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2024 Spring Report

A. INTRODUCTION AND CONCLUSION

1. Introduction

The Advisory Division of the Council of State has been charged with the independent budgetary monitoring of compliance with national and European fiscal rules.¹ It is the task of the independent budgetary monitoring institute to draw up an assessment of whether national and European fiscal rules are being met. The government's response to the Spring Report in the context of independent budgetary monitoring is included in full in this report.

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. The Advisory Division is charged with the more normative assessment of compliance with national and European fiscal rules.

In this 2024 Spring Report, the Advisory Division provides an assessment of budgetary developments in 2023, 2024 and 2025 as established by the government in the Stability Programme and the Spring Memorandum. The Advisory Division uses the budgetary analysis of the Spring Memorandum and the March forecast (the Central Economic Plan) of the CPB as the basis for the budgetary assessment.

In the interests of quality and meticulousness in drawing up the assessment, the Advisory Division was able to consult draft versions of the 2024 Spring Memorandum and the 2024 Stability Programme.

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¹ It concerns budgetary monitoring, as referred to in the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (TSCG), in Article 5 of Regulation (EU) 473/2013 and as included in Article 2 (8) of the Sustainable Public Finances Act.

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2. Summary conclusion and advice

The Coalition Agreement of the current, outgoing government historically contained many proposed intensifications. However, during this and also the previous government term, it proved difficult to actually spend the budgeted funds. This is partly due to expansionary fiscal policy, the extremely tight labour market and various administratively and politically complex issues. Due to a high level of underspending, an upturn and incidental revenue windfalls, the actual budget deficit has been lower than the estimated budget deficit each time. Partly because of this, in recent years, the Dutch budget has not exceeded the reference values in the corrective arm of the Stability and Growth Pact, namely a budget deficit of no more than 3% of GDP and government debt of no more than 60% of GDP.

In recent years, the current government has taken steps with regard to improving the budgetary process, compliance with national fiscal rules and transparency in budgetary policy. There is also increasing attention to the quality of public finances. For example, in this Spring Memorandum, the government has made efforts to establish a more realistic cash flow scenario for the budgeted funds and has made significant progress in providing a more transparent presentation of the budgetary choices and changes made as well as by adding a clear explanation of the rules and concepts used. In doing so, the government demonstrates that it is serious about the transparency of budgetary policy and the quality of public finances.

The incoming government will shape the budgetary policy to be implemented and formulate the budgetary anchors and fiscal rules during its term of office. To this end, developments in the economy and public finances in the medium and long term and the initial financial position are relevant, as are recent insights and future developments that have implications for public finances, including in the areas of defence, climate and the labour market. The Advisory Division has outlined relevant areas of concern in previous reports on the Stability Programme, the Spring Memorandum and the Budget Memorandum.

The initial economic position facing the incoming government differs from that of the current government: in the medium term, economic growth is expected to be

modest with lower inflation and higher interest rates than during the current government term. Moreover, public finances are expected to deteriorate. In the short term, the budget deficit will not be an issue, partly due to the high level of underspending in the budget. This will only provide a temporary improvement in public finances. Underspending does not structurally create additional budgetary margin because the funds are spent at a later date. In the medium term, Dutch public finances will deteriorate, in part due to an increase in population ageing-sensitive expenditure on healthcare and the state pension, among other things.

In the new European fiscal rules, politically agreed upon and expected to enter into force in May 2024, the single operational indicator for Member States, the net primary expenditure, includes a buffer in relation to the maximum budget deficit rule (3% of GDP) and maximum public debt criterion (60% of GDP), allowing Member States to pursue stabilising budgetary policy. Steering in terms of this indicator should ensure that the estimated government debt and the estimated budget deficit remain below the reference values of 60% of GDP and 3% of GDP, respectively, in the medium term (i.e., fourteen to seventeen years) based on different scenarios, thus ensuring sustainable public finances.

In the autumn of 2024, the Netherlands must submit an initial medium-term fiscal-structural plan. The plan must include relevant investments and reforms and a medium-term expenditure path, with a buffer in relation to the 3% maximum budget deficit. The submission process may overlap with the Budget Memorandum process.

The budget deficit exceeds 3% of GDP in most forecast years; between 2029 and 2032, the deficit increases to an average of 4.6% of GDP. Consequently, the initial budgetary position facing the upcoming government term is not particularly bright: in order to comply with European fiscal rules and maintain a margin for implementing trend-based fiscal policy, public finances must be structurally improved compared with the current level. This budgetary margin can be achieved through both higher taxes and lower expenditure.

In order to implement fiscal policy during the upcoming government term in which the basic principles of Dutch fiscal policy can be respected, i.e. an efficient allocation of public resources, control of public finances and macroeconomic stabilisation, the Advisory Division, in line with previous opinions and given the current economic and fiscal assumptions and recent insights and developments, identifies the following areas of concern:

- I. Pursue prudent budgetary policy and, when choosing a budgetary anchor, ensure there is sufficient budgetary margin so that the budget's automatic stabilisation function can do its job. This necessitates a medium-term budgetary task, taking into account the negative impact of spending cuts or tax increases on the economy and society.

- II. Adopt an approach focusing on broad prosperity when implementing fiscal policy and when elaborating the budgetary task. This contributes to long-term thinking, which can facilitate efficient and effective decisions.
- III. The quality of public finances is important for achieving societal goals. When justifying policy choices and elaborating budgetary tasks, consider not only the immediate consequence of the choices made, but also the consequences for the economy and society and the future impact of the proposal.
- IV. Over the past few years a solid foundation has been laid for a new, improved budgetary process in the spring. Continue on this path, in association with parliament, during the upcoming government term.
- V. The composition and level of government revenue and expenditure will change structurally and significantly due to climate change. Currently, the climate is not yet sufficiently incorporated in the considerations that apply to fiscal policy. Therefore, gradually make the budgetary framework climate-inclusive.

B. BUDGETARY ASSESSMENT AND OPINIONS

1. Relevant context

1.1 *Macroeconomic context*

Short-term (2023-2025)

After three consecutive quarters of economic contraction in 2023, the economy grew 0.3% in the fourth quarter of 2023 compared to the third quarter of 2023. GDP grew by 0.1% for 2023 as a whole.² Economic growth is expected to pick up in 2024 and 2025 with growth of 1.1% and 1.6%, respectively. After several economically turbulent years due to (the aftermath of) the Covid-19 crisis and the war in Ukraine, the economy appears to be returning to a path of modest growth.³

Table 1: Key figures of macroeconomic developments 2023-2025

(changes in % per annum)	2023		2024		2025	
	<i>MEO</i> 2024	<i>CEP</i> 2024	<i>MEO</i> 2024	<i>CEP</i> 2024	<i>MEO</i> 2024	<i>CEP</i> 2024
Euro area						
Gross domestic product (economic growth)	0.5	0.6	1.3	0.9	1.3	1.6
The Netherlands						
Gross domestic product (economic growth)	0.7	0.1	1.5	1.1	1.2	1.6
Companies' labour productivity (per hour)	-0.9	-0.4	0.8	0.4	1	1
Gross investments by companies (excl. Housing %)	8.5	3.4	0.5	-5.3	1	2.3
Investments by companies in housing	-0.4	-1.3	-6.2	-0.7	1.1	1.3
Household consumption	0.6	0.4	2.4	2.7	2	2.4
Static purchasing power	-1.1	-0.8	1.8	2.7	0.7	0
Inflation, national consumer price index	3.9	3.8	3.8	2.9	2.6	2.8
Persons in poverty (level in %)	4.8	4.8	4.8	4.7	6	4.9
Imports of goods and services	1.9	-0.7	2.1	1.1	3	3
Exports of goods and services	0.8	-1.2	1.5	0.6	2.3	2.5
Wages provided for by company CLAs	5.8	5.9	5.6	6	4.7	3.9
Employment (in hours)	1.2	0.5	0.6	0.6	0	0.6
Unemployed working population (level in %)	3.6	3.5	4	3.7	4.2	3.9

Source: CPB, 2024 Macroeconomic Outlook (September 2023) and 2024 Central Economic Plan (March 2024)

² The figures for 2023 are an initial calculation; new calculations will follow during 2024 based on the information available at the time. Source: Statistics Netherlands (CBS) (2024). Economic growth of 0.3 percent in Q4 2023. Via <https://www.cbs.nl/en-gb/news/2024/07/economic-growth-of-0-3-percent-in-q4-2023>.

