

# The French Experience with Developing a Medium Term Budget Framework

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**1. An Overview of 15 years of PFM Reform in France**

**2. Developing the MTBF**

**3. Benefits and Limitations**

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# **1. An Overview of 15 years of PFM Reforms in France**

# Introduction to the ‘culture’ of budgeting in France



- **A strong Budget Department...**
  - Budget is negotiated with line ministries and decided by the PM...
  - ... but within a total envelop decided ex-ante without Cabinet discussion
  - ... and decisions are made based on a ‘shadow’ budget prepared by the Budget Department
- **... in a strong Ministry of Finance**
  - Accounting and payments are performed only by MoF officials (public accountants) for ministries and agencies
- **Parliament has a limited role on budget matters**
  - Limited power to amend budget appropriations
  - No authority to create new spending programs
  - More focus on oversight
- **But a strong culture of ‘announcing’ more spending**

# Background in 1995 : an aging and fragmented framework

- **The PFM framework is highly fragmented...**
  - The State implements most public policies (education, security and defense, etc.) with the help of dedicated autonomous agencies (research, environment, etc.)
  - Social security is responsible for most of social spending (health, pensions, family benefits)
  - Local governments have a large autonomy for implementing some public policies (housing, infrastructure)
  - Financial relationships between level of governments are convoluted
- **... and existing institutions cover only the State budget (less than 30% of general government expenditure)**
- **The legal framework for the State budget is outdated**
  - Almost unchanged since 1959
  - Extremely detailed appropriations (a few thousands)
  - Tedious procedures to reallocate money
  - Poor information presented to support the budget

# 1996-2001: enhancing transparency and accountability

- **A complete revision of the State budget framework**
  - A new PFM law adopted in 2001, the “LOLF”, product of a **bipartisan parliamentary initiative**
  - Introduction of modern concepts: program budgeting, accrual accounting, multiannual commitments authorization ...
  - A strong focus on fiscal transparency (budget documentation) and government accountability (pre-budget debate, budget execution reports) = **Parliament wanted more information**
- **An improved coverage: giving a budget to Social Security funds**
  - A “second budget” for Social Security funds (1996) submitted to Parliament
  - Transparency: informs on current and future financial situation
- **Key characteristic of this phase: reforms are comprehensive and initiated through a revision of the legal framework**

# 2001-2005: implementing the new LOLF

- **The new PFM law – the LOLF – entailed a complete overhaul of PFM processes**
  - Secondary regulations needed to be drafted
  - Budget execution fully revised : classification changed, more flexibility provided to line ministries, accrual accounting
  - Devolution of transactional issues to line ministries
  - New IT systems were designed (adaptation of existing systems while a large new IFMIS was initiated)
  - Documenting the budget required a huge effort to describe analytically inputs, outputs and outcomes...
- **A phased introduction**
  - Budget 2005 presented both in old and new frameworks but executed in old framework
  - Some technical adjustments to the legal framework in 2005
  - Budget 2006 fully operational in the new framework
- **A dedicated department set up in MoF to monitor implementation, train staff in all ministries, etc.**

# 2003-2009: introducing strategic tools

- **Despite initial aspirations, the new framework fell short for pushing for fiscal reforms**
  - Flexibility did not lead naturally to responsibility...
  - ... neither performance indicators to savings !
- **At the same time, distributing large fiscal space was no longer possible**
- **Tools for improving the strategic phase in budgeting were gradually introduced**
  - Fiscal objectives/rules: an expenditure rule for State budget since 1990s
  - Spending reviews: experimented in 2005 (focused audits) and rolled over as a comprehensive exercise in 2007, then 2012
  - MTBF: detailed multiyear State budget first introduced for 2009 budget
- **Key characteristic of this phase: reforms were pushed step-by-step (no grand scheme) by “fiscal people” without changing the legal framework**



