

# Abstract

## Fiscal risks - international recommendations

International organisations issue economic policy recommendations on a regular basis. The European Union issues country-specific recommendations as part of the European Semester each year. The International Monetary Fund (IMF) issues Finland with recommendations each year on the basis of the consultations required under Article IV of the IMF's Articles of Agreement. OECD issues its country report on Finland every two years.

## The recommendations have a great deal in common

The recommendations issued by the three organisations between 2012 and 2016 were fairly similar. There are some differences in the detailedness and priorities of the recommendations and the subjects discussed in them. The recommendations were also repeated in more or less unchanged form during years under review.

There are differences between the recommendations with regard to their binding nature and the weight attached to them. As a rule, the recommendations are not binding. The country-specific recommendations issued by the EU that concern the Stability and Growth Pact and the implementation of the macroeconomic imbalances procedure are linked to processes that also include legislation-based sanctions. However, even if a member state is issued with recommendations based on the Stability and Growth Pact and the macroeconomic imbalances procedure during the European Semester, it does not automatically mean that the member state in question would be subject to more binding procedures and recommendations included in these processes.

Interaction between international organisations and national-level parties has an impact on the way in which the international recommendations are formulated. The recommendations do not usually have any direct or clear impact on decision-making in Finland but they shape the content of the economic policy debate, especially in the long term. The strong role of the Government Programme in the formulation of policies is one factor diminishing the practical importance of the recommendations: Complying with recommendations issued in the middle of the government term would be politically difficult.

## The recommendations should be communicated more effectively

International economic policy recommendations are important because they enrich the economic policy debate, add new perspectives to the process and give outsiders' view to the debate. For this reason, it is important that the new recommendations and, if possible, the monitoring information on implementing them are easily available and disseminated in a timely manner.

The latest recommendations issued as part of the processes taking place in the EU, IMF and the OECD are published by the Finnish authorities. However, under the current publication practices there is no guarantee that the recommendations would be easily available and clearly disseminated. There are no well-established practices under which the content of the latest recommendations would be available

and clearly presented in Finnish and Swedish, the official languages of Finland.

Parliament is regularly informed only of the recommendations issued as part of the European Semester. In addition to the new recommendations, the view of the Finnish authorities on how well Finland is complying with the recommendations is also part of the information provision arrangements. This view is included in the national reform programme. The description of the institutional arrangements contained in the national reform programme is brief and does not correspond to the guidelines of the European Commission. This makes the preparations of the reform programme and the role played by Parliament in the process less transparent.

#### Only the implementation of the EU recommendations is comprehensively monitored

The implementation of the recommendations is not comprehensively monitored. Monitoring carried out by the national authorities and the European Commission is an integral part of the process of EU's country-specific recommendations. The implementation of the recommendations issued by the IMF and the OECD is only monitored by the two international organisations themselves and the monitoring is not comprehensive.

When comparisons are made between decision-making in Finland and the recommendations issued for Finland, the conclusion is that the decisions made in Finland are largely in accordance with the international recommendations. This does not mean, however, that the measures have been carried out necessarily because they have been proposed by international organisations. Furthermore, there are also differences between the recommendations in respect of the degrees of implementation.

The report highlights a number of themes, in which there are differences between the measures adopted in Finland and the recommendations issued by the EU, IMF and the OECD between 2012 and 2016. These include cuts in research and development expenditure and in appropriations for active labour market programmes, progress of local-level bargaining, tightening of conditions for early-retirement and the duration of parental leave and child home care allowance.

#### Reducing the sustainability gap was a major factor in the drafting of the pension reform

All organisations have highlighted the need for structural reforms in their recommendations. The main aim of the structural reforms is to achieve improvements in Finland's fiscal balance in the long term. In practice, there is substantial variation between the structural reforms with regard to the risk sensitivity of their impacts. This can be illustrated by examining the pension reform (which entered into force in 2017) and the regional government and SOTE (social welfare and health care) reform (which is currently under preparation).

Clear target-setting, the central role of the economic targets as steering instruments in the drafting process, the low level of transition costs and the impacts assessments based on a number of different calculation models have increased the likelihood of the expected positive fiscal impacts of the pension reform and that the impacts of the reform can be transparently assessed. The transparency of the risk sensitivity of the pension reform has been negatively affected by the

fact that the impact assessments contained in the Government proposal were not subject to comprehensive sensitivity analyses and the background assumptions contained in the basic calculation were inadequately reported in the Government proposal.

As part of the report, the National Audit Office commissioned sensitivity analyses of the impacts of the reform. The analyses, which were produced by the Finnish Centre for Pensions, did not suggest a high level of risk sensitivity. However, they highlighted both short-term and long-term uncertainties that emphasise the need for systematic monitoring of the impacts of the reform.

### The impact of the regional government and SOTE reform on fiscal risks is uncertain

The wide-ranging regional government and SOTE reform is sensitive to risks and, at the moment, its impacts cannot be assessed in a reliable manner. The estimated savings generated by the reform are based on a funding model that is in accordance with the savings target and not on clear cost savings mechanisms. The regional government and SOTE reform also involves substantial transition costs that are more likely to become reality than the savings that the reform is expected to bring. When combined with the slow implementation of the targeted savings, this makes the impacts of the reform more uncertain.

The multiple objectives of the regional government and SOTE reform and the compromises between different elements resulting from it have increased the risk sensitivity of the reform from the perspective of fiscal balance. The main aim of the reform is to slow down the rise in costs and to narrow health gaps. Key decisions have been made in the reform process without a strong steering role of assessments aiming at ensuring the implementation of the main goals of the reform. This has made it less certain that the savings target, which is crucial from the perspective of fiscal sustainability, can be achieved.

Generally speaking, the risks arising from the regional government and SOTE reform are made more transparent by the fact that the difficulty of assessing the impacts of the reform, as well as the incomplete nature and uncertainty of the assessments are openly communicated in the drafting documents.

### Recommendations of the National Audit Office:

1. Practices concerning the publication of the recommendations issued by international organisations should be developed so that the content of the new recommendations is communicated to domestic audiences in a comprehensive manner.
2. The Ministry of Finance should design the communication practices for the European Semester as a whole, considering the different stages of the decision-making process connected with the Council recommendations and the other communication issues connected with the European Semester.
3. The Ministry of Finance should revise the content of the section "Institutional issues and stakeholder participation" of Finland's national reform programme introduced as part of the European Semester. The section should describe in greater detail such issues as the manner in which Parliament is informed and how stakeholders are involved in the preparation of the measures presented in the programme.

4. If possible, Government proposals on major structural reforms should include a description of the underlying assumptions of the impact assessments and sensitivity analyses of the impacts of the reforms if underlying assumptions are changed. Sensitivity analyses should be carried out at the level of sustainability gap and the variables impacting it.