas in a multi-candidate electoral area, the voters shall mark the name of the political party or social political movement (coalition) for whose candidates they are voting for” (see article 57 (1) of the 1992 election law). For 1996 elections, preference voting was introduced. Article 65(3) of the 1996 electoral law states: “On a ballot paper of a multi-candidate electoral area the voter may make appropriate marks in the table of candidates' rating - to express a positive or negative opinion about the candidate (candidates) included in the list of candidates whom he has voted for - to cross out the surname of the candidate or the number of the candidate on the list, and this shall mean voting for the estab-

lishment of a different sequence of candidates on this list." For 2000 elections, the law was modified further. This reform had to do with the establishment of the results in single-member districts. In 1996 elections, a candidate was considered elected when more than half of the voters participating in the elections vote for him/her in the elections. If more than two candidates were standing for election in the electoral area and none of them received the required amount of votes, a repeat voting was organised between the two candidates who received the most votes in the first voting (see article 87 (3) and (4) of the 1996 election law). In 2000 elections, a candidate is elected when the majority of voters participating in the elections vote for him/her (see art 88 (3) of the 2000 election law). Further, the number of preferred votes was reduced to five.

[4] In 1991 elections there was a 5 % threshold for national list or winning seats in at least 5 constituencies (no threshold for districts). For 1993 and 1997 elections, the thresholds were the following: 7% for national list, 5% nationwide for districts and 8% for coalitions. Finally, for 2001 elections, the national list was abolished, and the 5 % nationwide threshold for districts was implemented.

[5] For 1990 elections, assembly size was 391 and number of districts was 41. For the 1992 and 1996 elections the assembly size was 341 with 42 districts. For 2000 elections, the assembly size was 345, including 18 awarded seats to national minorities, up from 15 seats in 1992 and 1996. In 1990 elections, Romania did not have legal thresholds, but for 1992 elections 3 % national threshold (higher for coalitions) was introduced. For 1996, and successive, elections Romania employed 5 % national threshold (higher for coalitions).

[6] Slovenian electoral law establishes two single-member districts for Hungarian and Italian minorities. Legal threshold was introduced for 2000 elections, before that no legal threshold was applied.

Election system: PR=proportional representation, mv= multiple votes, voters can express preferences for some candidates over others, closed list= the order of candidates elected by that list is fixed by the party itself, and voters express preference for a party, not for a particular candidate, open list= voters can express preference for their favoured candidate.

Sources:

- electoral laws of the CEECs (several years),
- Inter-Parliamentary Union's Parline database (www.ipu.org),
- Berglund, Hellén, Aarebrot (Eds.), 1998.

Assembly size: Source: Inter-Parliamentary Union's Parline database (www.ipu.org)

District magnitude: Own calculations. Calculated by taking an average of district magnitudes. District magnitude refers to average number of MPs elected from district. Source: see 'Election system'.

Effective number of parliamentary parties: Own calculations. Calculated according to $N = 1/\sum s_i^2$, where N = effective number of parties in parliament and s_i = proportion of seats party i posses in the assembly (measure constructed by Laakso and Taagepera and presented in Lijphart, 1994, 68).

Sources:

- University of Essex's Project on Political Transformation and the Electoral Process in Post-Communist Europe (www.essex.ac.uk/elections/),
- Rose, Munro and Mackie, 1998,
- Centre For The Study Of Public Policy Database (www.cspp.strath.ac.uk/),
- Berglund, Hellén, Aarebrot (Eds.), 1998,
- contributions in several issues of European Journal of Political Research: 26, December, 1994; 28, December, 1995; 30, December, 1996; 32, December, 1997; 34, December, 1998; 36 December, 1999; 38, December, 2000.

Legal national threshold: Refers to legal threshold a country employs at the time of latest elections. Source: see 'Election system'.

Effective threshold: Own calculations. Refers to minimum level of support which party needs to gain representation in the assembly. Stated as a percentage of the total national vote. Calculated as: $T = \frac{50\%}{(M+1)} + \frac{50\%}{2M}$, where T = effective threshold, M = district magnitude. For rationale for using this measure, see Lijphart, 1994, 27. Following Lijphart, 1994, if mechanistically calculated effective threshold is lower than legal threshold, then the latter automatically becomes the effective threshold. For two- or higher-tier systems, T is calculated from higher-tier district. Source: see 'District magnitude'.

TABLE 4 Comparison of cleavage structures in the CEECs

source: Hellén, Berglund and Aarebrot, 1998 which, in turn, is based on contributions in Berglund, Hellén and Aarebrot, 1998. For a cleavage to be listed as relevant, a party representing it must have gained at least five per cent of the vote in recent general elections (at the time of writing). The same party may be salient in more than one cleavage. Number of cleavages has been attained by adding up the table entries (cleavages in parenthesis have been coded as "half of a cleavage").

Explanation for different cleavage types:

Core population vs. ethno-linguistic minorities: Refers to political parties that are clear-cut representatives of a linguistic or ethnic majority, or to any party appealing to the core population by negative references to national minorities

Religious vs. secular: Refers to parties which defend religious values, or parties which attack religious values and argue for secular society

Urban vs. rural: Refers to parties which represent cities or rural areas

Workers vs. owners: Refers to left-right division and manifest itself through parties which derive their support primarily from within organised labour or employers organisations

Social democrats vs. communists: Refers to parties derived from the traditional conflict between internationalist and nationally-oriented socialism

National vs. cosmopolitan: Refers to parties with the nation-state as the focal point, and parties strongly oriented towards international co-operation as a way

of solving political problems. Nationalist or cosmopolitan rhetoric must be a dominant feature of the party's appeal.
Protectionist vs. free market: Refers to parties which try to preserve subsidies for unprofitable industries, or to parties which argue for the benefits of free markets
Generational: Refers to parties which derive their support from people with a common generational experience (such as pensioners and youth)

Apparatus vs. forums/fronts: Refers to parties which are derived from the old communist ruling apparatus, or parties which represent a direct continuation of the early anti-communist popular forums and fronts.

TABLE 5 Comparison of government compositions in the CEECs

Own calculations. Calculated as a percentage of the days a government composition has been in office out of the total days of the respective period. The cut-off date is 31.12.2002. The years refer to years when the parliamentary elections have been conducted. A government is coded as "multi-party" if it includes two or more parties. The table does not make a distinction between party blocks and more uniform parties. Stability of government composition refers to a Herfindahl index, which is calculated as $\sum g_i^2$, where g_i refers to proportion of time a certain type of government composition has been in office. The types of government compositions used to calculate the index were "majority multi-party government", "majority single-party government", "minority government" and "acting/non-party government". Number of governments comes from Zárates Political Collection. Typically, a change in government means that there has been a change in the prime minister, or in the government parties.

<u>Sources</u>:
- Zárates Political Collection (www.terra.es/personal2/monolith/),
- University of Essex's Project on Political Transformation and the Electoral Process in Post-Communist Europe (www.essex.ac.uk/elections/),
- Rose, Munro and Mackie, 1998,
- Centre For The Study Of Public Policy Database (www.cspp.strath.ac.uk/),
- Berglund, Hellén, Aarebrot (Eds.), 1998,
- contributions in several issues of European Journal of Political Research: 26, December, 1994; 28, December, 1995; 30, December, 1996; 32, December, 1997; 34, December, 1998; 36 December, 1999; 38, December, 2000.

Annex 3 Questionnaires used to collect the institutional data

Annex 3a Questionnaire on fiscal frameworks

Section one: Planning Stage of the Budget

Please note that depending on the question, more than one answer can be possible.

Multi-annual budget framework

1. **Has your country employed any kind of multi-annual budget framework, and if yes, when did your country started employing it** (please indicate the year)**?**

   ____ Yes, what year: ________________________
   ____ No

2. **Legal base of the multi-annual budget framework, and the relationship with the annual budget**

- Please describe, what is the legal base for the multi-annual budget framework

____ Constitution
____ Ordinary/Budget law
____ Regulation or internal rules specified by the Finance Ministry
____ Regulation or internal rules, specified by some other authority
____ No formal basis, the degree of commitment is political
____ No formal basis, the degree of commitment is indicative
____ Other, please specify: _____________________

- How the macroeconomic forecasts included in the multi-annual budget programme are utilised when forming the annual budget?

____ They are used as a basis for annual budgets

____ They are used, but their status is only indicative

____ They are used rarely or never

- Is there any comparisons made between the objectives of the multi-annual budget programme and annual budget with explanations given for possible deviations?

____ Yes, the issue is discussed in a separate report
____ Yes, the issue is discussed in the budget
____ Yes, but only informally
____ Yes, other, please specify: __________________

____ No

- Are the accounting rules for preparing the multi-annual budget programme and the annual budget…?
____ Same, ____ Similar, ____ Different
- Is the calendar for preparing the multi-annual budget programme and the annual budget…?
____ Same, ____ Closely connected, ____ Somewhat connected, ____ Different
- Are the budget targets conceptually …? ____ Same, ____ Similar, ____ Different

3. **What is the time-frame that the multi-annual budget programme covers (note: "t" denotes the present year)?**

____ t-1 to t+3 (i.e., total of 5 years)
____ t-1 to t+2 (i.e. 4 years)
____ t-1 to t+1 (i.e. 3 years)
____ Other, please specify: ____________________________

4. **Please describe what is the procedure for revisions of the general targets when t+1 becomes t?**

____ No action is taken ("fixed framework")
____ Government updates the targets annually and they are extended to include one additional year of projections ("rolling framework")
____ Other kind of procedure, please specify: ______________________
____ No set procedure exist

5. **Where the multi-annual budget programme is formulated?**

____ In a coalition agreement between the Government parties
____ Budget agency or budget department within Finance Ministry
____ A different part of Finance Ministry
____ Legislature or other legislative body, please specify: ___________________
____ Other, please specify: _____________________________

6. **What is the nature of general fiscal targets included in the multi-annual programme?**

____ Total spending as a percentage of GDP, please describe the target:
____ Total spending in nominal terms, please describe the target: ____
____ Total spending in real terms, please describe the target: _______________

____ Total revenue in nominal terms, please describe the target:
____

____ Total revenue in real terms, please describe the target:
____

____ Budget balance as a percentage of GDP, please describe the target:
____

____ Debt as a percentage of GDP, please describe the target:
____

____ Other(s), please specify: __________________________

7. In case your country uses broad targets for total expenditure and revenue, are they presented…?

____ as separate targets, ____ together as one set of targets, ____ other, please specify:

8. What is the scope of multi-annual budget programmes?

____ Central government without including social funds such as social security
____ Central government including all social funds
____ General government (both central government and sub-national government)
____ Other, please specify: ___________________

9. Can you think of any other fiscal rules/targets, formal or informal, not mentioned so far that might be of interest?

____ Yes, please specify: ________________________
____ No

10. In additions for having general targets in their budgets, countries often use also more specific targets. Are specific expenditure targets used to reach general target in your country?

____ Specific expenditure ceilings are set for individual ministries,
- expressed: ____ in real terms, ____ in nominal terms
____ Specific expenditure ceilings are set for spending categories,
- please specify, for which categories: ________________
- expressed: ____ in real terms, ____ in nominal terms
____ Other, please specify: __________________________
____ No such specific expenditure targets exist (go to question no. 11)

- The expenditure targets are set before of after the individual ministries submit their budget bids?
____ Before, ____ After

- Who sets the expenditure targets?
  ____ Cabinet following the proposal by the Finance Minister,
  ____ Cabinet
  ____ Finance Minister/Prime Minister,
  ____ Parliament has to approve the targets
  ____ Parliament is informed on the targets
  ____ Other, please specify: ______________

11. Does your country have any extra-budgetary funds established by law (for example, state funds which operate alongside of state budget)?

____ No
____ Yes,
- if yes, are these funds taken into account in the multi-annual budget programmes?

____ No, ____ Yes

12. Who produces macro-economic estimates used in the budget for future years?

____ Government produces its own model and makes its own forecast
____ Other national authority, please specify: _______________
____ International authority, please specify: _______________
____ Other, please specify: ___________________________

13. Are growth assumptions used in the budget deliberately cautious?

____ Yes ____ No

14. Please indicate, are there explicit assumptions made in the budget about the following macroeconomic variables?

____ Annual inflation rate
____ Unemployment rate
____ Interest rate
____ Exchange rate
____ Other, please specify: ________________________

15. How future financial implications of policy changes are typically brought into consideration?

____ There is no set procedure
____ Ministries must present cost estimates, please describe for how many years: ___
____ Other, please specify: _________________________

The Pre-Accession Economic Programmes ("PEPs")

16. **Please describe the relationship between the Pre-Accession Economic Programmes ("PEPs") and the annual budget:**

- The PEP is the only multi-annual budget programme produced (ie. no other multi-annual budget programme is produced)? ____ Yes, ____ No
- Are the PEP and the annual budget produced in the same ministry?
____ Same, ____ Different
- In case they are produced in the same ministry, are they produced in the same department?
____ Same, ____ Different
- Are the accounting rules for preparing the PEPs and the annual budget…?
____ Same, ____ Similar, ____ Different
- Is the calendar for preparing the PEPs and the annual budget…?
____ Same, ____ Closely connected, ____ Somewhat connected,
____ Different
- Are the budget targets conceptually …? ____ Same, ____ Similar,
____ Different

Past and future changes

17. **Please describe, what have been the major changes in the above-described aspects of the multi-annual budget planning framework since your country started implementing it?**

    ____ Yes, there have been changes, please specify:
    ____
    ____ No changes

18. **The upcoming membership in the European Union and consequent responsibility to prepare the Convergence Programmes will increase the reporting requirements. Besides these obvious changes in the content of multi-annual budget plans, can you foresee any other changes to the multi-annual budget planning framework?**

    ____ Yes, please specify: ______________________
    ____ No

Section two: Details of the decision-making stage of the budget

Please note that depending on the question, more than one answer can be possible.

