Raad van State

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2021 Spring Report

A. ASSESSMENT

1. Introduction

The Advisory Division of the Council of State has been charged with the independent budgetary monitoring of compliance with (European) fiscal rules as referred to in the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (TSCG) and Article 5 of Regulation (EU) 473/2013. It is the task of the independent fiscal monitoring institute to draw up an assessment of whether European fiscal rules are being met. In its assessment the Advisory Division works closely with the CPB Netherlands Bureau for Economic Policy Analysis. The division of tasks entails that the drawing up of independent economic and budgetary forecasts and analyses are assigned to the CPB Netherlands Bureau for Economic Policy Analysis; the Advisory Division has been charged with the more normative assessment of compliance with (European) fiscal rules.

The Advisory Division generally publishes two reports a year, in April and September. In the reports it provides an assessment of the expected budgetary developments and intentions as adopted by the government in the Stability Programme and Budget Memorandum, respectively.

In the interests of quality and accuracy in drawing up the assessment, the Advisory Division was able to consult a draft of the Stability Programme for the Spring Report. On the basis of this, the Advisory Division has drawn up a draft assessment, which has been reviewed with the government on the principle of adversarial debate The Division has made its final assessment after being informed of the government's response. The government's response is included in full in this report.

Summary conclusion and advice

In this report the Advisory Division concludes that budgetary developments for 2020 and 2021 with an actual EMU balance of -4.3% of GDP respectively -5.9% GDP do not comply with *European fiscal rules* (with a reference value of -3.0% of GDP). If an assessment is made of the provision related to extraordinary events, the picture is expected to be more nuanced. For 2022, the structural EMU balance is estimated at -1.4% of GDP; as a result the Netherlands does not comply with the medium-term objective (MTO) of maximum -0.5% of GDP. By activating the general escape clause of the Stability and Growth Pact (SGP) this excess has no consequences. In any case, no excessive deficit procedure will be opened under this clause in 2020 and 2021. According to expectations the general escape clause will also apply in 2022. Government debt remains in all three years (2020: 54.4%, 2021: 58.6%, 2022: 56.9%) under the European target of 60% of GDP.

In the assessment of the *national budgetary rules,* the Advisory Division concludes that this year and next year there will be a deviation due to the budgetary consequences of the Covid-19 pandemic. The government, which has yet to be formed, must define the budgetary policy for the coming years.

Against the backdrop, the Advisory Division advises that *budgetary policy* be established transparently for the new government term, i.e. transparent and predictable. From the democratic perspective it is important that 'cornerstones' are formulated on the basis of which political decisions can be considered and accounted for. A transparent budgetary policy benefits from a fixed main decision-making point and expenditure and tax frameworks for the entire (four-year) government term.

The national budgetary policy to be defined for the next government's term of office must be reconcilable with European fiscal policy. In this context the Advisory Division advises the caretaker government to submit a Dutch Recovery and Resilience Plan, arising from the new European Recovery and Resilience Facility, to the European Commission before the summer, and not to leave this up to a new, incoming government. The Advisory Division sees possibilities, under certain conditions, to afford the Recovery and Resilience Facility a structural place in the European fiscal policy (fiscal framework) to be reviewed.

Lastly, the Advisory Division has inserted a number of marginal notes in the draft Stability Programme. The budgetary impact of the Covid-19 pandemic can be made more transparent with a more effective breakdown and explanation. The programme now includes a more positive and negative scenario as well as a basic projection. It strikes us that the downside risks are greater than the upward potential. It also contains an overview of European and international risk schemes under government guarantee; these now amount to over 30% of GDP.[1]

This Spring Report is structured as follows:

A. Assessment
   1. Introduction, summary conclusion and advice
   2. Macroeconomic and budgetary outlook
   3. Assessment in relation to European and national fiscal rules
   4. Advice for the (future) budgetary policy
   5. Conclusion and key message

[1] For the various marginal notes see sections B2,3, B3.1 and B4.

B. Analysis
1. Macroeconomic and budgetary forecasts
2. Further elaboration of the assessment of the fiscal rules
3. Focal points related to the budget information: transparency of the projections, Art 3.1 of the Government Accounts Act (CW), tax side of the budget, local and regional authorities.
4. Fulfilment of commitments previously made by the government
5. EU-wide state of affairs

2. The macroeconomic and budgetary outlook

Following an economic contraction of 3.7% in 2020, the CPB Netherlands Bureau for Economic Policy Analysis estimates economic growth of 2.2% in 2021 in the Central Economic Plan (CEP).[2] Due to a recovery that begins in the second quarter of this year, and a further acceleration in the second half of 2021, at the end of the year, the economy will surpass the level prior to the Covid-19 pandemic. In 2022, there will be further catch-up growth and GDP will grow by 3.5%. Compared with the eurozone (Contraction of 6.8% of GDP) the contraction of the Dutch economy has been limited in 2020. In 2021 and 2022, growth will lag behind the 4% growth of the eurozone in both years.

Table 1: Macroeconomic core data

(Changes in % per year)	2020	2021	2022
Gross domestic product Eurozone (economic growth)	-6.8	4.0	4.0
Gross domestic product the Netherlands (economic growth)	-3.7	2.2	3.5
Unemployment (rate, % of working population)	3.8	4.4	4.7
Actual EMU balance (% of GDP)	-4.3	-5.9	-1.7
Government debt (% of GDP)	54.4	58.6	56.9

Source: CBP Netherlands Bureau for Economic Policy Analysis, Macroeconomic Outlook 2021 and Central Economic Plan 2021

Government spending plays an important role in GDP development and has severely limited the number of bankruptcies and the rise in unemployment. In 2020, unemployment was, with an average of 3.8%, just 0.4 of a point higher than in 2019. It should be noted that there are considerable differences between groups: mainly young people and employees with a flexible employment contract have become unemployed. When the support measures come to an end, unemployment will increase by an average 4.4% in 2021 to an average of 4.7% in 2022. Consumption will rise sharply once the restrictions are removed, partly as a result of an increase in savings. This will provide an increase in company investments. Exports will also increase in both 2021 and 2022 due to a European and global recovery.

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[2] CPB Netherlands Bureau for Economic Policy Analysis (2021). Central Economic Plan 2021, https://www.cpb.nl/en/projections-march-2021-cep-2021

Unlike in previous recessions, the government has almost entirely absorbed the impact of the recession. Extensive support measures (including tax measures) amounted to €31.1 billion in 2020. In 2021, additional government spending in relation to the Covid-19 pandemic, amount to an estimated €29.8 billion. This includes additional healthcare expenditure in relation to the pandemic and the National Education Programme. As a result government spending shows a deficit of respectively 4.3% of GDP in 2020, and 5.9% of GDP in 2021, which means the deficit in 2010 of 5.2% during the Great Recession is exceeded. In 2022, the budget deficit will decrease to 1.7% of GDP. The structural balance (EC method) will show a deficit of 1.9% of GDP in 2020. In 2021, the balance will deteriorate further to -4.1% of GDP, to recover somewhat in 2022 to -1.4% of GDP. Due to the budget deficits and guarantees provided to businesses, government debt will increase from 54.4% of GDP in 2021 to respectively 58.6% and 56.9% in 2021 and 2022.

3. Assessment under European and national fiscal rules

3.1 Assessment under European rules

In its Spring Report, the Advisory Division assesses whether public finances in the previous year (*ex post*), in the current year (*in year*) and in the year ahead (*ex ante*) comply with the European fiscal rules.

Since the budget balance from 2013 up to and including 2019 complied with the maximum deficit of 3% of GDP, as permitted under the Stability and Growth Pact (SGP), the rules of the so-called ‘preventive arm’ of the Pact are relevant in terms of the assessment for these years. These rules impose requirements on the development of the so-called structural government balance (the budget balance corrected for the economic cycle and one-off measures) and for development in public expenditure. Furthermore, Government debt should be below 60% of GDP, or falling sufficiently in that direction, which was the case.

It goes without saying that there were extraordinary pandemic and economic circumstances in 2020 with the corresponding repercussions on public finances. These circumstances will (unfortunately) continue unabated this year. In March 2020, the European Commission declared the application of the provision in the SGP related to extraordinary events, thus excluding the budgetary impact of measures taken in response to the Covid-19 pandemic in assessing compliance with the SGP. In addition the general escape clause in the Stability and Growth Pact was activated, to offer Member States maximum flexibility within the SGP.[3]For Member States in the preventive arm (including the Netherlands) it

[3] European Commission, Communication from the Commission to the Council on the activation of the
general escape clause of the Stability and Growth Pact (General Escape Clause, GEC), COM (2020) 123 final, https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52020DC0123&from=EN

means that they may deviate from the path towards the medium-term objective (MTO) for the structural balance, providing it does not jeopardise sustainability of public finances in the medium term. No excessive deficit procedures will be opened either, due to the extreme uncertainty related to the macroeconomic and budgetary impact of the Covid-19 crisis. The general escape clause does not lead to the suspension of SGP procedures. Therefore, it remains important that the development of public finances is closely monitored and assessed.

Based on current projections it is expected that the general escape clause will also apply in 2022 and only be deactivated in 2023. The Commission will assess the deactivation or continuation of the general escape clause in May 2021 as part of the Spring Package of the European Semester.

Ex post assessment for the year 2020
Based on the actual figures of the CBS the Advisory Division concludes that in 2020 public finances did not temporarily comply with European fiscal rules. The actual budget balance in 2020 ended up showing a deficit of 4.3% of GDP (Table 3). As a result, the budget balance far exceeded the reference value of a maximum permitted deficit of 3.0% of GDP under the SGP. Due to the application of the provision related to extraordinary events, measures taken in response to the Covid-19 pandemic can be excluded. The government has not specifically assessed this provision, the outlook is expected to become more nuanced if the debt and balance are corrected for these measures.

The structural government balance does not comply with the MTO target for the Netherlands of -0.5% of GDP either. If it were to be measured against the growth of net adjusted government expenditure, it can be concluded that the target growth has been largely exceeded. Since the Netherlands is in the preventive arm, it may deviate from the path towards the MTO. At 54.4% of GDP in 2020, government debt remains below the European target of 60% of GDP.

Table 2: European budgetary rules data

(In % of GDP)	2020 *ex post*	2021 *in year*	2022 *ex ante*
EMU balance actual	-4.3	-5.9	-1.7
EMU balance structural (EC method)	-1.9	-4.1	-1.4
EMU debt	54.4	58.6	56,9

Source: CBS (Statline) and CPB Netherlands Bureau for Economic Policy Analysis, Central Economic Plan 2021, Table 3.1)

In year and ex ante
Based on the CEP projection by the CPB Netherlands Bureau for Economic Policy Analysis, the Advisory Division concludes that in 2021, the actual and structural balance currently exceeds the European fiscal targets. The actual and structural balance shows an improvement in 2022 and the actual balance complies once

more with the European targets. In 2021 and 2022, Dutch government debt remains within the limits of the European fiscal rules. Since the general escape clause has been activated in the SGP, in any case in 2021 no excessive deficit procedures will be opened and this year any overshoots will not have any consequences. According to expectations the general escape clause will also apply in 2022. When assessed against the provision regarding extraordinary events, the outlook is also expected to be more nuanced in 2021. As a result, despite the deterioration in the structural budget balance and government debt, European fiscal rules will not restrict budgetary policy.

