



# *Pacific Islands Workshop*

## *Building Resilience to Natural Disasters and Climate Change*



*April 4-6, 2017 | Suva, Fiji*



# Medium Term Budget Framework

## Why and How

**High level workshop**  
Suva, April 4-7 2017

**Presenter**  
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# Outline

- I. Introduction
- II. Motivation and key features of an MTBF
- III. Institutions to support MTBF

# Introduction

- Natura Noverca (Plinius the old)
  - Nature as Stepmother (Cinderella style)
- Life is a beach (Southern California rendition)
- .... Sheet happens (Forrest Gump)

And when it rains... it pours...

**Samoa,** 2009 tsunami: **21.4% of GDP**

2012 cyclone Evan **26.6% of GDP**

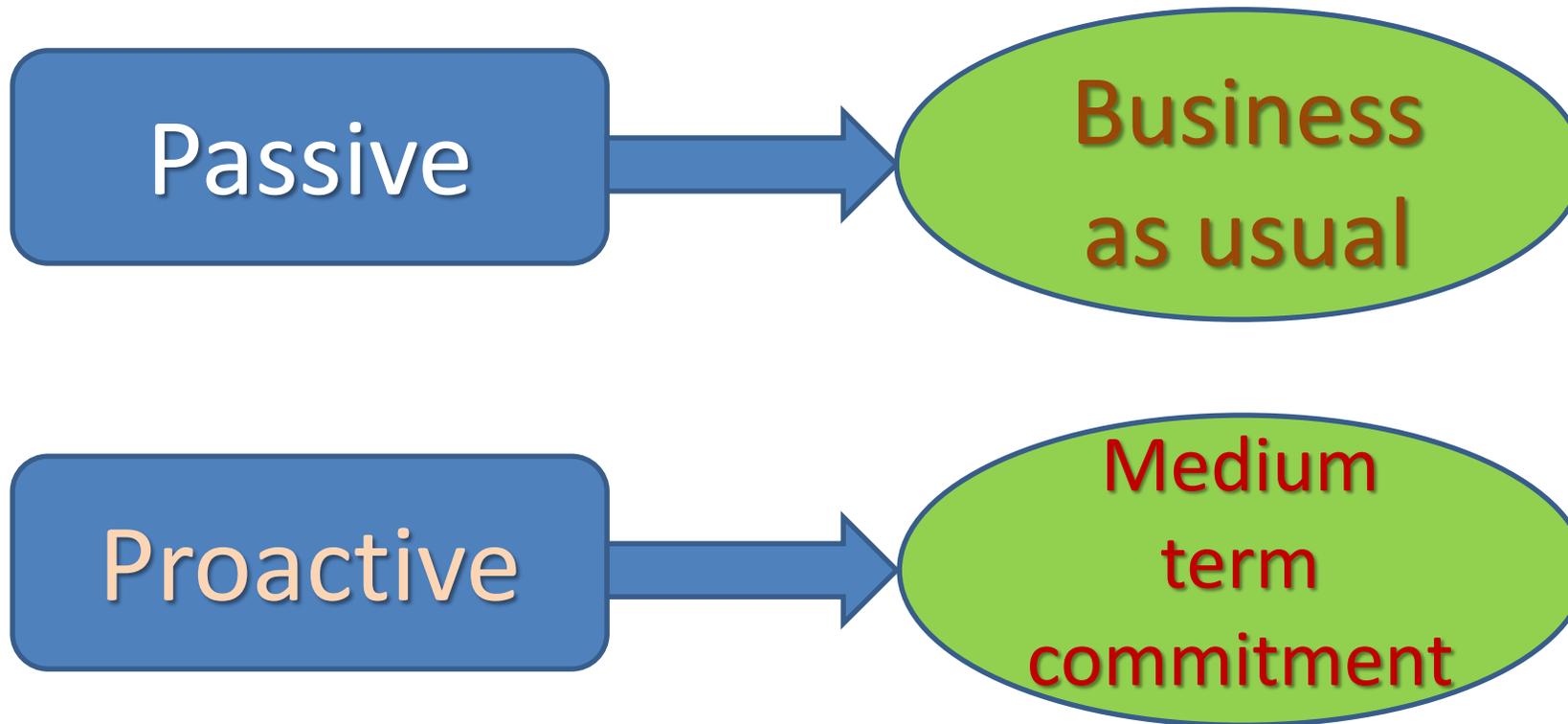
Projections are not encouraging...

