



Hertie School of Governance - working papers, No. 37, October 2008

**Fiscal Governance in Central and Eastern Europe Before and After  
European Union Accession: What Role Europeanisation?**

Mark Hallerberg (Hertie School of Governance and Emory University),  
Sami Yläoutinen (Finnish Ministry of Finance)

Hertie School of Governance – working papers, No. 37, October 2008

**Fiscal Governance in Central and Eastern Europe Before and After  
European Union Accession: What Role Europeanisation?**

Mark Hallerberg (Hertie School of Governance and Emory University),

Sami Yläoutinen (Finnish Ministry of Finance)

### **About the HSoG Working Paper Series**

The Working Paper Series of the Hertie School of Governance is intended to provide visibility, internally as well as externally, to the current academic work of core faculty, other teaching staff, and invited visitors to the School. High-quality student papers will also be published in the Series, together with a foreword by the respective instructor or supervisor.

Authors are exclusively responsible for the content of their papers and the views expressed therein. They retain the copyright for their work. Discussion and comments are invited. Working Papers will be made electronically available through the Hertie School of Governance homepage. Contents will be deleted from the homepage when papers are eventually published; once this happens, only name(s) of author(s), title, and place of publication will remain on the list. If the material is being published in a language other than German or English, both the original text and the reference to the publication will be kept on the list.

## **Fiscal Governance in Central and Eastern Europe Before and After European Union Accession: What Role Europeanisation?**

Mark Hallerberg

Hertie School of Governance and Emory University

Sami Yläoutinen

Finnish Ministry of Finance<sup>1</sup>

This Draft: August 2008

**Abstract:** Our paper focuses on the development of fiscal institutions in Central and East European countries from 1998 to 2007. Following the Europeanisation literature as well as the expectations that the European Union established in its dialogue with prospective members through annual “Pre-accession Economic Programmes,” one would anticipate that there would have been reform of fiscal institutions in the run-up to EU accession. Unlike in most other policy fields, there is an additional incentive to continue reform once a country has joined the EU, which is eurozone membership.

This paper explains how we measure fiscal institutions and fiscal reforms. We provide time series data on the fiscal institutions each country has had in place, and, based on a new set of surveys and interviews we conducted, we compare the state of these fiscal institutions in 2007, or after the

---

<sup>1</sup> The views of this author are not necessarily those of the Finnish Ministry of Finance.

countries had acceded to the EU, with the institutions in place before accession. We find that preparations for the EU accession prior to 2004 did lead to some changes in budget process in this set of countries. The carrot of EMU membership after acceding to the EU, however, has so far not had the same effect--the pace of reform has since stalled, with most countries leaving the same fiscal institutions in place. In some countries further reforms to develop medium-term fiscal frameworks are either planned or are in a process of being initiated but it is too early to say if the reforms will truly materialise and transform the frameworks into a vehicle that would impose a serious constraint for government spending.

The countries of Central and Eastern Europe have undergone enormous change since the end of Communism almost two decades ago. Their governments have transformed their socialist planned economies into capitalist economies. Politically, previous autocracies are now democracies with regular elections and frequent changes of government. Most of the countries of the region sought to join the European Union (EU), and, with few exceptions, they generally succeeded--Eight countries joined the EU in 2004 while another two joined in 2007.<sup>2</sup> A question that a growing literature examines is to what extent EU accession affected both the pace and the content of change in this group of countries (e.g., Börzel and Risse 2000; Dyson 2006).

Our paper focuses on possible changes in one set of institutions all polities have, namely the institutions that structure the way the budget is made. Spending and taxing decisions are visible manifestations of the priorities (or lack of them) of any particular government. Moreover, as we describe in more detail below, the EU has guidelines in place for what sorts of fiscal information states would have to provide to Brussels before and after accession. When these countries became Member States, they also fell under the rules of Economic and Monetary Union (EMU). They are expected to adopt the euro in the future when the Council of Ministers agrees that they have fulfilled the criteria first established in the Maastricht Treaty. While the goalposts are set, there is no EU requirement that sets how countries are to attain those goals. This policy area is therefore a good one to examine how EU impulses may or may not affect domestic institutions in this set of countries.

The first section of the paper provides more information about the EU-level rules and procedures. The second part explains how we measure fiscal institutions. We argue that all countries need to centralize their budget processes to address what are known as common pool resource problems. Based on previous work (Yläoutinen 2005, Hallerberg, Strauch, and von Hagen 2009), one can create indices that measure the extent to which a given budget process is centralized. More centralized processes usually lead to better fiscal discipline, and countries that seek to qualify for the euro presumably face external pressure to improve their fiscal institutions. Our third section provides time series data on the fiscal institutions each country has had in place. In particular, based on a new set of surveys and interviews, we can compare the state of these fiscal institutions in 2007, or after the countries had acceded to the EU, with the institutions in place before accession. Our general finding is that preparations for the EU accession prior to 2004 did lead to some changes in budget process in this set of countries. The carrot of EMU membership after acceding to the EU,

---

<sup>2</sup> Two countries outside the region, Cyprus and Malta joined the European Union in 2004.

however, has so far not had the same effect--the pace of reform has since stalled, with most countries leaving the same fiscal institutions in place. In some countries, further reforms to develop medium-term fiscal frameworks are planned or are in a process of being initiated, but it is too early to say if the reforms will eventually transform the frameworks into a serious constraint for government spending.

Section five concludes.

## **Europeanisation and the European Fiscal Framework**

The EU set conditions that the Central and East European applicant countries had to fulfill before the EU would invite them as members, and this conditionality provided a strong incentive for the governments in applicant countries to comply. According to the Copenhagen criteria, which were agreed to at the Copenhagen European Council meeting in 1993, applicants would have to be functioning democracies with market economies before the European Union would accept them as applicant countries. Once they had reached this stage, they began formal negotiations with the European Commission. Before they would be invited to join formally, they were expected to adopt the EU's *acquis communautaire*. The European Commission evaluated the progress each country made on the different chapters of the *acquis* and reported on this progress at regular intervals, and, once it determined that enough progress had been made, it recommended a date for entry to the Council of Ministers. To assist with the accession process, the EU established a series of programmes to prepare countries for joining it. They varied from twinning initiatives, which paired a prospective country's administration with a current member, to financial assistance, such as the PHARE program, which provided funds to strengthen public administrations.

As Schimmelfenning and Sedelmeier's (2005) review of changes in several policy areas illustrates, prospective membership led to major changes to the legal frameworks of these countries. They essentially adopted the *acquis* whole. The authors add, however, that there are clear limits to the effectiveness of conditionality. First, the requirement to be a democracy did not convince autocracies to democratize so that they could join. Second, adopting a law says little about how the law will be implemented. Indeed, once countries are Member States the power of conditionality is at an end. Looking at events after accession, Mungiu-Pippidi (2007) argues that there has been some backsliding especially in the area of media freedom in some countries in Central Europe, and she notes that "as for the day after accession, when conditionality has faded, the influence of the EU vanishes like a short-term anesthetic (p.16)."

Our focus in this paper is on fiscal matters and fiscal institutions in these countries, and there are some parallels to the concern about how conditionality may, or may not, constrain states once they get into the euro-zone. The Maastricht Treaty that the Member States agreed to in December 1991 and ratified two years later created Economic and Monetary Union. Member states were to regard their economic policies as a “common concern” and were expected to coordinate them (Article 99(1) of the Treaty). All but Denmark and the United Kingdom, which had formal opt-outs in the Treaty, were supposed to prepare themselves for introduction of a common currency. To join the euro-zone, a country would have to fulfill four Maastricht criteria. They would have to have their inflation rate no higher than 1.5% higher than the average of the three lowest rates in the EU. Long-term interest rates also could be no more than two percentage points higher than the rates in the three lowest inflation countries. In terms of exchange rates, they would be expected to join the Exchange Rate Mechanism II, which sets a given currency within a narrow band around the euro, for at least two years before they joined the common currency. Finally, two items composed the fiscal criteria, the expectation that general government budget deficits be no more than 3% of GDP and debt levels no higher than 60% of GDP.

While the focus of the Maastricht Treaty was on the creation of Economic and Monetary Union, the Stability and Growth Pact provided additional rules for how EMU would function once the euro was introduced. The Member States agreed to the Pact at the Dublin Summit in December 1996 after the German Finance Minister Theo Waigel in particular had expressed concerns that countries would not maintain the same fiscal discipline after they became eurozone members. Following the experiences of the first years of EMU, the Pact was reformed in 2005. One of the major elements of this reform was the introduction of the medium term budgetary objectives, or MTOs, which all of the Member States are required to set in their annual economic programmes. The MTOs are differentiated for individual Member States to take into account the diversity of economic and budgetary positions and developments as well as of fiscal risk to the sustainability of public finances, also in face of prospective demographic changes.

