Modern government – responsible management of public funds

When the re-elected government of PM Ferenc Gyurcsány announced its New Equilibrium Programme, immediately after its creation in June 2006, many felt doubt about it, both among professionals and others.

This Programme is fairly ambitious in terms of fiscal consolidation and public sector reforms, particularly to ensure a long-term sustainable path of economic growth, convergence and to prevent the decade-long practice of cyclical disequilibrium from returning.

Doubts are much understandable, mainly if we look back to the past 16 years or to an even longer period of time. It is not new that with elections coming up the government in office ais less susceptible to equilibrium criteria. Instead, they are prone to serve a comfort feeling of the voters.

We have worked on the implementation of the programme for a year or so. The views tend to change during such a long time in many respects. Today you cannot hear voices of whether the Government is serious enough about the fiscal consolidation. Results are convincing. Good progress was made in fiscal consolidation, and at the same time, reforms are about to come in healthcare, public administration (central government), education and pension system.

The ruling government did not hesitate to touch former taboos such as gas price subsidies, which had been rather expensive and socially unjust or the rules of drug subsidies, which had been unable to impede drug budget overruns. Also, the transformation of travelling and public transport subsidies is not to underestimate.

Government budget positions changed a lot from the previous years due to austerity measures. The measures are to make impacts in harmony with one another, resulting in a part of black and grey economy to be whitening, coupled with a better taxpayer morale and making tax avoidance or evasion much riskier in a period when the Government was forced to increase taxes to improve equilibrium including an increased tax burden for all.

Changes are sensible on both sides of the budget. Financial management in the public sector has become more severe and tightened. We could feel in the second six months of 2006, like in the first four months of 2007, that ministries and agencies were kept within the limits established. Significant overrun has not been seen. On the revenue-side, increasing amount of money come from taxes. Excise taxes have jumped due certainly to stricter and enhanced checking activity while contribution payments have been better as well. There is no worry about VAT and PIT receipts. As a result, monthly projections have been met from time to time for a year or so without any bad surprise.

Consequently, confidence is significantly growing towards the Hungarian economy. The key sign of the favourable sentiments is a very strong Hungarian forint for more than six months. In Hungary, we also attach high importance to the signals and warnings received from the European Commission, the International Monetary Fund or OECD. These institutes all confirm that our efforts are efficient and we have started to go on the right path.

A year is, of course, not so long time. Our programme is accordingly laid out for several years. All the more so, because we have to make up for a lot of deficiencies or actions what the previous governments failed to implement over a decade or more. The postponement of the relevant decisions is also explained by the necessary but unpopular moves of such a programme. However, now is the time to act. The Gyurcsány Government made the relevant decisions and insisting on those. This consistency is reflected in the first results and positive feedback from experts who add, however, that the process must go on.

Next steps are the reforms in the public sector as included in the Convergence Programme with the modernisation of government budget system.

Public sector reform is expected to modernise the state including the elimination of stresses whereby keeping the balance that was disallowed in the recent years. Nevertheless, it is not satisfactory. We also need to establish a regulatory framework to warn of emerging concerns, new developments that are to threaten the equilibrium and preventing from inconsiderate decisions, which may well result in more indebtedness on a longer term. In a word, this framework could provide for the equilibrium to be kept for real in the activity of government and Parliament.

In this context, not only the governments of all times should be contained but also the Parliament had better ensure that these rules are set out in laws and enforced with long-term interests of Hungary kept in mind.

That is the way we have started but we are in the beginning thereof.

We are aware ever so long of needing fiscal rules. The mechanism of budget planning, preparations and financial management of the public sector should be reformed. We knew but only now is the time to implement it.

Therefore, the government budget for 2007 contains some built-in rules in the context. The Parliament approved two such rules at the time of adoption of the government budget for 2007.

In particular, the primary balance shall not be negative from 2008 on while the budget accounts shall have to show increasing surpluses from year to year as laid down in the law. This is necessary for the indebtedness not to grow in proportion to GDP but to be lower.

Another budget rule is bound for the ministries – budget chapters – not to spend automatically their allowances – established by the Parliament – but to make equilibrium reserves from a part thereof. The Government is, at regular intervals, to decide on the availability of the funds in reserve, based on evaluation of the ministries' activity including their spending policy. This arrangement is in operation. The first evaluation was held in April 2007 following the quarter 1, and some 25 per cent of the funds in reserve were released for use in May.

However, more should be done because these do not result in an overall budget management reform.

Now we are preparing for a full-ranging new regulatory framework of public finances in co-operation with the State Audit Office and government experts in charge and with the significant knowledge basis of the wider professional community involved. We have changed the practice of law preparatory works. The new cooperation is expected to ensure that the proposals are considered more than a simple government plan but a document that reflects an opinion supported by a wider professional community.

The work underway is to cover almost all the sectors and fields of fiscal management set for reform.

The first draft legislation of public asset management was prepared in May so the Parliament can decide on it in the first six months of 2007. In the draft, the emphasis is on the management or utilization of public assets, rather than on privatisation. The fundamental phase of privatisation is over; the key privatisation transactions were finished. Accordingly, a new organisational structure will be established with updated operational rules.

Also, a first draft has been prepared of a status law applying to the operations of government agencies. The draft will probably be put forward to the Parliament in the second six months of 2007. Further consultations are needed to create a final form to be approved by the Government.

In addition, we have two bills under preparation.

One is about the responsibility for public finances, establishing the Parliament's Budget Office. In the law, there are three fiscal policy rules in the framework of equilibrium security scheme the most important of which is to keep the level of real indebtedness on hold. That is, government debt shall not increase faster than headline inflation. To this end, the primary balance should be in line. With local governments being a part of the public sector, their indebtedness should statutorily be regulated. In the context, the rule would be to limit net borrowings in relation to the investment projects.

The draft law contains detailed budget procedural rules. Government budget has to be adopted year by year in the future as well while we know that certain budget allowances could well be worked out in broad lines years beforehand. Equilibrium-securing annual budgets shall be elaborated only if the relevant decisions consider the following years' budget allowances. To this end, a mid-term government budget plan is prepared to set out the funding to budget chapters in a forward-looking approach to the following three years.

The law would forbid the Parliament to discuss any bill or amendment motion, which could increase the deficit in a year or next years failing which the most important rule of real indebtedness could not be met.

Finally, we plan to amend the public finance law expected to be streamlined due to the legislation mentioned above by adjusting and building in that in the new legislation structure.

Although the legislation changes are hoped to be prepared quickly enough, still in the year, their full impact will be felt only from the following year by the nature of the *new system. However, the change is significant even on a short run, partly because the decision-makers' approach or way of thinking will change as well and because more and more elements of the ruling scheme will prevail each year. The built-in brakes will retailor the room for manoeuvre of politicians as with elections coming up.*

It is a question at the same time how to create consensus in the present political field, allowing for the new rules to be adopted. The agreement on the fundamental issue, that the country or the national economy shall not be exposed to the risk of increasing indebtedness, is in place. There is no dispute over how important is to secure equilibrium.

Hopefully, we could create a consensus of providing for the necessary Parliamentary conditions required for the responsible management of public funds including the rules to guarantee and enforce those.

I think it is important and useful for Pénzügyi Szemle (Public Finance Quarterly) to take part, in its own way, in creating consensus by disclosing the efforts to update the mechanism of public funds management in its thematic issue as well as the studies, prepared by authentic domestic and foreign authors, presenting the relevant professional background.

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