Good Practices in Fiscal Risks Disclosure International Experience

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Sources of Fiscal Risk

- Fiscal risks arise from macroeconomic shocks and the realization of contingent liabilities.
- Sources of macroeconomic shocks include real GDP growth, inflation, commodity prices, and interest and exchange rates.
- Contingent liabilities are obligations triggered by an uncertain event and can be:
  - Explicit (i.e., those defined by law or contract, such as debt guarantees); and
  - Implicit (arising from government ownership of SOEs, expectations that CG "stands behind" subnational levels of government, public expectations that Government will provide assistance, e.g., following natural disasters, to depositors in event of bank failures, to deliver public services if PPPs fail).

Why Disclose Fiscal Risks?

- Strengthens incentives to ensure that all risks are identified, estimated and carefully managed.
- Promotes earlier, smoother policy responses.
- Increases confidence amongst stakeholders in the quality of fiscal management.
- Reduces uncertainty for investors and taxpayers.
- Improves access to international capital markets (some empirical evidence).
- There is an international trend to greater disclosure.

Macroeconomic Shocks

- Fiscal risks from macroeconomic shocks are disclosed by many countries, including all EU countries, most OECD members, and some emerging market countries (e.g., Brazil, Chile, Indonesia).
- Modalities:
  - Sensitivity analysis (e.g., minimum wage in Brazil).
  - Alternative macroeconomic scenarios (New Zealand).
  - Uncertainty surrounding baseline projections is sometimes illustrated through a fan chart (US).
  - Stress tests.

New Zealand

- Clear responsibilities for macroeconomic and fiscal forecasting (to ensure budgets are realistic and based on good technical judgments).
- Independent experts assess the fiscal forecasts, the macroeconomic forecasts on which they are based, and their underlying assumptions.
- Estimates are made of the sensitivity of the budget and medium-term fiscal forecasts to variations in the key assumptions on which the forecasts are based.
- Alternative macroeconomic and fiscal scenarios are considered alongside baseline scenario. (Scenario analysis involves the choice of alternative sets of variables that are internally consistent.)
- These approaches provide policy-makers with a better feel for the likely path of the fiscal aggregates and their sensitivity to economic developments.
- They improve the ability to judge whether the effects of a given fiscal shock are likely to be temporary or permanent, and for assessing whether a discretionary fiscal adjustment may be required.