³ CPB Netherlands Bureau for Economic Policy Analysis (2024). Central Economic Plan 2024 and Central Economic Plan 2024 Accountability Document. CPB Forecast, February 2024.

Inflation will continue to fall in 2024 and 2025 compared to 2023 due to a drop in core inflation and a further decrease in energy prices, according to the CPB in the Central Economic Plan 2024 (CEP Forecast). Collective labour agreement wages are expected to rise 6% in 2024. Purchasing power increases by 2.7% on average in 2024, due to strong collective labour agreement wage growth, low inflation and the government's purchasing power measures. The recovery in real incomes, along with the purchasing power measures, will drive growth in consumption in 2024, despite highly negative consumer confidence.

In 2025, collective labour agreement wages will rise more slowly than in 2024 by 3.9% because most employees' wages will have compensated for high inflation. In the current CPB forecast, the average purchasing power trend in 2025 compared to 2024 is stable (no growth), but low incomes and households with children will be slightly worse off on average.⁴ Poverty falls slightly in 2024 to 4.7% of the population and to 4.9% of children, but rises again from 2025 due to the expiration of incidental policy measures aimed at reducing poverty.

Due to high inflation in recent years, the CPB expects a slight decrease in average household purchasing power of 0.5% in 2025 compared to 2021. Policy measures have resulted in major differences between groups in purchasing power development between 2021 and 2025; low incomes in particular benefit from a number of structural income support measures implemented by the current government.

Government spending also drives the economy in 2024 and 2025, according to the CPB, due to increased spending, for example, on healthcare, defence and asylum. Business investment fell sharply in the second half of 2023 due to a pessimistic outlook regarding expected activity and high capital expenses resulting from an increase in interest rates. Business investment is expected to recover slowly during 2024, as industrial production is likely to pick up in the coming years. Economic growth in 2024 and 2025 is thus mainly driven by household consumption and government spending. Downward economic risks are mainly caused by geopolitical tensions.

The rise in employment will be moderate in 2024 and 2025; however, there is strong job growth in government and the healthcare sector. Labour supply flatlines in 2024 and 2025, due to a lower migration balance and an already high participation rate. Due to the high demand for labour, the labour market remains tight for the time being, although the unemployment rate rises slightly to 3.7% in 2024 and 3.9% in 2025. The labour market is expected to become more dynamic, though, due to an increase in bankruptcies and dismissal applications.

⁴ The Budget Memorandum usually contains decisions on any additional purchasing power measures to be taken for the following year.

Medium-term (2026-2032)

In the medium term, there will be modest economic growth. This is based on the assumption that economic growth will reach a balanced position. However, economic fluctuations are not easy to predict. The increase in labour supply is gradually declining, partly because of an ageing population and because participation rates are rising less within cohorts. This means the tightness in the labour market will continue in the medium term. The slowdown in structural productivity growth will continue. A shift of the Dutch economic structure to a service economy plays a role in this regard.⁵

Purchasing power will increase by an average of 0.8% per year in the medium term. However, poverty among Dutch households will increase without additional policies: the number of people and children in poverty is estimated by the CPB in the CEP forecast at 6.0% and 6.8%, respectively, in 2032.

Table 2: Key figures of macroeconomic developments 2026-2032

(changes in % per annum)	2026		2027		2028		2029-2032
	<i>MEO</i> 2024	<i>CEP</i> 2024	<i>MEO</i> 2024	<i>CEP</i> 2024	<i>MEO</i> 2024	<i>CEP</i> 2024	<i>CEP</i> 2024
Euro area							
Gross domestic product (economic growth)	1.2	1.3	1.1	1.1	1.1	1.1	
The Netherlands							
Gross domestic product (economic growth)	1.1	1.4	1.1	1.2	1.1	1.1	1.0
Companies' labour productivity (per hour)	1.0	1.2	0.9	1.0	0.9	1.0	1.0
Gross investments by companies (excl. Housing %)	0.8	-0.2	0.0	0.3	1.8	1.0	
Investments by companies in housing	1.1	1.4	1.0	1.2	1.0	1.1	
Household consumption	1.8	1.9	1.7	1.8	1.8	1.9	1.6
Static purchasing power	1.2	0.8	0.8	0.8	1.1	0.8	0.8
Inflation, national consumer price index	2.5	2.4	2.4	2.3	2.1	2.3	2.1
Persons in poverty (level in %)	5.9	5.0	6.0	5.2	6.1	5.4	6.0
Imports of goods and services	2.8	2.6	3.0	2.9	3.3	3.1	2.8
Exports of goods and services	2.2	2.2	2.1	2.1	2.1	2.0	2.0
Wages provided for by company CLAs	4.5	3.7	3.8	3.6	3.5	3.5	3.5
Employment (in hours)	0.1	0.3	0.1	0.2	0.2	0.1	0.0
Unemployed working population (level in %)	4.4	4.2	4.6	4.4	4.8	4.6	5.3

Source: CPB, 2024 Macroeconomic Outlook (September 2023) and 2024 Central Economic Plan (March 2024)

1.2 *Budgetary context*

⁵ CPB Netherlands Bureau for Economic Policy Analysis (2023). 2024 Draft Macroeconomic Outlook. CPB forecast, August 2023.

Short-term (2023-2025)

The Coalition Agreement of the current, outgoing government historically contained many proposed intensifications.⁶ The government opted for an ambitious investment agenda, with investments in societal challenges, including the climate, education and the housing market, with the goal of avoiding higher costs and a loss of broad prosperity in the future. In doing so, the government deemed a temporary deterioration of public finances to be justified because of the relatively low EMU debt at the beginning of the government term.⁷

However, during this and the previous government term, it proved difficult to actually spend the budgeted funds. As of 2016, underspending with regard to the state budget has increased in relative and absolute terms. From 2018 onwards, there has been a sharp increase in underspending, due to investments made by the previous and current government. The underspending relates to specific areas such as defence, infrastructure and education, but there is also generic underspending. Causes of this extensive underspending include the very tight labour market and various administratively and politically complex issues, such as the childcare benefits affair and the nitrogen crisis.⁸

Table 3: Difference between the forecasted and achieved EMU balances 2018-2023

Figures in % of GDP	2018	2019	2020	2021	2022	2023
Estimated EMU balance	0.8	1	0.3	-5.1	-2.3	-2.5
Achieved EMU balance	1.5	1.8	-3.7	-2.2	-0.1	-0.6

Source: CBS and CPB (MEO 2018-2023)

Underspending also constitutes a serious explanation for the difference between estimated and actual EMU balances, as examined in the 2023 Fiscal Policy Audit. As of 2018, the estimated EMU balance has been more negative than the balance ultimately achieved every year, except for 2020, when the world experienced an economic shock resulting from the Covid-19 virus (see Table 3).

The CPB expects underspending to continue due to the persistently tight labour market and multi-year ongoing intensifications by the current government.⁹ In 2024 and 2025, the CPB forecasts underspending of 1.4% and 1.3% of GDP, respectively. After 2024, the CPB assumes a gradual decrease in underspending, as the labour market becomes less tight and there is more time to develop and implement plans.