**The Marshall Islands:** next 50 years 10% chance of incurring a loss of about **80% of GDP**

<http://pcrafi.sopac.org/documents/>

# Fundamental choice of approach:

**Passive** (fatalistic) or **Pro-active**?



# Proactive approach

*ESSENTIAL FACTOR FOR SUCCESS*

**Unwavering political commitment**

*SUPPORTING POLICY TOOLS/INSTITUTIONS*

- ❖ *Medium Term Budget Framework*
  - ❖ *Top-Down Budgeting*

# Definition of MTBF...

**A set of systems, rules, and procedures** to ensure that fiscal plans take into consideration:

- their impact over several years
- future events which may affect government accounts

**It includes:**

- requirements to present medium-term information at specific times
- procedures for making multi-year forecasts and plans for revenue and expenditure
- obligations to set numerical expenditure targets, whether binding or indicative, beyond the annual budget horizon

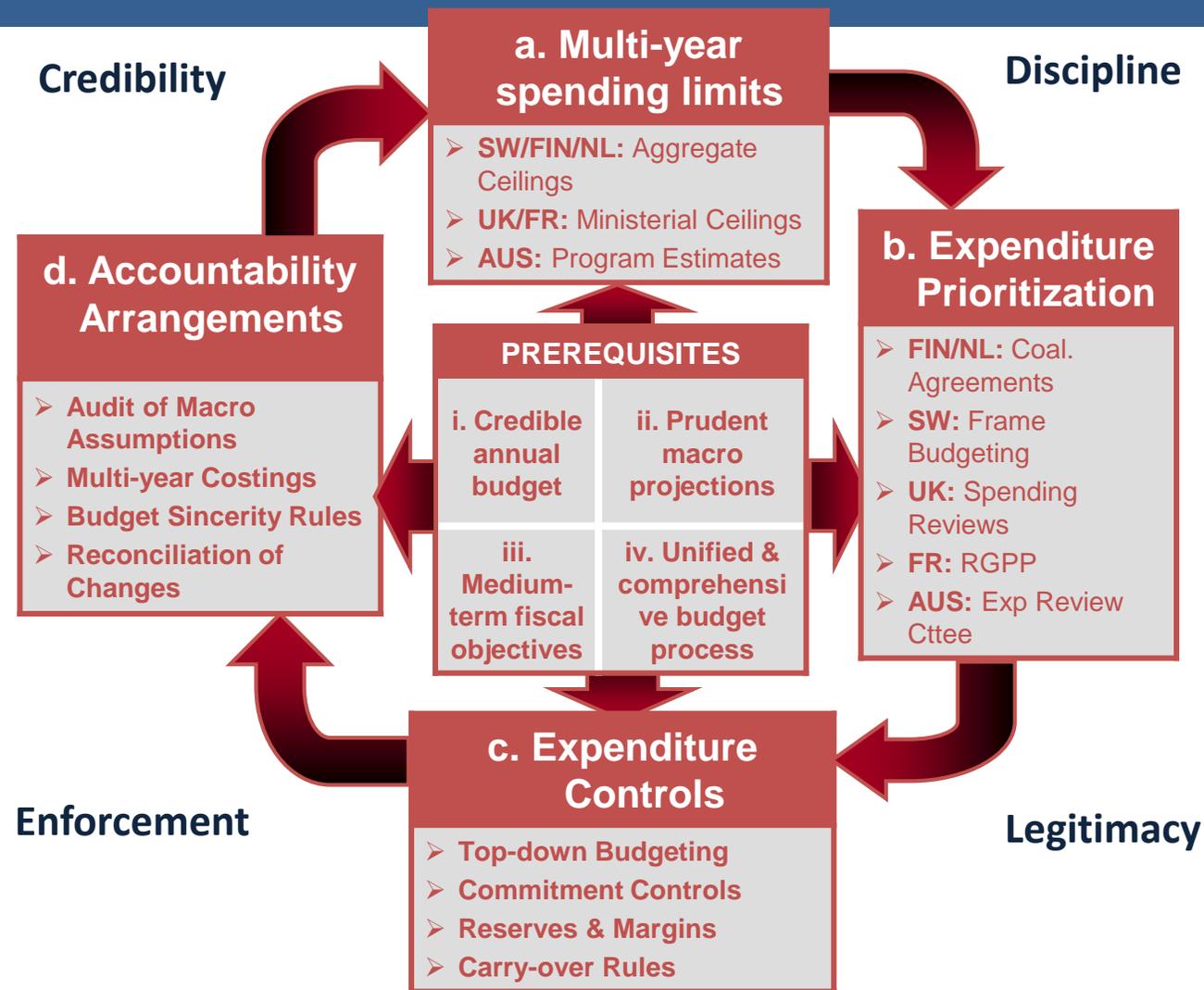
# Why MTBF matters

1. **Signaling future changes** → managing expectations and pressure to spend, and allowing time to adapt
2. **Capturing deferred effects** → decisions today have consequences tomorrow
3. **Making non-discretionary into discretionary** → all policies can be changed with enough time
4. **Committing to future expenditure limits** → binding limits addresses time-inconsistency of spending preferences
5. **Lags in public decision making** → decision and implementation and impact lags

# Goals of MTBF

- 1. To reinforce aggregate fiscal discipline** → presentation of deferred effects and restrictions on future budgets
- 2. To facilitate a more strategic allocation of expenditure** → early reaction to future adverse developments and provide an additional dimension in policy making
- 3. To encourage more efficient inter-temporal planning** → greater transparency and certainty to budget holders about their likely future resources