The Pact had, and continues to have, both preventive and corrective mechanisms. Under the preventive mechanism, countries submit updates of yearly economic programmes to the European Commission for evaluation. Those programmes are to have figures over a total period of five years, or t-1 to t+3, for items like general government budget balance and general government debt. The expectation is that Member States respect the Medium term objectives they have set themselves in their economic programmes. The Commission, for its part, considers how realistic the figures are and whether states are meeting their medium term objectives, and it makes a recommendation to the



Council of Ministers based on its analysis.<sup>3</sup> The Council then makes a formal recommendation to each respective country.

It is here that the preventive arm may become the corrective arm—the Council of Ministers can decide that a country has an “excessive deficit,” which then triggers the “excessive deficit procedure.” The definition of an “excessive deficit” is that a country has one if its general government deficit is above 3% of GDP and the deficit is neither exceptional nor temporary.<sup>4</sup> Once the Council decides that a country has such a deficit, the government in question is expected to recommend corrective measures. If the government refuses to comply, the Council can recommend that a Member State make a non-interest bearing deposit with the Commission based on the size of the deficit above the 3% reference value, and it can later decide to turn this amount into a fine.<sup>5</sup>

The early history of the SGP was mixed. On the one hand, one could argue that the size of budget deficits throughout the EU has been smaller since the SGP was in force than in the decade before.<sup>6</sup> On the other hand, there have been some notable violations of the Pact. In 2005, six of twelve Member States in the eurozone at the time had “excessive deficits,” and they together represented 80% of the eurozone economy (Hallerberg and Stéclebout-Orseau 2007). The most visible violators were France and Germany.

The framework as described so far has focused on its application to current Member States, and it affects the new states from Central and East Europe in the following ways. First, accession countries were required to submit Pre-accession Economic Programmes (PEPs). These programmes, which continue to be required for countries that have candidate status, are meant to clarify the medium-term economic policy framework, which includes both data on the budget as well as discussion of expected structural reforms. As with the convergence and stability programmes, the European Commission provides an evaluation of the programmes to the Council, and the Council issues recommendations for further action after a joint meeting between the ECOFIN and the ministers of the respective candidate countries.

In sum, the dynamic of accession states relaxing their reform efforts after EU membership is reached may be different for economic matters. Euro-zone membership represents another form of conditionality that is meant to create incentives for the states once they are EU Member States. Our

---

<sup>3</sup> The Economic and Financial Committee, which is composed of senior officials from finance and economics ministries as well from central banks, also provides an opinion on whether a given deficit is excessive.

<sup>4</sup> An “exceptional” deficit was one that arose when economic growth was below -2%, or when growth was between -.75% and -2% and when the Council agreed that the deficit under these circumstances was “exceptional.”

<sup>5</sup> More detail on the operation of the original SGP as well as the content of reforms can be found in Morris, Ongena, and Schuknecht’s (2006) excellent review.

<sup>6</sup> For example, if one compares general government deficits as a percent of GDP in years of weak economic growth, the average among the EU-15 was 5.5% in 1992-94 and just 1.5% in 2002-04 (AMECO 2007).

focus in this article is on domestic fiscal reforms. Did countries make reforms in the run-up to joining the European Union, and did they maintain, or even improve, those institutions once they were Member States?

In order to assess these institutions, the next section reviews briefly the literature on fiscal rules, institutions, and norms and establishes a common metric we use to judge the progress of each country.

### **Fiscal Institutions and Fiscal Governance**

In terms of the specific interest in this paper on *domestic* fiscal institutions, we rely on a framework that is increasingly common in the literature. The assumption is that knowing the preference of the actors who make budgets is not sufficient to explain outcomes. The rules that structure the budget-making process have an effect on the budgets that are passed and implemented.

One of the most pressing problems that can develop is known as the common pool resource (CPR) problem, with fiscal institutions affecting the scale of the problem in practice. The problem exists when policy-makers consider the full benefits and full tax implications of their decisions on their constituencies only rather than on the whole population. This means that they consider the full benefit of additional spending but only the part of the taxes that fall on the people they care most about. The problem was first discussed in the context of parliaments (Shepsle, Weingast, and Johnson 1981), where the expectation was that each member of parliament (MP) represented a specific geographic district. If the tax burden is distributed evenly across the country and there are  $n$  members of parliament, each MP is concerned with only  $1/n$  of the tax burden. Recent work has considered the presence of the problem in cabinets (e.g., Kontopolous and Perotti 1999) as well. An example in this realm is an agriculture minister who cares only about the effects of spending on farmers and about the tax burden that those farmers face. The gist of the model is that the greater the CPR problem the higher spending, and, in a multi-annual setting, the higher budget deficits over time (e.g., Velasco 1999).

The literature also identifies institutional ways to minimize the CPR problem. The focus is on institutions that encourage the players to consider the full tax implications of their spending decisions, which in practice means a centralization of the budget process. One can run through the different stages of the budget process and consider what institutions, rules, and norms lead to greater centralization (von Hagen 1992). In the empirical part of the paper, we will follow this framework in detail and provide definitions for what we mean by “centralization,” but it is useful here to review the stages of the budget process and why they are important. The first stage occurs when the government sets its plans for current and future years. One way to conceptualize the

common pool resource problem is across time instead of just space. Multi-annual planning is one way to make sure that future years are included in current calculations. Moreover, European Union countries have an institutionalized way to do such planning--as mentioned earlier in the paper, they must submit either stability or convergence programmes each year to the European Commission that cover the period  $t-1$  to  $t+3$ . One question to ask is whether a given government integrates this planning exercise into the annual budget process. The second stage is the formation of the budget in cabinet. Cabinets where the full cabinet votes on different parts of the budget allow “logrolling” among various spending ministers and are generally decentralized. The budget then goes to parliament where parliament considers it, may change it, and ultimately passes some form of the budget. It is generally assumed that individual parliamentarians care about less of the tax burden than the government, and that rules that restrict amendments to the government’s budget promote fiscal discipline (e.g., Wehner 2008). The final stage is implementation, or execution, of the budget. Here it is important that a budget that was passed using centralized procedures at the cabinet and parliamentary stage not be allowed to unravel when the money is spent.

This discussion so far presumes that centralization of the budget should proceed the same way in all countries, but one can imagine that some rules are more important in some settings than in others. In particular, the form of governance approach contends, the underlying political climate determines which institutions are effective in a given setting (e.g., Hallerberg 2004; Hallerberg, Strauch, and von Hagen 2009). The fiscal governance framework suggests that there are two ideal approaches in practice in the parliamentary democracies found in Europe, that is, in places where the main decisions on the budget are taken in cabinet and where cabinet is the main arena where the CPR problem needs to be minimized. Under *Delegation*, the key actors give a central player who is concerned about the full tax burden (usually the finance minister) strategic powers in the budget process. Such powers include serving as the agenda-setter on the first draft of the budget, negotiating individually instead of before the full cabinet with spending ministers, and the having the ability to make unilateral cuts in the budget during its execution. France and the United Kingdom are examples of countries where *delegation* is found in practice. The second ideal type is known as fiscal contracts. Under this form of fiscal governance, the relevant players (usually political parties) commit themselves to detailed fiscal targets that encompass all ministries and that are, as a rule, multi-annual. These contracts also include clauses for what to do under different scenarios, such as when revenues are higher than expected or when economic growth stalls. In practical terms, this approach suggests that sets of fiscal rules that strengthen the finance minister work best in “delegation” states while fiscal rules that amount to a contract, such as adherence to multi-annual fiscal frameworks, work best in “contract” states. It should be noted, however, that the

logic of the two is not completely compatible—a finance minister constrained by a detailed contract is not strong, while a detailed contract that allows the finance minister to do what she wants does not constitute a true constraint. How does one choose between the two ideal types?

There is a clear political logic to explain when one form of governance is most optimal. Delegation to a strong finance minister requires that the players share basic policy goals and that they see their political futures intertwined. If policy preferences differ or if the actors expect to run against each other in future elections, they will not delegate power to a finance minister in the first place. For this reason, *delegation* is found and works best under one-party majority governments or in cases where parties in government are ideologically close to one another and where they run together in future elections (i.e., France in the 1990s). *Contracts*, in contrast, work well when the policy differences among coalition partners differ and when those partners will not run jointly in the next election. The contract, by its very nature, makes explicit the priorities and tradeoffs to which the parties have agreed. It also means that partners can judge when another partner is defecting from the contract.