⁶ Economische Statistische Berichten (2022). Rutte IV intensificeert historisch veel. (Historically Rutte IV makes substantial use of intensifications). 107(4807), 17 March 2022.

⁷ 2023 Spring Report, Parliamentary Documents II 2022/23, 36350, No. B.

⁸ 17th Study Group on Fiscal Policy. (2023) Bijsturen met het oog op de toekomst. (Adjusting for the future.) Appendix to the Fiscal Policy Audit.

⁹ CPB Netherlands Bureau for Economic Policy Analysis (2024). Central Economic Plan 2024 and Central Economic Plan 2024 Accountability Document. CPB Forecast, February 2024.

Despite the expected underspending, the CPB forecasts a deterioration in public finances in 2024 and 2025. This is mainly due to rising expenditure for various budgetary funds, including the Climate Fund, the Transition Fund, the National Growth Fund and the Defence Material Fund. Spending is also increasing due to military support for Ukraine and the reception of Ukrainians. Social Security expenditure is rising, mainly due to higher wages, an ageing population and a slight rise in the unemployed working population. Healthcare expenditure is also increasing, due to the ageing population and higher wages and prices.

Table 4: Key figures of public finances 2023-2025

(in % of GDP)	2023		2024		2025	
	<i>MEO 2024</i>	2024 Spring Memorandum Budgetary Analysis	<i>MEO 2024</i>	2024 Spring Memorandum Budgetary Analysis	<i>MEO 2024</i>	2024 Spring Memorandum Budgetary Analysis
Gross general expenditure	44.1	43.5	44.9	44.4	45	45
General government revenue	38.8	39.1	38.7	38.8	38.5	38.9
Actual EMU balance	-1.5	-0.3	-2.4	-2.0	-2.6	-2.1
Structural EMU balance	-1.5	-0.3	-2.2	-1.5	-2.1	-1.6
EMU debt	47.7	46.5	46.9	46.8	48.3	48.1

Source: CPB, 2024 Macroeconomic Outlook (September 2023) and 2024 Spring Memorandum Budgetary Analysis (April 2024)

In 2024, the EMU balance will also deteriorate due to a decrease in the collective tax burden as a result of an expected decline in corporate and dividend tax revenues, as they were incidentally high in 2023, and corporate revenues are expected to lag behind GDP growth in 2024. In 2025, the collective tax burden will increase slightly, mainly due to the increase in revenue from payroll taxes. This is due in part to higher wages and an increase in the tax rate in the first bracket.

Medium-term (2026-2032)

At the beginning of the current government term, nominal interest rates were historically low. Moreover, real interest rates were negative due to high inflation. During the government term, government debt - despite expansionary fiscal policy - displayed a positive trend, partly due to the economic recovery after the Covid-19 crisis, low interest rates and high inflation, and a sharp increase in underspending.

The economic position facing the upcoming government differs from that of the current government: in the medium term, economic growth is expected to be modest with lower inflation and higher interest rates than during the current government term (see Section B1.1) and public finances are deteriorating (see Table 5).

Table 5: Key figures of public finances 2026-2032*

(in % of GDP)	2026		2027		2028		2029-2032
	<i>MEO 2024</i>	2024 Spring Memorandum Budgetary Analysis	<i>MEO 2024</i>	2024 Spring Memorandum Budgetary Analysis	<i>MEO 2024</i>	2024 Spring Memorandum Budgetary Analysis	CEP 2024
Gross general expenditure	46.1	45.6	45.9	45.4	46.7	45.9	47.6
General government revenue	38.9	38.7	38.9	39.1	39	39.1	39.7
Actual EMU balance	-3.4	-3.3	-3.3	-2.6	-3.6	-3.2	-4.6
Structural EMU balance	-2.9	-2.8	-2.7	-2.0	-3	-2.6	-4.1
EMU debt	50.1	49.5	51.8	50.4	53	52.0	63.5

Source: CPB, 2024 Central Economic Plan, 2024 Macroeconomic Outlook (September 2023), 2024 Central Economic Plan (March 2024) and 2024 Spring Memorandum Budgetary Analysis (April 2024)

* The key data from 2026 to 2028 inclusive compares the figures from the Macroeconomic Outlook (MEO) with the figures from the Spring Memorandum Budgetary Analysis calculation (BAV). Key data with a medium-term outlook (2029-2032) are from the 2024 Central Economic Plan (CEP).

During the upcoming estimated government term, between 2024 and 2028, general expenditure will increase, according to the CPB in its calculation of the Spring Memorandum's budgetary effects. Gross general expenditure will increase from 44.4% of GDP in 2024 to 45.9% of GDP in 2028.¹⁰ The collective burden in terms of percentage of GDP hovers around 39% of GDP. Due to the increase in the general expenditure ratio in the event of an unchanged total revenue ratio, there are annual budget deficits and an increase in public debt (see Tables 4 and 5).

If policy remains unchanged, the government deficit increases to 3.2% of GDP in 2028 and 4.6% of GDP in 2032. According to the CPB the increase in the government deficit is caused by additional expenditure already planned and an increase in interest charges. The reasons for the increase in government expenditure include an increase in spending on social security and healthcare, partly due to the ageing population, and an increase in spending on climate and nitrogen, defence and asylum costs. Interest expenditure is gradually increasing too due to higher interest rates on government bonds: in 2028, interest expenditure is estimated to reach €12.8 billion. This is €5.8 billion more than in 2023. In addition, underspending is expected to decrease.

According to the CPB, the structural balance, the budget balance adjusted for the economic cycle, is also expected to be profoundly negative at -2.6% of GDP in 2028 and -4.1% of GDP in 2032, implying expansionary fiscal policy. The debt ratio is expected to reach 52.0% of GDP in 2028. In the medium term, the debt

¹⁰ CPB Netherlands Bureau for Economic Policy Analysis. (2024) Budgetary Effects of the Spring Memorandum (April 2024). The budgetary effects of the spring decisions as presented in the 2024 Spring Memorandum are reflected in these figures.

ratio is expected to increase, partly because population ageing-sensitive expenditure will rise sharply after 2030. Government debt as a percentage of GDP is expected to reach 63.5% in 2032.

A focus on medium-term sustainability of public finances is key to the new European budgetary framework, which is likely to enter into force by May 2024. The new fiscal targets should ensure that the estimated government debt and the estimated budget deficit remain below or move in the direction of the reference values of 60% of GDP and 3% of GDP, respectively, in the medium term (a period of fourteen to seventeen years). The current forecast horizon will have to be extended in line with the medium-term path in the European budgetary framework.

2. Outcome and implications of the reform of the European budgetary framework

European fiscal rules are set out in the Stability and Growth Pact (SGP). The SGP was introduced as part of Economic and Monetary Union (EMU), with one of its essential objectives being to guarantee the sustainability of public finances also in the long term. Economic growth in Member States and convergence is the other essential objective. The SGP consists of the preventive and corrective arm, enshrined in two regulations that have been amended several times. The SGP has additional components enshrined in intergovernmental treaties,¹¹ regulations¹² and directives¹³.

Box 1: The current European budgetary framework

Regulations 1466/97 (preventive arm) and 1467/97 (corrective arm) establish the rules of the Stability and Growth Pact (SGP) (1997). These regulations have been amended three times. In 2005, the amendment aimed to strengthen and clarify the implementation of the SGP to promote transparency and national ownership and improve enforcement of the rules. In 2011, the amendment was part of a broader package of regulations and a new directive (the introduction of the so-called Six Pack within the SGP), aimed at tightening fiscal rules and broadening economic surveillance by including monitoring of macroeconomic imbalances. The third amendment of the regulations will take place in 2024 as part of the *Economic Governance Review*.