The role of finance minister

1. **Who proposes the budget within the cabinet and what is the legal basis for this?**

   ____ Finance Minister, ____ Prime Minister, ____ Other, please specify: _____

   - this is based on
   ____ Constitution,
   ____ Ordinary/budget law,
   ____ No formal basis
   ____ Other, please specify: _____________

2. **Please describe the level of discussions within the cabinet**

   ____ Total levels of spending
   ____ Specific budgets for individual ministries
   ____ Spending for particular projects within ministries
   ____ General budget guidelines
   ____ Other, please specify: __________________________

3. **Where the negotiations take place?**

   ____ Full cabinet participates in the negotiations
   ____ Bilaterally between the Finance Minister and spending ministers
   ____ Outside cabinet between the political parties
   ____ Other, please specify: __________________________

4. **Can individual ministers ask for a cabinet decision on their budget bids?**

   ____ Yes, ____ No

5. **How disagreements between Finance Minister and spending ministers are solved?**

   ____ Within the cabinet
   ____ Bilateral negotiations between the Finance Minister and spending minister
   ____ Prime Minister resolves the issue
   ____ Other, please specify: ________________________

6. **Can the full cabinet overrule a decision the Finance Minister takes?**

   ____ Yes, ____ No

7. **Please indicate which of the following budgetary powers the Finance Minister has within the cabinet and what is the basis for his/her powers:**

____ Finance Minister has veto power on budgetary issues,
- based on
  ____ Constitution,
  ____ Ordinary/budget law,
  ____ No formal basis, but MF has this power in practise
  ____ Other, please specify: ____________

____ Finance Minister must approve all changes to budget targets which were set for ministries in previous years,
- based on
  ____ Constitution,
  ____ Ordinary/budget law,
  ____ No formal basis, but MF has this power in practise
  ____ Other, please specify: ____________

8. **Are there usually any budget negotiations with the opposition parties, or does the opposition have any other role in budget formation?**

____ Yes, please specify: ______________________
____ No

9. **Regarding questions 1-8, have there been any major changes during 1994-2003?**

____ Yes, please specify: ______________________
____ No

The role of the Parliament

10. **Can Parliament propose the annual budget independent from the Government?**

____ Yes, ____ No

11. **Can Parliament propose amendments to the Government's budget proposal?**

____ Yes, ____ No (please go to question 15)

12. **Are the Parliament's amendments to the Government's budget proposal limited?**

____ Yes, ____ No (please go to question 14)

13. Describe the nature of restrictions on the parliamentary amendments?

____ Parliament can only give amendments that do not increase the deficit
____ Parliament can only give amendments that do not increase the spending
____ Parliament can only give amendments that do not increase the deficit nor spending
____ There are other restrictions, please specify:
____

14. Can parliamentary amendments cause the fall of government?

____ Yes. Has this ever happened?: _______________
____ No

15. Can the Government call a vote of confidence when the vote on the budget takes place?

____ Yes, this is the usual practise
____ Yes, but this rarely happens
____ No

16. Regarding questions 10-15, have there been any major changes during 1994-2003?

____ Yes, please specify: ________________________
____ No

17. Please describe the degree of party discipline in the budget votes. In particular, is it common that a Parliament member from the ruling party votes against the Government in budget votes (=defecting MP)?

____ Yes, it is very common and the number of defecting Parliament members is usually large
____ Yes, it is very common but the number of defecting Parliament members is usually small
____ No, it is not common (please go to question 18)

18. Can you provide an estimate, what is the usual number of defecting MPs in a budget vote?

____

19. Is there a time limit on the passage of the budget?

____ Yes, please describe: ________________________
____ No

20. Is the treatment of expenditure and revenues in the parliament done separately or simultaneously?

____ Separately, ____ Simultaneously

21. Please, provide an estimate of the typical total size of parliamentary amendments in practise (in % of GDP)

_____ % of GDP

22. Is there a vote on the total budget in the parliament, and if yes, when (in which phase of the budget process)**?**

____ Yes, when: ____________________
____ No

23. What is the procedure if the government and parliament fail to pass the budget in due time?

____ Government must resign
____ Government must accept the Parliament's amendments
____ Parliament will be dissolved
____ In practise this happens rarely or never
____ Other, please specify: __________________________

How the totals of the budget are decided if government and parliament fail to pass the budget in due time?

____ 1/12 of previous year's budget is used until agreement is reached
____ Draft budget is used until agreement is reached
____ Other, please specify: __________________________
____ Has this ever happened, please specify: _______________

The role of the President

24. Please indicate, what of the following powers the president have?

____ President has no budgetary powers (please go to section three of the questionnaire)
____ President can veto the budget
____ President can propose changes to the budget,

- please specify, is there any limitations for these changes: ___________________

____ President has other budgetary powers, please specify:_________________

25. **If president has budgetary powers, can the parliament overrule the president, and if yes, what is the procedure?**

    ____ Yes, please specify procedure: ____________________________
    ____ No

26. **Please provide an estimate, how many times during 1994-2002, the president has in practise proposed changes or vetoed the budget?**

    ____ times

27. **… And out of the times that the president has proposed changes or vetoed, how many times the parliament has overruled the president?**

    ____ times

28. **In case the President can propose changes to the budget, please provide an estimate of the total size of president's proposed changes in practise (in % of GDP)**

    _____ % of GDP

Section three: Details of the monitoring and implementation stages of the budget

Please note that depending on the question, more than one answer can be possible.

1. **What is the institution that monitors the implementation of the budget within the government?**

   ____ Finance Ministry
   ____ An independent body, please specify: _____________________
   ____ Other, please specify: __________________________

2. **In monitoring spending, what is the level of specificity?**

   ____ General government
   ____ Central government
   ____ Individual ministries

____ Specific chapters of the budget
____ Social Sector monitored separately
____ Regional governments monitored separately
____ Other, please specify: ___________________________

3. **In monitoring revenues, what is the level of specificity?**

____ Total revenue
____ Revenue according to the source
____ Other, please specify: ___________________________

4. **What is the lag between occurrence of cash flows for those sectors that are monitored in your country and reporting (days/weeks/months)?**
____

5. **What is the frequency of public reports on budget outcomes?**

____ Monthly, ____ Quarterly, ____ Yearly, ____ Other, please specify:
____

6. **What is the role of the parliament in monitoring the implementation of the budget?**

____ Parliament has no role
____ Parliament is informed automatically on the implementation of the budget
____ Parliament is informed only in case of deviations from the budget
____ Parliament is informed only if it requests information
____ Other, please specify: _________________________

7. **What is the role of the central bank in monitoring the implementation of the budget?**

____ Central bank has no role
____ Central Bank has a role, please specify: ____________________

The role of Finance Minister in implementation

8. **Can Finance minister block (in-year) expenditure?**

____ Yes, ____ No

9. **Must Finance minister (or a controller) approve disbursement of funds before they are spent?**

____ Yes, ____ No

10. Can Finance minister impose cash limits?

____ Yes, ____ No (please, go to question 12)

11. If yes, are the cash limits department specific?

____ Yes, ____ No

12. Is transfers allowed between budget chapters?

____ Yes, ____ No (please, go to question 14)

13. If transfers are allowed, do they require approval by Finance Ministry?

____ Yes, ____ No

14. Regarding questions 1-13, have there been any major changes during 1994-2003?

____ Yes, please specify: ________________________
____ No

15. Are the changes in budget law allowed during budget execution?

____ Yes, ____ No

16. Is it possible to carry over unused funds into following year?

____ Yes, ____ No

Unanticipated expenditure and shocks and sub-national government

17. Are there formal rules in place to deal with the following scenarios…?

- If *revenues* are <u>higher</u> than projected in the budget plan?
  ____ Yes, please specify what kind of formal rules: ____________
  ____ No,
    - If no, what typically happens in practise?
      ____ Government takes no action (overall budget balance improves)
      ____ Supplementary budgets are common in this situation and they are used to increase in-year expenditures
      ____ Supplementary budgets are common in this situation and they are used to cut in-year taxes
    ____ Other, please specify: ___________

- If *revenues* are lower than projected in the budget plan?
  ____ Yes, please specify what kind of formal rules: ____________
  ____ No,
    - If no, what typically happens in practise?
    ____ Government takes no action (overall budget balance worsens)
    ____ Supplementary budgets are common in this situation and they are used to cut in-year expenditures
    ____ Supplementary budgets are common in this situation and they are used to increase in-year taxes
    ____ Other, please specify: ___________

- If *expenditures* are higher than projected in the budget plan?

  ____ Yes, please specify what kind of formal rules: ____________
  ____ No
    - If no, what typically happens in practise?
    ____ Government takes no action (overall budget balance worsens)
    ____ Supplementary budgets are common in this situation and they are used to cut in-year expenditures
    ____ Supplementary budgets are common in this situation and they are used to increase in-year taxes
    ____ Other, please specify: ___________

- If *expenditures* are lower than projected in the budget plan?

  ____ Yes, please specify what kind of formal rules: ____________
  ____ No
    - If no, what typically happens in practise?
    ____ Government takes no action (overall budget balance improves)
    ____ Supplementary budgets are common in this situation and they are used to increase in-year expenditures
    ____ Supplementary budgets are common in this situation and they are used to cut in-year taxes
    ____ Other, please specify: ___________

18. Are there any arrangements in place between the national government and sub-national governments to ensure that budgetary targets for general government are met?

____ Yes, please specify what kind of arrangements: ____________
____ No

19. Does the national government have the ability to restrict lower levels of government borrowing?

____ Yes, please specify how: ________________________
____ No

20. **Do you foresee any changes to the fiscal rules and procedures dealt in this survey (for example, due to the upcoming membership in the European Union)?**

____ Yes, please specify: ________________________
____ No

Annex 3b Questionnaire on parliamentary committees

Please note that in case of bicameral legislature, the following questions concern <u>the lower house</u>

<u>Section one: Committee structures</u>

1. **Please indicate <u>how many</u> parliamentary committees your country has, according to the following grouping:**

____ ad hoc committees
____ permanent (standing) committees, *of which*
  ____ non-specialised law making committees (refers to permanent committees which consider all legislation of a particular type[210])
  ____specialised law making committees (refers to permanent committees which deal with most or all legislation in a particular policy area, or study matters in a particular area possibly including legislation)
  ____ non-law making committees (refers to permanent committees which deal all items of business other than legislation)
____ joint committees (refers to joint committees of both chambers in bicameral legislatures)

- have there been any major changes in the number of permanent committees between 1994-2003?

___ no, ___ yes, please specify: __________________

2. **Please indicate <u>how many</u> parliament members the <u>smallest</u> and <u>largest</u> committees – included above in categories "permanent law making committees" and "permanent specialised committees" – have:**

- smallest committee has ____ members (min size)
- largest committee has ____ members (max size)

[210] for example: one committee can deal with civil law and another constitutional law, or alternatively the committees may deal with legislation for one geographical region each. In sum; the committees in this category are not specialised by policy area.

- have there been any major changes in these numbers between 1994-2003?
___ no, ___ yes, please specify: _________________

3. **Is the size of the permanent committees regulated/fixed, or discretionary?**

____ the size of all of the permanent committees are regulated or fixed
____ the size of most of the permanent committees are regulated or fixed
____ the size of most of the permanent committees are discretionary
____ the size of all of the permanent committees are discretionary

4. **Please describe how jurisdictions of permanent committees are determined:**

___ committee jurisdiction correspond totally with those of government ministries
___ committee jurisdiction correspond mostly with those of government ministries
___ committee jurisdiction in general does not correspond with those of government ministries

5. **Are there formal restrictions in the number of committees a single parliament member may serve?**

___ yes, please specify: _________________
___ no,
 - if no, how common it is *in practise* for a parliament member to serve in more than one committee? ____ common, ____ uncommon

6. **Is it possible for permanent committees to establish (formal) subcommittees?**

___ yes
___ not possible, but informal working groups can be established
___ not possible

7. **If there have been major changes in the committee structures between 1994-2003, could you specify what kind of changes?**

____

Section two: Committee procedures

8. **Please describe, who selects the committee chairs?**

____ the house
____ the speaker of the house
____ the committee itself
____ the parties/party representatives negotiate who will chair the committees
____some other body, please describe: ________________

9. **Please describe how the committee chairs are allocated?**

____ all chairs usually belong to the majority party or parties forming the government
____ most of the chairs usually belong to the majority party or parties forming the government
____ chairs are allocated proportionally among parties
____ other procedure, please describe: ________________

10. **Please describe what happens to committee membership if a member changes his/her party?**

____ committee seat belongs to a party (in other words, if a member changes a party, his/her seat in the committee is replaced by a member from the 'old' party)
____ committee seat is personal (in other words, if a member changes a party, he continues to hold a seat in the committee)

11. **Are the committee deliberations public or private (please check all that apply)?**

____ all/most of the meetings are public
____ all/most of the meetings are private
____ all/most of the meetings are open to all parliament members
____ other, please describe: _______________________

12. **Are committee minorities allowed to submit minority reports[211]?**

____ yes ____ no

13. **At what stage the (legislative) Committee's deliberations usually take place?**

---

211 Ie. A member/members who disagrees with a Committee's majority's opinion is allowed to express his/her reservation for example by including it to the Committee's report.

____ before plenary stage
____ after plenary stage

14. If there have been major changes in the committee procedures between 1994-2003, could you specify what kind of changes?

____

Section three: Committee powers

15. Please describe what kind of initiative powers the (legislative) Committees have (please check all that apply):

____ committees have a right to initiate legislation,
- how many (legislative) committees have this right? ___ all, ___ most,
___ only few

____ committees have a right to consolidate or split legislative bills,
- how many (legislative) committees have this right? ___ all,
___ most, ___ only few

____ no committees have these rights

16. Please describe, what kind of rights the (legislative) Committees have to revise legislative bills (please check all that apply):

____ committees have a right to re-write legislative bills
- how many (legislative) committees have this right? ___ all,
___ most, ___ only few

____ committees have a right to amend legislative bills
- how many (legislative) committees have this right? ___ all,
___ most, ___ only few

____ no committees have these rights

Please describe the nature of the (legislative) Committee hearings (when preparing legislation):

- can the Committees compel witnesses?

____ yes, how many committees have this right? ___ all, ___ most,
___ only few

____ no

- can the Committees demand documents from the government?