If one examines the party constellations in government in Central and Eastern Europe to predict the appropriate form of fiscal governance in this group of countries, one comes to the conclusion that most of the states are potential *contract* states. Coalition governments that bring together parties that are quite different from one another are the norm in the countries in our sample with the exceptions of Bulgaria and Hungary (Yläoutinen 2005). In Bulgaria, the one party was in power during 2001-05, but during the remaining time it has had multi-party coalition governments, so it does not represent a true exception. In Hungary, in contrast, two blocks of parties face each other, with the MSZP on the left and Fidesz on the right, and one usually finds one of these big parties in coalition with a small party closely aligned with it. Hungary is the only country in the group where one would expect *delegation*. The remaining countries have regular multi-party coalition governments, and fiscal contracts are the most appropriate. Moreover, the use of some form of proportional representation as the electoral system in each country means that fiscal contracts are likely to remain the appropriate form of fiscal governance for some time to come. Proportional representation means that voters do not have the incentive found under plurality systems to vote for the top two parties. The result is a party system with more parties as well as one where no one party usually wins a majority of seats, and the consequence in terms of the form of government is regular multi-party coalition governments (e.g., Duverger 1954; Cox 1997).

With this theoretical framework in mind, the next section discusses the fiscal institutions in place both before and after accession to the European Union.

### 3. Presentation of the data for Central and Eastern Europe

As explained above, the fiscal deficit bias that stems from the CPR problem results from a failure of relevant decision-makers 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 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.

Some studies have also extended the approach to the newest member states from the CEECs. The details of the studies differ somewhat. Gleich (2003) as well as Fabrizio and Mody (2006) measure centralization along one dimension and use either a thirteen- or twelve-item index. Yläoutinen (2005) considers both the Gleich index as well as a broader measures of fiscal governance discussed above.

In our study, we adopt both approaches. We first walk the reader through the various stages of the budget process to document the rules and procedures as well as to evaluate whether they centralize process. The framework comes from von Hagen (1992), and we begin with the formation of long-term constraints. Because these countries include plans that run three years into the future in their convergence and/or stability programmes they submit to the European Commission, we also investigate the extent to which these plans are integrated into the domestic budget process.<sup>7</sup> The next section discusses how a draft budget is formulated in cabinet, and it pays particular attention to the role of the finance minister. Once the draft is ready, it goes to parliament for consideration, and this constitutes the third stage of the budget process. The final stage is the execution/implementation of the budget. In each section, we explain in some detail each of the rules and procedures we measure.

After going through the individual stages, we also present consolidated data in the form of two indices. The first is a delegation index, which measures features of the budget system that strengthen the ability of the finance minister to direct the budget, while the second measures fiscal contracts in a given country and matches the long-term constraint index.<sup>8</sup> As Yläoutinen (2005)

---

<sup>7</sup> Slovenia joined the euro in 2007 while Slovakia is expected to join in 2009. All of the other CEECs are not (yet) members of the euro area.

<sup>8</sup> This index corresponds to "structural index 2" in von Hagen (1992), and Gleich's (2003) index is very similar. Because it is highly correlated with this index (the main differences are on whether to code constitutional rules and the role of the president), we present only the "delegation" index in this paper.

documents that most of the CEECs should be “contract” states because of the prevalence of multi-party coalition governments, this latter measure is especially important for this group of countries. We use the data included in Yläoutinen (2005) and Gleich (2003) to form indices for 1998 and 2003, or before any of the countries had acceded to the European Union. The new data in our study for the period after accession is based on in-depth surveys (questionnaires and subsequent communication with the country authorities) conducted in each country at the end of 2006 through the middle of 2007. Updating the data allows us to track the changes in fiscal practises that have occurred since these countries have joined the EU and have therefore been subject to the economic policy coordination procedures of the EU. Finally, our data also allows for a comparison between the CEECs and the EU-15.

### **Long-term Planning Constraint**

The first item concerns the extent to which a country uses multi-annual budget plans. The European Commission has argued that multi-annual planning benefits all states. This type of planning is also most advantageous in countries where fiscal contracts can help address coordination problems among coalition partners. While the CEECs with the exception of Hungary should be “contract” states because of the prevalence of multi-party coalition governments, based on earlier studies these generally have had underdeveloped institutions to support such contracts. Long-term planning constraint is therefore particularly important aspect of the budget procedure in the case of the CEECs.

Following von Hagen (1992), the long-term planning index has four components. The first item indicates whether there is a multi-annual target, and, if so, what form that target takes. Countries with no targets receive a zero, those that focus on either total expenditures or total taxes receive a two, and those that have total budget size as their target receive a four. The second item considers the time-horizon of the plan. The longer the horizon, more points are awarded. Third item focuses on the nature of budget forecasts. If the forecasts are updated based on a consistent macro-economic model or framework, a country receives a score of four. If they are fixed (for example assuming simply a given growth rate) or ad-hoc, the score is lower.

The next component considers the degree of commitment to multi-annual fiscal targets. This is a crucial aspect of the multi-annual frameworks because it determines how binding the multi-annual targets really are.

The data for 1998 is stark—it indicates that no CEEC had employed multi-annual frameworks. The introduction of the frameworks coincides in most of the countries with the start of

Pre-Accession Fiscal Surveillance Procedure which started in 2001.<sup>9</sup> This indicates that in the run-up to EU accession, the CEECs did make an effort to improve their fiscal management.

However, there has been no change during the few years the CEECs have been EU members. In all countries the degree of commitment is indicative only. It is also worth pointing out that in virtually all countries, it is possible to submit supplementary budgets, which are not included in the original multi-annual targets.<sup>10</sup> Further, most of the countries report that such supplementary budgets are common and appear most years. In practise, this means that multi-annual targets have little practical meaning. Expenditure slippage can take place particularly during good economic times when expenditure overruns can be covered by sizable revenue windfalls. This can create serious problems during adverse economic developments when government revenues fall but new expenditure categories are, in practise, permanent.

Other aspects of the index show virtually no improvement. The only exception is the Czech Republic, where its “Public Finance Reform” entered into force in 2005. Prior to this, the Czech Republic did not have a multi-annual framework in place. More generally, the level of index-values remains low in many countries. It is also noteworthy that the EU-15 average is considerably higher compared to the CEEC average in all aspects of the long-term planning index.

This rather bleak assessment of state of the multi-annual frameworks in the CEECs hides the fact that many of the CEECs have made attempts to improve their frameworks. These improvements have to do, for example, with the way the coalition agreements take into account the medium-term budget plans. In many countries, the coalition agreements include specific fiscal targets and/or the medium-term budget plans. Only few years ago, this was not common. Furthermore, information in the most recent convergence and stability programmes implies that in some countries further reforms to develop medium-term fiscal frameworks are either being planned or are in a process of being initiated.<sup>11</sup> However, it is too early to say if the reform initiatives will truly materialise and transform the frameworks into a vehicle that would impose a serious constraint for government spending and thus improve the fiscal stringency. An experience from at least one budget cycle would be needed in making this judgement. Available evidence suggests these countries still lack a political commitment to the targets. Therefore, these steps are not reflected in the index-values.

---

<sup>9</sup> The Luxemburg European Council decided in December 1997 that the accession negotiations are initiated with Estonia, Poland, Hungary, the Czech Republic, Slovenia and Cyprus. The Helsinki European Council in 1999 decided in turn to include also Latvia, Lithuania, Slovakia, Romania, Bulgaria and Malta in the accession negotiations.

<sup>10</sup> See also the information on budget changes in the section on flexibility of budget execution, which confirms this claim.

<sup>11</sup> See an appendix for additional information about planned reforms.