The Treaty on European Union (TEU, 1992) contains the basis for EMU and for the introduction of a common currency. The principle of economic convergence is enshrined in the Treaty: Member States regard their economic policies as a matter of common interest and align their national policies. The Treaty on the Functioning of the EU (TFEU, 2009) establishes economic policy coordination, the fiscal rules

¹¹ Treaties are binding agreements on the contracting parties that can be included in a legislative framework.

¹² Regulations are directly applicable in each Member State.

¹³ Directives contain binding obligations to produce results and must be translated into national legislation.

of the corrective arm and the excessive deficit procedure. The TFEU is an amended version of the original Treaty (amended several times) establishing the European Economic Community (EEC, 1957).

The Treaty on Stability, Coordination and Governance in the EMU (TSCG, 2013) contains the Fiscal Compact, which prescribes detailed rules for the preparation of national budgets to promote compliance with European fiscal rules. The TSCG is a separate intergovernmental treaty outside the EU treaties and applies to those contracting parties whose currency is the euro. The TSCG also establishes the obligation for enshrining the role and independence of independent fiscal institutions, for monitoring the Fiscal Compact rules at the national level.

In addition to the regulations for the preventive and corrective arm, the SGP also has additional regulations from the Six Pack (2011) and Two Pack regulations (2013). In addition to amending Regulations 1466/97 and 1467/97 (by means of Regulations 1175/2011 and 1177/2011), the Six Pack consists of regulations to strengthen enforcement in the Euro area for both the preventive and corrective arms (Regulation 1173/2011), containing the Macroeconomic Imbalance Procedure (MIP) for the Euro area (Regulation 1174/2011), containing the MIP for the entire European Union (Regulation 1176/2011), and a directive containing rules for Member States' budgetary frameworks (Directive 2011/85/EU). It also requires the establishment of national independent fiscal institutions to monitor compliance with fiscal rules.

The Two Pack consists of two regulations and only applies to Member States in the Euro area. Regulation 472/2013 establishes provisions to strengthen economic and fiscal surveillance of Euro area Member States if they are experiencing, or are at risk of experiencing, serious difficulties with respect to financial stability or the sustainability of public finances, or receiving financial assistance. Regulation 473/2013 lays down rules to strengthen the monitoring of economic and fiscal policies in the Euro area and to ensure that national budgets are consistent with the economic policy guidelines under the SGP and the European Semester. This regulation establishes conditions for the independent fiscal institutions, regarding their tasks and the rules to which these institutions must adhere.

In 2020, just before the start of the Covid-19 crisis, the European Commission announced a reform of the current SGP¹⁴. The regulations for the preventive and corrective arm (Regulations 1466/97 and 1467/97) and the directive containing rules for budgetary frameworks and budgetary surveillance of Member States (Directive 2011/85/EU) are part of this reform. Thus, the reform focuses on both European fiscal targets and Member States' budgetary frameworks and budgetary surveillance.

¹⁴ The reform stems from an evaluation obligation in Regulation 1466/97 requiring the Commission to publish a report on the application of the regulation every five years.

During the Covid-19 crisis, the reform was temporarily put on hold. It resumed in November 2022, and included lessons learned from the Covid-19 crisis.¹⁵

Legislative proposals for the reform were then presented by the Commission in April 2023.¹⁶ In February 2024, an agreement was reached between the Council, the European Parliament and the European Commission on the new legal texts for the Regulations and the Directive. They are expected to formally enter into force in May 2024, following approval by the Council and a vote in the European Parliament.

The budgetary framework must be revised to take into account the heterogeneity in budgetary positions, the level of public debt, (future) economic challenges and other vulnerabilities of Member States more effectively than before. At the same time, the review should help address the European Union's medium and long-term challenges, such as achieving a fair digital and green transition, ensuring energy security, supporting strategic autonomy, demographic change, and strengthening social and economic resilience and sustainable convergence.¹⁷

Outcome of the reform of the preventive and corrective arms

The corrective arm sets requirements for reference values for the budget deficit (EMU balance of maximum 3% of GDP) and government debt (EMU debt of maximum 60% of GDP) of Member States. These reference values remain unchanged in the budgetary framework's reform. If any or all of the reference values are exceeded, the Commission may launch an excessive deficit procedure, after which the Council may issue a recommendation to correct the excessive deficit or debt. The purpose of the preventive arm is to prevent Member States from facing excessive deficits by maintaining a safe margin from the 3% deficit rule, so that Member States have a budgetary margin to pursue stabilising fiscal policies.

The rules in the current preventive arm, which formally apply up to and including spring 2024, consist of a medium-term objective (MTO) for the structural balance, and an expenditure rule. The structural balance is the budget balance adjusted for temporary measures and effects of the business cycle. For the structural balance

¹⁵ European Commission (2022). Communication from the Commission to the European Parliament, the Council, the European Central Bank, the European Economic and Social Committee and the Committee of the Regions. Communication on orientations for a reform of the EU economic governance framework. COM(2022) 583 final.

¹⁶ European Commission (2023). A proposal for replacing Regulation (EC) No 1466/97 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies. COM(2023) 240 final, A proposal for amending Council Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure. COM(2023) 241 final. A proposal for amending Council Directive 2011/85/EU on requirements for budgetary frameworks of the Member States. COM(2023) 242 final, Annexed 1-7 to the Proposal for Regulation COM(2023) 240 final.

¹⁷ European Commission (2024). Proposal for a Regulation of the European Parliament and of the Council on the effective coordination of economic policies and multilateral budgetary surveillance and repealing Council Regulation (EC) No 1466/97.

Member States have a country-specific MTO. The expenditure rule within the preventive arm requires that government spending should not increase faster than potential economic growth, also taking into account the distance to the MTO. The idea behind the expenditure rule is that revenues move with the economic cycle and expenditure does not increase faster than potential economic growth, preventing the structural balance from deteriorating. In the new budgetary framework, the rules in the preventive arm no longer apply.

The reformed preventive arm, which will formally apply from mid-2024, has multiple objectives, namely (1) to achieve sustainable public finances in the medium term and avoid excessive deficits, and (2) sustainable and inclusive growth and a resilient economy. To achieve these objectives, Member States submit national medium-term fiscal-structural plans every four years. This plan is considered to be the cornerstone of the new budgetary framework.

To achieve the first objective, a single country-specific indicator, called the expenditure path, is used for Member States in the medium term. The expenditure path is translated into the maximum annual growth of net primary expenditure for Member States, taking into account estimated budget deficits and the level of public debt in the medium term (see Box 2 for an explanation). By the end of the four or seven-year period covered by the plan, known as the fiscal adjustment period, government debt must be on a credible declining path or at prudent levels below 60% of GDP in the medium term, based on different scenarios. Moreover, the budget deficit must be brought below 3% of GDP by the end of the adjustment period and remain so in the medium term.¹⁸

To achieve the second objective, the national medium-term fiscal-structural plan must include reforms and investments that contribute to sustainable and progressive debt reduction and sustainable and inclusive economic growth in Member States. The reforms and investments must also be in line with country-specific recommendations from the European Semester and contribute to common European Union priorities, such as the transition to climate neutrality and defence capability building.

If Member States commit to a relevant set of reforms and investments, the fiscal adjustment period can be extended from four to seven years. This means more time for Member States to credibly reduce or maintain their public debt at prudent levels and to bring or maintain their budget deficits below the reference value. In return, they must demonstrate that the reforms and investments contribute to sustainable and progressive debt reduction and sustainable and inclusive growth. The reforms and investments must also contribute to common European Union priorities and be in line with country-specific recommendations from the European Semester.

¹⁸ The medium term refers to a period of ten years after the end of the national fiscal-structural plan.