3.2 Assessment under national budgetary rules

As the independent national fiscal monitoring institute, the Advisory Division also has the task of making public assessments regarding national fiscal rules. The years 2020 and 2021 are extraordinary due to the economic shock resulting from the Covid-19 crisis. This also extends to budgetary policy. Firstly, the Covid-19 crisis has resulted in support measures in addition to the automatic stabilisers on the income and expenditure side. The government has taken extensive support measures. After announcing the first emergency measures, 46 incidental supplementary budgetary laws were submitted by the government.[4]The budgetary impact of the Covid-19 crisis[5] and a total overview of the emergency measures[6] are presented in a single location.

On the expenditure side the government opted to keep the extra expenditure related to the Covid-19 pandemic outside the regular expenditure ceiling. Actual is separated via a ceiling correction.[7] The extra expenditure related to the Covid-19 pandemic thus leads to a deterioration of the EMU balance and an increase in the EMU debt. This means that no cuts need to be made to make room within the expenditure framework. This results in a temporary deviation from Dutch budgetary rules. For standard policy the government adheres to the applicable budgetary rules, to maintain as much calm and predictability as possible.

In addition to the extraordinary circumstance of extra expenditure related to the Covid-19 pandemic and the subsequent adjustment to the expenditure ceiling, this year there is a new government term. The tax and expenditure frameworks for the Rutte III government no longer apply after this year. A new government, yet to be formed must, of course, establish the frameworks for 2022 and subsequent years.

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4 Overview of supplementary budget financial Covid-19 measures, https://www.rijksoverheid.nl/documenten/begrotingen/2020/03/18/overzicht-suppletoire-begrotingen-financiele-maatregelen-coronavirus.

5 Public finances during the Covid-19 era, https://www.rijksfinancien.nl/overheidsfinancien-coronatijd?

6 Emergency Covid-19 measures, https://www.rijksfinancien.nl/overheidsfinancien-coronatijd/noodmaatregelen/uitgavenmaatregelen/noodmaatregelen-coronacrisis

7 Autumn Memorandum 2020, Parliamentary Documents 2019/20, 35650, no. 1, https://zoek.officielebekendmakingen.nl/kst-35650-1.html

4. Advice for improved performance and compliance with (European) fiscal policy.

The Advisory Division's task as an independent fiscal monitoring institute focuses on the performance and compliance of European and national fiscal policy.
Both European and national budgetary policy are currently in a state of flux.

New budgetary policy still has to be formulated...

Before the breakout of the Covid-19 pandemic, the European Commission had just started an evaluation of the current European fiscal policy (the Stability and Growth Pact, the Fiscal compact and the European Semester). The effects of the pandemic on European economies and public finances have understandably led to this evaluation being placed on hold. And in the meantime – as explained above – the provision related to extraordinary events and the general escape clause has been activated. The so-called stability programmes and budgets of the Member States are still being assessed, but last year, this year and (according to expectations) next year, they will not be ‘assessed' on the basis of the known deficit and debt criteria.

The European Commission has indicated that it will not continue the general escape clause when Member States - after next year in line with expectations - return to growth levels before the Covid-19 pandemic in 2019. In this context, the review of European fiscal policy will be undertaken at some point later this year.

When forming a new government, national budgetary policy is usually defined for the coming years. Against the background of the economic and budgetary forecasts during and after the Covid-19 crisis. The Netherlands Bureau for Economic Policy Analysis (CPB) recently published current projections (MLT, CEP).[8] The 16th Study Group on Fiscal Policy has issued opinions on the budgetary policy to be formulated.[9]

In the context of the necessary uncertainties

The extent to which the Covid-19 pandemic will cause lasting economic damage is a matter of debate. Some interpret the consequences as temporary: it is a temporary crisis the cause of which is not the economy itself, thus less disruptive than the financial and banking crisis 10 years ago, and the recovery to pre-Covid-

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[8] Central Economic Plan 2021, CPB (2021), https://www.cpb.nl/sites/default/files/omnidownload/Central-Economic-Plan-CEP-2021.pdf and Update of the Medium-Term Outlook 2022-2025, CPB Netherlands Bureau for Economic Policy Analysis (2021), https://www.cpb.nl/actualisatie-middellangetermijnverkenning-2022-2025-maart-2021

[9] 16th Study Group on Fiscal Policy (2020) Koers bepalen – Kiezen in tijden van budgettaire krapte (Setting the course - Decisions in times of budgetary constraint), https://www.rijksoverheid.nl/documenten/kamerstukken/2020/10/12/rapport-studiegroep-begrotingsruimte

19 levels will soon follow. Others expect structural consequences for global production and consumption chains, the exacerbation of differences between countries, and therefore structural damage.

The potential impact on sustainable public finances and on monetary and fiscal policy in the eurozone is also being debated. Elements include the future of (accommodative) monetary policy, debt sustainability estimates given future growth prospects, uncertainty about future interest rate levels and the more fundamental significance of demographics and the ageing population, respectively.

The state of public finances at the start of the new government term has two sides. On the one hand, although debt and deficit levels have deteriorated significantly over the past year, they are still on the safe side in European terms. On the other hand, the buffers for future crises have been sharply reduced, there is a sustainability deficit (1.8% of GDP) and the Netherlands faces major challenges with uncertainties regarding the future.

Democratic importance of national budgetary policy...

Uncertainties could be used to postpone the formulation of budgetary policy for a while. However, in its opinion on the Budget Memorandum 2021, the Advisory Division stressed the importance of orderly and predictable budgetary policy from a democratic perspective.[10] Budgetary policy is about ‘cornerstones' for political decisions, about ‘nailing one’s colours to the mast'. It requires a consideration of interests, topics and budgets and thus accountability to voters with regard to the decisions taken. Greater stability in political decision-making is achieved by performing integral considerations at fixed times. Therefore, the 16th Study Group on Fiscal Policy underlines the importance of a fixed main decision-making moment in the spring.[11]

The Netherlands is facing major long-term challenges (including the sustainability of healthcare spending, climate change, a housing shortage, labour market, education) that require political decision-making in the near future. The current crisis is expected to have a permanent impact on the economic structure, reinforcing previously initiated trends such as labour market dualisation, inequality of opportunities in education and digitisation. However, crises also provide momentum for structural and sustainability-enhancing reforms. In order to achieve economic recovery, expenditure is needed that is timely, temporary and targeted.

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[10] Draft Budget Memorandum 2021 and September Report on Budgetary Monitoring, Parliamentary Document II 2020/21, 35570, no. 3, W06.20.0288/III.

[11] 16th Study Group on Fiscal Policy (2020) Koers bepalen – Kiezen in tijden van budgettaire krapte (Setting the course - Decisions in times of budgetary constraint), https://www.rijksoverheid.nl/documenten/kamerstukken/2020/10/12/rapport-studiegroep-begrotingsruimte

The formulation of budgetary policy ensures that decisions and possible reforms are weighed up on the basis of politically chosen criteria. In addition to the long-term effects on public finances, these could include, for example, the impact on human capital (well-being) and natural capital (climate). In other words, aspects of broad prosperity can be taken into account when establishing cornerstones. *When* these cornerstones are established (politically), and used as the basis to formulate budgetary policy with fiscal rules, the (budgetary) considerations within that policy or within those rules, respectively, should take place *afterwards*.

In the Netherlands, the political formulation of budgetary policy has been well prepared by a new incoming government for many years because political parties have their election programmes calculated by the Netherlands Bureau for Economic Policy Analysis (CPB) (and recently also partly by the Netherlands Environmental Assessment Agency (PBL)). With all the limitations inherent to this type of calculation, this still represents best practice from a European perspective[12]

Of course, sufficient budget transparency is invariably an important democratic element as well.[13] Budgetary policy complements parliamentary fiscal law, and is thus also necessary to effectively improve the government's accountability to the House of Representatives and the Senate.

... and European fiscal policy.

In 2017, at the request of the House of Representatives, the Advisory Division issued guidance on improving compliance with the European budgetary agreements, and in 2019 on follow-up questions on the SGP.[14] Monetary union benefits from strengthened compliance with and enforcement of (fiscal) rules. This can be achieved - in addition to strengthening the no-bailout clause and completing the capital market and banking union - by reducing and simplifying rules, introducing positive incentives, making enforcement independent of political considerations and increasing decentralised enforcement. The latter guidance also emphasised a multi-year strategy aimed at debt reduction and structural reforms.

In the guidance the Advisory Division pointed out that much of the unease related to the performance of the eurozone can be traced back to insufficient convergence between the economies of the Member States. European fiscal policy must be strengthened as a means to achieve the ultimate goal: increased prosperity through higher, overall growth and reduced differences in growth.

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[12] CPB Netherlands Bureau for Economic Policy Analysis (2021). Charted Choices 2022-2025, https://www.cpb.nl/sites/default/files/omnidownload/Charted-Choices-2022-2025.pdf

[13] See also section B4 of this report, which explores transparency and in which previous government commitments in this regard are discussed in more detail.

[14] Parliamentary Documents II 2017/18, 34837, no. 6, W06.17.0059/III/Vo and Parliamentary Documents II 2018/19, 21501-20, no. 1457, W06.19.0007/III/Vo.

In the current European debate - revealed in the publications of, among others, the European Fiscal Board (EFB) and the EU Network of Independent Fiscal Institutions (EUIFI)- the following elements recur: simplification of rules by putting a debt anchor (instead of a debt ceiling) at the centre, combined with an expenditure rule (instead of deficit and a medium-term objective), only one exception rule (instead of abounding flexibility), and a separation of political decisions from economic analyses: 'less is more'. And 'less invasive surveillance through enhanced governance'; the EFB proposes that, if a Member State complies with EU fiscal rules, greater weight should be given to assessment and enforcement by national fiscal authorities and that the annual assessment by the European Commission should be abandoned.

The increasingly common suggestion in the European context of an expenditure rule, in addition to a debt anchor, is interesting for the Netherlands as an aspect of budgetary policy. After all, it resembles the multi-year expenditure frameworks with which we are familiar. The fixed (tax and expenditure) frameworks for a government term have been a successful part of Dutch budgetary policy ('Zalmnorm') over the past 30 years. This system contributes to trend-based budgetary policy and is also easy to enforce.

Invest = converge = grow

The Recovery and Resilience Facility (RRF) is a component of the European agreements made last year in June on the multi-year financial framework of the European Union and the post-Covid-19 recovery of European economies.[15] Each Member State will submit a Recovery and Resilience Plan (RRP). The Netherlands has not done so yet.[16] The new incoming government will submit an RRP to the European Commission.

The RRF contains a number of elements mentioned above. The ultimate goal is growth and convergence. One element of the RRPs is to make a long-term contribution to the European priorities of digital and green transitions.[17] Accordingly, the RRF must contribute to productive investments, which usually come under pressure during times of budgetary constraint. The Advisory Division has also pointed out the importance of investments in previous advice, partly in view of the long-term decline in the government investment ratio. RRPs are

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[15] Some reservation must be made regarding the release of RRF funds for Member States, due to the provisional suspension of the Own Resources Decision approval procedure by Germany (see https://www.bundesverfassungsgericht.de/SharedDocs/Entscheidungen/DE/2021/03/rs20210326_2bvr054721.html). The establishment of the financial contribution is pending the examination of the objections made by the German Constitutional Court.

[16] Most Member States will submit an RRP to the European Commission by the end of April. The RRF works on the basis of pre-agreed distribution keys. The Netherlands can submit an RRF for circa €5.6 billion (cumulative).

[17] The RRP to be drawn up by (for) the Netherlands will have to be assessed in terms of the quality and productivity of investments; this is linked to both climate transition and the perspective of broad prosperity.

shaped at the national level, also because challenges differ between Member States.