____ yes, how many committees have this right? ___ all, ___ most,
___ only few

____ no

- please describe the openness of the (legislative) Committee hearings:

____ hearings are always public
____ hearings are always private
____ hearings are public or private

17. If there have been major changes in the committee powers between 1994-2003, could you specify what kind of changes?

____

Budgetary committee

18. Please describe the role of the budget committee (check all that apply):

____ the budget committee can reject the budget amendments made by the standing committees
____ the budget committee can submit its own amendments to the draft budget
____ the budget committee only collects and summarises the reports and amendments by the standing committees
____ the budget committee deals with the draft budget but members from standing committees attend the meetings of the budget committee when expenditures in their jurisdiction are being death with

19. Please describe the role of the permanent/standing committees, not including the budget committee (check all that apply):

____ standing committees review only those parts of the draft budget that fall into their jurisdiction
____ standing committees reviews all parts the draft budget
____ standing committees can propose amendments to only those parts of the draft budget that fall into their jurisdiction
____ standing committees can propose amendments to all parts the draft budget

20. Who typically participates in the hearings of the committees <u>when they are dealing with the draft budget</u> (check all that apply)?

____ Finance Minister
____ other ministers
____ civil servants/experts from Finance Ministry

____ civil Servants/experts from other ministries
____ other parliamentarians
____ experts employed by legislature

____ outside experts

21. Is there a special budget research organisation within the legislature that analyses the budget and/or related issues?

____ no, ____ yes, what is the number of its staff? ___________

TABLE: 4a.1 The content of multi-annual fiscal frameworks (continued)

	First year when multi-annual framework was employed	Legal base	Time-frame the frame-work covers	Where the pro-gramme is for-mulated	Scope of the frameworks	Procedure for revision when t becomes t+1	Existence of extra-budgetary funds and their relation-ship with the multi-annual framework
Estonia	2001	Ordinary/budget law	t-1 to t+2	Budget agency/budget department within Finance Ministry	Central govern-ment including all social funds	Rolling framework (govt updates the targets annu-ally and they are extended to include one additional year of projections)	No
Hungary	1997 (Before 2001, the Govt presented occasionally a roll-over style medium-term fiscal framework as part of the budget documentation. Starting from 2001, the Act on Public Finances pre-scribed a 3-year fiscal framework A biennial budget – for 2001 and 2002 – was also intro-duced, but the new govt elected in May 2002 reverted to annual budgeting. The 3-year fiscal framework was also removed from the Act on Public Finances in July 2002. For 2003, a normal (one-year) budget proposal was prepared based on the PEP, which took over the role of medium-term fiscal framework.)	Ordinary/budget law	t-1 to t+3	Budget agency/budget department within Finance Ministry in cooperation with the Macro-economic Policy Department	General govern-ment	Rolling framework (govt updates the targets annu-ally and they are extended to include one additional year of projections)	Yes and these funds are included in the multi-annual pro-gramme.
Latvia	2001 ("elements" of the multi-annual framework was implemented the first time in 2001)	Ordinary/budget law	t to t+4	Budget agency/budget department within Finance Ministry	Central govern-ment including all social funds	Rolling framework (govt updates the targets annu-ally and they are extended to include one additional year of projections)	Yes and no extra-budgetary funds operate outside the budget
Lithuania	2000	Ordinary/budget law	t-1 to t+3	Budget agency/budget department within Finance Ministry	Central govern-ment without including social funds such as social security	Rolling framework (govt updates the targets annu-ally and they are extended to include one additional year of projections)	Yes and these funds are included in the multi-annual pro-gramme

Annex 4 Details of multi-annual fiscal frameworks and fiscal institutions

Annex 4a Executive planning stage

TABLE 4a.1 The content of multi-annual fiscal frameworks (continues)

	First year when multi-annual framework was employed	Legal base	Time-frame the frame-work covers	Where the pro-gramme is for-mulated	Scope of the frameworks	Procedure for revision when t becomes t+1	Existence of ex-tra-budgetary funds and their relationship with the multi-annual framework
Bulgaria	1998	Ordinary/budget law	t-1 to t+3	Budget agency/budget department within Finance Ministry	General govern-ment	Rolling framework (govt updates the targets annu-ally and they are extended to include one additional year of projections)	Yes and these funds are included in the multi-annual pro-gramme
Czech Republic	2001 (Informative multi-annual budget outlook. According to the reform fore-seen by the authorities, new rules will be implemented – as of 2004 – which should include a medium term budget-ary framework for 2 years with a bind-ing limit for expenditures covering expenditures of state budget and state extra-budgetary funds.)	Ordinary/budget law	t to t+2	Budget agency/budget department within Finance Ministry	Central govern-ment including social funds	Rolling framework (govt updates the outlook annu-ally and they are extended to include one additional year of projections)	Yes but these funds are not included in the multi-annual outlook

TABLE: 4a.1 The content of multi-annual fiscal frameworks (continued)

	First year when multi-annual framework was employed	Legal base	Time-frame the frame-work covers	Where the pro-gramme is for-mulated	Scope of the frameworks	Procedure for revision when t becomes t+1	Existence of extra-budgetary funds and their relation-ship with the multi-annual framework
Estonia	2001	Ordinary/budget law	t-1 to t+2	Budget agency/budget department within Finance Ministry	Central govern-ment including all social funds	Rolling framework (govt updates the targets annu-ally and they are extended to include one additional year of projections)	No
Hungary	1997 (Before 2001, the Govt presented occasionally a roll-over style medium-term fiscal framework as part of the budget documentation. Starting from 2001, the Act on Public Finances pre-scribed a 3-year fiscal framework A biennial budget – for 2001 and 2002 – was also intro-duced, but the new govt elected in May 2002 reverted to annual budgeting. The 3-year fiscal framework was also removed from the Act on Public Finances in July 2002. For 2003, a normal (one-year) budget proposal was prepared based on the PEP, which took over the role of medium-term fiscal framework.)	Ordinary/budget law	t-1 to t+3	Budget agency/budget department within Finance Ministry in cooperation with the Macro-economic Policy Department	General govern-ment	Rolling framework (govt updates the targets annu-ally and they are extended to include one additional year of projections)	Yes and these funds are included in the multi-annual pro-gramme.
Latvia	2001 (“elements” of the multi-annual framework was implemented the first time in 2001)	Ordinary/budget law	t to t+4	Budget agency/budget department within Finance Ministry	Central govern-ment including all social funds	Rolling framework (govt updates the targets annu-ally and they are extended to include one additional year of projections)	Yes and no extra-budgetary funds operate outside the budget
Lithuania	2000	Ordinary/budget law	t-1 to t+3	Budget agency/budget department within Finance Ministry	Central govern-ment without including social funds such as social security	Rolling framework (govt updates the targets annu-ally and they are extended to include one additional year of projections)	Yes and these funds are included in the multi-annual pro-gramme

TABLE: 4a.1 The content of multi-annual fiscal frameworks (continued)

	First year when multi-annual framework was employed	Legal base	Time-frame the frame-work covers	Where the pro-gramme is for-mulated	Scope of the frameworks	Procedure for revision when t becomes t+1	Existence of extra-budgetary funds and their relation-ship with the multi-annual framework
Poland	1998	Ordinary/budget law	t-1 to t+3	A different part of Finance Ministry	General govern-ment	Rolling framework (govt updates the targets annu-ally and they are extended to include one additional year of projections)	Yes and these funds are included in the multi-annual pro-gramme
Romania	2000 (Romania's '"medium-term national strategy of economic development" was initiated in 2000 but it did not include detailed fiscal targets, but an intention to hold "budget deficit of ca. 3% of the GDP". A somewhat more rigorous approach was introduced in 2002 Budget Law)	Ordinary/budget law	t-1 to t+3	Budget agency/budget department within Finance Ministry	General govern-ment	Rolling framework (govt updates the targets annu-ally and they are extended to include one additional year of projections)	Yes and these funds are included in the multi-annual pro-gramme
Slovakia	2000 (Since 2000, the MoF has produced "Midterm Financial Outlook". 2002 Act specified a legal base as well as a more rigorous multi-annual framework)	Ordinary/budget law established legal base in 2002	t-1 to t+3	A different part of Finance Ministry	General govern-ment	Rolling framework (govt updates the targets annu-ally and they are extended to include one additional year of projections)	Yes and these funds are included in the multi-annual pro-gramme
Slovenia	2000	Ordinary/budget law	t to t+4	Budget agency/budget department within Finance Ministry	General govern-ment	Rolling framework (govt updates the targets annu-ally and they are extended to include one additional year of projections)	Yes but these funds are not included in the multi-annual programme

TABLE 4a.2 The nature of targets (continues)

	Nature of general (multi-annual) targets	The existence of specific expenditure and other targets	Adjustment mechanism if actual inflation differs from expected	The degree of commitment to targets	Action in case of non-compliance	Other fiscal rules employed	How future financial obligations are brought into consideration
Bulgaria	Budget balance (% of GDP), estimates for budget parameters (spending categories) for three years, expressed in real terms for expenditure level	Before 1998; no targets, since 1998; specific nominal expenditure ceilings for individual ministries (exp. level), spending categories expressed in real terms for expenditure levels	Indexation of wages and pensions	The multi-annual targets are legally binding, annual budget targets is indicative (annual exp. ceilings legally binding)	No (ex-ante specified) action	No	Ministries must present cost estimates (for 3 years)
Czech Republic	Forecasts: total nominal spending, total nominal revenue.	Specific expenditure ceilings for individual ministries, expressed in nominal terms for expenditure levels	No mechanism	The multi-annual programme is indicative, annual targets serve as a non-binding benchmark , (annual exp. ceilings legally binding)	No (ex-ante specified) action	No	Ministries must present cost estimates
Estonia	Main target: budget balance (% of GDP). Also total nominal spending (% of GDP), four year exp. targets (on investments) by 'performance fields' (one ministry has 3-4 perf. fields). Strategy also includes total revenues but this is not regarded as a target as such	Specific expenditure ceilings for individual ministries, expressed in nominal terms for expenditure levels	No mechanism	Multi-annual targets typically serve as a non-binding benchmark for annual budget-making, degree of commitment for annual budget targets is indicative (annual exp. ceilings legally binding)	No (ex-ante specified) action	The amount of total (annual) foreign borrowing can not exceed 15 % of annual budget revenues, total foreign debt can not exceed 75 % of annual revenues. Foreign loans can only be taken for investments. Since 2000: public borrowing must not exceed expenditures for planned investment	Ministries must present cost estimates (for 4 years)

TABLE: 4a.2 The nature of targets (continued)

	Nature of general (multi-annual) targets	The existence of specific expenditure and other targets	Adjustment mechanism if actual inflation differs from expected	The degree of commitment to targets	Action in case of non-compliance	Other fiscal rules employed	How future financial obligations are brought into consideration
Hungary	Total spending, total revenue, budget balance, debt (all % of GDP), nominal exp. targets for individual ministries and spending categories for t+2 and t+3.	No specific expenditure targets (budget circular includes budget subsidy/transfer ceilings – as difference btw expenditures and own revenues – for ind. ministries)	No mechanism	The degree of commitment for multi-annual and annual targets is indicative (annual exp. ceilings legally binding)	No (ex-ante specified) action	No	Ministries must present cost estimates (for 1+2 years)
Latvia	Macroeconomic Development and Fiscal Policy Guidelines include: total nominal spending (% of GDP), total nominal revenue, Budget balance and debt (% of GDP). Annual state budget law is supplemented by a separate appendix which include planned liabilities for medium-term projects	Initial strategy proposal includes projections for main budget aggregates (serves as a non-binding benchmark). After initial budget bids, specific exp. targets for individual ministries, expressed in nominal terms	No mechanism	Multi-annual and annual targets typically serve as a non-binding benchmark for annual budget-making (annual exp. ceilings legally binding)	No (ex-ante specified) action	No	Ministries must present cost estimates
Lithuania	Budget balance and debt (% of GDP), target for 3 year expenditure, expressed as one figure, 3 year max. appropriations for each appropriation manager	Before 1999; no targets. Since 1999, initial "strategic priorities" includes general priorities. Based on initial budget bids, specific expenditure ceilings set for individual ministries, expressed in nominal terms	No mechanism	Multi-annual and annual targets typically serve as a non-binding benchmark for annual budget-making (annual exp. ceilings legally binding)	No (ex-ante specified) action	No	Ministries must present cost estimates for 3 years when 'PEPs' is formulated

TABLE 4a.2 The nature of targets (continued)

	Nature of general (multi-annual) targets	The existence of specific expenditure and other targets	Adjustment mechanism if actual inflation differs from expected	The degree of commitment to targets	Action in case of non-compliance	Other fiscal rules employed	How future financial obligations are brought into consideration
Poland	Budget balance and debt (both as % of GDP)	Before 1999; no targets, since 1999; initial budget circular does not include (numerical) fiscal targets. After initial projections on budget bids, specific expenditure ceilings set for spending categories, expressed in nominal terms for expenditure level	Indexation of some expenditures	The multi-annual targets typically serve as a non-binding benchmark for annual budget making. The degree of commitment to multi-annual and annual targets is indicative (annual exp. ceilings legally binding)	No (ex-ante specified) action	The Law on Public Finance provides for limits on govt borrowing and possibility of granting state guarantees, in case when public debt exceeds 50%, 55% and 60% of GDP (the limits on borrowing are relatively mild for the 50% threshold, while above the 60% threshold no more borrowing is allowed)	Ministries must present cost estimates (for each change in policy - estimated cost, usually for 1 year but depending on a change also for 3 next years)
Romania	Budget balance (% of GDP), targets for the budgetary year and estimations for 3 year expenditure for individual ministries and budget programmes	Before 2003: initial budget circular does not include (numerical) fiscal targets. After initial budget projections, specific expenditure ceilings set for individual ministries, expressed in nominal terms for expenditure levels. Since 2003, budget circular already includes exp. targets for ind. ministries.	No mechanism	The degree of commitment for multi-annual targets is indicative, annual targets serve as a non-binding benchmark. The 2002 Budget Law does state that budget bids must respect the limits set in the initial budget circular (annual exp. ceilings legally binding)	No (ex-ante specified) action	No	Ministries must present cost estimates (for t+3 years)
Slovakia	Total spending (% of GDP), total spending and revenue in nominal terms, budget balance and debt (% of GDP), expenditure targets for spending categories. Targets for revenues and expenditures included in the multi-annual programme should, according to the budget law, be treated as indicators "rather than binding specifications"	Initial budget circular includes figures for main budget aggregates. After consulting ind. ministers, specific expenditure ceilings set for individual ministries, expressed in nominal terms	No mechanism	Multi-annual and annual targets serve as a non-binding benchmark (annual exp. ceilings are legally binding but according to the budget law any budgetary chapter may go beyond the expenditure limit of its budget if permitted so by the MoF. Budget Law specifies conditions for this overdraft)	No (ex-ante specified) action	No	Ministries must present cost estimates (for the following year)