# 2010-2017: moving towards the next step?

- **All those reforms had missed one big issue : the fragmentation of the PFM framework**
  - Fiscal discipline on State expenditure motivated the use of loopholes (tax expenditure, extrabudgetary funds, public agencies...)
  - Complexity of intergovernmental fiscal relationships kept rising
- **“Game changing” initiatives failed**
  - Attempt in 2008 to merge the “two” budgets (central and social) and in 2011 to change the Constitution to provide legal force to the MTBF
  - Reforms designed in and pushed by the Budget Department on its own
  - Limited political ownership or bipartisanship
- **“Patches” have been gradually deployed**
  - Strengthened control of public agencies: payroll, debt, PPPs
  - Tax expenditure discussed only in the budget
  - Partial limitation of earmarking
  - Ad hoc simplification of some financial flows (incl. dismantling some extra-budgetary funds)
  - Reforms introduced on an ad-hoc basis (MoF/Parliamentary committees joint efforts)
- **European Fiscal Compact required action (2012)**
  - A limited reform to formalize existing practices and introduce additional benchmarks (structural balance rule) and a Fiscal Council
  - Next steps...?

## **2. Developing the Medium Term Budget Framework (MTBF)**

# Rationale for MTBF development

- **Overall fiscal strategy for the State budget was based since 1990s on an expenditure rule**
  - Containing total expenditure is the major concern for a country where public expenditure is above 50% of GDP
  - However, containing expenditure on the short term (annual budget) proved difficult
  - Loopholes included use of 'artifacts' such as carrying over some expenditure from one year to the other, or relying on extrabudgetary funds...
- **Main driver for moving to MTBF was fiscal discipline : enforce the expenditure rule and ensure its credibility both in budget preparation and execution**
  - Budget Department pushed for the MTBF to enhance its control over expenditure growth, while there was basically no more fiscal space to allocate
- **Secondary drivers included**
  - Giving more visibility to line ministries
  - Enshrining multiyear sectoral strategies (defense) into an overall fiscal framework to enhance their credibility

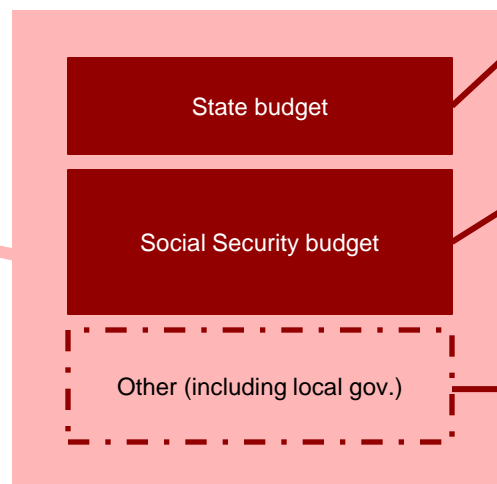
# A coverage tailored to existing institutional arrangements

- **Fragmentation of the fiscal framework was an issue for coverage**
  - Macro fiscal policy setting requires a broad coverage in principle (general government and the wider public sector)
  - But public finances arrangements vary largely among levels of government
  - State budget is more sophisticated than Social security budget
  - Local governments have a large autonomy
- **Solution adopted : a bundled framework**

A medium term **macrofiscal** framework covers the whole of general government and 'bundles' the more detailed frameworks for State and Social security budgets.

All revenue and expenditure are projected on the medium term, including autonomous local governments (pure forecasts)

The overall framework is anchored to a deficit fiscal rule, as prescribed by European Union



A **detailed** medium term framework for **State budget** (discussed later)

Similarly to the State budget, the **Social security budget** is projected over the medium term, but with less sophistication.

Projections of expenditure separate baseline and new measures and are anchored to a fiscal objective for health expenditure growth.

**Local Government** fiscal position is evaluated. However, MTBF provides medium term outlook on transfers and since 2015, a benchmark for expenditure growth

# A multi-year budget for the State (2 binding + 1 indicative)

The detailed MTEF for State budget covers 3 years : 2 fixed and binding and 1 indicative. This framework is 'encased' in the broader general government macrofiscal framework which covers 4 to 5 years.

The first year = the annual budget

The second year is binding. The budget is already approved at public policy level : in the following year, discussion focus on the allocation within each public policy envelop.

The third year is indicative. Only the total for state expenditure is approved and binding. Allocation between public policies will be reassessed in the context of the MTEF 2015-17 preparation process.