The aim of RRPs is to promote economic convergence between Member States. In other words, differences in prosperity between Member States must be reduced. This has been taken into account in the distribution of the RRF (share) to Member States. The RRPs must also include Member State specific reforms, based on weaknesses in the economy, which vary from one Member State to another. Substantial reforms are also necessary to achieve growth, convergence and the necessary transitions. In discussions to set up the RRF, the Netherlands therefore advocated that this instrument should focus firmly on economic reforms. For the Netherlands, the European Commission's country-specific recommendations point, among other things, to necessary reforms in the housing and labour markets.

The RRPs are assessed by the European Commission with regard to their substantiation and their compliance with the recovery and reform objective. At the same time, the aim is for RRPs to promote synergy on the Europe-wide priorities of green transitions and digital transitions. Member States' RRPs must contain these priorities; the European Commission will also assess them accordingly.

The CPB Netherlands Bureau for Economic Policy Analysis and the Advisory Division, in its capacity as the fiscal monitoring institute, will assess the Netherlands' (draft) RRP in terms of the elements of the RRF, i.e. the digital and green transition and reforms and investments, in line with the European Commission's recommendation to this effect. In this assessment the Advisory Division will examine whether a draft RRP complies in letter and spirit with the main elements the European Commission has defined for the RRF.

Both the priorities (digital and green) and the reform character (in light of the Netherlands-specific recommendations) must be substantial and visible.
It is also important to establish a substantive link between the Dutch RRP, the National Growth Fund and other investment funds, in order to make optimal use of the potential for complementarity.[18][19] All of this enhances the set of instruments' credibility and enforceability.

A Dutch RRP can thus contribute to economic recovery in the short term; in the long term, to increasing structural growth and implementing necessary transitions and reforms. At least, if it is started in time, partly to avoid pro-cyclical policies. Moreover, the RRP must be assessed by the European Commission and approved

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[18] Besides being complementary, investments should supplement existing (policy) initiatives, in order to provide the economy with an extra boost. This is also a condition for claiming RRF funds.

[19] In previous advice (see Draft 2020 Budget Memorandum, Parliamentary Documents II 2019/20, 35300, no. 3, W06.19.0195/III and Draft 2021 Budget Memorandum and September Report on Budgetary Monitoring (OBT), Parliamentary Documents II 2020/21, 35570, no. 3, W06.20.0288/III), the Advisory Division has pointed out, among other things, the possibility of promoting/protecting public investment by means of a standard for investment expenditure or a capital-serving approach.

by the European Council before the end of 2021, to be able to claim pre-financing of maximum 13% of the subsidy. In this context the Advisory Division advises the current caretaker government to submit an RRP to the European Commission before the summer, and not to wait for a new government to take office after the summer.

In the longer term, the RRF could be a more structural element of future European fiscal policy. It is, as explained above, substantive, focused on investment, growth and convergence, and it is concrete and verifiable,[20] elements that the Netherlands consistently advocates. With such a proposal, the Netherlands can make a substantive, positive contribution to the debate on future fiscal policy, without abandoning prudence and the sustainability of national and European public finances.

To summarise, opportunities for improving performance and compliance

The Advisory Division sees opportunities to promote the performance and compliance of national and European fiscal policies, in conjunction.
Multi-year budgetary frameworks (national) and multi-year expenditure rules (European) can form the core of budgetary policy. There is a strong case for it from a macroeconomic point of view (performance) and it is easy to enforce (simple and unambiguous). The multi-year frameworks and expenditure rules should not have too limited a horizon. Nationally, the four-year (government) period is obvious. Too short a period increases the scope for incidental policies without regard for the structural consequences.[21] From a democratic point of view, an orderly budgetary process is important because it forces necessary choices to be made. If exceptional circumstances require policy interventions outside the structural frameworks, it is important to formulate the conditions under which a return to policy within structural frameworks should take place.

The RRF can contribute in the short term to economic recovery and necessary transitions and reforms. In this regard the Advisory Division recommends that the Dutch RRP be submitted before the summer of 2021 in order to maximise its impact. It is also worth considering making the RRF a more structural part of the European fiscal policy to be reviewed.

Independent enforcement of European and national fiscal policies can be strengthened by disentangling the different roles of the European Commission, and strengthening the role of national budgetary authorities.

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[20] A special form of financing has been chosen for the current RRF, albeit incidental (as emphasised by the European Commission and the outgoing government), which is subject to the necessary marginal notes. A condition for a structural RRF would then be that it is embedded in the Multi-year Financial Framework (MFF), which is quite feasible.

[21] Should there be a need for some flexibility (nationally), there are known techniques (prudent projections, budgetary reserves) that can provide a solution; a mid-term review approach risks shortening the multi-year period. In the short term, Covid-19-related expenditure is calculated outside the expenditure ceiling, providing more flexibility during the Covid-19 crisis.

In conclusion, there is every reason to formulate national and European fiscal policies for the coming years. This is important from a democratic perspective (‘cornerstones'). And it is possible, now that we always look ahead to the coming period of recovery and renewal.

5. Conclusion

The findings and conclusions, as well as the government's response to the draft assessment (see section C), lead the Advisory Division of the Council of State to the following assessment.

I. In 2020, Dutch public finances did not comply with all the agreements of the SGP. In 2021 and 2022, not all targets in the SGP are expected to be met either. In March 2020, due to the extraordinary crisis, the European Commission activated the provision related to extraordinary events, allowing measures taken in response to the Covid-19 pandemic to be excluded. The general escape clause of the SGP has also been activated. This means that the Netherlands may temporarily deviate from the path towards the medium-term objective for the structural balance (MTO) if it does not endanger the sustainability of public finances in the medium term.

II. Nationally, the additional expenditure related to the Covid-19 pandemic has been excluded from the regular expenditure ceiling, thus temporarily deviating from the Dutch budgetary rules. The incoming government will establish new tax and expenditure frameworks for 2022 and subsequent years.

III. From a democratic point of view, an orderly budgetary process is important because it forces necessary choices to be made. The formulation of budgetary policy ensures that decisions and possible reforms are weighed up on the basis of politically chosen criteria. Aspects of broad prosperity can be taken into account when establishing cornerstones. A transparent budgetary policy benefits from a fixed main decision-making point and tax and expenditure frameworks for the entire (four-year) government term.

IV. The national budgetary policy to be defined for the next government’s term of office must be reconcilable with European fiscal policy. In this context, the Advisory Division advises the outgoing government submit a Dutch Recovery and Resilience Plan before the summer of 2021, in order to achieve maximum economic effect. Moreover, the RRP must be assessed by the European Commission and approved by the European Council before the end of 2021, to be able to claim pre-financing of maximum 13% of the subsidy. The Advisory Division sees possibilities, under certain conditions, to afford the Recovery and Resilience Facility a structural place in the European fiscal policy (fiscal framework) to be reviewed.

B. ANALYSIS

1. Macroeconomic and budgetary forecasts

1.1 The macroeconomic outlook

The Dutch economy contracted by 3.7% in 2020. This is mainly due to the contraction in the second quarter of 2020 of 8.4% of GDP compared to the first quarter, caused by the sudden closure of a large part of the economy in relation to the Covid-19 pandemic. The contraction of GDP in the fourth quarter was limited to -0.1%. Unlike in the first wave of the pandemic, industry and the international trade in goods did not suffer in the fourth quarter.

In the first quarter of 2021, GDP is expected to decrease further, following the tightening of restrictive measures. The recovery starts gradually in the second quarter and accelerates in the second part of the year, so that by the end of this year the economy rebounds and surpasses the pre-Covid-19 level. GDP will therefore increase by 2.2% in 2021. The CPB Netherlands Bureau for Economic Policy Analysis assumes that the support measures will expire in June, in accordance with the government's current policy intentions. In 2022, the CPB Netherlands Bureau for Economic Policy Analysis expects further catch-up growth and GDP growth of 3.5%. The output gap is then expected to narrow from -2.6% of GDP to -0.5% of GDP.

The economy in the eurozone contracted by 6.8% in 2020. As in the Netherlands, the recovery in industrial manufacturing continued in late 2020, limiting the contraction in the second half of 2020. There were major differences between eurozone countries, differences such as in the size of support packages and differences in sectoral structure, which played a role. In 2021 and 2022, the eurozone is expected to grow by 4%. In both years, vaccination and generous fiscal policies ensure global economic growth of 4.8% and 4.2% respectively.

Table 3: Macroeconomic developments core data

(Changes in % per year)	2020 MEV 2021	2020 CEP 2021	2021 MEV 2021	2021 CEP 2021	2020 CEP 2021
Eurozone					
Gross domestic product (economic growth)	-8.3	-6.8	6.5	4.0	4.0
The Netherlands					
Gross domestic product (economic growth)	-5.0	-3.7	3.5	2.2	3.5
Household consumption	-5.8	-6.4	4.4	0.6	6.1
Investment in housing	-5.0	-1.6	-3.1	0.0	1.1
Business investment (excl. stocks)	-8.9	-6.5	-6.8	1.0	4.8
Exports of goods and services	-5.2	-4.3	4.7	2.6	5.2
Employment market sector (hours)	-3.6	-3.5	1.2	2.0	1.5
Unemployment market sector (rate, % of working population	4.3	3.8	5.9	4.4	4.7
Actual EMU balance (% of GDP)(a)	-7.6	-4.3	-5.1	-5.9	-1.7
Government debt (% of GDP)(a)	59.9	54.4	62.0	58.6	56.9

Source: CBP Netherlands Bureau for Economic Policy Analysis, Macroeconomic Outlook 2021 and Central Economic Plan 2021
(a) Actual EMU balance and government debt 2020 based on CBS (Statline) actual figures

In the Netherlands, the economic contraction in the second half of 2020 remained limited, so that compared to the Macroeconomic Outlook (September 2020), the contraction is less than expected. In 2021, on the other hand, expected economic growth has been revised downwards, due to the severe restrictive measures in the first quarter of this year and despite the strong recovery in the remaining quarters.

Public spending plays an important role in GDP development. The extensive support measures have therefore severely limited the number of bankruptcies and the rise in unemployment. Unemployment averaged 3.8% in 2020, 0.4 percentage points higher than in 2019. Young people and those on flexible contracts, in particular, have lost their jobs, partly because the recession has reduced production in the services sector, where these groups are over-represented. The fall in demand for labour has mainly been absorbed by a decrease in the hours worked per worker. After the end of the support measures, unemployment will rise and reach an average of 4.4% in 2021 and 4.7% in 2022.