TABLE 4a.2 The nature of targets (continued)

	Nature of general (multi-annual) targets	The existence of specific expenditure and other targets	Adjustment mechanism if actual inflation differs from expected	The degree of commitment to targets	Action in case of non-compliance	Other fiscal rules employed	How future financial obligations are brought into consideration
Slovenia	Total spending in nominal terms (limits by spending areas for t+1 only), budget balance (% of GDP), general orientation: total revenues as % of GDP should be kept at around same level and total expenditure as % of GDP should decline	Specific expenditure ceilings set for individual ministries, expressed in nominal terms for expenditure level	No mechanism (if annual inflation is significantly different from expected, a supplementary budget might follow)	Multi-annual targets serve as a non-binding benchmark for annual budget-making, annual targets typically serve as a non-binding benchmark, (annual exp. ceilings are legally binding)	No (ex-ante specified) action	Organic Budget Law and the Annual Law on implementation of the budget limit the total for newly issued debt each year	Ministries must present cost estimates

TABLE 4a.3 The relationship between the multi-annual fiscal frameworks and the annual budgets

	Use of forecasts in multi-annual programmes when annual budget is formed	**Comparisons between the objectives and possible deviations**	**Accounting rules for preparing multi-annual programme and annual budget**	**Calendar for preparing multi-annual programme and annual budget**	**The budget targets conceptually**
Bulgaria	Used as a basis for annual budgets	Discussed in the budget	Same	Closely connected	Same
Czech Republic	Used but status only indicative	No	Similar	Same	Same
Estonia	Used as a basis for annual budgets	Yes, but informally	Same	Same	Same
Hungary	Used as a basis for annual budgets	Discussed in the budget	Same	Same	Same
Latvia	Used as a basis for annual budgets	No	Similar	Closely connected	Same
Lithuania	Used as a basis for annual budgets	Discussed in the budget	Same (but annual budget more detailed)	Same	Same
Poland	Used as a basis for annual budgets	No	Same	Same	Same
Romania	Used as a basis for annual budgets	Discussed in a separate report	Similar	Closely connected	Similar
Slovakia	Used as a basis for annual budgets	The issue is mentioned in the updated multi-annual programme	Similar	Closely connected	Same
Slovenia	Used but status only indicative	No	Same	Same	Same

TABLE 4a.4 The relationship between the "PEPs" and the annual budgets

	PEP is the only multi-annual budget programme produced	**Are they produced in the same ministry**	**... if yes, are they produced in the same department**	**Accounting rules for preparing multi-annual programme and annual budget**	**Calendar for preparing multi-annual programme and annual budget**	**The budget targets conceptually**	**Similarity index** [1]
Bulgaria	No	Same	Different (0)	Similar (1)	Closely connected (2)	Same (2)	5
Czech Republic	No	Same	Different (0)	Different (0)	Somewhat connected (depending on the time-schedule for the PEP) (1)	Same (2)	3
Estonia	No	Same	Different (0)	Different (0)	Closely connected (2)	Same (2)	4
Hungary	Yes (from 2003, PEP took over the role of medium term fiscal framework)	Same	Different (0)	Same (aggregation level is slightly different) (2)	Same (2)	Same (2)	6
Latvia	No	Same	Same (2)	Different (0)	Different (0)	Same (2)	4
Lithuania	No	Same	Different (0)	Similar (annual budget more detailed) (1)	Closely connected (2)	Same (2)	5
Poland	No	Same	Same (2)	Same (2)	Somewhat connected (1)	Same (2)	7
Romania	No	Same	Same (2)	Similar (1)	Somewhat connected (1)	Same (2)	6
Slovakia	No	Same	Different (0)	Similar (1)	Somewhat connected (1)	Same (2)	4
Slovenia	No	Same	Same (2)	Similar (1)	Closely connected (2)	Same (2)	7
						mean all	*5,1*
						mean commitment	*4,8*
						mean delegation	*6,5*

1 Similarity index: Formed by taking into account the following characteristics (max 8 points): Are PEPs produced in the same department, similarity of accounting rules, connectedness of calendar and similarity of the budget targets (2 points for replies "same", "connected", "closely connected", full point for replies "similar", "somewhat connected", and 0 points for replies "different", "disconnected"). Numbers in parentheses refer to awarded points.

TABLE 4a.5 The role of the Finance Minister in the planning and decision-making stage (continues)

	Govt's involvement in setting the multi-annual targets and the role of Govt programme	Sequence of decision-making in setting the targets	Proposer of the budget within the cabinet	Level of discussions in the cabinet	Arena for the budget negotiations	Spending ministers can ask for a cabinet decision for their budget bids	Way to solve disagreements between the MoF and spending ministers	The full cabinet can overrule MoF's decision	Budgetary powers of MoF	Basis for MoF's budgetary powers	The role of opposition in the budget formation in the decision-making stage	Finance Minister index[1]
Bulgaria	MoF prepares budget projection (which includes preliminary estimations for state budget parameters for the next three years) and cabinet approves before detailed budgeting starts. Multi-annual targets not included in the coalition agreement.	Since 1998: MoF proposes expenditure targets, cabinet adopts, budget bids are made (-98: 0, 98-: 2)	Finance Minister	Total levels of spending, Specific budgets for ind. ministries, general budget guidelines	Bilaterally btw the MoF and spending ministers, full cabinet (1.5)	Yes	First bilaterally between the MoF and spending ministers, then within the cabinet (0)	Yes (0)	Agenda setter (3)	Ordinary/ budget law	No role	-98: 4,5 98-: 6,5
Czech Republic	The outlook is discussed and approved by the govt (together with a draft state budget). The 2002 Coalition Agreement includes a numerical range for medium term (indicative) fiscal targets. Previous agreements included verbal policy intentions.	MoF proposes expenditure targets, cabinet adopts, budget bids are made (2)	Finance Minister	Total levels of spending, specific budgets for individual ministries, spending for particular projects within ministries, general budget guidelines	Bilaterally btw the MoF and spending ministers, full cabinet (1.5)	Yes	First bilaterally between the MoF and spending ministers, then within cabinet (0)	Yes (0)	Agenda setter (3)	Ordinary/ budget law	No, when there is a majority govt, when minority govt in office, agreements with opposition common	6,5

TABLE 4a.5 The role of the Finance Minister in the planning and decision-making stage (continued)

	Govt's involvement in setting the multi-annual targets and the role of Govt programme	**Sequence of decision-making in setting the targets**	**Proposer of the budget within the cabinet**	**Level of discussions in the cabinet**	**Arena for the budget negotiations**	**Spending ministers can ask for a cabinet decision for their budget bids**	**Way to solve disagreements between the MoF and spending ministers**	**The full cabinet can overrule MoF's decision**	**Budgetary powers of MoF**	**Basis for MoF's budgetary powers**	**The role of opposition in the budget formation in the decision-making stage**	**Finance Minister index [1]**
Estonia	Multi-annual budget strategy approved by the Govt before composition of annual budget starts. Coalition Agreements typically include verbal policy intentions (no numerical budget targets)	MoF proposes expenditure targets, cabinet adopts, budget bids are made (2)	Finance Minister	Total levels of spending, specific budgets for ind. ministries	Bilaterally btw the MoF and spending ministers, full cabinet (1.5)	Yes (3)	First bilaterally between the MoF and spending ministers, then within cabinet (0)	Yes	Agenda setter, veto power (6)	Agenda setter: ordinary/ budget law, veto power: no formal basis but MoF has this power in practise	No role	12,5
Hungary	2001-2002 multi-annual guidelines were approved by the govt before detailed budgeting starts. Since then PEPs have been approved by the govt before draft budget is sent to the P-ment. The 2002 Government Programme includes an intention to reduce the debt/GDP ratio and to reach deficit of 2,5 % of GDP by 2006.	MoF elaborates and reconciles the baseline scenario chapter-level figures and general indications with the spending ministries while spending ministers prepare budget bids., MoF proposes targets, cabinet adopts (in 1999 the P approved fiscal targets already in June, but it was done 'on experimental basis') (1)	Finance Minister	Total levels of spending, general budget guidelines	Bilaterally btw the MoF and spending ministers (MoF also provides information to the parties forming the government coalition) During 98-02 Min. of Economic Affairs had primary responsibility of the macroec. policies. More decisions were taken by full govt during this time. (3, 98-02: 1.5)	Yes (3, 98-02: 0)	First bilaterally between the MoF and spending ministers, then within the cabinet, finally PM resolves (3)	Yes	Agenda setter, (limited) veto power, MoF must approve all changes to budget targets which were set for ministries in previous years. (Again note: During 98-02 Min. of Economic Affairs had primary responsibility of the macroec. policies. More decisions were taken by full govt during this time) (9, 98-02: 3)	Agenda setter: ordinary/ budget law, other powers: no formal basis but MoF has these powers in practise (in most cases)	No role	19 (98-02: 8,5)

TABLE 4a.5 The role of the Finance Minister in the planning and decision-making stage (continued)

	Govt's involvement in setting the multi-annual targets and the role of Govt programme	**Sequence of decision-making in setting the targets**	**Proposer of the budget within the cabinet**	**Level of discussions in the cabinet**	**Arena for the budget negotiations**	**Spending ministers can ask for a cabinet decision for their budget bids**	**Way to solve disagreements between the MoF and spending ministers**	**The full cabinet can overrule MoF's decision**	**Budgetary powers of MoF**	**Basis for MoF's budgetary powers**	**The role of opposition in the budget formation in the decision-making stage**	**Finance Minister index** [1]
Latvia	Multi-annual targets adopted by the Govt. 1999 and 2000 Govt Declarations included intention to avoid the fiscal deficit that exceeds 1%; Govt Declaration of 2002 declaration included a provision to ensure compliance with Maastricht deficit criteria and medium term intention of non-deficit budgets.	MoF proposes expenditure targets, cabinet adopts, budget bids are made (2)	Finance Minister	Total levels of spending, specific budgets for individual ministries, spending for particular projects within ministries, general budget guidelines	Bilaterally btw the MoF and spending ministers, outside cabinet between political parties, full cabinet (1)	Yes (0)	First bilaterally between the MoF and spending ministers, then within the cabinet, finally PM resolves (3)	Yes	Agenda setter (3)	Ordinary/ budget law	No role	9
Lithuania	Multi-annual targets adopted by the Govt before detailed budgeting starts. Govt Programme for 2001-2004 includes verbal policy intentions (incl. the aim to prevent growth of GDP percentage of the total public debt)	Since 1999: Spending ministers prepare initial projections on budget bids (based on general framework set by "strategic goals and priorities" adopted by the cabinet), MoF proposes targets, Cabinet Committee considers, cabinet decides, budget bids are made (-99: 0, 99-: 1)	Finance Minister	Total levels of spending, specific budgets for individual ministries, spending for particular projects within ministries, general budget guidelines	Bilaterally btw the MoF and spending ministers, cabinet committee (since 1999), full cabinet (-99: 1.5, 99-: 1)	Yes (3)	First bilaterally between the MoF and spending ministers, then in cabinet committee (since 1999), finally within cabinet (0)	Yes	Agenda setter, veto power (6)	Agenda setter: ordinary/ budget law, veto power: no formal basis but MoF has this power in practise	No role	-99: 10,5 99-: 11

TABLE 4a.5 The role of the Finance Minister in the planning and decision-making stage (continued)

	Govt's involvement in setting the multi-annual targets and the role of Govt programme	Sequence of decision-making in setting the targets	Proposer of the budget within the cabinet	Level of discussions in the cabinet	Arena for the budget negotiations	Spending ministers can ask for a cabinet decision for their budget bids	Way to solve disagreements between the MoF and spending ministers	The full cabinet can overrule MoF's decision	Budgetary powers of MoF	Basis for MoF's budgetary powers	The role of opposition in the budget formation in the decision-making stage	Finance Minister index [1]
Poland	The Government adopts the multi-annual programme. The targets included in the multi-annual programme are not included in the coalition agreement between the govt parties.	Since 1998: Spending ministers prepare initial projections on budget bids (based on informational circular by MoF), MoF proposes targets, cabinet decides, budget bids are made (-98: 0, 98-: 1)	Finance Minister	Total levels of spending, specific budgets for individual ministries, spending for particular projects within ministries, general budget guidelines	Bilaterally btw the MoF and spending ministers, full cabinet (1.5)	Yes (3)	First bilaterally between the MoF and spending ministers, then in cabinet committee, then within the cabinet, finally PM resolves (3)	Yes	Agenda setter, veto power (6)	Ordinary/ budget law, veto power: no formal basis but MoF has this power in practise	No role	-98: 13,5 98-: 14,5
Romania	Since 2003: Multi-annual targets adopted by the govt before detailed budget-drafting begins. Governance Programme for 2001-2004 includes mainly verbal policy intentions (incl. intention to "focus on a budget deficit of ca. 3% of the GDP").	Until 2003: Spending ministers prepare initial projections on budget bids (based on informational circular by MoF), MoF – after an approval from PM – sets targets, budget bids are made. Since 2003: MoF proposes the targets, cabinet approves, budget bids are made (-03:1, 03-:2)	Finance Minister	Total levels of spending, specific budgets for individual ministries, spending for particular projects within ministries, general budget guidelines	Bilaterally btw the MoF and spending ministers, full cabinet (1.5)	Yes (0)	First bilaterally between the MoF and spending ministers, then within the cabinet (0)	Yes	Agenda setter, MoF must approve all changes to budget targets which were set for ministries in previous years (6)	Ordinary/ budget law	No role	-03: 8,5 03-: 9,5