Box 2: Changes in the fiscal targets of the preventive arm

The purpose of the preventive arm is to prevent Member States from facing excessive deficits by maintaining a safe margin from the 3% deficit rule. The current preventive arm consists of a medium-term objective for the structural balance and an expenditure rule. The new budgetary framework focuses on a single indicator, which is a country-specific expenditure path expressed as net primary expenditure, with the aim of simplification and increased transparency. This means the rules in the preventive arm will be abolished.

A Member State's total expenditure is expressed in terms of net primary expenditure. This is national government expenditure adjusted for interest expenditure, temporary and one-off expenditure, expenditure paid for with revenues from EU funds and national co-financing for EU programmes, cyclical unemployment expenditure, and any measures that provide higher revenues. Adjusting the expenditure for interest expenditures allows Member States to focus primarily on expenditure they can directly influence. Adjusting the expenditure for cyclical unemployment expenditure creates a margin for it to move in tandem with the economic cycle, which helps with the implementation of trend-based fiscal policy.

Expenditure is also adjusted for any discretionary revenue measures, which means there is no margin for increased spending if an increase in tax rates or a broadening of the base, resulting in higher tax revenues, occurs. Moreover, expenditure paid for with revenues from EU funds, national co-financing for EU programmes, and one-off and temporary measures are excluded. Adjusting for these items omits costs that have little or no impact on the Member State's structural budgetary position.

The country-specific expenditure path, which prescribes maximum annual growth of net primary expenditure, will be derived from the structural primary balance at the end of the adjustment period. The structural primary balance is the regular EMU balance adjusted for the economic cycle and interest rates (that is, the structural balance adjusted for interest rates). The rule for the structural primary balance recalculates the fiscal adjustment required by a Member State to bring or maintain government debt on a credible declining path or at prudent levels below 60% of GDP in the medium term, and to bring or maintain the budget deficit below 3% of GDP in the medium term.

To do so, the Commission will use a debt sustainability analysis, which considers multiple scenarios of interest rate differentials, GDP growth and the burden resulting from population ageing, among other things. This enables the Commission to assess how government debt and the budget deficit might evolve in different situations (windfalls and negative developments), over a ten-year period following the adjustment period. In addition, the Commission assesses whether there is a sufficiently low probability that the debt will still increase

within five years of the plan's implementation. Debt must also remain within a certain margin under a set of possible economic shocks.

The maximum nominal growth of a Member State's net financed primary expenditure is determined by (annual) potential GDP growth plus inflation minus the required adjustment in the structural primary balance relative to primary expenditure expressed as a percentage of GDP.

The structural primary balance is not a control variable per se, but forms the starting point for calculating the country-specific expenditure path. For enforcement and annual monitoring purposes, the Commission will perform its assessment in relation to expenditure path overshoots, not structural primary balance overshoots.

In the reformed corrective arm, the reference values for the budget deficit - 3% of GDP - and government debt - 60% of GDP - continue to be pivotal. An excessive deficit procedure can be opened by the Council, on the recommendation of the European Commission, if Member States exceed the 3% reference value or if Member States with a debt above 60% of GDP deviate from the expenditure path above the annual and cumulative thresholds.

Overspending and underspending in the expenditure path are tracked annually by the Commission in the control account: Member States with a debt above 60% of GDP are allowed to deviate from their expenditure path by up to 0.3% of GDP annually and by up to 0.6% of GDP added up over several years. The Commission takes into account all the relevant factors when examining whether an excessive deficit exists.¹⁹ These relevant factors may result in no excessive deficit procedure being opened.

If the Council decides to open an excessive deficit procedure and makes a recommendation for the correction of the excessive deficit, the Member State involved must take action to correct the excessive deficit. If there is an excessive deficit based on an overshoot of the deficit rule of maximum 3% of GDP, the Member State must include a corrective expenditure path in the multi-year plan that includes an annual fiscal adjustment of at least 0.5% of GDP in structural terms.

If there is an excessive deficit based on the debt criterion of maximum 60% of GDP, the Member State must include a corrective expenditure path in the fiscal-structural plan that is at least as demanding as the expenditure path recommended by the Council. Moreover, as a rule, overshoots in the control account must be

¹⁹ Relevant factors concern a Member State's economic and budgetary circumstances (including potential growth and deviations from the expenditure path). If a Member State faces a substantial debt challenge, the Commission considers this a decisive factor in its assessment. In addition, any increase in defence spending is considered a relevant factor.

corrected before the end of the adjustment period of the expenditure path recommended by the Council.

If the Member State in the excessive deficit procedure does not take sufficient effective action to reduce the excessive deficit, the Council may, on a recommendation from the Commission, impose a fine of up to 0.05% of GDP. This amount must be paid every six months thereafter until the Council decides that the Member State in question has taken effective action. In the event of exceptional circumstances beyond the control of the Member State, the Council, on a recommendation from the Commission, may decide that a Member State (through a country-specific escape clause) or all Member States (through a general escape clause) may deviate from the expenditure path for a specific period of time.

Difference in the initial budgetary position

In the current corrective arm of the European fiscal framework still formally in force, if the reference values of the corrective arm are not met, the budget deficit must be reduced to below 3% of GDP and the debt above 60% of GDP must be reduced by 1/20th per year to ensure the debt declines sufficiently. This may require a major fiscal effort by Member States, with potentially negative consequences for the economy.²⁰

The new European budgetary framework has a more country-specific premise of reducing high debt and large deficits while ensuring sustainable and inclusive growth. It is therefore important that debts and deficits are gradually reduced so that stabilising budgetary policy can be implemented. A budgetary margin must also be maintained for necessary investments.²¹

The medium-term fiscal-structural plan should accomplish this. In compiling this plan, not only are country-specific circumstances in the expenditure path taken into account, but the initial budgetary position of the Member State is equally important: it determines the requirements the plan must meet.

If a Member State meets the rules of the corrective arm at the time the plan is submitted (*ex ante*), the Member State compiles a plan containing a multi-year net expenditure path along with relevant reforms and investments and indicate how the reforms and investments relate to common EU priorities, reflecting the impact of already implemented reforms and investments and information about key budgetary and macroeconomic assumptions. If the Member State commits to a relevant set of reforms and investments, an extension of the plan's time frame may be requested of up to three years.

²⁰ CPB Netherlands Bureau for Economic Policy Analysis. (2023) Cyclisch begrotingsbeleid (Cyclical fiscal policy). CPB - September 2023

²¹ European Commission (2024). Proposal for a Regulation of the European Parliament and of the Council on the effective coordination of economic policies and multilateral budgetary surveillance and repealing Council Regulation (EC) No. 1466/97.

The expenditure path must ensure that the estimated government debt and the estimated budget deficit remain below the reference values of 60% of GDP and -3% of GDP, respectively, in the medium term (i.e., up to and including ten years after the plan expires, so in total 14 and 17 years in the event of an extension) under different scenarios arising from the Commission's debt sustainability analyses. At the Member State's request, the Commission can provide the former with technical information in terms of a structural primary balance required at the end of the adjustment period (see Box 2). This technical information can subsequently be used to compile the plan.

Before submitting the plan, the Member State engages in a technical dialogue with the Commission to ensure that the plan complies with the requirements of the regulation. After the Member State submits the plan, the Commission assesses whether the plan meets all the requirements, including for the net expenditure path. The Council, based on a recommendation from the Commission, then issues a recommendation to the Member State on the net expenditure path. If there is an extension of the adjustment path, the Council approves the investments and reforms underlying the extended adjustment period.

If there are macroeconomic imbalances, identified in the macroeconomic imbalance procedure (MIP), there will also be recommendations to correct these imbalances. If the requirements of the expenditure path are not met by the Member State, the Council must recommend that the Member State submit an adjusted plan. However, the Council cannot recommend an alternative expenditure path to the Member State.