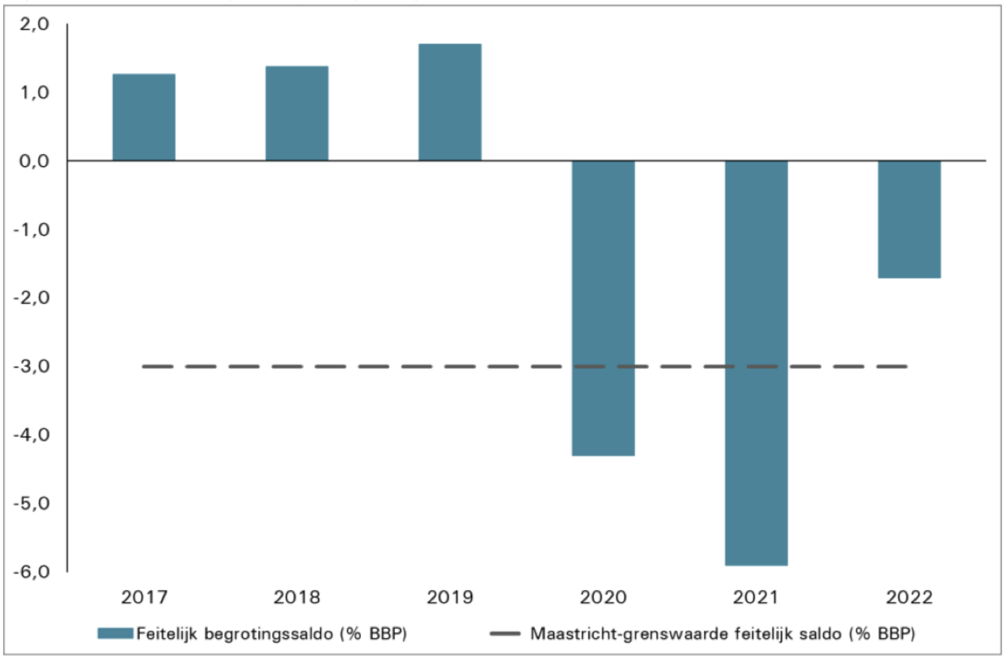
Consumption is expected to increase significantly once the restrictive measures are lifted. This is partly due to the greatly increased savings rate of consumers during the pandemic. There are considerable differences between consumers. For example, many self-employed and flexible workers have had to draw on their savings. Corporate investment will increase in 2021 on the back of a favourable outlook combined with low financing costs, but is somewhat constrained by additional bankruptcies after support measures end and balance sheet recovery.

The international trade in goods is increasing, with a positive effect on Dutch exports.

1.2 The budgetary outlook

Unlike in previous recessions, the government has almost entirely absorbed the impact of the recession. Extensive support measures (including tax measures) amounted to an estimated €29.8 billion in 2021. This includes the additional healthcare expenditure due to vaccination and track and trace research and the additional education expenditure to make up for learning deficits due to the pandemic. In 2020, the volume of support measures will amount to €31.1 billion. Tax and contribution receipts fell in 2020, both due to the Covid-19 crisis and tax-relief measures. However, the contraction is smaller than that of the economy as a whole, which is why the tax burden has increased by 0.4 percentage points to 39.7% in 2020 compared to 2019. The CPB Netherlands Bureau for Economic Policy Analysis projection takes limited account of tax adjustment from tax deferral. Companies still have €13.3bn in deferred payments, some of which are not expected to be repaid.

Figure 1: Development of the actual budget balance



Actual budget balance (% of GDP) Maastricht threshold value actual balance (% of GDP)

Source: CEP 2021

Due to the support measures and lower tax revenues resulting from the recession, the government budget turns from a surplus of 1.7% of GDP in 2019 to a deficit of 4.3% of GDP in 2020 and 5.9% of GDP in 2021, exceeding the 2010 deficit of 5.2% of GDP during the Great Recession. With the end of the support measures and the economic recovery, the deficit will fall to 1.7% of GDP in 2022. The structural balance (EC method), adjusted for the economic cycle, turned into a

negative balance of 1.9% of GDP in 2020. In 2021, the balance will deteriorate further to -4.1% of GDP, to recover somewhat in 2022 to -1.4% of GDP. This means that the structural balance does not meet the European Medium Term Objective (MTO) of
-0.5% of GDP. Due to the activation of the escape clause in the SGP, the European Commission will not currently impose restrictions for exceeding the MTO (see section 2.1 for further explanation).

Budget deficits and guarantees to corporations increase public debt to 58.6% and 56.9% of GDP in 2021 and 2022 respectively. This is on average nine percentage points of GDP higher than in 2019, before the pandemic. The debt ratios in the CEP are estimated to be lower than in the CPB Netherlands Bureau for Economic Policy Analysis Macroeconomic Outlook and November projection due to the more favourable than expected economic developments resulting in less government expenditure, more revenue and a larger economy (denominator effect). Debt remains below the 60% Maastricht target, despite substantial government expenditure.

Table 4: Public finances core data

(in % of GDP)	2017	2018	2019	2020	2021	2022
Net public expenditure	37.4	37.4	37.6	44.0	45	40.5
Tax and national insurance contributions	38.7	38.8	39.3	39.7	39.1	38.8
Actual EMU balance	1.3	1.4	1.7	-4.3	-5.9	-1.7
Of which EMU balance decentralised authorities	-0.1	-0.2	-0.2	-0.2	-0.2	-0.2
Structural EMU balance	0.5	0.6	0.7	-1.9	-4.1	-1.4
Government debt	56.9	52.4	48.7	54.4	58.6	56.9

Source: CBS (Statline) and CBP Netherlands Bureau for Economic Policy Analysis, (Central Economic Plan 2021)

In the recently published update of the Medium Term Outlook 2022-2025 (MLT), the CPB Netherlands Bureau for Economic Policy Analysis looks ahead to economic developments in the next four years and beyond.[22] The CPB Netherlands Bureau for Economic Policy Analysis will update the Medium Term Outlook again after the Coalition Agreement has been concluded. Due to the current Covid-19 pandemic and the uncertainty about its development, the basic principle of the projection is even more uncertain. One relative certainty is the ageing population, with consequences for spending on the state pension and healthcare. It also dampens the increase in labour supply, with implications for structural growth. The Medium Term Outlook anticipates average annual GDP growth of 2% in 2022-2025.

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[22] CPB Netherlands Bureau for Economic Policy Analysis (2021). Update Medium Term Outlook 2022-2025 (March 2021), https://www.cpb.nl/actualisatie-middellangetermijnverkenning-2022-2025-maart-2021

The government budget will remain in deficit in 2022-2025, decreasing from 5.9% of GDP in 2021 and 1.7% in 2022 to 1.0% of GDP in 2025. Collective healthcare expenditure will increase by €7 billion in real terms between 2021 and 2025. Policy-related tax increases by almost €8 billion (in 2021 prices), mainly due to higher cost-covering health insurance contributions, both for households and companies, and to increases in wage and income tax. The increase is greatest for families, at €4.8 billion. For the business sector, this is €2.8 billion. Public debt will decrease in 2022-2025 to 54.9% of GDP and remain below the 60% Maastricht target. The decrease is mainly due to the dampening denominator effect caused by the increase in nominal GDP and despite the persistent deficits. The financial burden on future generations, the sustainability gap, is estimated by the CPB Netherlands Bureau for Economic Policy Analysis at 1.8% of GDP. Covid-19 expenditure negatively affected the sustainability balance due to the higher public debt, resulting in a heavier burden for future generations.

2. Further elaboration of the assessment of the fiscal rules

2.1 International assessment framework

In its Spring Report, the Advisory Division assesses whether public finances in the previous year (*ex post*), in the current year (*in year*) and in the year ahead (*ex ante*) comply with the European fiscal rules. Since the budget balance from 2013 up to and including 2019 complied with the maximum deficit of 3% of GDP, the rules of the so-called 'preventive arm' of the Pact are relevant in the assessment. The rules of the preventive arm impose requirements on the development of the so-called *structural budget balance* (the budget balance adjusted for the state of the economy and incidental items) and on the *development of government expenditure*. In addition, *public debt* should be below 60% of GDP, or at least it should decrease sufficiently in that direction.

In the preventive arm, the assessment of the past year is particularly important, as the European Commission, on the basis of its own Spring projection, can propose to the European Council that if a country has not done enough in the past year to get or keep its budget in order, a formal procedure can be launched, which may lead in the last resort to (financial) sanctions.

In March 2020, the European Commission declared the application of the provision in the SGP related to extraordinary events, thus excluding the budgetary impact of measures taken in response to the Covid-19 pandemic in the assessment of compliance with the SGP. In addition the general escape clause in the Stability and Growth Pact was activated, to offer Member States maximum flexibility within the SGP.[23]For Member States in the preventive arm (including the Netherlands) it means that they may deviate from the path towards the medium-

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[23] European Commission, Communication from the Commission to the Council on activating the general escape clause of the Stability and Growth Pact, COM (2020) 123 final, https://eur-lex.europa.eu/legal-content/NL/TXT/PDF/?uri=CELEX:52020DC0123&from=EN

term objective (MTO) for the structural balance, providing it does not jeopardise sustainability of public finances in the medium term. Therefore, it remains important that the development of public finances is closely monitored and assessed.

The general escape clause does not lead to the suspension of SGP procedures. Thus, the reporting obligation for Member States to prepare a Stability Programme and Draft Budgetary Plan remains in force. In the Stability Programmes, Member States will have to account for the use of RRF funds (see box 1).[24] Based on the Stability Programme, the Commission will formulate country-specific recommendations, which will be mainly qualitative, with a single quantitative element for steering medium-term fiscal policy. The Commission will prepare its usual 126(3) reports in the spring, if Member States have exceeded the deficit rule. However, the Commission will take into account the ongoing uncertainty, the agreed fiscal policy stance and the Council recommendations for the eurozone for 2021. Moreover, no excessive deficit procedures will be opened, due to the extreme uncertainty related to the macroeconomic and budgetary impact of the Covid-19 crisis.

In a recently published communication, the Commission states, among other things, that the decision to deactivate the general escape clause (GEC) should be taken on the basis of an integral assessment of economic indicators at the European level.[25] The main criterion is the achievement of the pre-crisis real GDP level. Based on current projections, it is expected that the general escape clause will also apply in 2022 and be deactivated in 2023. The Commission will assess the deactivation or continuation of the GEC in May 2021 as part of the Spring Package of the European Semester.

The Commission communication also calls for Member States to continue to pursue stimulus-oriented fiscal policies in 2021 and 2022. Early withdrawal of support should be avoided by Member States due to possible pro-cyclical effects. The Commission states that fiscal support measures should be temporary and targeted, should gradually shift from emergency support to measures aimed at sustainable recovery, and should provide the right incentives for work and future-proof business models.

The Commission postponed the review and possible revision of the SGP due to the Covid-19 crisis. The Commission says it wants to resume the public debate on the future of the SGP as soon as there is robust economic recovery in the European Union. The (now caretaker) government is of the opinion that the evaluation and possible revision of the SGP should be considered separately from the debate on

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[24] As the Netherlands has not yet submitted a plan for the RRF, the Netherlands does not address it in the Stability Programme 2021.

[25] European Commission, Communication from the Commission to the Council, 3.3.2021 COM(2021) 105 final, https://eur-lex.europa.eu/legal-content/NL/TXT/PDF/?uri=CELEX:52020DC0123&from=EN

the general escape clause.[26] However, the government appreciates the Commission's clarification of the process surrounding the GEC. This is necessary for Member States to define their medium-term budgetary policy. The government considers it crucial that member states guarantee debt sustainability in the medium term.

Box 1: The Recovery and Resilience Facility (RRF)
The Recovery and Resilience Facility (RRF) is part of the European recovery fund, Next Generation EU, which has a volume of €750 billion and aims to stimulate economic recovery in Member States, contribute to convergence and cohesion in the European Union and to the green and digital transition. The RRF consists of loans (€360 billion) and subsidies (€312.5 billion). The Netherlands only claims subsidies from the RRF. The allocation of RRF subsidies is based on a calculation that includes the population size, GDP per capita, average unemployment and loss in real GDP for 2020 and 2021. The final distribution among Member States will be determined in mid-2022. The Netherlands is expected to receive a €5.6 billion subsidy from the European Commission's RRF (EC). To this end, the Netherlands must submit a Recovery and Resilience Plan (RRP) to the European Commission.