TABLE 4a.5 The role of the Finance Minister in the planning and decision-making stage (continued)

	Govt's involvement in setting the multi-annual targets and the role of Govt programme	**Sequence of decision-making in setting the targets**	**Proposer of the budget within the cabinet**	**Level of discussions in the cabinet**	**Arena for the budget negotiations**	**Spending ministers can ask for a cabinet decision for their budget bids**	**Way to solve disagreements between the MoF and spending ministers**	**The full cabinet can overrule MoF's decision**	**Budgetary powers of MoF**	**Basis for MoF's budgetary powers**	**The role of opposition in the budget formation in the decision-making stage**	**Finance Minister index** [1]
Slovakia	Multi-annual targets adopted by the Govt at the beginning of the budget process before detailed budget drafting starts. Govt Policy Statements typically include only verbal policy intentions. The 2002 Statement include a goal for meeting the requirements for the entry into the EMU by 2006 and an aim to reduce public debt as a percentage of GNP during the term of office.	MoF prepares forecasts and discusses with spending ministers, then proposes targets, cabinet approves, budget bids are made (1)	Finance Minister	Total levels of spending, specific budgets for individual ministries, spending for particular projects within ministries	Bilaterally btw the MoF and spending ministers, full cabinet. Also state secretaries and Economic Council are involved (in an advisory capacity). (1)	Yes (0)	First bilaterally between the MoF and spending ministers, then at the level of state secretaries, finally within the cabinet (0)	Yes	Agenda setter (3)	Constitution, ordinary/ budget law	No role	5

TABLE 4a.5 The role of the Finance Minister in the planning and decision-making stage (continued)

	Govt's involvement in setting the multi-annual targets and the role of Govt programme	Sequence of decision-making in setting the targets	Proposer of the budget within the cabinet	Level of discussions in the cabinet	Arena for the budget negotiations	Spending ministers can ask for a cabinet decision for their budget bids	Way to solve disagreements between the MoF and spending ministers	The full cabinet can overrule MoF's decision	Budgetary powers of MoF	Basis for MoF's budgetary powers	The role of opposition in the budget formation in the decision-making stage	Finance Minister index [1]
Slovenia	The government adopts the budget memorandum which contains the multi-annual scenario before detailed budget drafting begins. The 2001 Govt Work Programme includes only vague verbal policy intentions. The 2000 coalition agreement includes a goal to stabilise share of public finance revenue and expenditure at the 42% level of GDP and a goal to achieve a surplus in public finances. Public debt should be kept between 35 and 40 % of GDP.	MoF proposes targets, cabinet adopts, budget bids are made (2)	Finance Minister	Total levels of spending, specific budgets for individual ministries, general budget guidelines	Bilaterally btw the MoF and spending ministers (3)	Yes (3)	First bilaterally between the MoF and spending ministers, then within the cabinet, finally PM resolves (3)	Yes	Agenda setter, veto power (6)	Agenda setter: ordinary/ budget law, veto power: no formal basis but MoF has this power in practise	No role	17
											mean all	*11,1 (pre-98: 10,6)*
											mean commitment	*9,3 (pre-98: 8,8)*
											mean delegation	*18,0*

1 Finance Minister index (formed by the following criteria, max 24 points): bilateral negotiations between the MoF and spending ministers exist: three points if that is the only (main) arena, fractions if not, individual ministers can not ask cabinet decisions (three points), MoF has proposal power over fiscal targets (three points if MoF *sets* the targets, two points if MoF *proposes* the targets *before* initial budget bids are made, full point if MoF *proposes* the targets *after* initial budget bids are made , 0 if no targets), MoF has budgetary powers – agenda setter, veto power, MoF must approve all changes to targets (three points for each), disputes are not resolved finally by full cabinet (three points), MoF can not be overruled by full cabinet (three points). Following Hallerberg et al, 2001, if MoF has a veto power, full points are also awarded from the category "individual ministers can not ask cabinet decisions". Numbers in parentheses refer to awarded points.

Annex 4b Legislative approval stage

TABLE 4b.1 The role of the Parliament in the legislative stage (continues)

	Parliament can propose the annual budget independently from the government	Parliament can amend the govt's budget proposal	Are the amendments limited, and if so, in what way	Amendments can cause a fall of the govt	Estimation of the total size of Parl. amend'ts (% of GDP)	Govt can call a vote of confidence when the budget vote takes place	The degree of party discipline in budget votes	Treatment of expenditure and revenues	Vote on the total budget in the Parliament	Existence of a time limit on the passage of the budget	Procedure if the budget is not passed in due time	Decision on budget totals if budget is not passed in due time	Parliament index[1]
Bulgaria	No (0)	Yes (1)	No (1+1)	No (0)	0,1 %	Yes, but this happens rarely	Defecting MPs not common	Simultaneously	At the start of the parliamentary deliberation (0)	Yes: before the beginning of the budget year (0)	Govt must accept parliament's amendments	1/12 of previous year's budget until agreement is reached (1)	4
Czech Republic	No (0)	Yes (1)	Yes: P can only give amendments that do not increase deficit (0)	No (0)	0,3-0,5 %	Yes, but this happens rarely	Defecting MPs not common	Simultaneously	During the first reading (0)	No (not formally, informally the end of the preceding year) (1)	Happens rarely or never	Before 2001: Draft Budget is used, since 2001: 1/12 of previous year's budget until agreement is reached (-01:0, 01-:1)	-01: 2 01-: 3
Estonia	No (0)	Yes (1)	Yes: P has to present financial calculations showing the source of revenue to cover the expenditures. Since 2003 in addition motions submitted after suspension of the 2nd and 3rd reading which are not supported by the Govt and not accepted by the leading committee shall not be put to a vote (0)	No (0)	~ 0,2 %	Until 2003 no, since 2003 yes	Defecting MPs not common	Simultaneously	During the final reading (1)	Yes: two months (0)	Happens rarely or never. P will be dissolved	1/12 of previous year's budget until agreement is reached (1)	3

TABLE 4b.1 The role of the Parliament in the legislative stage (continued)

	Parliament can propose the annual budget independently from the government	Parliament can amend the govt's budget proposal	Are the amendments limited, and if so, in what way	Amendments can cause a fall of the govt	Estimation of the total size of Parl. amend'ts (% of GDP)	Govt can call a vote of confidence when the budget vote takes place	The degree of party discipline in budget votes	Treatment of expenditure and revenues	Vote on the total budget in the Parliament	Existence of a time limit on the passage of the budget	Procedure if the budget is not passed in due time	Decision on budget totals if budget is not passed in due time	Parliament index[1]
Hungary	No (0)	Yes (1)	Yes: Only after the voting of Parliament (by 30 November) on the grand total of revenues and expenditures of the central budgetary chapters and on the extent of the deficit or surplus of the draft Budget, any amendment that may result in an increase in the expenditures or in a decrease in the revenues must include a solution to preserve the budgetary balance. Thus this restriction does not apply to amendments which can be introduced in the debate before the above-mentioned vote. (1+0)	No (theoretically it is possible but never happened) (0)	~ 0 %	Not 'legally' (theoretically yes, but this has never happened)	Defecting MPs not common	Simultaneously	P shall decide by 30 November about the proposed amendments and the chapter amounts. Vote after amendments. (1)	Yes: first vote 30 Nov (this deadline included in law), final vote in practise 20-23 Dec (0)	This never happens	The organic budget law prescribes a temporary authorisation by Parliament for Government for collecting budget revenues and spending within an identified scope of budget implementation (0)	3
Latvia	No (0)	Yes (1)	Yes: according to Constitution, if P makes "a decision that involves expenditures not included in the Budget", it has to allocate funds to cover such expenditures. (0)	Yes but it has never happened (1)	~0.06 %	Yes (Structure of Cabinet Law states that "Lack of confidence in the Cabinet shall be expressed by the Saeima […] by rejecting the annual State budget proposal submitted by the Cabinet"	Defecting MPs not common	Simultaneously	Final vote (1)	No (1)	This happens rarely or never	1/12 of previous year's budget until agreement is reached (or during election years draft budget until there is a agreement but no longer than 3 months from the beginning of the year or draft budget) (1)	5

TABLE: 4b.1 The role of the Parliament in the legislative stage (continued)

	Parliament can propose the annual budget independently from the government	Parliament can amend the govt's budget proposal	Are the amendments limited, and if so, in what way	Amendments can cause a fall of the govt	Estimation of the total size of Parl. amend'ts (% of GDP)	Govt can call a vote of confidence when the budget vote takes place	The degree of party discipline in budget votes	Treatment of expenditure and revenues	Vote on the total budget in the Parliament	Existence of a time limit on the passage of the budget	Procedure if the budget is not passed in due time	Decision on budget totals if budget is not passed in due time	Parliament index[1]
Lithuania	No (0)	Yes (1)	Yes: P can only give amendments that do not increase deficit, P can propose changes to spending if source for financing is provided (0)	No (0)	MoF: 0,05-0,1%, P: 3 %	No	Defecting MPs not common (3-4 MPs/budget vote)	Simultaneously	Final stage (1)	Yes: not later than 14 calendar days before start of the budget year (0)	This happens rarely or never, the Govt must accept the P's amendments (majority of MPs can pass amendments during the last reading even if the Govt is against)	1/12 of previous year's budget until agreement is reached (1)	3
Poland	No (0)	Yes (1)	Until 1998 no. Since 1998 yes: P can only give amendments that do not increase deficit (-98: 1+1, 98-:0)	No (0)	> 0,5 %	Yes, but this rarely happens	- In the 1993 - 1997 term: about 3 MPs - In the 1997 - 2001 term: about 10 such MPs - present term: no such cases	Simultaneously	At the end of proceedings (As a rule, some opposition party has made a motion to reject the draft budget in the first reading (in 1993-1998, 2000, 2002 and 2003) but motions have always been rejected. These votes have not fixed the budget totals but only given a green light to continue consideration of the draft budget.) (1)	Until: 1998: three months (from the day of submission to the day of passing the budget by the Sejm only). Since 1998: four months from the submission of the draft budget. The govt should submit draft budget by Sept 30 of the previous year unless there are 'exceptional instances' (before 1998 Oct 31st). But it has been common for the Govt to appeal to 'exceptional instances' and fail the deadline. (0)	Parliament will be dissolved, in practise this happens rarely or never (the budget has not been late due to the P's failure to respect time limit)	Draft budget is used until the agreement is reached (0)	-98: 4 98-: 2

TABLE 4b.1 The role of the Parliament in the legislative stage (continued)

	Parliament can propose the annual budget independently from the government	Parliament can amend the govt's budget proposal	Are the amendments limited, and if so, in what way	Amendments can cause a fall of the govt	Estimation of the total size of Parl. amend'ts (% of GDP)	Govt can call a vote of confidence when the budget vote takes place	The degree of party discipline in budget votes	Treatment of expenditure and revenues	Vote on the total budget in the Parliament	Existence of a time limit on the passage of the budget	Procedure if the budget is not passed in due time	Decision on budget totals if budget is not passed in due time	Parliament index[1]
Romania	No (0)	Yes (1)	Until 2003: no, since 2003: yes, P can only give amendments that do not increase deficit (-03: 1+1, 03-: 0)	No (0)	No answer provided	Yes (according to the constitution)	Defecting MPs common but the number is usually small	Simultaneously	Final vote (1)	Yes: 3 days before the end of budgetary year (0)	Since 2001 the budget has been passed in due time, prior to 2000, as a rule the budget was not passed in due time (often due to Govt's failure to respect the deadlines)	1/12 of previous year's budget until agreement is reached (since 2003: 1/12 from the previous year's budget *or* if the budget provisions are smaller in the draft budget, then 1/12 from the draft budget) (-03:1, 03-: 0)	-03: 5 03-: 2
Slovakia	No (0)	Yes (1)	No (1+1)	Yes, but this has never happened (1)	> 1 %	Yes, but this rarely happens	Defecting MPs not common	Simultaneously	At the end of proceedings (1)	Yes: by the end of the calendar year (0)	In practise this happens rarely or never	Draft budget is used until the agreement is reached (0)	5
Slovenia	No (0)	Yes (1)	Yes: P can only give amendments that do not increase deficit nor spending (0)	Yes (indirectly), but this has never happened (1)	~ 0,2 %	Yes, but this happens rarely	Defecting MPs common but the number is usually small (MoF: 2-10/budget vote, P: 1-5 /budget vote)	Simultaneously	After amendments to draft budget are tabled (1)	Yes: by the end of the calendar year (0)	In practise this happens rarely (the 1997 budget was adopted by P in the beginning of December 1997)	Temporary financing is done for 3 months (limited by the real expenditures in previous year's budget for the equal period), if budget is still not passed, temporary financing might be extended for another 3 months (limited as above). (1)	4
												mean all	*3,4 (pre-98: 3,8)*
												mean commitment	*3,4 (pre-98: 3,9)*
												mean delegation	*3,5*

1 Parliament index (formed by adding one for each of the following criteria, max 8 points): P can propose separate budget, amendments allowed, amendments not limited, amendments do not have to be offsetting, amendments can cause fall of govt, vote on budget totals at the end of proceedings, no time limit in place, budget proposal not used if agreement delayed. Numbers in parentheses refer to awarded points.