If a Member State does not meet (ex ante) any of the reference values of the corrective arm when the plan is submitted, the Commission provides the Member State concerned with a reference path. The reference path covers a four or seven-year period and includes a risk-based expenditure path. If the Member State commits to a relevant set of reforms and investments, an extension of three up to a maximum of seven years is possible.

The reference path serves as the starting point for the expenditure path compiled by a Member State and must ensure that at the end of the adjustment period, estimated government debt is on a credible downward growth path or at prudent levels below 60% and/or remains below 60% in the medium term and that the estimated budget deficit has been brought below 3% of GDP during the adjustment period and that it also remains below 3% of GDP in the medium term. For both debt and deficit reduction, the adjustment must be sufficient based on different scenarios arising from the Commission's debt sustainability analyses (see Box 2).

In addition, the fiscal adjustment must be linear and at least proportional during the adjustment period. In other words, the fiscal adjustment must not be postponed. If there is already an excessive deficit procedure, the reference path must be consistent with the corrective expenditure path.

The reference path also takes into account various safeguards depending on the initial budgetary position when the plan was drawn up.²² These safeguards are designed to ensure that anticipated debt decreases by a minimum annual average and/or that a sufficient buffer in relation to the 3% reference value is built up. As such, the safeguards act as a minimum requirement for the budgetary task underlying the reference path.

The reference path is characterised by the following safeguards:

- Ex ante deficit safeguard: requires an annual reduction of 0.4% of GDP in the structural primary balance, and 0.25% of GDP if the adjustment period is extended, until a margin of 1.5% of GDP in structural terms relative to the 3% of GDP deficit norm is achieved.
- Structural balance adjustment: requires an annual minimum adjustment to the structural balance of 0.5% of GDP.
- Ex ante debt safeguard: requires a debt reduction of at least 1% of GDP annually if the debt is > 90% of GDP and at least 0.5% of GDP annually if the debt is < 90% of GDP.

The most stringent criterion, which requires the most significant fiscal adjustment, is decisive for a Member State's expenditure path.

Table 6: Safeguards for the reference path

Type of reference path	Ex ante deficit safeguard	Structural balance adjustment	Ex ante debt safeguard
deficit > 3% of GDP and debt > 60% of GDP	x	x	x
deficit < 3% of GDP and debt > 60% of GDP			x
deficit > 3% of GDP and debt < 60% of GDP	x	x	

The Member State must then submit a medium-term fiscal-structural plan. This includes a multi-year net expenditure path with relevant reforms and investments and their relationship to common EU priorities. In addition, the plan reflects the implications for already implemented reforms and investments, information about key budgetary and macroeconomic assumptions and, if applicable, a relevant set of reforms and investments for an extension of the adjustment period. The plan must also include the reference path provided by the Commission. If the expenditure path is less ambitious than the reference path provided by the Commission, it must be data-driven and justified with economic arguments.

Before submitting the plan, the Member State engages in a technical dialogue with the Commission to ensure that the plan complies with the requirements of the regulation. After the Member State submits the plan, the Commission assesses

²² The technical information prepared by the European Commission at the request of Member States if they do request technical information will be consistent with the deficit safeguard.

whether the plan meets all the requirements, namely whether the expenditure path meets the requirements of sufficient debt and/or deficit reduction. The macroeconomic and budgetary assumptions are also assessed if a Member State submits a plan with an expenditure path that is less ambitious than the reference path issued by the Commission.²³

Furthermore, the requirements for reforms and investments are reviewed. The Council, based on a recommendation from the Commission, then issues a recommendation on the Member State's expenditure path. If there is an extension of the adjustment period, the Council approves the investments and reforms underlying the extended adjustment period. If there are macroeconomic imbalances, identified in the macroeconomic imbalance procedure (MIP), there will also be recommendations to correct these imbalances.

If the requirement to ensure debt is on a plausible downward path and to bring the medium-term budget deficit below 3% of GDP is not met and, if applicable, the investments and reforms underlying the extension of the adjustment period are not sufficient, the Council must recommend that the Member State submit an adjusted plan. If a Member State does not meet the reference values and does not submit an adjusted plan in a timely manner (within one month, with a possible extension of one month) or if the adjusted plan is not satisfactory, the reference path issued by the Commission will serve as the expenditure path to which the Member State must adhere. If the requirements for extending the adjustment path are not met, the four-year time frame applies.

Progress and monitoring

During the years of the plan's implementation, all Member States must submit a progress report by April 30 of those years, providing information on the expenditure path and implementation of reforms and investments in the context of the European Semester and, if applicable, progress in the implementation of reforms and investments underlying the extension of the adjustment period.

As part of the European Semester Spring Package, the Commission subsequently monitors the implementation of the plan, proposed reforms and investments and numerically assesses whether a Member State is overshooting the expenditure path and/or the 3% deficit norm. Cumulative overspending and underspending of the expenditure path are recorded in the control account (see also the description of the corrective arm).

If the reference values of the corrective arm are exceeded, or the maximum allowable deviation from the control account for a Member State is exceeded,²⁴ the Commission can investigate whether it concerns an excessive deficit. If the

²³ In particular, estimates of government debt if policy remains unchanged must be comparable to the Commission's forecasts.

²⁴ Member States with a debt above 60% of GDP are allowed to deviate from their expenditure path by up to 0.3% of GDP annually and up to 0.6% of GDP added up over several years.

Council, on the recommendation of the Commission, finds that there is an excessive deficit in the Member State, the latter must include a corrective expenditure path in the medium-term fiscal-structural plan.

In the case of a newly appointed government, a Member State may submit a revised plan for a new four or five-year period, depending on its government's usual term of office. The new plan must not delay the fiscal adjustment effort, if there is a reference path, and should not result in reduced efforts to achieve the fiscal adjustment.

The involvement of supervisory bodies and parliaments in the preventive arm

When a Member State submits the medium-term fiscal-structural plan, it may request an opinion from the national independent fiscal institution on the macroeconomic forecasts and assumptions underlying the expenditure path. This will become mandatory in 2032, provided the independent fiscal institutions have built up sufficient capacity to accomplish this task (see also Directive reform below).

Moreover, the Member State may ask the national independent fiscal institution to assess compliance with the expenditure path as reported in the annual progress report. Where appropriate, the Member State may request the independent fiscal institution analyse the factors underlying a deviation from the net expenditure path. This analysis is non-binding and complements the analysis provided by the Commission.

Each Member State must consult civil society organisations, social partners, regional authorities and other relevant national stakeholders prior to submitting its plan, in accordance with the national legal framework. In addition, each Member State can discuss its plan, in accordance with the national legal framework, in the national parliament. The annual progress report can also be discussed in the national parliament and with civil society, social partners and relevant stakeholders.

The advisory role of a permanent and more independent European Fiscal Board (EFB) in the European budgetary framework must be enhanced. The EFB must continue to review the implementation of the SGP and the future Euro area-wide fiscal stance and advise the Commission and the Council on the implementation of the SGP, including the extension of escape clauses. The EFB must work closely with national independent fiscal institutions. The independence of and access to information by the EFB needs to be increased.

The Commission should involve the European Parliament in the European Semester in a regular and structured manner. Accordingly, the Commission transmits to the European Parliament the national medium-term fiscal-structural plans submitted by Member States and its assessment of the plans. The relevant European Parliament committee may ask the Commission to present the assessment. Moreover, the presidents of the Council, the Commission and the Eurogroup should inform the

European Parliament about annual multilateral surveillance. They may also be invited to discuss the conclusions of multilateral surveillance with the European Parliament.