# Key Features of MTBFs

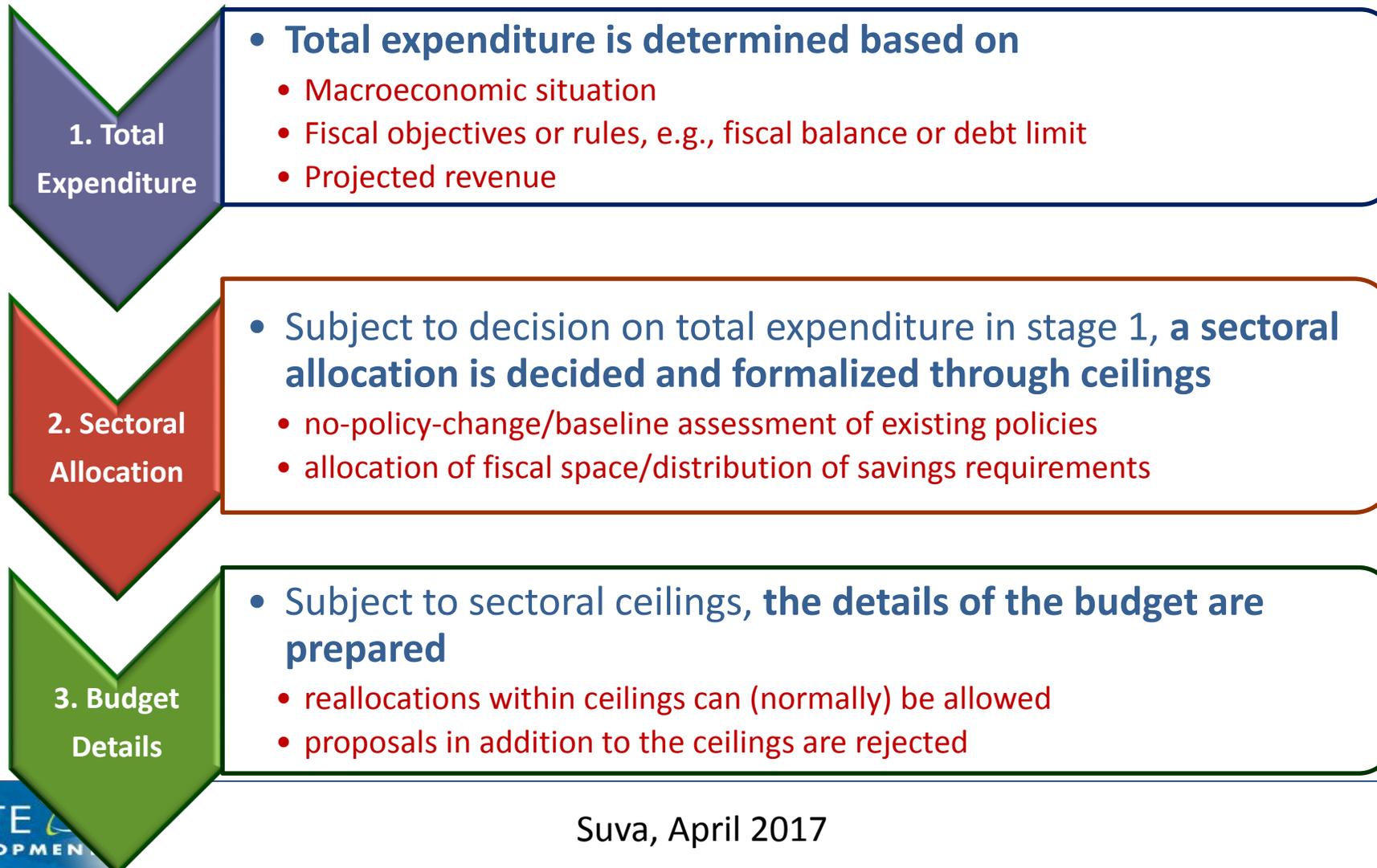


# Prerequisites

- a. Credible annual budget
- b. Prudent medium-term macroeconomic projections
- c. Stable medium-term fiscal objectives
- d. Comprehensive and unified budget process

# MTBF to be accompanied by...

## Top-Down Budgeting



# Key Features of a successful MTBF

- a. Multi-year spending limits
- b. Expenditure prioritization
  - Ex: Wage increase or investment in **resilient infrastructure**? (in the hands-on exercise)
- c. Expenditure controls
  - Ex: cost drivers and how to protect **reserves**
- d. Accountability arrangements

# Expenditure Controls

## i. Commitment Controls

MoF authorization needed before line ministries or ministers can enter into multi-year:

- **contractual** commitments
- **legal** commitments
- **policy** commitments