TABLE 4b.2 The role of the President in the legislative approval stage

	Budgetary powers of the President	**Can Parliament overrule the President**	**How many times during 1994-2002 the President has in practice used his/her budg. powers**
Bulgaria	President can veto the budget	Yes (majority of all MPs)	0
Czech Republic	President can veto the budget	Yes (majority of all MPs)	0
Estonia	President can veto the budget	Yes (majority of MPs present)	0
Hungary	President can veto the budget	Yes (majority of MPs present)	0
Latvia	President can propose changes to the budget	Yes (majority of MPs present)	0
Lithuania	President can veto the budget	Yes (majority of all MPs)	0
Poland	President can made reference to the Constitution Tribunal for an adjudication upon the conformity to the Constitution to the Budget (since 1997)	Until 1997: 2/3 majority	0
Romania	President can veto the budget	Yes (majority of MPs from both champers present)	0
Slovakia	President can veto the budget	Yes (majority of MPs present)	0
Slovenia	No budgetary powers	-	-

TABLE 4b.3 Structure of parliamentary committees (continues)

	Number of committees						Size of permanent committees (min/max)	How the size of permanent committees are determined	How the jurisdictions of permanent committees are determined	Existence of formal restrictions in the number of committees a single parliament member may serve	Possibility to establish sub-committees
		permanent									
	ad hoc	legislative by function	specialised	non-law making	joint committees	total					
Bulgaria	0	1	19	1	-	21	16/28	Size of all committees are discretionary	Committee jurisdiction corresponds mostly with those of govt ministries	Yes (two committees at most as well as to the European Integration or the Anti-Corruption Actions Committees)	Yes
Czech Republic	0	2	9	3	0	14	11/21	Size of all committees are discretionary	Committee jurisdiction in general does not correspond with those of govt ministries	Yes (two committees at most in addition to membership in Mandate and Immunity Committee, Petition Committee and Organisational Committee)	Yes

TABLE: 4b.3 Structure of parliamentary committees (continued)

	Number of committees						Size of permanent committees (min/max)	How the size of permanent committees are determined	How the jurisdictions of permanent committees are determined	Existence of formal restrictions in the number of committees a single parliament member may serve	Possibility to establish sub-committees
		permanent									
	ad hoc	legislative by function	specialised	non-law making	joint committees	total					
Estonia	3	0	10	0	-	10	7/12	Size of all committees are discretionary	Committee jurisdiction corresponds mostly with those of govt ministries	Yes (only in one committee)	Not possible but informal working groups can be established
Hungary	9	1	17	7	-	25	10/28	Size of all committees are discretionary	Committee jurisdiction corresponds mostly with those of govt ministries	No (in practise it is common that MPs serve in more than one committee)	Yes
Latvia	0	0	9	8	-	17	6/16	Size of all committees are discretionary	Committee jurisdiction corresponds mostly with those of govt ministries	Yes (in one specialised/law-making committee and in one non-legislative committee)	Yes
Lithuania	0	0	14	0	-	14	7/16	Size of all committees are discretionary (max and min size is regulated)	Committee jurisdiction corresponds mostly with those of govt ministries	Yes (each MP may serve as a member of only one committee, except participation in the Committee on European Affairs)	Yes

TABLE 4b.3 Structure of parliamentary committees (continued)

	Number of committees						Size of permanent committees (min/max)	How the size of permanent committees are determined	How the jurisdictions of permanent committees are determined	Existence of formal restrictions in the number of committees a single parliament member may serve	Possibility to establish subcommittees
	ad hoc	permanent									
		legislative by function	specialised	non-law making	joint committees	total					
Poland	5	1	23	1	-	25	7/55	Size of all committees are discretionary	Committee jurisdiction corresponds mostly with those of govt ministries	Yes (each MP can serve in no more than two standing committees)	Yes
Romania	0	1	13	3	4	21	5/31	Size of all committees are discretionary (max size is regulated – 40 MPs)	Committee jurisdiction corresponds mostly with those of govt ministries	Yes (each MP can serve only in one committee and in addition be a member in one of the following: Committee for Standing Order, Commission for information technologies and communications, Committee for European Integration)	Yes
Slovakia	0	1	11	5	-	17	11/14	Size of all committees are discretionary	Committee jurisdiction corresponds mostly with those of govt ministries	No (in practise it is common that MPs serve in more than one committee)	Yes
Slovenia	2	0	13	5	1	19	5/25	Size of most committees are discretionary	About a half of the committee jurisdictions corresponds with those of govt ministries	No (in practise it is common that MPs serve in more than one committee)	Yes

TABLE 4b.4 Committee procedures (continues)

	How the membership is determined	Who selects committee chairs	How committee chairs are allocated	Procedure if a member changes his/her party	Publicity of committee deliberations	Are committee minorities allowed to submit minority reports	Committee stage in deliberation
Bulgaria	Allocated according to the proportionality principle	Committee itself	Allocated proportionally among parties	Committee seats belong to a party	All/most meetings are public, all/most meetings are open to parliament members, committee deliberations are open to the press	Yes	Before plenary stage (After receiving a draft act, the President of the National Assembly will assign a main Rapporteur Committee on the bill. Standing Committees submit a "motivated" report to the President of the National Assembly and the Chairperson of the main Rapporteur Committee. Reports on the bill are presented to the National Assembly by the Committees for the purposes of the first reading.)
Czech Republic	Chamber of Deputies elects the members	Committee itself	Allocated proportionally among parties (in 1992-1996 term, opposition had no chairs)	Committee seat is personal (except the seat in Organisational Committee)	All/most meetings are public (Immunity Committee always non-public; Organising Committee as a rule non-public)	Yes	Before plenary stage (Draft acts are first assigned to the Organizing Committee. A leading committee is proposed and a reporting person for the first reading is designated. In the 1st reading, the draft act is introduced by the proposer, after that a reporting person shall speak. Following the general parliamentary debate, if the Chamber of Deputies decides to proceed with the draft act, it will assign the draft act for discussion to a committee)
Estonia	The Board of the Riigikogu distributes the positions based on requests by parties. Memberships in practice allocated proportionally among parties	Committee itself (the parties also negotiate who will chair the parties)	Most of the chairs belong to the majority parties forming the government	Committee seats belong to a party	As a rule non-public, most meetings are open to parliament members	Yes	Before plenary stage (After receiving a draft act, the Board shall appoint a leading committee. The first reading of draft legislation shall be entered on the agenda on the motion of the leading committee. At the first reading of draft legislation, the general principles of the draft legislation shall be deliberated.)

TABLE 4b.4 Committee procedures (continued)

	How the membership is determined	Who selects committee chairs	How committee chairs are allocated	Procedure if a member changes his/her party	Publicity of committee deliberations	Are committee minorities allowed to submit minority reports	Committee stage in deliberation
Hungary	Memberships in practice allocated proportionally among parties	The house	On the basis of political agreement between parliamentary parties. Most of the chairs usually belong to the majority parties forming the govt	Committee seats belong to a party	All/most meetings are public, all/most meetings are open to parliament members, committee deliberations are open to the press	Yes	Before plenary stage (After receiving a draft act, the Speaker names the designated committee. In the beginning of the general debate, the rapporteur of the designated committee presents the recommendation of the committee. After this, proposed amendments may be introduced to the bill until the closure of the general debate after which the designated committee assesses the proposed amendments and take a position on whether it supports them or not and the committee shall submit to Parliament the proposed amendments in its recommendation preparing the debate in detail)
Latvia	Memberships in practice allocated proportionally among parties	The committee itself	Most of the chairs usually belong to the majority parties forming the govt	Committee seats are personal or belongs to a party depending on a situation	All/most meetings are public, all/most meetings are open to parliament members	Yes	Before plenary stage (After a draft act is received, a leading committee is appointed (unless Saeima reject the draft act). The committees to which the Saeima has forwarded a draft law may prepare their alternative draft law to be considered at the first reading)
Lithuania	Assembly of Elders decide the 'norms of representation' in the committees according to principle of proportional representation	The committee itself	All chairs usually belong to the majority parties forming the govt	Committee seats belong to a party	All/most meetings are public, all meetings are open to parliament members, all/most meetings open to the press	Yes	After plenary stage (After the draft act is submitted it is referred to different quarters, incl. different committees. The initiator of the act presents the draft and whatever conclusions have been received (incl. conclusions from committees) to the Seimas. If the Seimas decides to commence the procedure of consideration of the draft, a principal committee is decided upon.)

TABLE 4b.4 Committee procedures (continued)

	How the membership is determined	Who selects committee chairs	How committee chairs are allocated	Procedure if a member changes his/her party	Publicity of committee deliberations	Are committee minorities allowed to submit minority reports	Committee stage in deliberation
Poland	The Chancellery's Office of the Sejm Committees decides the allocation. Allocated according to the proportionality principle	The committee itself (the parties also negotiate who will chair the parties)	Allocated proportionally among parties (but govt parties have bigger proportion of the chairs than their share of seats in the Sejm)	Committee seats are personal (typically MPs who change their parties remain in the committee and parties appoint new members to the "party" seat.)	All/most meetings are public	Yes	Before plenary stage (received bill is put on a plenary session of the Sejm for a general debate and then referred to a committee.)
Romania	Agreement between the leaders of parliamentary groups. In practice allocated proportionally among parties	Committee itself (in practise the parties negotiate who will chair the parties)	Allocated proportionally among parties	Committee seats belong to a party	As a rule the meetings are not public (committee can make exception)	Yes	Before plenary stage (Received draft laws are forwarded to standing committees. The deputies, the parliamentary groups or the Government have the right to submit amendments to the leading committee which shall draw up a report which includes proposals regarding the passing or the modification or rejection of the draft. Leading committee presents its report and a general debate is held.)
Slovakia	Memberships in practice allocated proportionally among parties. Method of allocation is based on a custom	The house (the parties also negotiate who will chair the parties)	Allocated proportionally among parties	Committee seats belong to a party	All/most meetings are public, all/most meetings are open to parliament members	Yes	Before plenary stage (After receiving the draft act, the President of the National Council shall propose a lead committee responsible for such a bill. The bill shall be presented by the person introducing it and followed by the Rapporteur designated by the lead committee. The bill, in particular the fundamental merits of the bill, shall be discussed in a general debate, in which no proposals or amendments shall be made.)

TABLE 4b.4 Committee procedures (continued)

	How the membership is determined	Who selects committee chairs	How committee chairs are allocated	Procedure if a member changes his/her party	Publicity of committee deliberations	Are committee minorities allowed to submit minority reports	Committee stage in deliberation
Slovenia	The Bureau of the President of the National Assembly makes the decision. Broad rules determined by the rules of procedure, in practise allocated proportionally among parties	The Bureau of the President of the National Assembly (president, vice-presidents and leaders of parliamentary groups)	Allocated proportionally among parties	Committee seats belong to a party	All/most meetings are public	Yes	Before plenary stage (Before submitting a draft law, the proposer of the law may propose a preliminary reading be held. If the Bureau accepts the proposal to hold a preliminary reading, the President of the National Assembly also determines in which working body such reading will be held. Then, at least ten deputies may request the National Assembly further hold a general debate after which a decision is made whether the draft law is eligible for further reading. If decision is affirmative, the legislative procedure continues. The President of the National Assembly appoints the working body responsible)

TABLE 4b.4 Committee procedures (continued)

	How the membership is determined	Who selects committee chairs	How committee chairs are allocated	Procedure if a member changes his/her party	Publicity of committee deliberations	Are committee minorities allowed to submit minority reports	Committee stage in deliberation
Hungary	Memberships in practice allocated proportionally among parties	The house	On the basis of political agreement between parliamentary parties. Most of the chairs usually belong to the majority parties forming the govt	Committee seats belong to a party	All/most meetings are public, all/most meetings are open to parliament members, committee deliberations are open to the press	Yes	Before plenary stage (After receiving a draft act, the Speaker names the designated committee. In the beginning of the general debate, the rapporteur of the designated committee presents the recommendation of the committee. After this, proposed amendments may be introduced to the bill until the closure of the general debate after which the designated committee assesses the proposed amendments and take a position on whether it supports them or not and the committee shall submit to Parliament the proposed amendments in its recommendation preparing the debate in detail)
Latvia	Memberships in practice allocated proportionally among parties	The committee itself	Most of the chairs usually belong to the majority parties forming the govt	Committee seats are personal or belongs to a party depending on a situation	All/most meetings are public, all/most meetings are open to parliament members	Yes	Before plenary stage (After a draft act is received, a leading committee is appointed (unless Saeima reject the draft act). The committees to which the Saeima has forwarded a draft law may prepare their alternative draft law to be considered at the first reading)
Lithuania	Assembly of Elders decide the 'norms of representation' in the committees according to principle of proportional representation	The committee itself	All chairs usually belong to the majority parties forming the govt	Committee seats belong to a party	All/most meetings are public, all meetings are open to parliament members, all/most meetings open to the press	Yes	After plenary stage (After the draft act is submitted it is referred to different quarters, incl. different committees. The initiator of the act presents the draft and whatever conclusions have been received (incl. conclusions from committees) to the Seimas. If the Seimas decides to commence the procedure of consideration of the draft, a principal committee is decided upon.)

TABLE 4b.4 Committee procedures (continued)

	How the membership is determined	Who selects committee chairs	How committee chairs are allocated	Procedure if a member changes his/her party	Publicity of committee deliberations	Are committee minorities allowed to submit minority reports	Committee stage in deliberation
Poland	The Chancellery's Office of the Sejm Committees decides the allocation. Allocated according to the proportionality principle	The committee itself (the parties also negotiate who will chair the parties)	Allocated proportionally among parties (but govt parties have bigger proportion of the chairs than their share of seats in the Sejm)	Committee seats are personal (typically MPs who change their parties remain in the committee and parties appoint new members to the "party" seat.)	All/most meetings are public	Yes	Before plenary stage (received bill is put on a plenary session of the Sejm for a general debate and then referred to a committee.)
Romania	Agreement between the leaders of parliamentary groups. In practice allocated proportionally among parties	Committee itself (in practise the parties negotiate who will chair the parties)	Allocated proportionally among parties	Committee seats belong to a party	As a rule the meetings are not public (committee can make exception)	Yes	Before plenary stage (Received draft laws are forwarded to standing committees. The deputies, the parliamentary groups or the Government have the right to submit amendments to the leading committee which shall draw up a report which includes proposals regarding the passing or the modification or rejection of the draft. Leading committee presents its report and a general debate is held.)
Slovakia	Memberships in practice allocated proportionally among parties. Method of allocation is based on a custom	The house (the parties also negotiate who will chair the parties)	Allocated proportionally among parties	Committee seats belong to a party	All/most meetings are public, all/most meetings are open to parliament members	Yes	Before plenary stage (After receiving the draft act, the President of the National Council shall propose a lead committee responsible for such a bill. The bill shall be presented by the person introducing it and followed by the Rapporteur designated by the lead committee. The bill, in particular the fundamental merits of the bill, shall be discussed in a general debate, in which no proposals or amendments shall be made.)