**Table 1: Long-term Planning Constraint**

| Country              | Multi-annual Target |          |          | Planning Horizon |          |      | Nature of Plan |          |          | Dgr of Commitment |          |          | Sum Long-Term |            |           |             |          |             |
|----------------------|---------------------|----------|----------|------------------|----------|------|----------------|----------|----------|-------------------|----------|----------|---------------|------------|-----------|-------------|----------|-------------|
|                      | 1998                | 2003     | 2007     | 1998             | 2003     | 2007 | 1998           | 2003     | 2007     | 1998              | 2003     | 2007     | 1998          |            | 2003      |             | 2007     |             |
|                      |                     |          |          |                  |          |      |                |          |          |                   |          |          | score         | % of total | score     | % of total  | score    | % of total  |
| Bulgaria             | 0                   | <b>2</b> | 2        | 0                | <b>2</b> | 2    | 0              | <b>4</b> | 4        | 0                 | <b>2</b> | 2        | 0             | 0          | <b>10</b> | <b>62,5</b> | 10       | 62,5        |
| Czech                | 0                   | 0        | <b>2</b> | 0                | <b>1</b> | 1    | 0              | <b>1</b> | <b>4</b> | 0                 | <b>1</b> | <b>2</b> | 0             | 0          | <b>3</b>  | <b>18,8</b> | <b>9</b> | <b>56,3</b> |
| Estonia              | 0                   | <b>4</b> | 4        | 0                | <b>3</b> | 3    | 0              | <b>4</b> | 4        | 0                 | <b>2</b> | 2        | 0             | 0          | <b>13</b> | <b>81,3</b> | 13       | 81,3        |
| Hungary              | 0                   | <b>2</b> | 2        | 0                | <b>2</b> | 2    | 0              | <b>4</b> | 4        | 0                 | <b>2</b> | 2        | 0             | 0          | <b>10</b> | <b>62,5</b> | 10       | 62,5        |
| Latvia               | 0                   | <b>2</b> | 2        | 0                | <b>2</b> | 2    | 0              | <b>4</b> | 4        | 0                 | <b>2</b> | 2        | 0             | 0          | <b>10</b> | <b>62,5</b> | 10       | 62,5        |
| Lithuania            | 0                   | <b>2</b> | 2        | 0                | <b>2</b> | 2    | 0              | <b>4</b> | 4        | 0                 | <b>2</b> | 2        | 0             | 0          | <b>10</b> | <b>62,5</b> | 10       | 62,5        |
| Poland               | 0                   | <b>2</b> | 2        | 0                | <b>2</b> | 2    | 0              | <b>4</b> | 4        | 0                 | <b>2</b> | 2        | 0             | 0          | <b>10</b> | <b>62,5</b> | 10       | 62,5        |
| Romania              | 0                   | <b>2</b> | 2        | 0                | <b>3</b> | 3    | 0              | <b>2</b> | 2        | 0                 | <b>2</b> | 2        | 0             | 0          | <b>9</b>  | <b>56,3</b> | 9        | 56,3        |
| Slovakia             | 0                   | <b>2</b> | 2        | 0                | <b>2</b> | 2    | 0              | <b>4</b> | 4        | 0                 | <b>2</b> | 2        | 0             | 0          | <b>10</b> | <b>62,5</b> | 10       | 62,5        |
| Slovenia             | 0                   | <b>4</b> | 4        | 0                | <b>3</b> | 3    | 0              | <b>4</b> | 4        | 0                 | <b>2</b> | 2        | 0             | 0          | <b>13</b> | <b>81,3</b> | 13       | 81,3        |
| <b>CEEC Average</b>  | 0,0                 | 2,2      | 2,4      | 0,0              | 2,2      | 2,2  | 0,0            | 3,5      | 3,8      | 0,0               | 1,9      | 2,0      | 0,0           | 0,0        | 9,8       | 61,3        | 10,4     | 65,0        |
| <b>EU-15 Average</b> |                     | 4,0      |          |                  | 2,7      |      |                | 4,0      |          |                   | 3,0      |          |               |            | 13,7      | 85,6        |          |             |

Notes: **Multi-Annual Target:** 4 Total Budget Size; 2 Spending or taxation; 0 None; **Planning Horizon:** 4 Five years 3 Four Years 2 Three Years 1 Two Years 0 None; **Nature of Plan:** Updated Based on Consistent Macro-economic Framework 3 Updated, but Not Based on Consistent Framework 2 Fixed Forecast 1 Ad Hoc Forecast 0 No Forecast; **Degree of Commitment:** 4 Legal 3 Political 2 Indicative 1 Internal Only. Changes from 2003 to 2007 that increase the index appear in **bold**. Figures for the EU-15 are from 2004 and come from Hallerberg, Strauch, and von Hagen (2009). The maximum value is 16.

### Connectedness of the Convergence Programmes with the Annual Budget Process

In this section we try to establish the relationship between Convergence Programmes and the annual budget. During the pre-EU era, the CEECs were involved with the Pre-Accession Fiscal Surveillance Procedure, which started in the beginning of the millennium. Part of this Procedure was 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 was to develop the capacities of the CEECs to engage medium-term macroeconomic planning.

The respondents were asked to evaluate the link between the Convergence Programmes and the annual budgets based on four different criteria. Ideally, the two should be closely linked. Interestingly, the index-values have dropped significantly in almost all countries, Slovakia being the only country that has recorded a rise, which ties it with Slovenia for the two highest scores. Not coincidentally, these are also the first two countries to adopt the euro.



These results provide direct evidence for the arguments about the effects of EU accession on these countries. That is, in the run-up to membership the countries relied more on multi-annual frameworks in the form of PEPs, which had a closer connectedness with the annual budget process, that they do today after accession in the form of their convergence programmes. Some technical considerations, to be sure, also were relevant—the main purpose of the PEPs was not to coordinate the fiscal policies of the CEECs, but rather to make these countries familiar with the multi-annual fiscal frameworks. As the pre-accession procedures included a greater degree of flexibility, it could have been easier for these countries to continue applying domestic accounting rules, budget norms and calendars. Convergence Programmes in turn are a part of a more rigorous policy coordination procedure, which has its basis in the EU Treaty. Nevertheless, it is revealing that the two countries that wanted to join the eurozone fairly soon after accession also had the strongest integration of the convergence programmes. They presumably wanted to signal to the European Commission, which was the body that is required to make a positive recommendation on euro membership before the Council of Ministers considers the request, that they are able to reach the goals they set in their programmes, and this was more likely if the budgets and the programmes were indeed connected. There were institutional implications for countries that cared about the additional carrot of eurozone membership after accession.

**Table 2: Relationship between Convergence programmes and annual budgets**

| Country             | Same dep |          | Acc rules |          | Calendar |          | Budg targets |          | Sum, CP |            |          |             |
|---------------------|----------|----------|-----------|----------|----------|----------|--------------|----------|---------|------------|----------|-------------|
|                     | 2003     | 2007     | 2003      | 2007     | 2003     | 2007     | 2003         | 2007     | 2003    |            | 2007     |             |
|                     |          |          |           |          |          |          |              |          | score   | % of total | score    | % of total  |
| Bulgaria            | 0        | 0        | 1         | <i>0</i> | 2        | <i>1</i> | 2            | <i>1</i> | 5       | 62,5       | 2        | <i>25,0</i> |
| Czech               | 0        | 0        | 0         | 0        | 1        | 1        | 2            | <i>1</i> | 3       | 37,5       | 2        | <i>25,0</i> |
| Estonia             | 0        | 0        | 0         | <b>2</b> | 2        | <i>0</i> | 2            | 2        | 4       | 50,0       | 4        | 50,0        |
| Hungary             | 0        | 0        | 2         | <i>0</i> | 2        | <i>0</i> | 2            | <i>0</i> | 6       | 75,0       | 0        | <i>0,0</i>  |
| Latvia              | 2        | <i>0</i> | 0         | 0        | 0        | <b>1</b> | 2            | 2        | 4       | 50,0       | 3        | <i>37,5</i> |
| Lithuania           | 0        | 0        | 1         | <i>0</i> | 2        | <i>1</i> | 2            | 2        | 5       | 62,5       | 3        | <i>37,5</i> |
| Poland              | 2        | 2        | 2         | <i>0</i> | 1        | 1        | 2            | <i>1</i> | 7       | 87,5       | 4        | <i>50,0</i> |
| Romania             | 2        | 2        | 1         | <i>0</i> | 1        | <i>0</i> | 2            | <i>1</i> | 6       | 75,0       | 3        | <i>37,5</i> |
| Slovakia            | 0        | 0        | 1         | <b>2</b> | 1        | 1        | 2            | 2        | 4       | 50,0       | <b>5</b> | <b>62,5</b> |
| Slovenia            | 2        | 2        | 1         | <i>0</i> | 2        | <i>1</i> | 2            | 2        | 7       | 87,5       | 5        | <i>62,5</i> |
| <b>CEEC Average</b> | 0,8      | 0,6      | 0,9       | 0,4      | 1,4      | 0,7      | 2,0          | 1,4      | 5,1     | 63,8       | 3,1      | 38,8        |

Notes: Each answer is coded on a 0-2 scale, with affirmative answers coded as 2, negative answers 0, and answers in between the two extremes as 1. Changes from 2003 to 2007 that increase the index appear in **bold** while changes that decrease the index appear in *italics*. The maximum value is 8.