The RRP must contain both investments and reforms that contribute to the Member State's recovery and make a long-term contribution to digital and green transitions. At least 37% of the national envelope should be spent on the green transition, at least 20% on the digital transition. It should also contribute effectively to challenges identified in the country-specific recommendations (CSRs) in 2019 and 2020. Investments and reforms decided after 1 February 2020 are eligible.

The European Commission is asking Member States to be ambitious and implement the plans quickly in order to strengthen the economic recovery in 2021 and 2022. RRPs should have a positive long-term impact on economies and should complement stimulative national budgetary policies. After approval of the plan, up to 13% of the funds are pre-financed. The remainder of the funds will be disbursed based on achieved milestones and targets, which must be met by mid-2026.

Late 2020, the Dutch government decided to leave the decision-making for the Dutch RRP to the new government after the elections to the House of Representatives, expressing the aspiration to submit an ambitious and robust package. The implementation of reforms was an important condition for the government to agree to the establishment of the RRF, therefore it is important that its own reforms are substantial.

The ex post assessment for 2020
The actual budget balance ended with a deficit of 4.3% of GDP in 2020

[26] Letter to Parliament with follow-up to the annotated agenda of the European Commission, https://www.rijksoverheid.nl/documenten/kamerstukken/2021/03/09/nazending-ga-europese-commissie

(Table 5). As a result, the budget balance far exceeded the reference value of a maximum permitted deficit of 3.0% of GDP under the SGP. Due to the application of the provision related to extraordinary events, measures taken in response to the Covid-19 pandemic are excluded. The government has not specifically assessed this provision, the outlook is expected to be more nuanced if the debt and balance are corrected for these measures.

For Member States in the preventive arm (such as the Netherlands), the assessment focuses on the normal operation of the SGP, on whether *the structural government balance* meets the medium-term objective (MTO) and *expenditure growth* falls short of the estimated potential growth of the economy. For the Netherlands, the current MTO is -0.5% of GDP: the structural budget deficit should not exceed 0.5% of GDP. This objective – arising from the European budgetary agreements – is updated every three years and derived from the long-term sustainability of a Member State's public finances.

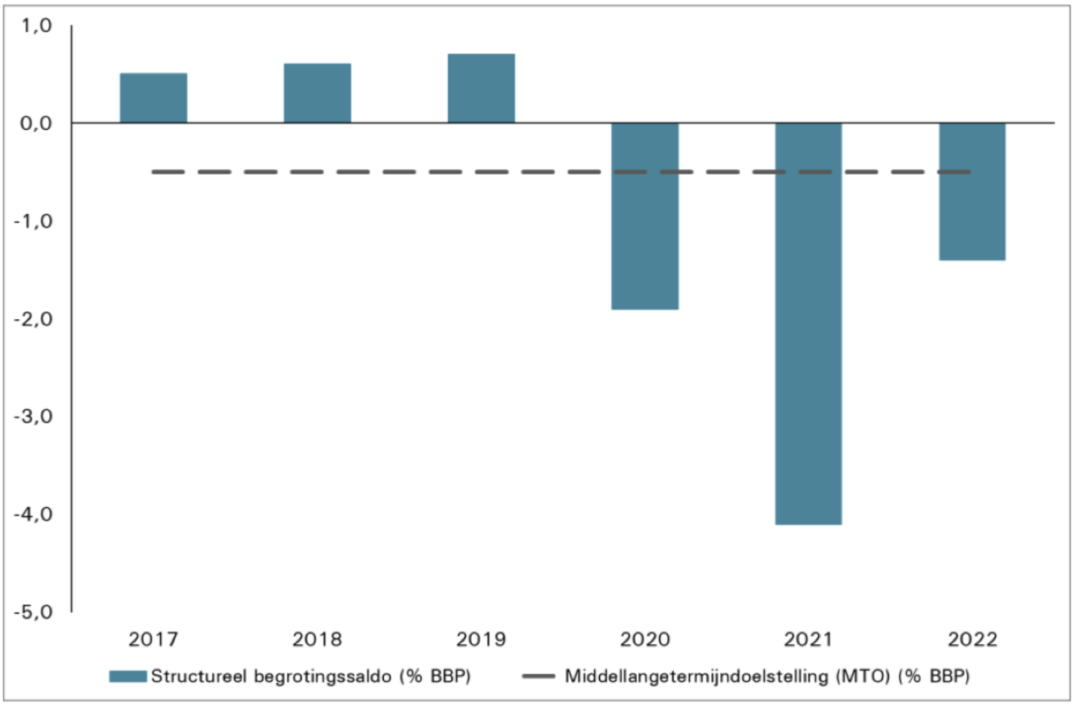
Table 5: European budgetary rules data

	2020 *ex post*	2021 *in year*	2022 *ex ante*
Rule related to the development of the structural balance (in % of GDP)			
EMU balance actual	-4.3	-5.9	-1.7
Of which cyclical component	-2.3	-1.7	-0.3
Of which one-off and other temporary measures	0.0	0.0	0.0
EMU balance structural (EC method)	-1.9	-4.1	-1.4
Expenditure rule			
Adjusted net public expenditure (real change in %)	14.5	2.3	-6.0
Max. permitted growth adjusted net public expenditure	4.3	-2.7	-6.0
Debt criterion (% of GDP)			
EMU debt	54.4	58.6	56.9

Source: CBS (Statline) and CPB Netherlands Bureau for Economic Policy Analysis, Central Economic Plan 2021, Table 3.1)

The activation of the general escape clause allows Member States in the preventive arm (including the Netherlands) to deviate from the path towards the medium-term objective for the structural balance (MTO) if it does not jeopardise the sustainability of public finances in the medium term. Looking at the structural government balance, the structural balance for 2020 appears to be -1.9% of GDP, thus falling short of the MTO target.

Figure 2: The structural balance and MTO



Structural budget balance (% of GDP) Medium-Term Objective (MTO) (% of GDP)

Source: CEP 2021

The expenditure rule sets requirements for the maximum permitted growth in government expenditure less discretionary revenue measures. The government expenditure is adjusted for, among other things, the cyclical component of unemployment expenditure, interest charges and fluctuations in investment expenditure. The maximum permitted growth in government expenditure is based on the distance of the structural balance from the medium-term objective and the long-term, trend-based economic growth.

This is especially important in a situation in which the structural balance is below the MTO. Despite the fact that the expenditure rule is not considered in the current situation, it can be concluded that the growth of the adjusted net government expenditure has exceeded the growth threshold if it were to be assessed (Table 3). In a situation where the reference values for the maximum permitted deficit and the MTO provide only limited guidance as an cornerstone, the expenditure rule provides insight into the development of debt sustainability over the medium term.

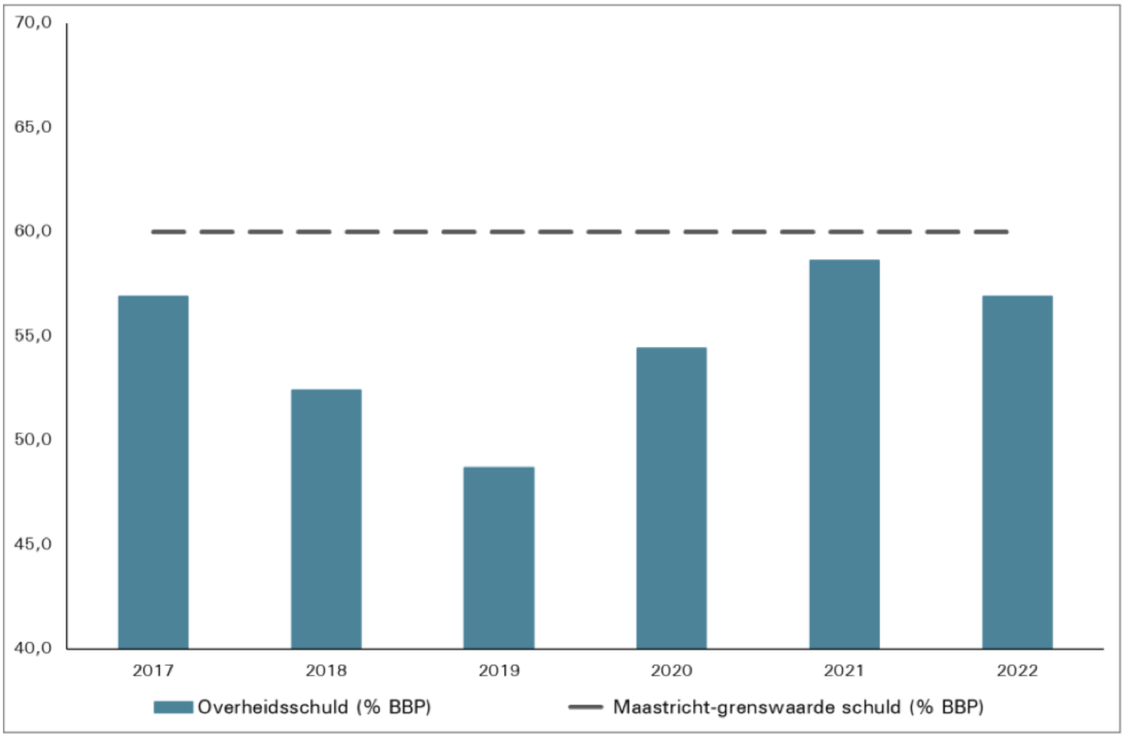
The European debt criterion stipulates that government debt must be below 60% of GDP or, if it exceeds the threshold, and must decrease by at least one-twentieth of the difference between actual government debt and the reference value. From 2015 to 2019, government debt development was on a downward path, reaching 48.7% of GDP at the end of 2019. Since the Covid-19 crisis, debt has been rising again, but at 54.4% of GDP in 2020 it remains below the European standard of 60% of GDP. For 2021 and 2022, debt is also estimated to develop within the European standards.

Assessment for the 2021 and 2022
The actual budget balance also remains negative in 2021 and 2022. With a deficit of 5.9% of GDP in 2021, the balance again does not meet the -3.0% threshold value of the SGP, and also exceeds the 5.2% of GDP deficit in 2010 during the Great Recession. The overshoot in 2021 will have no impact as, based on current projections, no excessive deficit procedures will be opened this year. When assessed against the provision related to extraordinary events, the outlook is expected to be more nuanced in 2021.

This year, expenditure related to the Covid-19 crisis continues to determine developments in the government budget. The deficit continues to grow due to the expansion of the support package and additional spending on healthcare and education. Parents in the child allowance affair are being compensated and there is an extra budget for the implementing organisations. Total public expenditure on Covid-19 support measures (including tax measures) will reach about €30 billion (3.6% of GDP) in 2021. In addition, there is a €12 billion impact on debt due to tax deferrals, loans and cash differences related to Covid-19 measures.

With the end of the support measures and the economic recovery, the deficit will fall to 1.7% of GDP in 2022. Public debt is increasing as a result of budget deficits, tax deferrals and additional government loans to businesses. On average, debt will be nine percentage points of GDP higher than in 2019. In 2021, debt will increase to 58.6% of GDP and then decrease to 56.9% of GDP in 2022. Despite debt being substantially higher than in 2019, due to lower interest rates, interest payments on government debt will be lower in 2022 than in 2019 (0.4% of GDP compared to 0.8% of GDP). This means the EMU balance and government debt remain well below the eurozone average.