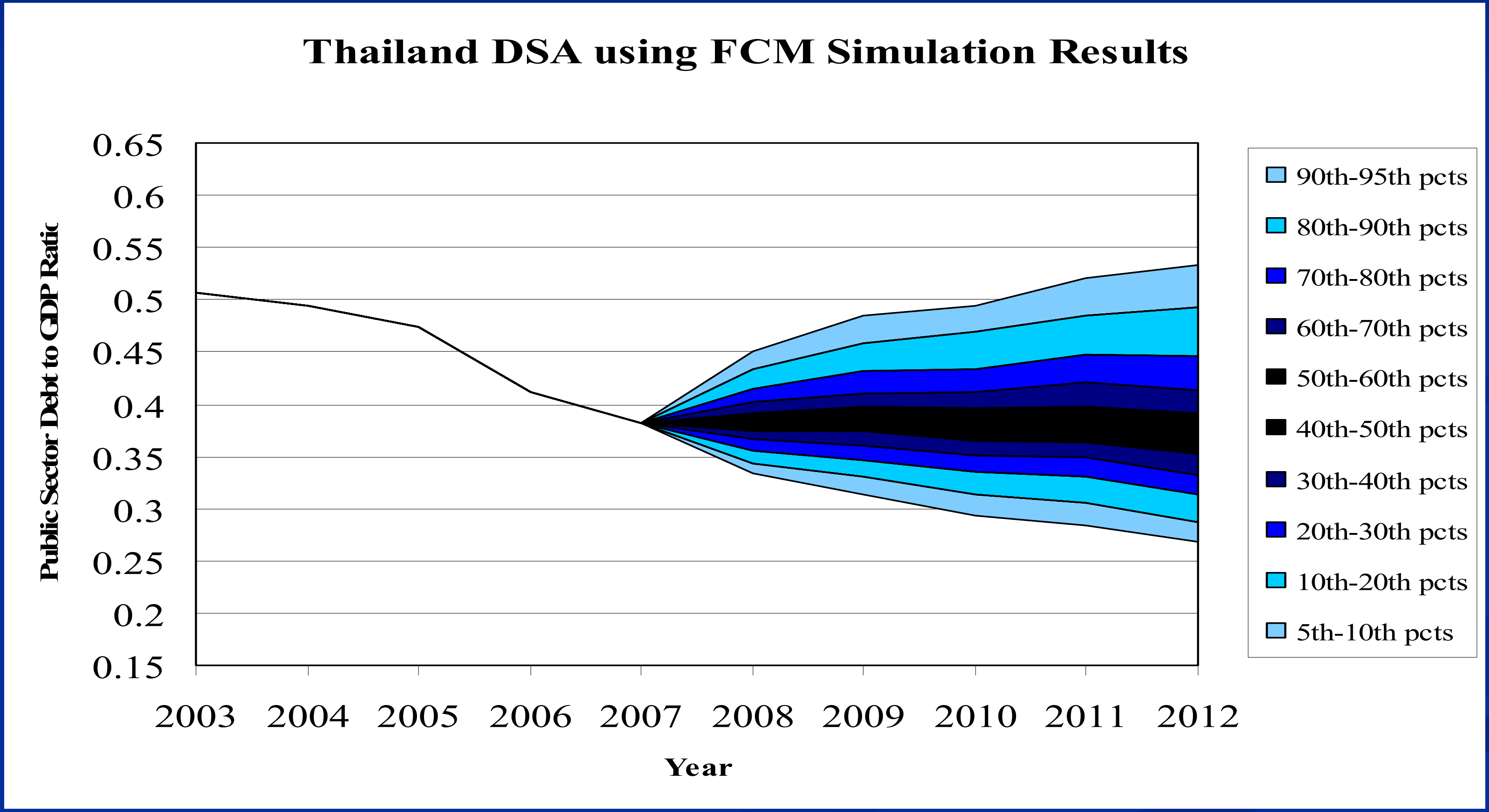
Thailand—Interest and Exchange Rate Sensitivity of Public Debt

	1 year impact	3 year impact	5 year impact
	(in percent of GDP)		
1. Interest Rate Sensitivity (1 percent change)	0.1	0.3	0.9
Direct Government Debt	0.0	0.2	0.5
SOEs' Debt	0.0	0.1	0.3
Domestic Debt	0.0	0.1	0.3
External Debt	0.0	0.0	0.1
2. Foreign Exchange Rate Sensitivity (10 percent depreciation)	0.1	0.2	0.3
Government External Debt	0.0	0.1	0.1
SOEs' External Debt	0.1	0.1	0.2

Source: PDMO. This information is not yet publicly disclosed but does not seem to be sensitive information.

1/ Based on central government and SOEs debt stock as of April 2008.