## **Structure of negotiations in cabinet**

Von Hagen (1992) examines how easily spending ministers can enforce a budget which reflects their needs. As explained earlier, cabinet ministers have reason to consider the full benefits of any spending in their ministries but to consider only part of the tax burden. This means in practice that the CPR problem will be large if the negotiations amount to summing up the various ministry proposals formulated in isolation of one another.

Following von Hagen (1992), four different aspects are considered. The maximum value is 16 points. First, we examine whether there is a general constraint on the budget before the cabinet consider it. The more comprehensive the constraint is, the higher the index value is. Countries with both pre-established expenditure cap and deficit target receive four points and no constraint at all receives a zero.

The second aspect tries to capture the agenda-setting power of the finance minister within government. If the finance minister only collects budget bids from spending ministers, the score on agenda setting equals zero, while the maximum score is awarded to countries where the finance minister determines the budget parameters for the spending ministers. In all of the countries, it is the finance minister who proposes the budget to the rest of the cabinet, but in case of disagreements, spending ministers can ask for a vote on their bids and potentially overrule the finance minister.

The third aspect focuses on the “breadth” of the budget norms. In other words, the countries were asked if there are more specific expenditure targets (such as specific expenditure ceilings for individual ministries or programmes) in addition to general targets. This category also tries to capture the decision-making sequence regarding the budget targets. The earlier in budget process the finance minister suggests or sets the targets, the larger his/her influence in steering the budget process probably is. In some of the CEECs, the finance ministry proposes the targets only after (not before) initial budget bids are made. The broader the budget norms are in the sense as described above, bigger the score.

The final aspect has to do with structure of budget negotiations, and more specifically, the cabinet’s involvement. 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. If the main arena for the budget negotiations is bilateral negotiations between finance minister and spending minister, a country receives four points. In almost all countries also bilateral negotiations do exist, but the disagreements are solved with the entire cabinet present. These countries are scored a two.

When considering the structure of negotiations within cabinet, a look at the index-values in 2003 and 2007 makes it clear that there has been virtually no change in this aspect of the budget process during EU accession. Romania and Hungary are the only countries that have recorded a modest rise. In Romania the change took place in 2003/2004 when the initial budget circular were reformed to include numerical expenditure targets. Before the reform, no numerical targets in Romania were in place. Similar reforms were made already earlier in Bulgaria, Lithuania and Poland. Hungary adopted a budget balance rule in 2006. More variation can be found between the countries, particularly regarding the two aspects that focus on the budget targets. Finally, the EU-15 countries record higher average scores in all aspects of the index. The difference is particularly large in the case of budget norms, which tried to capture the existence of more specific expenditure targets in addition to general targets.

**Table 3: Structure of negotiations in cabinet**

| Country              | General Constraint |          |      | Agenda Setting |          |      | Budget Norms |             |             | Str of Negot |          |      | Sum, Negot |            |             |             |             |             |
|----------------------|--------------------|----------|------|----------------|----------|------|--------------|-------------|-------------|--------------|----------|------|------------|------------|-------------|-------------|-------------|-------------|
|                      | 1998               | 2003     | 2007 | 1998           | 2003     | 2007 | 1998         | 2003        | 2007        | 1998         | 2003     | 2007 | 1998       |            | 2003        |             | 2007        |             |
|                      |                    |          |      |                |          |      |              |             |             |              |          |      | score      | % of total | score       | % of total  | score       | % of total  |
| Bulgaria             | 0                  | <b>4</b> | 4    | 0              | <b>2</b> | 2    | 0            | <b>4</b>    | 4           | 2            | 2        | 2    | 2          | 12,5       | <b>12</b>   | <b>75,0</b> | 12          | 75,0        |
| Czech                | 2                  | 2        | 2    | 2              | 2        | 2    | 4            | 4           | 4           | 2            | 2        | 2    | 10         | 62,5       | 10          | 62,5        | 10          | 62,5        |
| Estonia              | 4                  | 4        | 4    | 2              | 2        | 2    | 4            | 4           | 4           | 2            | 2        | 2    | 12         | 75,0       | 12          | 75,0        | 12          | 75,0        |
| Hungary              | 2                  | 2        | 2    | 2              | 2        | 2    | 1,33         | 1,33        | <b>2,66</b> | 2            | 2        | 2    | 7,33       | 45,8       | 7,33        | 45,8        | <b>8,66</b> | <b>54,1</b> |
| Latvia               | 4                  | 4        | 4    | 2              | 2        | 2    | 4            | 4           | 4           | 2            | 2        | 2    | 12         | 75,0       | 12          | 75,0        | 12          | 75,0        |
| Lithuania            | 0                  | <b>4</b> | 4    | 0              | <b>2</b> | 2    | 0            | <b>1,33</b> | 1,33        | 0            | <b>2</b> | 2    | 0          | 0          | <b>9,33</b> | <b>58,3</b> | 9,33        | 58,3        |
| Poland               | 0                  | <b>2</b> | 2    | 0              | <b>2</b> | 2    | 0            | <b>1,33</b> | 1,33        | 2            | 2        | 2    | 2          | 12,5       | <b>7,33</b> | <b>45,8</b> | 7,33        | 45,8        |
| Romania              | 2                  | 2        | 2    | 2              | 2        | 2    | 0            | 0           | <b>1,33</b> | 2            | 2        | 2    | 6          | 37,5       | 6           | 37,5        | <b>7,33</b> | <b>45,8</b> |
| Slovakia             | 4                  | 4        | 4    | 2              | 2        | 2    | 1,33         | 1,33        | 1,33        | 2            | 2        | 2    | 9,33       | 58,3       | 9,33        | 58,3        | 9,33        | 58,3        |
| Slovenia             | 4                  | 4        | 4    | 2              | 2        | 2    | 4            | 4           | 4           | 4            | 4        | 4    | 14         | 87,5       | 14          | 87,5        | 14          | 87,5        |
| <b>CEEC Average</b>  | 2,2                | 3,2      | 3,2  | 1,4            | 2,0      | 2,0  | 1,9          | 2,5         | 2,8         | 2,0          | 2,2      | 2,2  | 7,5        | 46,7       | 9,9         | 62,1        | 10,2        | 63,7        |
| <b>EU-15 Average</b> | 3,5                |          |      | 3,1            |          |      | 4,0          |             |             | 2,6          |          |      | 13,1       |            | 81,9        |             |             |             |

Notes: **General Constraint:** 4 Size of overall budget/expenditure cap, and deficit target; 3 Golden Rule; 2 Deficits and Debt; 1 Overall Size; 0 None; **Agenda-Setting:** 4 MF proposes, no individual vote on budget bid; 2 Spending Minister can ask for individual vote on bid, cabinet can override MF; 0 MF collects budget bids; **Budget Norms:** 4 “broad”; 2.66 “broad” and “specific”; 1.33 “specific”; 0 expenditure/deficit only; **Structure of Negotiations** 4 MF bilateral only; 2 multilateral; 0 all cabinet ministers involved. Changes from 2003 to 2007 that increase the index appear in **bold**. Figures for the EU-15 are from 2004 and come from Hallerberg, Strauch, and von Hagen (2009). The maximum value is 16.

## Strength of finance minister

This section and the attached table consider the role of finance minister in the planning and decision-making stage focussing especially on his/her fiscal powers relative to spending ministers. There is some overlap with the first table with the difference that this section focuses only to the finance ministers. The coding scheme in this case is based on Hallerberg, Strauch, and von Hagen (2001).

The only aspect were there seems to have been variation in has to do with a question if finance minister has any special powers, such as a veto power on budgetary issues. It is noteworthy that the countries which reported an affirmative answer to this question mentioned that the powers do not have a legal basis but that the finance minister has these powers in practise. This can also explain the evolution of the scores in many countries. As these powers are not cemented into law but are rather controlled by informal norms, it is possible that a change of government or finance minister also changes the budget practise.

In general the index-values are not very high, as the countries with highest scores receives as score of only 12 out of 24. There is also a considerable uniformity across countries in the case of most of the sub-items, although there is clearly some improvement in scores from 1998 to 2003.