The medium term expenditure framework has the same structure, and details, as the State budget

Public policy or transfer to other levels of government	2013	2014	2015
Agriculture	3.5	3.1	3.0
Defense	30.4	30.2	30.2
Education	45.4	45.7	46.1
Public safety	11.6	11.6	11.8
...	...	...	...
Contribution to European Union	19.6	20.4	21.2
Transfers to local governments	55.7	55.0	54.3
<b>Total for State expenditure</b>	<b>278.7</b>	<b>278.7</b>	<b>278.7</b>
Debt service	46.9	48.4	50.9
Civil service pensions	45.2	46.4	48.3

The expenditure rule guides the preparation of the MTEF. For 2013-15, the objective was to stabilize in real terms total expenditure (out of debt service and pensions).

Debt service and pensions are projected over the medium term. The figures are not binding and do not count in the expenditure rule.

# A policy plan published and approved

- The medium term framework is presented every other year to Parliament for discussion and approval ( a multi-year finance program law supported by a 60 page document)

Évolution du solde public de la dépense publique et du taux de prélèvements obligatoires

(En points de PIB)	2011	2012	2013	2014	2015	2016	2017
Solde structurel	-4,8	-3,6	-1,6	-1,1	-0,5	0,0	0,0
Solde public	-5,2	-4,5	-3,0	-2,2	-1,3	-0,6	-0,3
Ratio de dépenses publiques	56,0	56,3	56,3	55,6	54,9	54,2	53,6
Ratio de prélèvements obligatoires	43,9	44,9	46,3	46,5	46,7	46,6	46,3
dont ratio de PO hors contentieux	43,8	45,0	46,5	46,5	46,7	46,6	46,3
Ratio de recettes hors prélèvements obligatoires	7,2	7,1	7,2	7,2	7,2	7,2	7,2

Principales hypothèses du scénario macroéconomique 2013-2017

En %	2011	2012	2013	2014	2015	2016	2017
PIB	1,7	0,3	0,8	2,0	2,0	2,0	2,0
Déflateur de PIB	1,3	1,7	1,8	1,75	1,75	1,75	1,75
Indice des prix à la consommation	2,1	2,0	1,8	1,75	1,75	1,75	1,75
Masse salariale privée	3,4	2,5	2,3	4,0	4,0	4,0	4,0
Croissance potentielle	1,1	1,3	1,4	1,5	1,5	1,6	1,6
Écart de production (% du PIB)	-0,8	-1,7	-2,3	-1,9	-1,4	-1,0	-0,6

Crédits de paiement, en Md€	PROGRAMMATION PLURIANNUELLE (format 2013)			
	LFI 2012 Format 2013	2013	2014	2015
Action extérieure de l'État	2,79	2,83	2,81	2,81
Administration générale et territoriale de l'État	2,22	1,96	2,19	1,95
Agriculture, alimentation, forêt et affaires rurales	3,47	3,10	3,00	2,92
Aide publique au développement	3,30	3,10	3,07	3,07
Anciens combattants, mémoire et liens avec la nation	3,12	3,04	2,95	2,83
Conseil et contrôle de l'État	0,48	0,49	0,50	0,50
Culture	2,54	2,43	2,38	2,35
Défense	30,35	30,15	30,15	30,15
Direction de l'action du Gouvernement	1,10	1,10	1,08	1,08
Écologie, développement et aménagement durables	8,00	7,64	7,28	7,08
Économie	1,59	1,56	1,53	1,52
Égalité des territoires, logement et ville	8,20	7,77	7,73	7,73
Engagements financiers de l'État	1,15	1,11	1,04	0,98
Enseignement scolaire	45,40	45,70	46,10	46,58
Gestion des finances publiques et des ressources humaines	9,08	8,91	8,83	8,66
Immigration, asile et intégration	0,59	0,67	0,66	0,64
Justice	6,02	6,20	6,30	6,32
Médias, livre et industries culturelles	1,41	1,22	1,09	0,97
Outre-mer	1,90	1,99	2,07	2,14
Politique des territoires	0,34	0,32	0,31	0,30
Provisions	0,15	0,16	0,21	0,16
Recherche et enseignement supérieur	25,12	25,64	25,74	25,86
Régimes sociaux et de retraite	6,37	6,54	6,75	6,84
Relations avec les collectivités territoriales	2,56	2,61	2,57	2,56
Santé	1,41	1,29	1,30	1,30
Sécurité	11,58	11,61	11,78	11,96
Sécurité civile	0,39	0,39	0,40	0,41
Solidarité, insertion et égalité des chances	12,53	13,17	13,48	13,74
Sport, jeunesse et vie associative	0,49	0,46	0,48	0,56
Travail et emploi	9,95	10,12	9,68	9,74
Pour mémoire : Pouvoirs publics	1,00	0,99	0,99	0,99