Reform of the Directive

Directive 2011/85/EU stipulates rules for Member States' budgetary frameworks and budgetary surveillance. The directive includes standards on accounting, statistics and forecasts. Each Member State should also have country-specific numerical fiscal rules, which promote compliance with European fiscal rules, especially with regard to the deficit rule and debt criterion. The directive also requires the establishment of national independent fiscal institutions, which monitor compliance with country-specific numerical fiscal rules.

Its reform aims to strengthen fiscal monitoring and enforcement procedures that promote sound and sustainable public finances and sustainable and inclusive growth. Independent fiscal institutions are considered an important link to achieve this. Moreover, independent fiscal institutions can help boost national ownership of European fiscal rules.

In the reform, the rules for independent fiscal institutions in Euro area Member States, such as the Netherlands, remained virtually unchanged because they were already part of the Two Pack, which only applies to Euro area Member States (see Box 1). The changes are more far-reaching for non-Euro area Member States, because in the original 2011/85/EU directive, they were only tasked with monitoring compliance with fiscal rules.

Under the amended directive, fiscal institutions are tasked with monitoring compliance with (national and European) fiscal rules; producing, assessing or endorsing multi-year macroeconomic and budgetary forecasts; and assessing the consistency, coherence and effectiveness of the national budgetary framework. By invitation, independent fiscal institutions can also participate in briefings and debates in national parliaments. The independent fiscal institutions must assess the Member State based on the tasks outlined above. The comply-or-explain principle applies to Member States: within two months of publication by the independent fiscal institution, the Member State must publicly report on how it will comply with the recommendations, or justify why it will not.

Furthermore, the amended directive outlines standards for independent fiscal institutions. These include adequate and stable funding, adequate access to information, guarantees of independence and the possibility for the independent fiscal institutions to publicly communicate their reports in a timely manner. By 31 December 2025 at the latest, the Commission will report on, among other things, progress on the capacities and tasks of independent fiscal institutions, with the prospect of exploring minimum standards for independent fiscal institutions.

The reformed directive also addresses fiscal risks posed by climate change. Understanding the potential channels through which climate-related shocks affect

public finances is considered critical for national strategies to mitigate and manage fiscal risks posed by climate change. This focus on identifying fiscal risks posed by climate change is consistent with the Advisory Division's opinion on the 2024 Budget Memorandum to develop a climate-inclusive budgetary framework.²⁵

In their national medium-term budgetary frameworks Member States must include procedures for assessing whether proposed policies affect the medium and long-term sustainability of public finances and promote sustainable and inclusive growth. Insofar as possible, this assessment should take into account fiscal risks posed by climate change and the impact of climate change on the environment and distribution of the burden. Member States must also devote attention to contingent liabilities, if possible also related to the climate. Relevant information on contingent liabilities with a potentially major impact on the government budget must also be published for all government subsectors. Insofar as possible, this must include climate-related contingent liabilities. Costs to the government budget arising from climate shocks should also be considered to the extent possible.

Process

In February 2024, a trilogue agreement was reached between the Council, the European Parliament and the European Commission on the modified legal texts in the Regulations and the Directive. The legislative package of the reform of the European budgetary framework (Regulation 1466/97, Regulation 1467/97 and Directive 2011/85/EU) is currently being formally submitted to the European Parliament and the Council. The European Parliament is expected to vote in April and the legislative package will be submitted to the Council for approval in April or May. The legislative package appears to benefit from sufficient support: the necessary majority or unanimity in the Council is expected to be achieved.²⁶ Once approved, the rules will be officially adopted and published, after which they enter into force, and Member States and the European Commission can start preparing to compile the national medium-term fiscal-structural plans.²⁷

Since the new budgetary framework is expected to enter into force in May, the old framework formally applies until then. After it enters into force, the Commission will provide Member States with a reference path or, upon request, technical information for the purpose of compiling the fiscal-structural plan by June 21 this year. Member States must then submit their first medium-term fiscal-structural plan by 20 September 2024.

²⁵ Opinion on the 2024 Draft Budget Memorandum and 2023 September Report on Budgetary Monitoring, Parliamentary Documents II, 2023/24, 36410, No. 4.

²⁶ Parliamentary Documents II 2023/24, 21501-07, No. 2004.

²⁷ The amendment to Regulation 1467/97 formally enters into force on the day it is published in the Official Journal of the European Union, the amendment to Regulation 1466/97 (probably) 20 days after publication.

Implications of the reform of the European budgetary framework for the Netherlands

The national medium-term fiscal-structural plans are the cornerstone of the new budgetary framework. The Netherlands will also have to submit a budget plan that satisfies the requirements of the amended regulations. Because the Netherlands meets ex ante reference values of the corrective arm, the Commission will not provide the Netherlands with a reference path. However, the Netherlands can receive technical information for compiling the expenditure path upon request. Before submitting the plan, a technical dialogue is held with the Commission to ensure that the plan complies with the requirements.

The deadline for submitting the first medium-term fiscal-structural plan (20 September 2024) may coincide with the Budget Memorandum process (publication on 17 September 2024). In line with the requirements of the preventive arm, the Dutch Ministry of Finance will have to reflect on how to structure the process, including possible involvement of the independent fiscal institutions and parliament.

Each Member State must interpret the directive according to its national context. The amended Directive 2011/85/EU must be implemented by 31 December 2025. In addition, the government will have to determine the extent to which the amended regulations involving the preventive and corrective arm will lead to amendments in Dutch legislation. In the Netherlands, the main elements of fiscal policy to be pursued are legally enshrined in the Sustainable Public Finances Act (Wet Houdbare Overheidsfinanciën, 'Wet HOF'). Therefore, the expectation is that a review of the Sustainable Public Finances Act will be prepared.

The Dutch budgetary process will also change with the submission of the fiscal-structural plans. This will take place against the backdrop of the national budgetary process already under development. For example, in the budgetary process greater emphasis has been placed on the spring and the national budgetary process will be aligned more effectively with the European Semester. To further endorse this development, this year, for the first time, the spring decision-making is integrated into the Stability Programme the Netherlands submits to the European Commission, and the CPB is calculating the main elements of the spring decisions and interpreting them in relation to the budgetary rules (see also Section B.3.1).

Currently, the Stability Programme fulfils the role of a Member State's multi-year budget in the European Semester. The Stability Programme contains the key basic principles for a Member State's budget and provides information on the development and sustainability of public finances. Together with the Stability Programme, each Member State submits a Reform Programme that addresses the progress and implementation of planned reforms and investments in response to the country-specific recommendations of the previous year in the context of the European Semester.

The reform of the European budgetary framework means that the Stability and Reform Programmes will expire. The fiscal-structural plan will become the multi-year budget in the context of the European Semester and must be submitted every four to seven years. The plan must address both the development and sustainability of public finances and the progress of included reforms and investments. Every year, the Member State must submit a progress report monitoring the progress of the submitted plan. The progress report is subject to the same time frame as the current Stability and Reform Programmes, namely, submission by 30 April.

The reform of the European budgetary framework also has implications for budgetary surveillance. Thus, both the CPB's forecast and the Council of State's assessment of compliance with European fiscal rules will have to relate to the new budgetary framework. This includes extending the period of the multi-year forecasts to 14 to 17 years, mimicking the different scenarios in the Commission's debt sustainability analyses and calculating and assessing the expenditure path in the preventive arm.

Moreover, the role of budgetary surveillance is likely to be different with the submission of periodic fiscal-structural plans and annual progress reports. The regulations and directive do not include specific requirements related to the involvement of budgetary monitoring institutes prior to submitting a fiscal-structural plan.²⁸ However, in the Dutch context, the role of budgetary monitoring is anchored in the budgetary process and partly anchored in law in the Sustainable Public Finances Act. Therefore, in the coming period, the Ministry of Finance will have to consider how the independent fiscal institutions will be involved in the budgetary process.