**Table 4: Strength of finance minister**

| Country             | Bil negotiations |      |      | Can ask bugd bids |      |      | Bil. negotiat at all |      |      | Special powers |          |          | Full cab resolves |      |      | Cab.can override |      |      | Sum, FM strenght |            |          |            |           |             |
|---------------------|------------------|------|------|-------------------|------|------|----------------------|------|------|----------------|----------|----------|-------------------|------|------|------------------|------|------|------------------|------------|----------|------------|-----------|-------------|
|                     | 1998             | 2003 | 2007 | 1998              | 2003 | 2007 | 1998                 | 2003 | 2007 | 1998           | 2003     | 2007     | 1998              | 2003 | 2007 | 1998             | 2003 | 2007 | 1998             |            | 2003     |            | 2007      |             |
| Bulgaria            | 4                | 4    | 4    | 0                 | 0    | 0    | 4                    | 4    | 4    | 0              | 0        | <b>4</b> | 0                 | 0    | 0    | 0                | 0    | 0    | score            | % of total | score    | % of total | score     | % of total  |
| Czech               | 4                | 4    | 4    | 0                 | 0    | 0    | 4                    | 4    | 4    | 0              | 0        | 0        | 0                 | 0    | 0    | 0                | 0    | 0    | 8                | 33,3       | 8        | 33,3       | <b>12</b> | <b>50,0</b> |
| Estonia             | 4                | 4    | 4    | 0                 | 0    | 0    | 4                    | 4    | 4    | 4              | 4        | 4        | 0                 | 0    | 0    | 0                | 0    | 0    | 12               | 50,0       | 12       | 50,0       | 12        | 50,0        |
| Hungary             | 4                | 4    | 4    | 0                 | 0    | 0    | 4                    | 4    | 4    | 4              | <i>0</i> | 0        | 0                 | 0    | 0    | 0                | 0    | 0    | 12               | 50,0       | <i>8</i> | 33,3       | 8         | 33,3        |
| Latvia              | 4                | 4    | 4    | 0                 | 0    | 0    | 4                    | 4    | 4    | 0              | 0        | <b>4</b> | 0                 | 0    | 0    | 0                | 0    | 0    | 8                | 33,3       | 8        | 33,3       | <b>12</b> | <b>50,0</b> |
| Lithuania           | 4                | 4    | 4    | 0                 | 0    | 0    | 4                    | 4    | 4    | 4              | 4        | 4        | 0                 | 0    | 0    | 0                | 0    | 0    | 12               | 50,0       | 12       | 50,0       | 12        | 50,0        |
| Poland              | 4                | 4    | 4    | 0                 | 0    | 0    | 4                    | 4    | 4    | 0              | 0        | 0        | 0                 | 0    | 0    | 0                | 0    | 0    | 8                | 33,3       | 8        | 33,3       | 8         | 33,3        |
| Romania             | 4                | 4    | 4    | 0                 | 0    | 0    | 4                    | 4    | 4    | 0              | 0        | 0        | 0                 | 0    | 0    | 0                | 0    | 0    | 8                | 33,3       | 8        | 33,3       | 8         | 33,3        |
| Slovakia            | 4                | 4    | 4    | 0                 | 0    | 0    | 4                    | 4    | 4    | 0              | 0        | 0        | 0                 | 0    | 0    | 0                | 0    | 0    | 8                | 33,3       | 8        | 33,3       | 8         | 33,3        |
| Slovenia            | 4                | 4    | 4    | 0                 | 0    | 0    | 4                    | 4    | 4    | 4              | 4        | <i>0</i> | 0                 | 0    | 0    | 0                | 0    | 0    | 12               | 50,0       | 12       | 50,0       | <i>8</i>  | <i>33,3</i> |
| <b>CEEC Average</b> | 4,0              | 4,0  | 4,0  | 0,0               | 0,0  | 0,0  | 4,0                  | 4,0  | 4,0  | 1,6            | 1,2      | 1,6      | 0,0               | 0,0  | 0,0  | 0,0              | 0,0  | 0,0  | 9,6              | 40,0       | 9,2      | 38,3       | 9,6       | 40,0        |

Notes: With the exception of the question whether ministers can ask cabinet for decisions on the budget bids, all answers are scored a 4 if they are yes and a 0 if they are no. Changes from 2003 to 2007 that increase the index appear in **bold** while changes that decrease the index appear in *italics*. The maximum value is 24.

## Structure of the Parliamentary Process

After the executive has formulated the budget proposal, the legislature debates, amends and finally votes on it. The data presented in this section describes the legislatures' role in the budget process. A considerable body of literature has examined decision-making within legislatures, and the relative powers between the executive and legislature. It has focused on the functioning of parliamentary committees in general, and on procedural rules, which determine how the legislature can alter the executive's budget proposal. 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<sup>12</sup>. The voting and the amendment rules are in the heart of this discussion.

The index for parliamentary process includes four components. The first three have to do with the existence of amendments and the nature of those amendments. A larger score is received if the amendments are limited and if expenditure increases require expenditure cuts elsewhere. 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. The third component asks if the amendments can cause a fall of government. The parties supporting the government may refrain from defeating the budget proposal for fear of creating a political crisis. 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. The final component asks if the parliament votes first on total size and only then on individual items in the budget, or vice versa. One can also make a 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). The argument is that a more top-down approach should lead to better fiscal discipline.

Once again, the changes in the index-values have been negligible. In Poland the amendments were not limited until 1998/1999 and the same was the case in Romania until 2003/2004. There is a rather large variation between the countries ranging from just a score of four representing in percentage terms a score of only 25 % of possible points (Bulgaria and the Czech Republic) to 12 or 75 % of the total (Latvia, Slovenia). Again, the EU-15 has, in general, higher average scores.

---

<sup>12</sup> 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".

**Table 5: Structure of the Parliamentary Process**

| Country              | Amend Limited |          |          | Amend Offsetting |          |          | Amend Cause Fall |      |      | Global Vote |      |      | Sum Parliament |            |          |             |           |             |
|----------------------|---------------|----------|----------|------------------|----------|----------|------------------|------|------|-------------|------|------|----------------|------------|----------|-------------|-----------|-------------|
|                      | 1998          | 2003     | 2007     | 1998             | 2003     | 2007     | 1998             | 2003 | 2007 | 1998        | 2003 | 2007 | 1998           |            | 2003     |             | 2007      |             |
|                      |               |          |          |                  |          |          |                  |      |      |             |      |      | score          | % of total | score    | % of total  | score     | % of total  |
| Bulgaria             | 0             | 0        | 0        | 0                | 0        | 0        | 0                | 0    | 0    | 4           | 4    | 4    | 4              | 25,0       | 4        | 25,0        | 4         | 25,0        |
| Czech                | 0             | 0        | 0        | 0                | 0        | 0        | 0                | 0    | 0    | 4           | 4    | 4    | 4              | 25,0       | 4        | 25,0        | 4         | 25,0        |
| Estonia              | 4             | 4        | 4        | 2                | 2        | 2        | 0                | 0    | 0    | 2           | 2    | 2    | 8              | 50,0       | 8        | 50,0        | 8         | 50,0        |
| Hungary              | 0             | 0        | 0        | 0                | 0        | 0        | 0                | 0    | 0    | 2           | 2    | 2    | 2              | 12,5       | 2        | 12,5        | 2         | 12,5        |
| Latvia               | 4             | 4        | 4        | 2                | 2        | 2        | 4                | 4    | 4    | 2           | 2    | 2    | 12             | 75,0       | 12       | 75,0        | 12        | 75,0        |
| Lithuania            | 4             | 4        | 4        | 2                | 2        | 2        | 0                | 0    | 0    | 2           | 2    | 2    | 8              | 50,0       | 8        | 50,0        | 8         | 50,0        |
| Poland               | 0             | <b>4</b> | 4        | 0                | <b>2</b> | 2        | 0                | 0    | 0    | 0           | 2    | 2    | 0              | 0,0        | <b>8</b> | <b>50,0</b> | 8         | 50,0        |
| Romania              | 0             | 0        | <b>4</b> | 0                | 0        | <b>4</b> | 0                | 0    | 0    | 2           | 2    | 2    | 2              | 12,5       | 2        | 12,5        | <b>10</b> | <b>62,5</b> |
| Slovakia             | 0             | 0        | 0        | 0                | 0        | 0        | 4                | 4    | 4    | 2           | 2    | 2    | 6              | 37,5       | 6        | 37,5        | 6         | 37,5        |
| Slovenia             | 4             | 4        | 4        | 2                | 2        | 2        | 4                | 4    | 4    | 2           | 2    | 2    | 12             | 75,0       | 12       | 75,0        | 12        | 75,0        |
| <b>CEEC Average</b>  | 1,6           | 2,0      | 2,4      | 0,8              | 1,0      | 1,4      | 1,2              | 1,2  | 1,2  | 2,2         | 2,4  | 2,4  | 5,8            | 36,3       | 6,6      | 41,3        | 7,4       | 46,3        |
| <b>EU-15 Average</b> | 1,6           |          |          | 2,1              |          |          | 3,2              |      |      | 2,9         |      |      | 9,8            |            | 61,3     |             |           |             |

Notes: **Amendments Limited:** 4 Yes; 0 No; **Amendments Offsetting:** 4 any expenditure increases require expenditure cuts elsewhere; 2 expenditure increases require corresponding expenditure cuts and/or revenue increases; 0 no; **Amendments Can Cause Fall of Government:** 4 Yes 0 No **Expenditures in One Vote** 4 Chapter by Chapter 0 Not Chapter by Chapter **Global Vote on Total Budget:** 4 Yes 0 No. Changes from 2003 to 2007 that increase the index appear in **bold**. Figures for the EU-15 are from 2004 and come from Hallerberg, Strauch, and von Hagen (2009). The maximum value is 16.