- Macro projections, with their economic assumptions, as well as the detailed multi-year State budget are published, with a discussion of the policy measures supporting the plan
- In 2012, the macrofiscal framework was covering 5 years, while the detailed multi-year State budget covered only 3 years.

- Annual budgets are then compared to the plan and any deviation is explained and justified

# Medium term perspective has been gradually implemented

- **The medium term perspective was developed in sequence**
  - From the macro framework to the detailed multi-year budget: macro projections were implemented first to guide annual budget; details were developed later
  - Inside MoF before line ministries: detailed multi-year budget proposals were tested inside the budget department several years before moving towards a real multi-year budget negotiation
- **Budget preparation process was partially reshaped to adapt but its core structure remained unchanged, reflecting preexisting institutional arrangements**
  - Already an iterative top-down/bottom-up process
  - Stronger integration between the negotiation with ministries (May-October) and the strategic phase in the Budget Department (February-April)
  - The fixed ceilings of the MTBF serve as baseline for following year budget preparation

# Capacity in forecasting was strengthened first

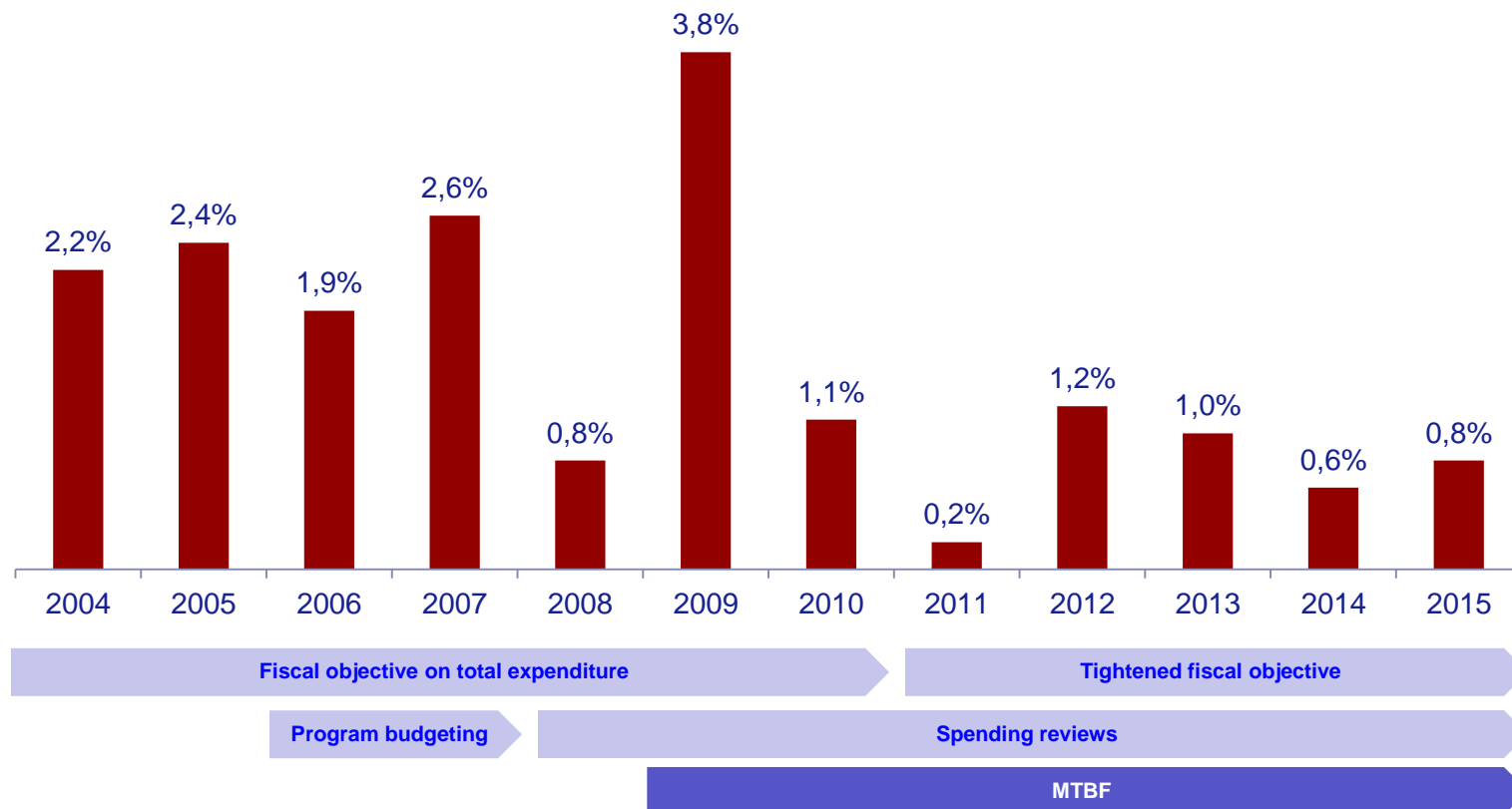
- **Move to the detailed multi-year State budget was implemented in 2009 in less than a year but...**
- **... medium term baseline forecasts had been regularly prepared inside MOF since 2000**
- **... intensive work on expenditure drivers already performed for implementing 'program budgeting' and multiannual commitments authorizations (2006)**
- **Budget Department organization was adapted to take charge of MTBF preparation**
  - **Creation or strengthening of units in charge of macrofiscal policy, revenues forecasting, social security funds, local governments**
- **Line ministries were not associated much before the exercise was rolled over**