Figure 3: Development of government debt and Maastricht threshold value debt (in % of GDP)



Government debt (% of GDP) Maastricht threshold value debt (% of GDP)

Source: CEP 2021

As the general escape clause will remain in force for the time being, an assessment based on the MTO and in relation to the expenditure rule will be excluded in 2021 and is expected to apply in 2022 as well. Nevertheless, if we look at the projections, we can conclude that the MTO target will not be met in 2021 and 2022 either. In 2021, standard growth for the expenditure line will also be exceeded and will fall within the target again in 2022. In the most recent Medium-Term (MLT) projection, the structural balance will fall to 1.0% of GDP in 2025 and the MTO will not be met in the period up to 2025 either. Moreover, standard growth in the expenditure rule will be exceeded in the projections until 2025, which puts pressure on the medium-term sustainability of the government budget and leads to a sustainability gap of 1.8% of GDP in 2025.

Table 6: Summary of the outcome of the assessment under European fiscal rules

	2020	2021	2022
Actual budgetary balance	x	x	√
Structural budgetary balance (a)	x	x	x
Government debt	√	√	√

Explanation of the symbols used: √ = denotes compliance with the rule concerned; O = denotes a deviation from the rule, but this deviation is not significant; x = denotes a deviation from the rule, and this deviation is, calculated over one year and/or over an average of two years, significant (only applies to the structural balance and the expenditure rule, see note)

(a) The structural budget balance and the expenditure rule show a 'significant' deviation if the deviation (in the negative sense) calculated over one year amounts to at least 0.5% point of GDP. There is also a significant deviation if, over two years there is a cumulative deviation of at least 0.5% points of GDP.

(b) As long as the structural budget balance complies with the Medium-Term Objective an assessment related to the expenditure rule can be excluded.

2.2 National assessment framework

As the independent national fiscal monitoring institute, the Advisory Division also has the task of making public assessments regarding national fiscal rules. Since 1994, a trend-based budget policy has been adopted. The Rutte III government has confirmed in the Initial Policy Memorandum to the Coalition Agreement that it will pursue a trend-based budget policy.[27] It also mentions the objective of trend-based budgetary policy: controlling public finances, allocating resources efficiently and contributing to economic stability. This objective is best achieved through stability in political decision-making by performing integral considerations at fixed times. This also promotes orderly political accountability of the government to Parliament.

Under trend-based budgeting, frameworks are used for both expenditure and revenue (taxes). Agreements on this are made at the beginning of a government term. For each year a ceiling is agreed on the total expenditure that may not be exceeded, the so-called expenditure ceiling. There is a general expenditure ceiling and within it there are three sub-frameworks with their own ceilings: State Budget, Social Security and Healthcare. On the revenue side of the budget, the policy-based tax development is set for the entire government term in the so-called revenue framework. This ceiling must be complied with on a cumulative

[27] Appendix 1: Budgetary rules 2018-2022, as established by the Rutte III Government, Appendix 1 to the Initial Policy Memorandum: Parliamentary Documents II 2017/18, 34775, no. 54.

basis over the full government term, but unlike the expenditure ceiling, this does not apply for each individual year of the government term. On the revenue side of the budget, the principle of automatic stabilisation also applies: revenue windfalls benefit the government balance, revenue shortfalls burden the government balance.

The ex post and in year assessment for 2020 and 2021
The years 2020 and 2021 are extraordinary due to the economic shock resulting from the Covid-19 crisis. This also extends to budgetary policy. Firstly, the Covid-19 crisis has resulted in support measures in addition to the automatic stabilisers on the income and expenditure side. The government has taken extensive support measures. After announcing the first emergency measures, 46 incidental supplementary budgetary laws were submitted by the government.[28]The budgetary impact of the Covid-19 crisis[29] and a total overview of the emergency measures[30] are presented in a single location.

On the expenditure side the government opted to keep the extra expenditure related to the Covid-19 pandemic outside the regular expenditure ceiling. Actual is separated via a ceiling correction.[31] The extra expenditure related to the Covid-19 pandemic thus leads to a deterioration of the EMU balance and an increase in the EMU debt.[32] This means that there is no need to make cuts to make room within the expenditure ceiling. This results in a temporary deviation from Dutch budgetary rules. For standard policy the government adheres to the applicable budgetary rules, to maintain as much calm and predictability as possible.

The ex ante assessment for 2022
In addition to the extraordinary circumstance of extra expenditure related to the Covid-19 pandemic and the subsequent adjustment to the expenditure ceiling, this year there is a new government term. The tax and expenditure frameworks for the Rutte III government will no longer apply after this year; a new cabinet yet to be formed will, of course, have to establish the frameworks for 2022 and subsequent years. The implementation of the ceiling test by CPB Netherlands Bureau for Economic Policy Analysis is technically complex. In addition, due to the lack of multi-year frameworks between two government terms, the ceiling test is not relevant in the current situation. Due to this circumstance, the CPB Netherlands

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[28] Overview of supplementary Covid-19 budget financial measures, https://www.rijksoverheid.nl/documenten/begrotingen/2020/03/18/overzicht-suppletoire-begrotingen-financiele-maatregelen-coronavirus
[29] Public finances during the Covid-19 era, https://www.rijksfinancien.nl/overheidsfinancien-coronatijd?
[30] Emergency Covid-19 measures, https://www.rijksfinancien.nl/overheidsfinancien-coronatijd/noodmaatregelen/uitgavenmaatregelen/noodmaatregelen-coronacrisis
[31] Autumn Memorandum 2020, Parliamentary Documents 2019/20, 35650, no. 1, https://zoek.officielebekendmakingen.nl/kst-35650-1.html

Bureau for Economic Policy Analysis has not included a ceiling test in the projections.

2.3 Uncertainties and risks

Due to the Covid-19 pandemic and the associated uncertainties in the short term (when can society and the economy be fully reopened) and in the long term (what are the structural consequences and changes following the pandemic), the uncertainty surrounding the projections is greater than usual. The CPB Netherlands Bureau for Economic Policy Analysis has therefore included a pessimistic and an optimistic scenario in the CEP.

In the pessimistic scenario, new variants of Covid-19 cause a new outbreak of the virus, resulting in a new recession. This includes the assumption that current vaccines do not provide optimal protection against the new variants. The economy enters a new recession through decreasing consumption, declining international trade and business investment. New support packages are needed to cushion the economic downturn. In this scenario, GDP falls by 0.8% in 2021. In 2022, growth will be limited to 0.8% of GDP. Unemployment rises to 6.1%.

In the optimistic scenario, the removal of contact-restrictive measures leads to a sharp increase in consumer and producer confidence. Unemployment is lower due to additional spending, investments and exports and wage growth picks up due to a tight labour market. This benefits public finances. In this scenario, the economy grows by 2.6% in 2021 and 5.1% in 2022. Unemployment falls to 4.2%.

In addition to the development of the Covid-19 pandemic, there are uncertainties in the area of the economic relationship between the EU and the UK, the trade relationship between China and the US, and the impact of the effects of the extensive American fiscal incentive on inflation and interest rates in the eurozone. There is also uncertainty about the economic effects of the European Recovery and Resilience Facility (RRF) (see box 1 section B2.1) and bottlenecks due to the nitrogen issue.

In the Stability Programme 2021, the government has included an additional simulation analysis regarding the development of national debt. In this analysis, produced using CPB Netherlands Bureau for Economic Policy Analysis figures, uncertainties are simulated on the basis of historical data. As a result of the analysis, the government concludes that in more than 90% of the simulated situations, debt will remain between 35% and 70% of GDP up to and including 2030. It should be noted that new shocks may continue to occur, with more extreme scenarios conceivable.

What is striking is that the estimated indicators in the pessimistic scenario deviate considerably more from the basic projection than the optimistic scenario. In other words, the possible negative outliers are a lot higher than the possible positive outliers. The earlier projections and scenarios produced by the CPB Netherlands Bureau for Economic Policy Analysis during the Covid-19 crisis also turned out to be overly pessimistic in retrospect, partly due to the effects of the extensive support packages of governments nationally and internationally. Projections are also made on the basis of historical data. There has never been a crisis like this before, resulting in the widening of margins of uncertainty around projections. However, credibility is an important foundation for our budgetary policy. It is therefore important to continue to critically reflect, including on the scenario analyses.

3. Focal points for budgetary information

3.1 Transparency of projections

In a democratic polity, openness and transparency of the budget are fundamental for the credibility of public policies. This is the only way elected representatives and society can develop an informed opinion about the policy. The CPB Netherlands Bureau for Economic Policy Analysis projections and the Stability Programme try and meet this need. It is the Advisory Division's task to reflect on this and to indicate possible focal points. It also supports the House of Representatives and the Senate in exercising their rights associated with the budget.

The Advisory Division noted in 2018 that examination of the total public expenditure and
total revenue ratios only provide partial insight into the underlying development of government revenue and expenditure. In the 2020 September Report on Budgetary Monitoring, the Advisory Division also expressed a preference for presenting expenditure on account of the Covid-19 pandemic and related support measures separately (whether or not in a separate box) from the expenditure ceilings. This is to improve the visibility of expenditure related to combating the Covid-19 crisis and the visibility of regular expenditure.

The Stability Programme 2021 provides an insight into the distribution of the total Covid-19-related expenditure among the budget chapters in 2020. Nevertheless, the question remains as to which emergency packages and budgetary measures underlie this expenditure per budget chapter. This breakdown is made by the CPB Netherlands Bureau for Economic Policy Analysis in the CEP for 2020 and 2021. From a social point of view, such a presentation is more appealing as it provides an insight into the various schemes. Moreover, the Division notes that the total amount of Covid-19 expenditure by the government and the CPB Netherlands Bureau for Economic Policy Analysis for 2020 does not tally, which is caused by different assumptions of the projections.

The Stability Programme 2021 also addresses the sustainability balance, which measures the long-term affordability of public services. It is noted that the CPB Netherlands Bureau for Economic Policy Analysis estimates a sustainability gap of 1.8% of GDP and the European Commission a sustainability gap of 3.3% of GDP. The Advisory Division recognises that model-based assumptions play a role in quantifying the future sustainability of current government arrangements and that these may differ. This results in differences in the projected sustainability balances. However, in the context of transparent and predictable fiscal policy, it is important to opt for an unambiguous concept. From this point of view, it is preferable to have one balance with similar basic principles.

In addition to additional expenditure in response to the Covid-19 crisis, the decision was for measures on the revenue side, including €12.5 billion additional tax deferral for businesses in 2020, with an impact on EMU debt. The basic principle of tax deferral is that it is temporary and therefore repayable at a later date. However, part of the deferred tax liabilities is not expected to be met, according to the CPB Netherlands Bureau for Economic Policy Analysis in the CEP. This depends on the number of bankruptcies, which is difficult to predict. The Advisory Division notes that for the sake of transparency, in the Stability Programme it is relevant to discuss the composition of the deferred tax liabilities and the government's expectation of fulfilling the liabilities, due to possible effects on public finances.

3.2 Article 3.1 Government Accounts Act (CW)

The Sneller et al. motion adopted on 1 October 2020 asks the Advisory Division of the Council of State, when advising on legislative proposals, to pay explicit attention to the way in which the obligations of Section 3.1 of the Government Accounts Act (CW) have been fulfilled.[33] Article 3.1 of the Government Accounts Act (CW) provides for the assessment of the pursuit of objectives, effectiveness and efficiency, policy instruments and financial consequences (for the state and social sectors) of budgetary and financial management and requires a so-called ex ante explanation: an explanation that is provided in advance, during policy preparation. This is a different approach than ex post evaluations, which are performed after the event. An ex ante explanation of a policy proposal can look at the impact of the proposed policy on society as a whole; what are the total social costs and benefits?