### Flexibility of Budget Execution

The final section presents information about the finance ministry's role in implementation of the budget. The easier it is to change the budget during its execution, the easier it is to undermine the discipline in the budget. If the implementation of the budget respects the plans and targets set in the planning stage, fiscal discipline should be enhanced.

Von Hagen (1992) focuses on six items in the implementation stage. The first component considers whether or not the finance minister can block the expenditure. Second component asks if the finance minister can impose cash limits and the third component if the finance minister must approve disbursement of funds before they are spent. Affirmative answers to the first three questions receive a score of four and negative answers a score of zero. The fourth aspect considers how easily funds can be transferred between chapters. More restricted this is, more points are awarded. The fifth component asks if it is possible to carry over unused funds into the following year. Negative answers receive a score of four and affirmative answers a score of zero. Final item shows if the changes in budget law allowed during budget execution. Again, negative replies receive most points and affirmative a score of zero. If changes are allowed but has to be voted by Parliament, two points are awarded.

Based on the data, the practises on budget execution have not evolved before or after the EU membership. In general, the level of index-values is rather low, suggesting that the implementation stage of the budget process is not particularly strong in most of the countries. In almost all of the countries it is possible to change the budget law in the middle of the year. It is common that the changes has to be approved by the Parliament but this seems to be a formality in many countries and the changes have typically appeared most years. This, coupled with the fact that the expenditure plans are in many cases only indicative, is contributing to fiscal laxity.

**Table 6: Flexibility of Budget Execution**

| Country              | MF can Block |      |      | Cash Limits |      |      | Disbursement |      |      | Transfers |      |      | Carry-over |      |      | Budget Changes |      |      | Sum Execution |            |       |            |       |            |
|----------------------|--------------|------|------|-------------|------|------|--------------|------|------|-----------|------|------|------------|------|------|----------------|------|------|---------------|------------|-------|------------|-------|------------|
|                      | 1998         | 2003 | 2007 | 1998        | 2003 | 2007 | 1998         | 2003 | 2007 | 1998      | 2003 | 2007 | 1998       | 2003 | 2007 | 1998           | 2003 | 2007 | 1998          |            | 2003  |            | 2007  |            |
| Bulgaria             | 4            | 4    | 4    | 4           | 4    | 4    | 0            | 0    | 0    | 1,6       | 1,6  | 1,6  | 4          | 4    | 4    | 2              | 2    | 2    | score         | % of total | score | % of total | score | % of total |
| Czech                | 0            | 0    | 0    | 4           | 4    | 4    | 0            | 0    | 0    | 1,6       | 1,6  | 1,6  | 1,33       | 1,33 | 1,33 | 0              | 0    | 0    | 15,6          | 65,0       | 15,60 | 65,0       | 15,60 | 65,0       |
| Estonia              | 0            | 0    | 0    | 0           | 0    | 0    | 0            | 0    | 0    | 4         | 4    | 4    | 2,66       | 2,66 | 2,66 | 0              | 0    | 0    | 6,93          | 28,9       | 6,93  | 28,9       | 6,93  | 28,9       |
| Hungary              | 0            | 0    | 0    | 0           | 0    | 0    | 0            | 0    | 0    | 4         | 4    | 4    | 1,33       | 1,33 | 1,33 | 0              | 0    | 0    | 6,66          | 27,8       | 6,66  | 27,8       | 6,66  | 27,8       |
| Latvia               | 4            | 4    | 4    | 0           | 0    | 0    | 0            | 0    | 0    | 4         | 4    | 4    | 1,33       | 1,33 | 1,33 | 0              | 0    | 0    | 5,33          | 22,2       | 5,33  | 22,2       | 5,33  | 22,2       |
| Lithuania            | 0            | 0    | 0    | 4           | 4    | 4    | 4            | 4    | 4    | 1,6       | 1,6  | 1,6  | 4          | 1,33 | 1,33 | 0              | 0    | 0    | 9,33          | 38,9       | 9,33  | 38,9       | 9,33  | 38,9       |
| Poland               | 4            | 4    | 4    | 0           | 0    | 0    | 4            | 4    | 4    | 1,6       | 1,6  | 1,6  | 1,33       | 1,33 | 1,33 | 2              | 2    | 2    | 13,6          | 56,7       | 10,93 | 45,5       | 10,93 | 45,5       |
| Romania              | 0            | 0    | 0    | 0           | 0    | 0    | 4            | 4    | 4    | 1,6       | 1,6  | 1,6  | 1,33       | 1,33 | 1,33 | 0              | 0    | 0    | 12,9          | 53,9       | 12,93 | 53,9       | 12,93 | 53,9       |
| Slovakia             | 4            | 4    | 4    | 0           | 0    | 0    | 0            | 0    | 0    | 1,6       | 1,6  | 1,6  | 1,33       | 1,33 | 1,33 | 0              | 0    | 0    | 6,93          | 28,9       | 6,93  | 28,9       | 6,93  | 28,9       |
| Slovenia             | 4            | 4    | 4    | 4           | 4    | 4    | 0            | 0    | 0    | 0,8       | 0,8  | 0,8  | 1,33       | 1,33 | 1,33 | 0              | 0    | 0    | 10,1          | 42,2       | 10,13 | 42,2       | 10,13 | 42,2       |
| <b>CEEC Average</b>  | 2,0          | 2,0  | 2,0  | 1,6         | 1,6  | 1,6  | 1,2          | 1,2  | 1,2  | 2,2       | 2,2  | 2,2  | 2,0        | 1,7  | 1,7  | 0,4            | 0,4  | 0,4  | 9,4           | 39,3       | 9,2   | 38,2       | 9,2   | 38,2       |
| <b>EU-15 Average</b> | 2,9          |      |      | 2,7         |      |      | 2,1          |      |      | 1,8       |      |      | 1,7        |      |      | 1,4            |      |      | 12,8 53,3     |            |       |            |       |            |

Notes: **Finance Minister Block:** 4 Yes; 0 No; **Finance Minister Cash Limits:** 4 Yes; 0 No; **Finance Minister Disbursement Approval:** 4 Yes; 0 No; **Transfers:** 4 only w/in depts, require FM consent; or not allowed/ only w/in departments; 2.4 only within chapters; 1.6 limited, require FM approval; 0.8 limited; 0 Unrestricted; **Carryover Provisions:** 4 Carryovers not possible 2.66 limited, require Finance Minister approval 1.33 limited 0 unlimited; **Budget Changes:** 4 no changes allowed; 2 changes allowed but has to be voted by Parliament; 0 changes allowed. Changes from 2003 to 2007 that increase the index appear in **bold**. Figures for the EU-15 are from 2004 and come from Hallerberg, Strauch, and von Hagen (2009). The maximum value is 24.

### Aggregate Measures

This section considers to aggregate measures of the centralization of the budget process. The first corresponds to a “Delegation” index, which are the attributes that one would expect to find in a country with a delegation form of fiscal governance. In practice, this is the average of the formulation, parliamentary, and execution stages. As explained earlier in the paper, this form of fiscal governance is expected in countries with one-party majority governments, or in governments where parties run in two opposing ideological blocks and where the parties in coalition are ideologically very close to one another. There is only one example of such a country in our dataset, which is Hungary. The other countries are expected fiscal contract states, and we include a “contacts” index, which is simply the long term constraints index that appeared earlier in the paper. A country that has the most centralized institutions would have all attributes expected, and it would have a score of 100. Also, for comparison, we include the average scores from the EU-15 for 2004, which appear in Hallerberg, Strauch, and von Hagen (2009).

If one looks at these figures in broad terms, in the run-up to EU accession the biggest change has been the introduction of the multi-annual frameworks. However, it is clear that there has been no effort to change institutions once countries entered the European Union. If one looks at 2003 and 2007, the institutions are the in all countries but the Czech Republic and Romania



according to these measures, and in both cases a country moved from the worst country in the respective group to somewhat below average. When one considers the expected form of fiscal governance and actual institutions in place, Hungary is noteworthy for being a place where delegation should be especially effective but also where the score in 2007 on delegation is the lowest in the group after reforms in Romania. One would expect fiscal performance to be poor once one takes account of cyclical factors, and indeed, Hungary had budget deficits of over 9% of GDP in 2006, or three times the Maastricht limit for countries seeking to join the euro. The remaining countries are expected fiscal contract countries. While Slovenia's score of 81.3 out of 100 is the highest for the group (along with Estonia) and it was the first country from this group to join the eurozone, it is still below the EU-15 average in 2004.