### **3. Benefits and Limitations**

# An increased capacity to contain expenditure growth

Public Expenditure Real Growth Rate (excl. tax credits)



# A powerful tool to set a medium term fiscal strategy... but vulnerable to shocks

- **MTBF successful to set and deliver a path when political commitment is strong**
  - 2010-2012 consolidation period in the wake of the Euro crisis
  - 2014-2017 cuts to local government transfers
    - MTBF announced an 11 bn cut on central government transfers
    - Strong political commitment = plan delivered despite protests of local officials
    - Signal and visibility for LG : expenditure trend adjusted; in 2015 first balanced fiscal position of LG since 2003 !
- **Binding approach less successful to adjust to shocks**
  - Preparing a detailed and partially binding MTBF needs everything to go as planned...
    - Difficult for decision makers to think into the medium term
    - Cannot totally oppose the plan: new decisions are regularly taken
  - 2009 – economic crisis hit the very first MTBF
  - 2015 – surge of security spending after the terror attacks

# Giving more visibility to managers was partially successful

- **Forward years' allocation between line ministries had to be revised**
  - Due mainly to pressures from the entitlement programs, which are dependant on the macroeconomic environment
  - No real buffer included in the initial plan
  - Political choice to prefer overall expenditure ceiling to the allocation between sectors
- **However, apart from 2016-17, those adjustments were limited in amount**
- **Second year of MTBF used to be a credible, yet imperfect, baseline for budget preparation**
  - It was decided not to move to more sophisticated updating models such as 'real terms ceilings'
  - Internal discussion about next steps ?
- **And, persisting fragmentation means the MTBF process is complex and subject to trickery**

## **4. Lessons from the French experience**

# A few lessons for discussion

- **MTBF was designed to fit to the French requirements**
  - Existing budget and institutional framework
  - Fiscal policy needs (contain expenditure)
- **MTBF transformed the way the budget department worked**
  - More capacity in forecasting and in public policies strategic design
  - More focus to general government issues (and not just the State budget)
- **MTBF helped improve the credibility of fiscal plans by focusing attention on the reconciliation:**
  - Between macro-fiscal framework and detailed budget allocations
  - Between policy measures and budget allocations
- **But MTBF was also part of a broader set of budget reforms (program budgeting, spending reviews)**
  - Apart from going from 1 to 3/5 years – which was implemented gradually – little has changed
  - But other reforms implemented before have ‘paved the way’ for MTBF
  - Ultimate goal was to make medium term perspective ‘natural’ in the budget process
- **Commitment is key...**

# Thank You!