As announced in the Rutte III government 'Confidence in the Future' Coalition Agreement, the government launched the 'Insight into Quality' Operation in 2018.[34] The aim of the operation is to increase the social added value of public money by better understanding the impact of policies and acting on it. It is about immediate results (applying new insights) and structural change in the way of working (learning government).

In order to make the required CW 3.1 explanatory notes easier for the House of Representatives to locate, a pilot project was announced in the third Operation Insight into Quality progress report to improve the way the CW 3.1 are located, by adding a separate CW 3.1 appendix to Letters to Parliament. Meanwhile, the

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[33] Motion by member Sneller c.s., Parliamentary Documents 2020/21 35570-IX, no. 14, https://zoek.officielebekendmakingen.nl/kst-35570-IX-14.html

[34] Letter on improving accountability and budget, Parliamentary Document 2017/2018 31865, no. 118, https://zoek.officielebekendmakingen.nl/kst-31865-118.html

external evaluation of the pilot has started.[35] In preparing the required explanatory notes to policy and legislative proposals in the appendix to Letters to Parliament, the 'Integral Assessment Framework for Policy and Regulation' (IAK) can be used to ensure the quality of the analysis.

The IAK has existed since 2011 and has become more complex over the years. This is one of the reasons why it is not used enough. Therefore, the government considers it important to simplify the IAK and to promote its use. The plan for revising the IAK consists of four lines of action: simplifying the IAK, making it more user-friendly, raising its profile and promoting its improved application. The government's attention is thus focused on both adjustments to the tool and the way of working.

Procedural compliance with CW 3.1 in 2020 (including the pilot) will be reported in the Annual Financial Report of the Kingdom (FJR). The individual departmental annual reports will also reflect on application and compliance in 2020. The Covid-19 crisis has made compliance with CW 3.1 more difficult and the annual reports will explicitly address compliance with the article of law in Covid-19-related measures and compliance before and after the pilot. Furthermore, the results of the Court of Audit's compliance study are expected in April 2021. The role of the pilot appendix in the (possible) use of CW 3.1 explanations by MPs will be examined in an external evaluation by Leiden University. The aim is to have the various insights from the pilot available for the 2021 Accountability Debate.

The Advisory Division agrees that further attention to compliance with CW 3.1 and the use of ex ante evaluations remains necessary to continue to improve the substantiation and ability to evaluate policy choices. The Division also sees the House of Representatives motion by the member Sneller c.s. as an incentive to think carefully about the proper and transparent substantiation of the budgets in its budgetary reports. This serves to support the budget rights of the House of Representatives and the Senate. Therefore, the Advisory Division will periodically focus on the general outlook regarding Article 3.1 CW when advising on the Budget Memorandum and the report within the framework of independent budgetary monitoring. The Advisory Division has written to all ministers, and the Minister of Finance in particular given his responsibility, drawing their attention to the aforementioned motion.[36]

3.3 Tax side of the budget

In addition to the quality of expenditure, the Advisory Division also calls for attention to the revenue side of the government's budget in the budgetary report.

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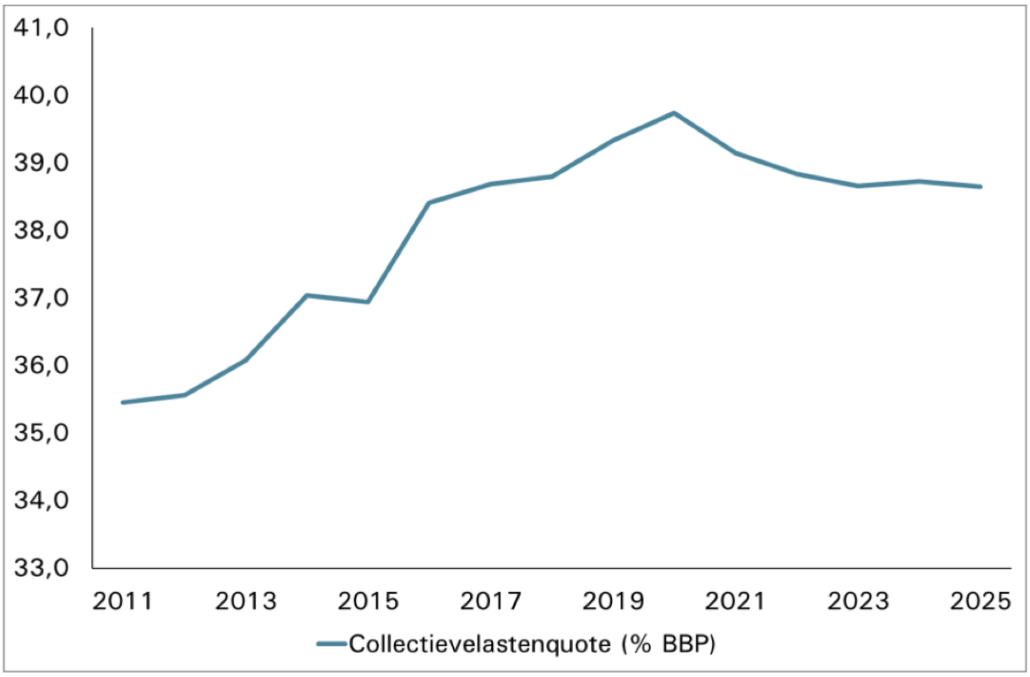
[35] Letter about the fourth Operation Insight into Quality progress report, Parliamentary Documents 2020/21 31865, no. 184, https://zoek.officielebekendmakingen.nl/kst-972716

[36] Letter from the Advisory Division of the Council of State on the assessment of policy proposals in accordance with Article 3(1) of the Government Accounts Act (2020). House of Representatives, session year 2020–2021, 35570 IX, no. 35.

The total revenue ratio provides insight into the development of government revenue and is the simplest tax concept. It expresses the total of tax and contribution receipts as a percentage of GDP. Figure 4 shows the development of the total revenue ratio for the period 2010-2025. The total revenue ratio increased by over four percentage points of GDP between 2010 and 2020.

Figure 4: Total revenue ratio



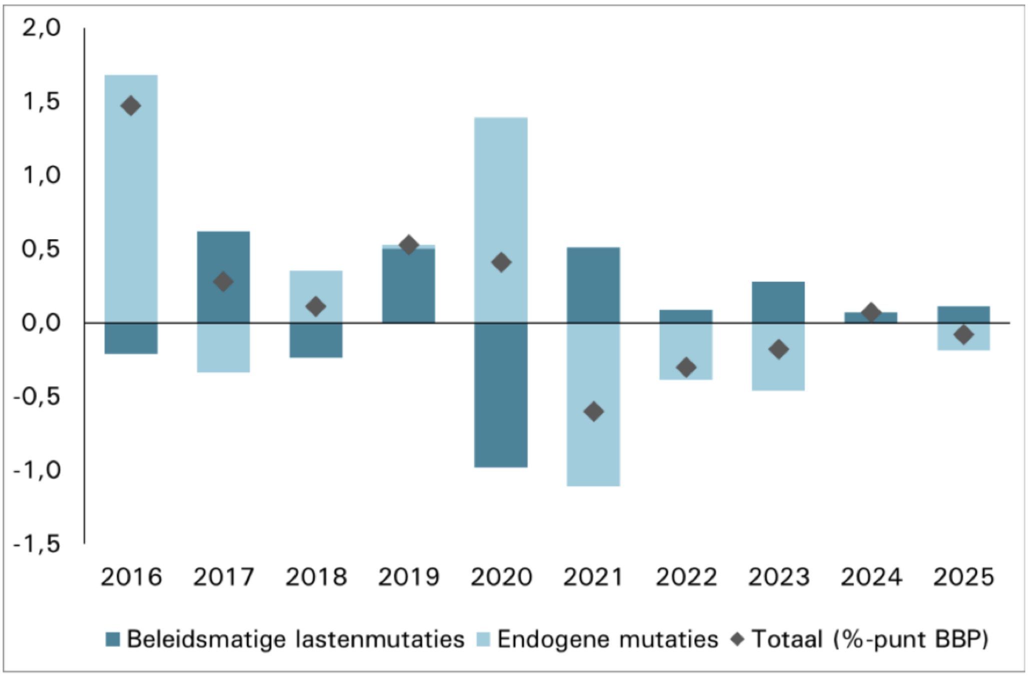
Total revenue ratio (as a % of GDP)

Source: CPB Netherlands Bureau for Economic Policy Analysis, Update Medium Term Outlook 2022-2025, March 2021

The total revenue ratio may change as a result of policy measures (e.g. increase or decrease in a tax rate and/or a change in the tax base) and the so-called endogenous development of tax revenues, which depends on the business cycle. If economic growth is relatively tax-rich (e.g. driven by domestic consumption), then tax and national insurance contributions as a percentage of GDP will increase endogenously: tax revenues will increase faster than economic growth.

Figure 5 provides greater insight into the increase in the total revenue ratio. This total change in the total revenue ratio is the balance of the endogenous tax development and the policy-based tax development.[37] In the years prior to 2020, the total revenue ratio increased due to a combination of endogenous developments and tax measures. In the years after 2020, the total revenue ratio will gradually decrease, but the policy-related tax trend will remain positive. Policy-related tax will increase by almost €8 billion in the period 2022-2025 (2021 prices), mainly due to higher cost-covering health insurance premiums (due to the ageing population) and tax measures related to wage and income tax. Of this, €4.8 billion will be borne by households and €2.8 billion by businesses. This change does not yet include the effect of a new Coalition Agreement, which may lead to changes in the amount and distribution of the policy-related tax. A Coalition Agreement will also indirectly, through its impact on the economy, have an effect on endogenous tax development.

Figure 5: Change in tax and national insurance contributions



Policy-based tax changes *Endogenous changes* *Total (% point of GDP)*

Source: CPB Netherlands Bureau for Economic Policy Analysis, Update Medium Term Outlook 2022-2025, March 2021

3.4 Local and regional authorities

The Advisory Division has pointed out the importance of investments in previous advice, partly in view of the long-term decline in the government investment ratio.

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[37] The policy-based tax development reflects the budgetary impact of all policy measures on tax and premium revenues, whereby policy measures are understood as all adjustments to rates and tax bases. It also includes adjustments to tax brackets, tax credits and deductible items, as well as the introduction of new taxes and the abolition of existing taxes.

Half of Dutch public investments are related to the local and regional authorities.[38] Local and regional authority investment tends to come under pressure at times of economic downturn, when productive public investment can boost the economy. The Advisory Division therefore considers it relevant to elaborate on the financial position of local and regional authorities following the Covid-19 crisis.

From the beginning of the Covid-19 pandemic, the government has made regular agreements with municipalities, provinces and water boards on compensation for the extra costs and loss of income resulting from the Covid-19 crisis.[39] The basic principle is that local and regional authorities should not suffer financially as a result of the pandemic. It has been agreed to compensate local and regional authorities in real terms, whereby it has been expressed that all governments together will take responsibility for keeping their income and expenditure manageable as far as possible in the new situation.

The compensation paid to local and regional authorities to date is, unless explicitly stated to be advance payments, unconditional.[40] Payment of compensation is aligned as much as possible with the regular system of funding and financing. The agreements on the real compensation of the additional expenditure and loss of income apply at least until the second quarter of 2021. For the period after the second quarter of 2021, the government has promised to consult with local and regional authorities in good time on the real compensation.