TABLE 4b.4 Committee procedures (continued)

	How the membership is determined	Who selects committee chairs	How committee chairs are allocated	Procedure if a member changes his/her party	Publicity of committee deliberations	Are committee minorities allowed to submit minority reports	Committee stage in deliberation
Slovenia	The Bureau of the President of the National Assembly makes the decision. Broad rules determined by the rules of procedure, in practise allocated proportionally among parties	The Bureau of the President of the National Assembly (president, vice-presidents and leaders of parliamentary groups)	Allocated proportionally among parties	Committee seats belong to a party	All/most meetings are public	Yes	Before plenary stage (Before submitting a draft law, the proposer of the law may propose a preliminary reading be held. If the Bureau accepts the proposal to hold a preliminary reading, the President of the National Assembly also determines in which working body such reading will be held. Then, at least ten deputies may request the National Assembly further hold a general debate after which a decision is made whether the draft law is eligible for further reading. If decision is affirmative, the legislative procedure continues. The President of the National Assembly appoints the working body responsible)

TABLE 4b.5 Committee powers (continues)

	Initiative powers of committees	Powers to revise legislative bills	Powers to compel witnesses in hearings	Powers to demand documents from the government	Openness of hearings	Existence of a special budget research organisation within the legislature	Distributional attributes index[1]
Bulgaria	Can consolidate or split legislative bills, (ind. MPs can propose legislation) (1)	All committees have a right to re-write and amend legislative bills (2)	All committees have this right	All committees have this right	Public unless a committee decides otherwise	No	3
Czech Republic	No committee has these rights (ind. MPs can propose legislation) (0)	Can propose amendments, House considers original bill, amendments included in a Committee resolution (1)	All committees have this right	All committees have this right	Public unless a committee decides otherwise (in practise rarely non-public)	No	1
Estonia	All committees have a right to initiate legislation (in practise used 'sometimes but not very often') and to consolidate or split legislative bills (1+1)	All committees have a right to re-write and amend legislative bills (2)	All committees have this right	All committees have this right	Private	Analysis department which helps committees and MPs to do research, including budgetary research	4
Hungary	All committees have a right to initiate legislation (in practise used rarely: 1-2 times every 4 years) (1)	Can propose amendments, House considers original bill, amendments included in a Committee recommendation (1)	All committees have this right	All committees have this right	Public or private; committee decides (in practise rarely non-public; the hearings of the committee on national security are usually non public)	No	2
Latvia	All committees have a right to initiate legislation and to consolidate or split legislative bills (in 2002: total of 420 draft bills presented, 62 by committees, 252 by cabinet) (1+1)	All committees have a right to amend legislative bills. (Prior to 1st reading, the Committees can re-write legislative bills. The re-written draft bill is then considered in the House together with the original text (if the orig. text is submitted by cabinet) and one of these versions is adopted. The committees are again permitted to submit amendments for the 2nd reading.) (2)	No	All committees have this right	Public or private (in practise rarely non-public; only hearings of National Security Committee as a rule non-public)	No	4

TABLE: 4b.5 Committee powers (continued)

	Initiative powers of committees	Powers to revise legislative bills	Powers to compel witnesses in hearings	Powers to demand documents from the government	Openness of hearings	Existence of a special budget research organisation within the legislature	Distributional attributes index [1]
Lithuania	All committees have a right to initiate legislation (1)	All committees have a right to re-write and amend legislative bills (2)	All committees have this right	All committees have this right	As a rule public (committee can decide otherwise)	No	3
Poland	All committees have a right to initiate legislation, consolidate or split legislative bills (during 93-97 term, about a half of the bills were presented by the Govt and less than 7 % by the committees. Over 66 % and over 10 % of the enacted bills were proposed by the Govt and the Committees, respectively). (1+1)	All committees have a right to re-write and amend legislative bills (in practise re-writing happens very rarely) (2)	No (only the Inquiry Committee)	All committees have this right	Always public	Yes (number of staff: 8+3 professors working in collaboration with the parliament)	4
Romania	All committees have a right to initiate legislation, consolidate/split bills (1+1)	Committees have a right to re-write and amend legislative bills (2)	All committees have this right	All committees have this right	As a rule, non-public	No	4
Slovakia	All committees have a right to initiate legislation (in practise used rarely) (1)	Can propose amendments, House considers original bill, amendments included in a Committee report (1)	All committees have this right	All committees have this right	Public or private (in practise rarely non-public)	No	2
Slovenia	Most committees have a right to consolidate or split legislative bills (1)	Until 2002: Can propose amendments, House considers original bill, amendments included in a Committee report. Since 2002: Most committees have a right to re-write and amend legislative bills (-02:1, 02-:2)	Most committees have this right	Most committees have this right	Public or private (in practise rarely non-public)	No	-02:2 02-: 3
						mean all	*3,0 (pre-02:2,9)*
						mean commitment	*3,1*
						mean delegation	*2,5*

1 Distributional attributes index (formed by adding one for each of the following criteria, max 4 points): PCs can initiate legislation, PCs can consolidate/split legislation, PCs can amend legislation and amendments are included in a report/recommendation (1 point), PCs can re-write original government bill (2 points). Numbers in parentheses refer to awarded points.

TABLE 4b.6 Informational attributes of the parliamentary committees

	Ministry correspondence	**Procedure to allocate chair**	**Powers to compel witnesses**	**Powers to demand documents**	**Informational attributes index**[1]
Bulgaria	Yes (1)	Proportional (1)	Yes (1)	Yes (1)	4
Czech Republic	Partial (0)	Until 2002: majoritarian; since 2002: prop. (-02:0, 02-:1)	Yes (1)	Yes (1)	-02: 2; 02-: 3
Estonia	Yes (1)	Majoritarian (0)	Yes (1)	Yes (1)	3
Hungary	Yes (1)	Majoritarian (0)	Yes (1)	Yes (1)	3
Latvia	Yes (1)	Majoritarian (0)	No (0)	Yes (1)	2
Lithuania	Yes (1)	Majoritarian (0)	Yes (1)	Yes (1)	3
Poland	Yes (1)	Proportional (1)	No (0)	Yes (1)	3
Romania	Yes (1)	Proportional (1)	Yes (1)	Yes (1)	4
Slovakia	Yes (1)	Proportional (1)	Yes (1)	Yes (1)	4
Slovenia	Partial (0)	Proportional (1)	Yes (1)	Yes (1)	3
				mean all	*3,2 (pre-02: 3,1)*
				mean commitment	*3,3*
				mean delegation	*3,0*

1 Informational attributes index (formed by adding one for each of the following criteria, max 4 points): PCs' jurisdiction corresponds with those of ministries, committee chairs are allocated proportionally, PCs can compel witnesses and demand documents. Numbers in parentheses refer to awarded points.

TABLE 4b.7 The role of budgetary committee (continues)

	Role of standing committees			Role of budget committee			Who participates in the hearings of the committees when they are dealing with the draft budget
	revision of draft budget	**proposal of amendments**	**attendance in budget committee**	**collects and summarises the reports and amendments by the standing committees**	**can submit its own amendments to the draft budget**	**can reject the budget amendments made by the standing committees**	
Bulgaria	Review only those parts that fall into heir jurisdiction	Can propose amendments to only those parts that fall into their jurisdiction	No	Yes	Yes	Yes	Finance minister, other ministers, civil servants from MoF and other ministries, an expert employed by legislature, outside experts
Czech Republic	Review only those parts that fall into heir jurisdiction	Can propose amendments to only those parts that fall into their jurisdiction	Yes	Yes	Yes	No	Finance minister, other ministers, civil servants from MoF and other ministries, an expert employed by legislature
Estonia	Review all parts of the budget	As a rule, can propose amendments to only those parts that fall into their jurisdiction, sometimes also to all parts	Yes	Yes	Yes	Yes	Finance minister, other ministers, civil servants from MoF and other ministries
Hungary	Review only those parts that fall into heir jurisdiction	Can propose amendments to all parts of the draft budget	No	Yes	Yes	No (but it negotiates about the amendments)	Civil servants from MoF and other ministries, experts employed by legislature
Latvia	Review only those parts that fall into heir jurisdiction	Can propose amendments to all parts of the draft budget	No	Yes	Yes	No	Finance minister, other ministers, civil servants from MoF and other ministries

TABLE 4b.7 The role of budgetary committee (continued)

	Role of standing committees			Role of budget committee			Who participates in the hearings of the committees when they are dealing with the draft budget
	revision of draft budget	proposal of amendments	attendance in budget committee	collects and summarises the reports and amendments by the standing committees	can submit its own amendments to the draft budget	can reject the budget amendments made by the standing committees	
Lithuania	Review only those parts that fall into heir jurisdiction	Can propose amendments to all parts of the draft budget	Yes	Yes	Yes	Yes	Other ministers, civil servants from MoF and other ministries
Poland	Review all parts of the draft budget	Can propose amendments to all parts of the draft budget	Yes	Yes	Yes	Yes	Finance minister, other ministers, civil servants from MoF and other ministries, experts employed by legislature, other MPs
Romania	Review only those parts that fall into heir jurisdiction	Can propose amendments to only those parts that fall into their jurisdiction	Yes	Yes	Yes	No	Finance minister, other ministers, civil servants from MoF and other ministries
Slovakia	Review all parts of the draft budget	Can propose amendments to all parts of the draft budget	No	Yes	Yes	No	Finance minister, other ministers, civil servants from MoF and other ministries, experts employed by legislature, other MPs
Slovenia	Review only those parts that fall into heir jurisdiction	Can propose amendments to only those parts that fall into their jurisdiction	No	Yes	Yes	No	Finance minister, other ministers, civil servants from MoF and other ministries

Annex 4c Monitoring and implementation stages

TABLE 4c.1 Monitoring of the budget implementation (continues)

	Institution that monitors the implementation of the budget within the govt	**Level of specificity in monitoring spending**	**Level of specificity in monitoring revenue**	**Lag between cash flows and reporting**	**Frequency of public reports on budget outcomes**	**Parliament's role in monitoring of the budget**	**Central Bank's role in monitoring of the budget**
Bulgaria	Independent body (Agency for internal financial control)	General and central government, individual ministries specific chapters of the budget, social sector monitored separately, regional governments monitored separately	Revenue according to the source	Real time information for the cash flows	Monthly, quarterly, yearly	Informed only if it requests information and in case of deviations from the budget	No role
Czech Republic	Finance Ministry	Central govt, individual ministries, specific budget chapters, social sector and regional govts monitored separately	Total revenue, revenue according to source	Days for state budget chapters, some months for social sector and regional govts	Monthly, quarterly, annually	Informed automatically on the implementation of the budget	No role
Estonia	Finance Ministry	Central government, individual ministries	Total revenue, revenue according to source	No answer provided	Monthly, bi-annually, annually	Informed automatically on the implementation of the budget	No role
Hungary	Finance Ministry and Hungarian State treasury supervised by the MoF.	Central govt, individual ministries, specific budget chapters, social sector and local govts monitored separately	Revenue according to the source	2-5 days for central level of government (including extra-budgetary funds and social security funds), 30 days for quarterly report of local governments	Monthly	Informed automatically on the implementation of the budget (monthly)	No role

TABLE 4c.1 Monitoring of the budget implementation (continued)

	Institution that monitors the implementation of the budget within the govt	Level of specificity in monitoring spending	Level of specificity in monitoring revenue	Lag between cash flows and reporting	Frequency of public reports on budget outcomes	Parliament's role in monitoring of the budget	Central Bank's role in monitoring of the budget
Latvia	Finance Ministry	Central and general government, individual ministries	Total revenue, revenue according to source	1-15 days, for some sectors months	Monthly, quarterly, annually	Informed automatically on the implementation of the budget	Central Bank monitors fiscal developments: the president of the Bank of Latvia may participate in the Cabinet meetings and has a consultative role on the fiscal matters; in case of disagreements on fiscal policy, the president of the Bank of Latvia makes public statement; regular reports of the Central Bank cover the fiscal situation in Latvia.
Lithuania	Finance Ministry	Individual ministries, specific chapters of the budget. social sector monitored separately, regional governments monitored separately	Total revenue, revenue according to source	Days for central level of government	Monthly, quarterly, annually	Informed automatically on the implementation of the budget	No role
Poland	Finance Ministry	General govt (annually), Central government, individual ministries specific chapters of the budget. social sector monitored separately, regional governments monitored separately (quarterly)	Total revenue, revenue according to the source	Usually one month, depending on the type of data, one day in case of budget account monitoring	Central budget – monthly, local government – quarterly, social security and labour funds – monthly, other funds – bi-annually or annually	Informed automatically on the implementation of the budget	No role (CB: The central bank is consulted regarding availability of funds in government accounts)

TABLE 4c.1 Monitoring of the budget implementation (continued)

	Institution that monitors the implementation of the budget within the govt	Level of specificity in monitoring spending	Level of specificity in monitoring revenue	Lag between cash flows and reporting	Frequency of public reports on budget outcomes	Parliament's role in monitoring of the budget	Central Bank's role in monitoring of the budget
Romania	Finance Ministry, Court of Accounts	Central and general government, individual ministries, specific chapters of the budget. social sector monitored separately	Total revenue, revenue according to source	For monthly data 25 days, quarterly data 3 months, annual data 6 months	Monthly, quarterly, annually	Informed automatically on the implementation of the budget	No role
Slovakia	Finance Ministry, Supreme Audit Office	Central and general government, individual ministries	Total revenue, revenue according to source	State administration: days	Quarterly	Informed automatically on the implementation of the budget	No role (the central bank makes independent analysis on the budget implementation)
Slovenia	Finance Ministry	Central govt, individual ministries, specific budget chapters, social sector monitored separately	Total revenue, revenue according to source	0 days for central government, individual ministries and specific chapters of the budget; 1-3 months for social security funds and regional govt	Monthly (Bulletin of govt finance), quarterly, annually (Annual Financial Report)	Informed automatically on the implementation of the budget (bi-annually)	No role