**Table 7: Aggregate Scores for Delegation and Contracts**

| Country              | Sum, Delegation |      |      | Sum, Contracts |      |      |
|----------------------|-----------------|------|------|----------------|------|------|
|                      | 1998            | 2003 | 2007 | 1998           | 2003 | 2007 |
| Bulgaria             | 34,2            | 55,0 | 55,0 | 0              | 62,5 | 62,5 |
| Czech                | 38,8            | 38,8 | 38,8 | 0              | 18,8 | 56,3 |
| Estonia              | 50,9            | 50,9 | 50,9 | 0              | 81,3 | 81,3 |
| Hungary              | 26,8            | 26,8 | 29,6 | 0              | 62,5 | 62,5 |
| Latvia               | 63,0            | 63,0 | 63,0 | 0              | 62,5 | 62,5 |
| Lithuania            | 35,6            | 51,3 | 51,3 | 0              | 62,5 | 62,5 |
| Poland               | 22,1            | 49,9 | 49,9 | 0              | 62,5 | 62,5 |
| Romania              | 26,3            | 26,3 | 45,7 | 0              | 56,3 | 56,3 |
| Slovakia             | 41,6            | 41,6 | 41,6 | 0              | 62,5 | 62,5 |
| Slovenia             | 68,2            | 68,2 | 68,2 | 0              | 81,3 | 81,3 |
| <b>CEEC Average</b>  | 40,7            | 47,2 | 49,4 | 0,0            | 61,3 | 65,0 |
| <b>EU-15 Average</b> |                 | 65,0 |      |                | 85,5 |      |

Figures for the EU-15 are from 2004 and come from Hallerberg, Strauch, and von Hagen (2009). The maximum score is 100.

## Conclusion

This paper assesses the development of fiscal institutions in Central and East European countries pre- and post-accession to the European Union. Others have found that these countries made efforts to reform domestic institutions in the run-up to accession, but that they then relaxed such efforts, and even moved backwards, after they joined. In the case of fiscal policy, one can speculate that eurozone membership can serve as an additional carrot to the one of initial accession. To qualify for membership, one must be in compliance with the "Maastricht criteria," which include direct restrictions on fiscal policy (deficits and debts) as well as more indirect restrictions (there are restrictions on the level of inflation, and expansionary fiscal policy can contribute to increased prices). The centralization of the budget process strengthens fiscal discipline and makes it

more likely that a given country will be able to qualify. The fact that Slovenia had the highest score on the “contracts” index is consistent with the view that one needs stronger institutions for EMU, and any moves by Slovakia to improve its fiscal institutions would reinforce this conclusion. Moreover, data from these countries that indicates that have increased their linkage of their domestic budgets to their EU-submitted convergence and/or stability programmes, which is not included in the aggregate indices, suggests that euro adoption does have some effect on domestic budget-making.

Our findings have implications for the Europeanisation literature. The focus of most arguments in this tradition is on the effect that EU accession played in encouraging domestic reforms. Moreover, work done after accession indicates that there has been a general pause in reform efforts, with some countries in some policy fields even moving “backwards.” Our expectation was that the fiscal policy realm may have been different because of the additional carrot that is present once one accedes to the European Union, namely eurozone membership. We therefore expected that, unlike in other policy fields, there may have been continued change after these countries became EU members. This expectation was not met. Consistent with the broader literature, we find that preparations for the EU accession did lead to some changes in budget process in this set of countries. There has been almost no change after accession. Moreover, relative to the EU-15, their budget processes are not particularly centralized—no country in this group has a score higher than the EU-15 average. It is clear that all countries have further reforms before them if they wish to improve fiscal discipline. In some countries further reforms to develop medium-term fiscal frameworks are either planned or being initiated but it is too early to say if the reforms will transform the frameworks into a vehicle that would impose a serious constraint for government spending.

## Appendix

| Country   | Planned reforms  |
|-----------|--|
| Bulgaria  | The Decision of the Council of Ministers concerning the budget procedure for 2008; medium-term fiscal framework and expenditure ceilings by first-level spending units (2008-2010). The rules allow amendments to the expenditure ceilings if there are substantial changes in the macroeconomic forecasts or in the policies pursued.                             |
| Czech     | No major reforms planned   |
| Estonia   | Plans for a new organic budget law, including more stable medium-term framework  |
| Hungary   | Act on Public Finances amended in 2007: the Government may only submit to Parliament a budget bill that assures the primary surplus of the Maastricht balance indicator of the government sector. The 2008 budget bill intends to introduce medium-term expenditure ceilings with the appropriation and expenditure figures for ministries three years in advance. |
| Latvia    | For 2008 budget, a new medium-term framework with a budget law for one year and maximum spending amount for the following two years broken down by ministry.   |
| Lithuania | New revenue and expenditure rules entered into force in 2008   |
| Poland    | New draft public finance law presented   |
| Romania   | No major reforms planned   |
| Slovakia  | No major reforms planned   |
| Slovenia  | No major reforms planned   |

Notes: Source: 2006 and 2007 Convergence/Stability Programmes

## Bibliography

- Börzel, Tanja, and Thomas Risse. (2000) 'When Europe hits home: Europeanization and domestic change', *European Integration Online Papers* 4(15), available at <<http://eiop.or.at/eiop/texte/2000-015a.htm> >
- Dyson, Kenneth. (ed.) (2006). *Enlarging the Euro Area: External Empowerment and Domestic Transformation in East Central Europe*. Oxford: Oxford University Press.
- Fabrizio, Stefania and Ashoka Mody. 2006. Can Budget Institutions Counteract Political Indiscipline? *Economic Policy* 21(48):689-739.
- Gleich, Holger. 2003. "Budget Institutions and Fiscal Performance in Central and Eastern European Countries." ECB Working Paper No. 215. February.
- Hallerberg, Mark, Rolf Strauch, and Jürgen von Hagen. 2009. *Fiscal Governance: Evidence from Europe*. Cambridge University Press.
- Hallerberg, Mark, and Eloïse Stéclebout-Orseau. 2007. "Who Provides Signals to Voters About Governance Competence on Fiscal Matters? The Importance of Independent Watchdogs." *European Economy-Economic Papers*. Number 275 (April): 243-268.
- Hallerberg, Mark. 2004. *Domestic Budgets in a United Europe: Fiscal Governance from the End of Bretton Woods to EMU*. Ithaca, NY: Cornell University Press.
- Kelley, Judith. 2006. "New Wine in Old Wineskins: Promoting Political Reforms through the New European Neighborhood Policy." *Journal of Common Market Studies*. 44, 1: 29-55.
- Kontopoulos, Yanas., Perotti, Roberto., 1999. "Government fragmentation and fiscal policy outcomes: evidence from OECD countries." In: Poterba, James, von Hagen, Jürgen. (Eds.), *Fiscal Institutions and Fiscal Performance*. University of Chicago Press, Chicago, pp. 81–102.

- Morris, Richard, Hedwig Ongena, and Ludger Schuknecht. 2006. "The Reform and Implementation of the Stability and Growth Pact." European Central Bank Occasional Paper No. 47, June.
- Mungiu-Pippidi, Alina. 2007. "Is East-Central Europe Backsliding? EU Accession is no 'End of History.'" *Journal of Democracy*. 18, 4 (October): 8-16.
- Schimmelfennig, Frank. 2003. *The EU, NATO and the Integration of Europe. Rules and Rhetoric*, Cambridge: Cambridge University Press.
- Schimmelfennig, Frank, and Ulric. Sedelmeier. 2004. "Governance by Conditionality: EU Rule Transfer to the Candidate Countries of Central and Eastern Europe." *Journal of European Public Policy*. 11. 4: 661-679.
- Schimmelfennig, Frank, and Ulric. Sedelmeier, Eds. 2005?. *The Europeanization of Central and Eastern Europe*, Ithaca: Cornell University Press.
- Vachudova, Milada Anna. 2005. *Europe Undivided: Democracy, Leverage, and Integration after Communism*. Oxford: Oxford University Press.
- Yläoutinen, Sami. 2005. "Development and Functioning of Fiscal Frameworks in the Central and Eastern European Countries." Dissertation, Jyväskylä Studies in Business and Economics 42, University of Jyväskylä.