Thailand—Fan Chart



Contingent Liabilities

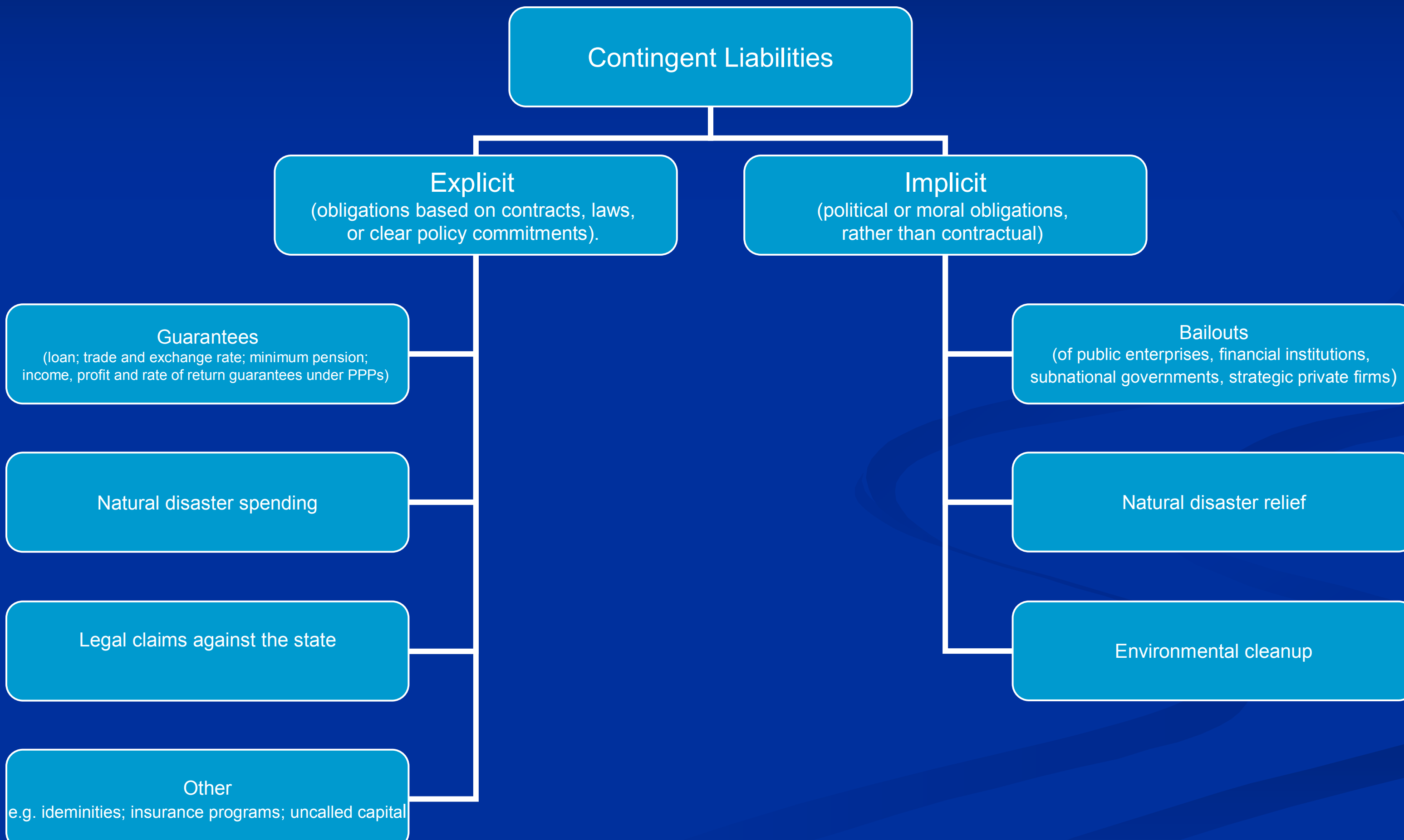
General definition

- Contingent liabilities are obligations that have been entered into, but the timing and amount of which are contingent on the occurrence of some uncertain future event outside the control of the Government.

Other definitions

- Off-balance sheet contingent obligations (accounting).
- Guarantees and NPV of accrued social security obligations (GFSM 2001).

Contingent Liabilities



CL Disclosure in Practice

- Disclosure practices driven by accounting, reporting and transparency standards.
  - Accounting Standards (IPSAS):

Likelihood and measurability of loss	Loss more likely than not (probability > 50%)	Loss less than likely but more than remote	Loss remote
Loss can be measured	Record in financial statements and disclose nature of contingency	Disclose nature of contingency and amount	No Disclosure
Loss cannot be reasonably measured	Disclose nature of contingency	Disclose nature of contingency	No Disclosure

  - Statistical Standards (GFSM 2001).
  - OECD Best Practices (2001), IMF Fiscal Transparency Code and Manual (2007).