In addition to real compensation, it has been decided to freeze the accruals for 2020 and 2021 at the level of the Spring Memorandum 2020, in order to offer local and regional authorities greater predictability and to limit revenue fluctuations. In addition, the increase in the scaling-up rebate for municipalities in the years 2020 and 2021 has been cancelled on an incidental basis, leading to an increase in the general distribution of the municipal fund of €70 million in 2020 and €160 million in 2021.

The government recognises that, in addition to temporary financial problems for municipalities due to the Covid-19 pandemic, there are also concerns about the structural financial position of municipalities. Municipalities indicate that they are experiencing pressure at the level of services. Moreover, during recessions, additional expenditure in the social domain tends to crowd out investment in the

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[38] CPB Netherlands Bureau for Economic Policy Analysis (2018). Why have municipal investments fallen significantly since 2009? https://www.cpb.nl/sites/default/files/omnidownload/CPB-Notitie-11juli2018-Waarom-zijn-de-gemeente-investeringen-sinds-2009-sterk-gedaald.pdf

[39] Covid-19 crisis compensation package for local and regional authorities (2020). House of Representatives, session year 2019–2020, 35420, no. 43; Supplementary Covid-19 crisis compensation package for local and regional authorities (2020). House of Representatives, session year 2019–2020, 35420, no. 104; Supplementary compensation package for local and regional authorities December 2020 (2020), House of Representatives, session year 2020–2021, 35420, no. 207.

[40] Responses to Parliamentary Questions on the letter Supplementary Compensation Package for the Covid-19 Crisis, Parliamentary Documents II 2020/21, 35420, no. 104.

physical domain. In particular, municipalities with less equity are forced to implement cutbacks and tax increases and to reduce the level of services. Before the start of the Covid-19 crisis, six out of ten municipalities had an operating deficit. The combined equity capital of municipalities also decreased by 14% in the period between 2009 and 2019.

In the recently published guidance on intergovernmental relations, the Advisory Division concludes that municipalities and provinces are heavily dependent on the state for their income, which has led to several problems.[41]
The Advisory Division recommends that the causes of the problems be addressed. For example, the costs of carrying out the tasks to be transferred in the case of decentralisation, and the associated resources, must be given due consideration. A better understanding of what resources are needed should be provided in advance, and the CPB Netherlands Bureau for Economic Policy Analysis could play a role in this. Secondly, a system is needed that offers more financial security over the longer term than the current standardisation system. Increasing the municipal tax area only makes sense if the funding system of local governments is put in order.

Maintaining the level of state contributions to local and regional authorities and providing stability and financial security over the longer term are expected to have a positive impact on local and regional authority investment. Involving local and regional authorities in drafting the Dutch RRP is also appropriate, as the plans will have an impact on regions, but also because this will allow optimal use of opportunities for complementarity. The European Commission therefore recommends that Member States duly consult and involve local and regional authorities in the drafting RRF.

4. Fulfilment of commitments previously made by the government

In response to the comment of the Advisory Division in the April 2020 letter on the Stability Programme and in the Autumn 2020 report that the sustainability of public finances must not be overlooked, the government has endorsed the importance of sustainable public finances and a controlled development of the debt level, and has therefore asked the (16th) Study Group on Fiscal Policy for advice with a view to the coming government term.[42] In the autumn of 2020, the 16th Study Group on Fiscal Policy issued advice on the budgetary target and the budgetary system for the coming government term, which also addresses a controlled development of the public debt.[43]

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[41] Council of State guidance on intergovernmental relations, W04.20.0440/I/Vo.
[42] Letter about the Stability Programme, Parliamentary Documents II 2019/20, 21501-07, no. 1688. No.W06.20.0106/III and Draft Budget Memorandum 2021 and September Report on Budgetary Monitoring, Parliamentary Documents II 2020/21, 35570, no. 3, W06.20.0288/III.
[43] 16th Study Group on Fiscal Policy (2020) Koers bepalen – Kiezen in tijden van budgettaire krapte (Setting the course - Decisions in times of budgetary constraint), https://www.rijksoverheid.nl/documenten/kamerstukken/2020/10/12/rapport-studiegroep-begrotingsruimte

In addition, to test the sustainability of public finances, a simulation analysis is included in the Stability Programme 2021, which concludes that the risks to public debt are manageable in the medium term. At the same time, it cannot be ruled out that new shocks could lead to extremes in the future. The importance of sustainable public finances also remains relevant in the context of (the escape clause of) the SGP. The Advisory Division therefore asks a new government to pay constant attention to this.

The Advisory Division’s second comment in the 2020 September Report on Budgetary Monitoring concerned the preference for presenting expenditure on account of the Covid-19 pandemic and related support measures separately (whether or not in a separate box) from the expenditure ceilings. This is to improve the visibility of expenditure related to combating the Covid-19 crisis and the visibility of regular expenditure. The Advisory Division also advised to increase the insight into the (growth of) healthcare expenditure.

In response, the government stated that it is trying to maintain a transparent view of the budget as a result of the Covid-19 measures. The government also intends to use various budgetary documents to provide information on adjustments under the healthcare expenditure ceiling and the developments in healthcare expenditure.

The Advisory Division notes that the Stability Programme 2021 provides an insight into the distribution of the Covid-19-related expenditure among the budget chapters in 2020. Nevertheless, the question remains as to which emergency packages and budgetary measures underlie this expenditure per budget chapter (see further explanation in section B3.1). The development of healthcare expenditure crops up several times in the Stability Programme. The adjustments under the expenditure ceiling for healthcare in 2021 can be found in the departmental budget of the Ministry of Health, Welfare and Sport (VWS), where it has been laid out in a convenient manner.

The third comment by the Advisory Division in the 2020 September Report on Budgetary Monitoring concerned the financial impact of the newly established risk schemes and the expansion and relaxation of conditions of various existing guarantee schemes within the framework of the support and recovery packages. In its response to the September Report, the government acknowledged that guarantees are a potential risk to the budget and it is therefore important to critically monitor them, but that they are also an effective crisis instrument and contribute to economic recovery by removing uncertainty.

The government provides an overview of the outstanding state risk schemes twice a year (with the Budget Memorandum and the Annual Financial Report of the Kingdom). The next one is due in May 2021. In order to control the risks to public finances and to promote the trade-off between different policy instruments, the government pursues a ‘no-unless' policy with regard to risk schemes.

In response to the Covid-19 crisis, the government has tried to partially remove uncertainties in the economy by means of various risk schemes. At the European level too, risk schemes have been set up for this purpose, for which the Netherlands is a partial guarantor. As a result, the outstanding risk of government guarantees in 2020 increased sharply from €181 billion in 2019 to €240 billion in 2020 (30.5% of GDP). More than two-thirds of government guarantees are linked to the financial sector, most of which result from international agreements. The government argues that it is important to reduce the outstanding risk in good economic times, so that more risks can be borne in bad times. The Advisory Division points to the large share of guarantees at the European level, which has increased the risks of developments in other EU countries having an impact on the Dutch budget. This underlines the need for convergence of EU Member States in order to reduce risks.

5. EU-wide state of affairs

The recently strengthened EU fiscal framework for budgetary management formalises the tasks and broadens the role of national Independent Fiscal Institutions (IFIs) in an effort to promote fiscal discipline and strengthen national incorporation of EU fiscal rules.

In order to promote debate within the EUIFI network and improve the quality of budgetary monitoring, the network produces regular publications. The most recent publications are:

- *'The public debt outlook in the EMU post-Covid: a key challenge for the EU fiscal framework"'* which briefly reviews the gradually improved public finances ex ante Covid-19. EUIFI notes 'mixed compliance' with fiscal rules and shows the major impact of the pandemic on the economy and public finances.
- *'How to strengthen fiscal surveillance towards a medium-term focus?'*, which assesses the characteristics and conditions of effective medium-term frameworks in the EU based on national experiences.
- *'The role of the Independent Fiscal Institutions in the new era of high public debt',* which discusses the 'CPB task' of IFIs (namely: '*debt modelling in times of more unpredictability, higher public debt and low interest rates'*). In conjunction with the previous two publications, a more general, institutional question about the role of the IFIs also emerges.
- *'European Fiscal Monitor (March 2021)',* which provides an overview of the activities of 32 IFIs and the fiscal measures taken in 26 EU Member States and the UK.

Box 2: The European Independent Fiscal Institutions (National Independent Fiscal Institutions) and European fiscal rules.

The IFIs are defined as impartial public authorities, which aim to promote sustainable public finances. This can be done through various functions, including monitoring compliance with fiscal rules, producing or approving macroeconomic forecasts for the budget and/or advising the government on budgetary policy issues. In the Netherlands the Advisory Division of the Council of State along with the CPB Netherlands Bureau for Economic Policy Analysis forms the Dutch IFI. There is a Network of EU IFIs (EUIFI) of which 32 organisations from 27 EU Member States and the UK are members. The current chairman of the network is State Councillor Richard van Zwol. EUIFI meets bi-annually with the European Commission (DGECFIN), has contact with other EU institutions such as the Economic and Financial Committee (EFC) and the European Fiscal Board (EFB), and is part of a larger OECD Network of Parliamentary Budget Officials and Independent Fiscal Institutions (OECD PBO).

EUIFI supports efforts to strengthen and maintain the EU fiscal framework and strives to promote synergies between the various institutions in their assessments and recommendations in the area of fiscal policy. The IFIs in the network are heterogeneous in tradition, mandates, specific tasks performed, functional organisation, size and/or resources. The Netherlands has had a highly regarded, very experienced and robust CPB since 1945. In most EU Member States, independent IFIs and/or bureaus for economic policy analysis are much more recent and often, especially in smaller Member States, a modest size. EUIFI also serves as a platform and provides an opportunity to exchange expertise and experiences. This enhances the quality of assessments regarding compliance with the rules, the sustainability of public finances and stability-oriented fiscal policies. EUIFI monitors the
minimum standards for the independence and ability of IFIs to function. With this in mind, EUIFI recommends active engagement with parliaments and other stakeholders, in addition to the common consultation with the government.

The European Fiscal Board (EFB) was established by the European Commission in 2015 to serve as an independent fiscal advisor. The EFB also cooperates with the national IFIs. In previous reports, the Advisory Division has referred to the EFB's recommendations to simplify budget rules.[44] The EFB advocates a reformed SGP that would be based on a single objective (sustainable public debt), a single instrument (controlling the growth of net expenditure) and a single, general escape clause. These can be based on the current rules, whereby it is important that independent advice ensures transparency also in a reformed SGP. The latest assessment of the fiscal stance for the eurozone indicates that downside risks are substantial and that the current fiscal support measures by Member States are justified.[45] The current crisis and the response of Member States risk exacerbating

[44] European Fiscal Board (2019). *Assessment of EU fiscal rules with a focus on the six and two-pack legislation,* https://ec.europa.eu/info/sites/info/files/2019-09-10-assessment-of-eu-fiscal-rules_en.pdf

[45] European Fiscal Board (2020). *Assessment of the fiscal stance appropriate for the euro area,* https://ec.europa.eu/info/sites/info/files/2020_06_25_efb_assessment_of_euro_area_fiscal_stance_en.pdf

differences in economic performance and debt sustainability. Therefore, the EFB recommends that a simplified SGP be complemented by more structural central fiscal capacity or a dedicated investment fund to effectively support growth-enhancing public expenditure in Member States.

The Vice-President of the Council of State