TABLE 4c.2 The role of Finance Minister in implementation

	Finance Minister can block expenditure (in-year)	**Finance Minister must approve disbursement of funds**	**Finance Minister can impose cash limits**	**Cash limits are department specific**	**Transfers are allowed between budget chapters**	**Finance Minister must approve transfers**	**Changes in budget law allowed during budget execution**	**Unused funds can be carried over into following year**	**Finance Minister index[1]**
Bulgaria	Yes (1)	Yes (1)	Yes (1)	Yes	Yes	Yes (1)	Yes	No	4
Czech Republic	No (0)	No (0)	Yes (1)	Yes	Yes (within certain limits)	No (requires authorisation from the govt, above certain limits P's Budgetary Committee has to approve) (0)	Yes	Yes (since 2001 within certain limits)	1
Estonia	No (if expenditure has been approved by parliament. MoF does have a right to amend the distribution of expenditure, or – on the proposal of the Treasury – to place temporary restrictions) (0)	Yes (1)	Yes (1)	No	No (only expenditures not classified in budget)	- (0)	Yes	Yes (in case of certain expenditures)	2
Hungary	No (can only make proposals to the govt) (0)	No (0)	No (0)	-	No (allowed only if reallocation does not affect the aim or purpose of the appropriations).	No (government) (0)	No	Yes (according to special rules established by the organic budget law)	0

TABLE 4c.2 The role of Finance Minister in implementation (continued)

	Finance Minister can block expenditure (in-year)	Finance Minister must approve disbursement of funds	Finance Minister can impose cash limits	Cash limits are department specific	Transfers are allowed between budget chapters	Finance Minister must approve transfers	Changes in budget law allowed during budget execution	Unused funds can be carried over into following year	Finance Minister index[1]
Latvia	Yes in practise (the govt makes the final decision) (1)	No (0)	No (0)	-	No (requires supplementary budget)	No (0)	Yes	Yes (for certain programmes)	1
Lithuania	No (0)	Yes (1)	No (0)	-	No (requires supplementary budget. Allowed: co-financing EU-related expenditure)	(Yes) (0)	Yes (in case of considerable deviation from the budget)	No until 2000, since 2001 yes for certain programmes	1
Poland	Yes (cabinet can revoke the MoF's decision, also cabinet can block expenditure) (1)	Yes (1)	Yes (cabinet agreement required) (1)	Yes	Yes (since 1999 only in state of emergency)	Yes (until 1998 by MoF, since 1999 by the govt) (-98: 1, 98-:0)	Yes	Yes (for certain programmes)	-99: 4 99-:3
Romania	No (the govt) (0)	Yes (1)	No (govt) (0)	Yes	Yes (within limits)	Yes (1)	Yes	No	2
Slovakia	Yes (in certain cases the govt must authorise MoF) (1)	No (0)	Yes (1)	Yes	Yes	Yes (1)	Yes	Yes (for some very limited categories)	3

TABLE 4c.2 The role of Finance Minister in implementation (continued)

	Finance Minister can block expenditure (in-year)	**Finance Minister must approve disbursement of funds**	**Finance Minister can impose cash limits**	**Cash limits are department specific**	**Transfers are allowed between budget chapters**	**Finance Minister must approve transfers**	**Changes in budget law allowed during budget execution**	**Unused funds can be carried over into following year**	**Finance Minister index[1]**
Slovenia	No (Govt can on the proposal of the MoF) (0)	No (0)	Yes (1)	Yes	Yes	No (as a rule, transfers between chapters are in jurisdiction of Govt, but on some limited issues, MoF can decide without Govt) (0)	No (Organic Budget Law can not be changed during the year; Annual Law on implementation of budget can be changed if for example supplementary Budget is prepared)	Yes (but only for donations and some other minor expenditures for special purposes)	1
								mean all	*1,8 (pre-98: 2,0)*
								mean commitment	*2,1*
								mean delegation	*0,5*

1 Finance Minister index (formed by adding one for each of the following criteria, max 4 points): MoF can block expenditure in-year, MoF must approve disbursement of funds, MoF can impose cash limits, MoF must approve transfers of funds between chapters. Numbers in parentheses refer to awarded points.

TABLE 4c.3 Unanticipated revenue and expenditure shocks (continues)

	Positive shock to the budget balance		**Negative shock to the budget balance**	
	Revenues are higher than projected in the budget plan	**Expenditures are lower than projected in the budget plan**	**Revenues are lower than projected in the budget plan**	**Expenditures are higher than projected in the budget plan**
Bulgaria	The Law on the Structure of the State Budget states that the MoF can authorize supplementary expenditure when such expenditure is offset by a surplus of own resources or by resorting to new sources of revenue, without causing the balance of the state budget to deteriorate. This is also what typically happens in practise.	No formal rules, in practise govt takes no action (overall budget balance improves), or supplementary budgets are used to increase in-year expenditures	No formal rules, supplementary budgets are common in this situation and they are used to cut in-year expenditures	The Council of Ministers approves supplementary budget (using the reserve for the event of urgent unexpected expenditure). In addition, MoF can shift credit from one budget chapter to another, provided that the state budget balance is maintained. This is also what typically happens in practise.
Czech Republic	In practice overall budget balance improves. (According to 2000 budget law, unanticipated revenue can no longer be spent without Parliamentary agreement. Approved expenditure thus represents an overall cap. This is subject to some minor exceptions).	In practise overall budget balance improves	Formal rules (included in the 2000 law on budget rules): the limits for the ministries are decreased, in case of lower tax income, the deficit will increase	Formal rules (included in the 2000 law on budget rules): higher expenditures must be compensated by decreasing other spending
Estonia	No formal rules, supplementary budgets are common in this situation and they are used to increase in-year expenditures	No formal rules, supplementary budgets are common in this situation to increase in-year expenditures	No formal rules, supplementary budgets are common in this situation and they are used to cut in-year expenditures	No formal rules, supplementary budgets are common in this situation and they are used to cut in-year expenditures

TABLE 4c.3 Unanticipated revenue and expenditure shocks (continued)

	Positive shock to the budget balance		**Negative shock to the budget balance**	
	Revenues are higher than projected in the budget plan	**Expenditures are lower than projected in the budget plan**	**Revenues are lower than projected in the budget plan**	**Expenditures are higher than projected in the budget plan**
Hungary	No formal rules, in practise govt takes no action (overall budget balance improves) or General Reserve is increased	No formal rules (has not happened in the previous years)	Govt has to take measures within authorisation provided by the organic or annual budget law (eg. cut or freeze expenditures). If the situation is critical for the deficit-target and can not be balanced by government measures, supplementary budget should be submitted to the Parliament.	Govt has to make measures within authorisation provided by the organic or annual budget law. Government must present supplementary budget to the Parliament, if the projected overall balance of aggregated central level of government (including Central Budget, Extra-budgetary Funds, Social Security Funds) is to deviate from the originally approved balance with more than 5 % of total expenditure of aggregated central level of government.
Latvia	No formal rules, in practise govt takes no action (overall budget balance improves) or supplementary budgets are used to increase in-year expenditures	No formal rules, in practise govt takes no action (overall budget balance improves)	In practise govt takes no action (overall budget balance worsens) or supplementary budgets are used to cut in-year expenditures. The Budget Law also states that if it is anticipated that fiscal deficit will exceed the level approved in the budget, the MoF shall propose to the govt to cut spending in the middle of the year and P has to approve the cuts (this has happened once in 1995).	Not allowed according to the Law on Budget and Financial Management
Lithuania	No formal rules (according to the 2000 Law on the Budget Structure the revenue received in excess of the plan while implementing the State budget and appropriations that are no longer valid may be used for the repayment of public debt and for covering the shortfalls of municipal budget tax revenue).	No formal rules (the 2000 Law on Budget Structure state that appropriations that are no longer valid may be used for the repayment of public debt and for covering the shortfalls of municipal budget tax revenue).	No formal rules (according to the 2000 Law on the Budget Structure when the amount of revenue received is less than the planned amount and the working capital of the State budget is not sufficient to cover temporary revenue shortfall until an appropriate amendment to the budget law is passed, financing of the programmes shall be carried out on the recommendation of the MoF in the manner prescribed by the Law on State Treasury).	No formal rules, supplementary budgets are common in this situation

TABLE 4c.3 Unanticipated revenue and expenditure shocks (continued)

	Positive shock to the budget balance		**Negative shock to the budget balance**	
	Revenues are higher than projected in the budget plan	**Expenditures are lower than projected in the budget plan**	**Revenues are lower than projected in the budget plan**	**Expenditures are higher than projected in the budget plan**
Poland	No formal rules, in practise govt takes no action (overall budget balance improves)	No formal rules, in practise govt takes no action (overall budget balance improves)	No formal rules, in practise expenditure is blocked so as to maintain the balance (at the end of the year) within the limits set	Would constitute a breach of the budget law
Romania	No formal rules, supplementary budgets are common in this situation and they are used to increase in-year expenditures (1996 Budget law: the revenue exceeding the level approved in the state budget shall be used to finance actions established by law or to reduce budgetary deficit or to increase budgetary surplus)	No formal rules, supplementary budgets are common in this situation to increase in-year expenditures	No formal rules, supplementary budgets are common in this situation and they are used to cut in-year expenditures	No formal rules, supplementary budgets are common in this situation and they are used to cut in-year expenditures
Slovakia	No formal rules. (General comment: Act on Budgetary Rules did not – prior to 2002 amendment – allow the possibility of supplementary budgets. As of 2002, this has been possible. Act of Budgetary Rules states that any budgetary chapter may go beyond the expenditure limit of its budget if permitted so by the Ministry. The overdraft may be up to the amount of higher revenues really achieved)	No formal rules (Act of Budgetary Rules states that unused resources in the current budgetary year - with the exception of the expenditures for salaries and levies - are passed to the following budgetary year with an approval of the MoF. These funds shall be transferred to a special current account for the usage for the same purpose in the following year.	No formal rules (Act of Budgetary Rules states that the Govt can authorise MoF to impose time or content constraint on the utilisation of budg. resources).	No formal rules (Act on Budgetary Rules only states that in certain cases specified by the Act any budg. chapter may go beyond the expenditure limit of its budget if permitted so by the MoF).
Slovenia	No formal rules, in practise govt takes no action (overall budget balance improves)	No formal rules, in practise govt takes no action (overall budget balance improves)	No formal rules, supplementary budgets are common in this situation and they are used to cut in-year expenditures	No formal rules, supplementary budgets are common in this situation and they are used to cut in-year expenditures (decrease in other expenditures allowed according Organic Budget Law)

TABLE 4c.4 The relationship between national government and sub-national governments (continues)

	Arrangements between the national government and sub-national governments to ensure that budgetary targets for general government are met	**Ability of the national government to restrict lower levels of government borrowing**
Bulgaria	Protocol of Agreement is in place between the national govt and sub-national govts	Restricted by law (MoF's approval is required)
Czech Republic	Yes (partially through the revenues of sub-national governments, which are limited by transfers from the state budget). Municipalities are required to report on budgetary developments each semester (see also the next column)	The system of sub-national govt was reformed in 2001, the reform eliminated existing limits on borrowing. Under the new system, municipalities can take on debt and may approve a deficit budget (provided municipal guarantees or collateral cover the planned shortfall). The central government regularly monitors sub-national public borrowing and has at its disposal penalties for municipalities that fail to provide required levels of collateral.
Estonia	Limits in place for taking financial obligations	The total sum of local government borrowing can not exceed 60 % of their annual budget revenue (except for targeted transfers from state budget). Payments to finance debt of local governments must not exceed 20% of budget income planned in the budget year (except for targeted transfers from state budget).
Hungary	Amount and composition of the budget transfers to local governments and distribution rules of taxes and certain revenues are established in budgeting process with respect to overall budget targets.	Law on Local Governments establishes restrictions and preconditions for borrowing by local govt
Latvia	Local govts are required by the law to submit information to the MoF regarding approved budgets.	Local govts have the right to make borrowings and issue guarantees only in the allowed total increased amount provided for in the annual state budget. Total local borrowing is overseen by an interministerial Council for Loans and Guarantees. Local governments borrow from treasury, which adds 50 basis points to market borrowings for onlending to local authorities. The Local Government Financial Stabilization Act of May 1998 applies a financial stabilization process to councils that are unable to meet their obligations.

TABLE 4c.4 The relationship between national government and sub-national governments (continued)

	Arrangements between the national government and sub-national governments to ensure that budgetary targets for general government are met	**Ability of the national government to restrict lower levels of government borrowing**
Lithuania	Law on Budgeting states that the budgets of local govts must be adopted without deficit (during the year the municipalities may be granted loans from the state budget). Law on Local Self-Government and Law on the Methodology of Determination of Municipal Budgetary Revenues specify state delegated functions.	(see previous column)
Poland	Public Finance Act sets limitations to earmarked reserves (may not exceed 5 % of budget expenditures) and general reserves (1 %). (See also next column)	There are limits on local government borrowing in the Public Finance Act. These limits are stricter than those for the central budget. Furthermore, local government borrowing is further restrained in case when public debt rises above 55% of GDP (no borrowing is allowed if debt reaches 60% of GDP)
Romania	According to the 2002 Budget Law, the openings of the credits to performs transfers on local budgets, within the limits provided by the state budget, are made through local general public finances boards of Ministry of Finance, on demand of the local primary credit orders and depending on the necessities of the budgetary with the observance of destination. Law on Local Public Finance specifies the distribution of revenues btw State Budget and local govt budgets.	Law on Local Public Finance states that local govt borrowing is allowed only to the extent that the debt service will not exceed 20 % of total current revenue of the local budget
Slovakia	Municipalities' share of expenditures and revenues of general govt has been small but fiscal decentralisation is now being increased. As a result new practices are being developed.	Borrowing in excess of a prescribed level of municipalities' own revenue requires approval from the MoF
Slovenia	No	In practise MoF must approve any borrowing of local govt. Local govt liquidity borrowing is limited to 5 % of the local budget.

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