## ii. Key Cost Drivers & Risks

Residual MoF controls on:

- Workforce, pay, & pensions
- Guarantees and PPPs
- Acquisition/disposal of assets
- Tax expenditures

## iii. Reserves and Margins

Multiyear projections make provision for:

- **Reserve** for contingencies that arise during the budget year
- **Planning margin** to fund new policy measures in future budgets

## iv. Carryover Restrictions

Numerical restrictions on one or more of:

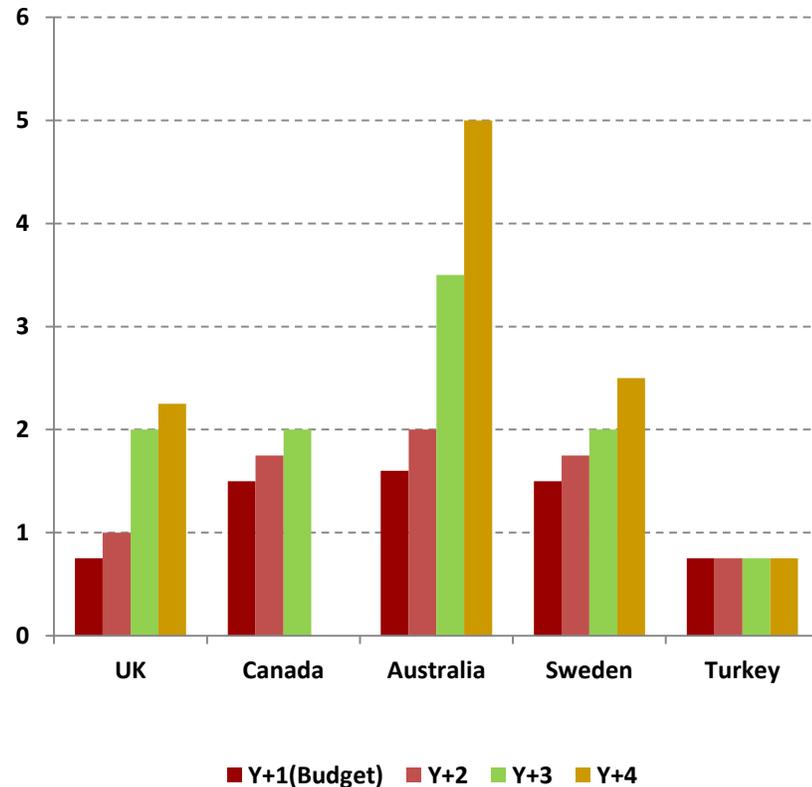
- Annual **accumulation** of underspends
- Total **stock** of accumulated carryover “entitlement”
- Annual **drawdown** of accumulated underspending over forthcoming year

# Contingency Reserves

## Size and Access Rules

### Contingency & Planning Reserves

(% of Government Expenditure)



### Typical Reserve Rules

Access Criteria: Expenditure must be:

- Unforeseeable
- Unavoidable
- Un-absorbable

Access Procedure: Ministry must state:

- How pressure matches criteria
- Mitigating actions taken
- Remaining pressure
- Action to address underlying cause

Reporting on Utilization:

- Qtrly to Cabinet on claims & “threats”
- Qtrly to Parliament on claims & balance
- NAO audit of claims against criteria
- Claims deducted from carryover stock

# Lessons from international experience

- MTBF preparation process follows a similar pattern in successful examples
  - Assessing the medium term impact of present decisions
  - Integration with budget process
  - Reconciliation of top-down/bottom-up approaches
  - Separation of baseline estimates from discussion of savings and new policies
- But diversity in role of forward years in future budget preparation
  - From rolling and indicative to fixed and binding...
  - ... but tailoring is common (UK, France, Sweden)
  - Reflects different objectives for the reform and pre-existing institutions
- Need to align MTBF preparation with fiscal objectives
  - Mutual reinforcement of MTEF and fiscal rules
  - Importance of scope consistency
- The MTBF development must be thought within the PFM reform agenda
  - In the end “medium term approach” should be a natural component of decision making

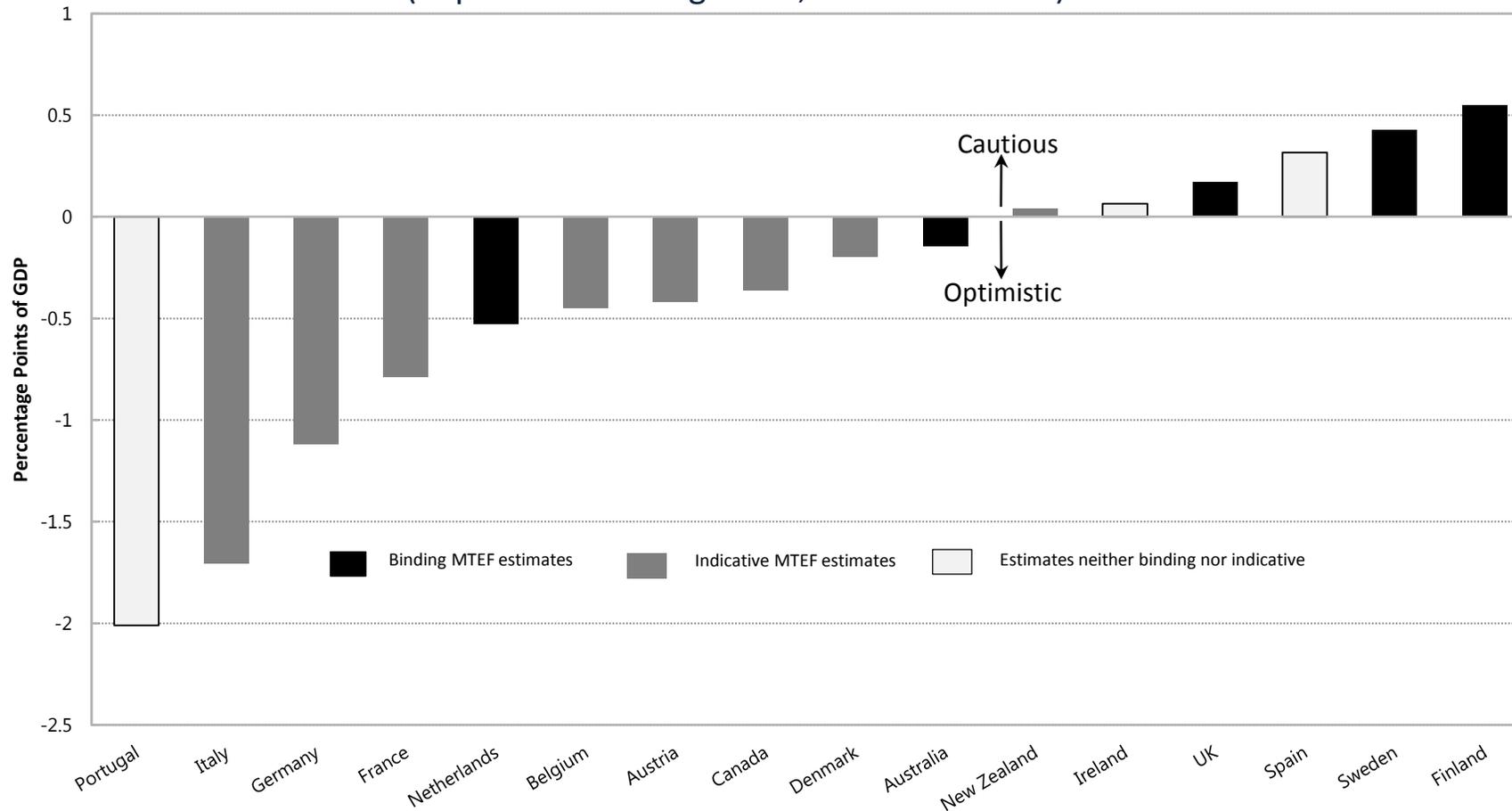
Thank you for your attention

# Annex

Extra slides covering different aspects  
touched in the presentation

# Prudent medium-term macroeconomic projections

Average Error in Forecasting Real GDP Growth, 2000-2007  
(In percent of real growth, Actual-Forecast)



# Medium-term fiscal objectives

Country	National objective	Supranational objective	Statutory base		Coverage		Time-frame	
			Political	Legal	Central	General	Annual	Multi-year
Australia	Balance, Debt	---	X			X		X
Brazil	Expenditure, Debt	---		X	X		X	
Chile	Balance	---	X		X			X
Canada	Expenditure, Balance, Debt	---	X		X		X	
France	Expenditure	Balance, Debt	X	X	X	X		X
Indonesia	Balance, Debt	---	X		X		X	
Japan	Expenditure	---		X	X			X
Mexico	Balance	---		X		X		X
Netherlands	Expenditure	Balance, Debt	X		X	X		X
Switzerland	Balance	---		X	X			X
UK	Balance, Debt	Balance, Debt	X			X		X

# A unified budget process

Issue	Explanation	Typical Challenges