- Required also by PFM or fiscal transparency legislation (Australia, Brazil, Canada, Chile, Colombia, France, New Zealand, Nigeria, Pakistan, Peru, UK).
- Good practices spearheaded by New Zealand, Australia, and more recently by emerging markets (Brazil, Chile, Colombia).

CL Disclosure in Practice

- Disclosure venues:
  - Financial statements (Australia, Canada, New Zealand, US).
  - Budget documentation

Table 2: **Are Government's contingent liabilities noted in the budget documentation (or in other documents) presented to the Legislature?**

	Number	Percentage	Countries
Yes	18	60.0	*Australia, Austria, Canada, Czech Republic, Denmark, France, Hungary, Iceland, Ireland, Mexico, Netherlands, New Zealand, Poland, Portugal, Slovakia, Sweden, United Kingdom, USA*
No	10	33.3	*Belgium, Germany, Italy, Japan, Luxembourg, Norway, South Korea, Spain, Switzerland, Turkey*
Missing	2	6.7	*Finland, Greece*
TOTAL	30	100.0	

  - Medium-term fiscal framework (Colombia, Peru).
  - Debt management reports (Japan, Czech Republic, Turkey).
  - Statements of fiscal risks (Australia, Brazil, Chile, Colombia, Indonesia, New Zealand).
  - Stand-alone CL reports (Chile "Report on Contingent Liabilities" since November 2007).

CL Disclosure in Practice

- Disclosure statements include:
  1. Classification of CLs by major category.
  2. Fiscal significance, nature, and rationale for taking CLs.
     - Total exposure, expected cost, and "unexpected" loss.
     - Explanations for changes in CLs between periods.
     - When quantification hard, discussion of nature and scope of liabilities.
  3. For major individual CLs: description of their nature, scope and quantification where possible (often face value).
  4. Information on past calls on the government.
  4. For each new CL: its public policy purpose, duration, and the intended beneficiaries.
  5. Information about reserve assets set aside against specific CLs (e.g., deposit insurance fund).

CL Disclosure in Practice

- Exemptions from disclosure:
  - Implicit CLs, to minimize moral hazard.
  - Information that – if quantified – would prejudice:
    - Substantial economic interests of the country.
    - Security or defense of the country.
    - International relations of the government.
    - Ongoing litigation and negotiation.

- Exemptions primarily apply to quantification of CLs; the existence, nature and overall scope should still be disclosed (except implicit CLs).

CL Disclosure in Practice

What countries disclose	SELECTED COUNTRIES	QUANTIFIABLE INFO DISCLOSED
Loan Guarantees Guarantee and Insurance Programs	Australia, Canada, Chile, Colombia, New Zealand, South Africa, US	Maximum authorized, face value, expected loss (annual & NPV), unexpected loss (annual & NPV; 95% & 99% probability), details of guarantee and guaranteed loan (maturity, currency, interest)
Infrastructure Guarantees	Chile, Colombia	Maximum loss, expected loss (annual & NPV), unexpected loss (annual & NPV; 5, 50, 95, 99% probability), evolution of NPV expected costs
Pension Guarantees	Chile, South Africa, US	Face value, expected payments (annual & NPV), calls on past guarantees
Lawsuits	Australia, Brazil, Canada, Chile, Colombia, New Zealand, US	Face value (amounts claimed), expected losses (annual, NPV), range of expected losses, unexpected losses (99%), past success rates
Environmental Liabilities	Canada, New Zealand, US	Expected costs
Quasi-fiscal deficit Central Bank	Australia, Chile	Quasi-fiscal deficit and capital position of CB; guaranteed CB liabilities
Callable Capital (International Org.)	Australia, Canada, New Zealand	Face value
Unquantifiable Liabilities	Australia, Canada, New Zealand	Description of liability
Implicit Liabilities	Chile, Pakistan, US	Fiscal cost of past banking crisis, past costs of stabilizing fuel prices

Thank you!