Budget Coverage	No large extra-budgetary funds	Large Social Security and Health Funds
Budget Fragmentation	All expenditure authorized together	Budget split between current and capital
Earmarked Revenues	Limited earmarking of revenue to expenditure	Fuel surcharges for road maintenance
Standing Commitments	No input commitments that can conflict with overall ceiling	Laws requiring fixed budget transfer to specific purposes
Parliamentary Approval	Limited scope for Parliament to amend budget	Parliament can increase without finding reductions
Supplementary Budgets	Supplementary budgets are rare or expenditure neutral	Supplementaries are significant and impact policy

# Expenditure prioritization

COUNTRY	NO. OF 1 <sup>st</sup> LEVEL PRIORITIZATION UNITS	FIXITY		MEDIUM-TERM PRIORITIZATION DECISION IN GOV'T	PARLIAMENTARY STATUS	
		FIXED	INDICATIVE		LEGISLATED	FOR INFO
<b>MINISTERIAL ALLOCATIONS</b>						
United Kingdom	25	✓		✓		✓
Finland	12		✓	✓		✓
<b>FUNCTIONAL/PROGRAM ALLOCATIONS</b>						
Australia	270		✓	✓		✓
Austria	32		✓	✓	✓	
France	35	✓		✓	✓	
Netherlands	20		✓	✓		✓
Sweden	27		✓	✓		✓
<b>ECONOMIC CATEGORIES</b>						
Belgium	13		✓			✓
Japan	5		✓			✓
Mexico	7		✓			✓

# Accountability Arrangements

## Budget Sincerity Provisions

What are they?

Legal obligation on the MoF to certify that budget projections presented to Parliament reflect:

- all policy decisions announced by the government; and
- any other circumstances that may have an impact on the economic or fiscal outlook.

Examples

- NZ Fiscal Responsibility Act (1994)
- Australia Charter of Budget Honesty (1998)
- UK Code for Fiscal Stability (1998)

## Reconciliation of Changes to Ceilings

Factor	Explanation	Examples
<b>Macro-economic</b>	Revisions to macroeconomic parameters	GDP, inflation, exchange rate
<b>Other Parameters</b>	Revisions to operational parameters	Prices of goods, volumes of claimants
<b>Accounting Adjustments</b>	Revisions in accounting treatment	Reclassifying expenditure between ministries
<b>Policy Measures</b>	Discretionary additions or cuts to ceilings	New investment, efficiency savings
<b>Carryovers</b>	Net drawdown or accumulation of carryovers	As authorized by MoF at start of year
<b>Over/Under Spending</b>	Operational overruns or underspends	Claims on reserve, unauthorized overspending