In addition to the Advisory Division and the surveillance bodies, other parties also have a potential role in the compilation of the fiscal-structural plan (see the involvement of surveillance bodies and parliaments in the preventive arm). A basic principle in the reform of the budgetary framework involves boosting national ownership by Member States. The plan must specify how the consultation process evolved along with the relevant stakeholders.

It is also necessary to consider how the new European budgetary framework relates to Dutch fiscal rules. In the Netherlands, successive governments have pursued trend-based fiscal policy since 1994. This means that on the expenditure side, multi-year expenditure frameworks are established with an annual expenditure ceiling that may not be exceeded. On the revenue side, there is a revenue framework with a margin for automatic stabilisation that seeks to avoid pro-cyclical fiscal policy. In principle, the expenditure ceiling and revenue

²⁸ One exception is the provision in the preventive arm that a Member State may request an opinion from the national independent fiscal institution on the macroeconomic forecasts and assumptions underlying the expenditure path. This will become mandatory in 2032, provided the independent fiscal institutions have built up sufficient capacity to accomplish this task.

framework are not adjusted during the government term, which means that the frameworks set de facto policy-based upper limits for public finances.

The operational indicator of the new European budgetary framework, nationally financed net primary expenditure, also strives for stabilising fiscal policy. The indicator adjusts for interest expenditure, cyclical unemployment expenditure, and any measures that provide higher revenues. By adjusting this expenditure it is possible to steer in terms of expenditure Member States can actually influence, and provide a margin for spending to move in conjunction with the economic cycle. The outcomes are subsequently translated into an annual nominal expenditure path. The system thus corresponds to the Dutch annual expenditure ceiling, which is expressed in real terms.

3. Assessment under European fiscal rules

3.1 *Relevant context*

In the 2024 Spring Report, the Advisory Division assesses public finances in the previous year (*ex post*), in the current year (*in year*) and in the year ahead (*ex ante*). This year's assessment takes place against the backdrop of the general escape clause's deactivation and the outcome of the SGP reform. This section discusses the relevant context and explains what is assessed and in which year in this Spring Report.

In 2020, the European Commission activated the SGP's general escape clause to allow Member States maximum flexibility within the SGP to make additional fiscal efforts in response to the Covid-19 crisis. Specifically, this means that Member States in the current preventive arm of the SGP, including the Netherlands, may deviate from the path towards the medium-term objective (MTO) for the structural balance, providing it does not jeopardise the sustainability of public finances in the medium term. The guidelines for the budgetary assessment for the years in which the general escape clause is active, are largely qualitative. However, the regular procedures of the SGP were not suspended.

As of 2024, flexibility within the SGP comes to an end, due to the deactivation of the general escape clause. At the same time, because of the ongoing uncertain economic situation and the reform of the European budgetary framework, the Commission did not deem it appropriate to revert in full to the fiscal rules of the current framework before 2024.²⁹ Moreover, a trilogue agreement was reached in February 2024 between the European Parliament, the Council and the European Commission on the reform of the European budgetary framework (see Section B2). This means 2024 is a transition year before the intended entry into force of the new budgetary framework in mid-2024.

²⁹ European Commission (2023). Communication on fiscal policy guidance for 2024, COM(2023) 141 final.

The reform of the European budgetary framework means that the 2024 Stability Programme will be the last Stability Programme. In the new framework, the medium-term fiscal-structural plan will be the new multi-year budget (see Section B2). Because Member States must submit their first medium-term fiscal-structural plan in September 2024, the European Commission has reduced the reporting requirements of Stability Programmes submitted in 2024 compared to previous years. The reporting requirements approximate those in place during the Covid-19 crisis. The Stability Programme can thus be limited to the economic outlook and development of public finances, with some quantitative and qualitative information on the expected development of government debt and the deficit and the budgetary impact of the proposed policies presented in the Stability Programme.³⁰

Although formally the current rules of the European budgetary framework still apply, the Commission has announced that in the transition year 2024, it will no longer perform an assessment in relation to the rules of the old preventive arm, as they will be dropped in the reformed framework. Moreover, the new budgetary framework is expected to enter into force in mid-2024 and Member States will have to submit their first medium-term fiscal-structural plans based on the new fiscal rules in the autumn of 2024.³¹

In anticipation of the new budgetary framework, in their Stability Programme Member States are asked to justify how the budget deficit will remain below, or move towards, the 3% deficit rule and the 60% debt criterion in the medium term.³² Furthermore, the fiscal policies of Member States must strive to ensure debt sustainability in the medium term and to increase potential growth in a sustainable manner.

Prudent fiscal policy, consisting of gradual fiscal consolidation and, where appropriate, targeted measures to support the most vulnerable households and businesses against rising energy prices, can thus contribute to the stability of the European economy and facilitate the effects of monetary policy during a period of high inflation. For the Reform Programmes, the Commission asks Member States to step up reforms and investments that contribute to fiscal sustainability and sustainable and inclusive growth.

In 2023, Member States were called upon to adopt a broadly neutral (taken as an average for the entire Euro area) fiscal policy, i.e. neither debt-increasing (expansionary) nor debt-reducing (consolidating). At the same time, Member States were called on to boost nationally funded public investment, phase out

³⁰ European Commission (2020). Guidelines for a streamlined format of the 2020 Stability and Convergence Programmes in light of the COVID-19 outbreak. 2020.

³¹ Parliamentary Documents II 2023/24, 21501-07, No. 2004.

³² European Commission (2023). Communication on fiscal policy guidance for 2024, COM(2023) 141 final.

public debt, and work towards sustainable growth through reforms and investment.³³

Furthermore, the Council's country-specific recommendations from 2023 are relevant to the Netherlands. The Netherlands was advised to phase out temporary energy support measures in 2024 and use the related savings to reduce the budget deficit. It was also advised to retain public investment and effectively use the grants from the Recovery and Resilience Facility, especially to promote the green and digital transition. Lastly, the Netherlands was recommended to pursue fiscal policies beyond 2024 that focus on prudent public finances in the medium term, combined with investments and reforms that contribute to sustainable economic growth.³⁴

Despite this being a transition year, the Commission announced that it is going to recommend to the Council that excessive deficit procedures be opened in spring 2024 based on an overshoot of the 3% reference value. This is because the 3% reference values remain relevant in the new budgetary framework. Excessive deficit procedures will be opened in 2024 on the basis of budgetary achievements in 2023 and expectations in the European Commission's spring forecast.

3.2 *Assessment under the rules of the corrective arm*

The rules of the corrective arm set requirements for the (annual) reference values for the budget deficit (EMU balance of no more than 3% of GDP) and government debt (EMU debt of a maximum of 60% of GDP). Based on the budgetary analysis of the 2024 Spring Memorandum by the CPB, it appears that the Netherlands meets the requirements of the corrective arm both in 2023, and is expected to do so in 2024 and 2025 (see Table 7).

³³ European Commission (2022). Communication on fiscal policy guidance for 2023. COM(2022) 85 final.

³⁴ European Commission (2023). Recommendation for a Council Recommendation on the 2023 National Reform Programme of the Netherlands and delivering a Council opinion on the 2023 Stability Programme of the Netherlands. COM(2023) 141 final.

Table 7: Figures for the corrective arm 2023-2025

	2023	2024	2025
	<i>ex post</i>	<i>in year</i>	<i>ex ante</i>
Deficit criterion (% of GDP)			
<i>Maximum actual EMU balance</i>	-3.0	-3.0	-3.0
Actual EMU balance	-0.3	-2.0	-2.1
Debt criterion (% of GDP)			
<i>Maximum EMU debt</i>	60	60	60
EMU debt	46.5	46.8	48.1

Source: CPB, 2024 Spring Memorandum Budgetary Analysis (April 2024)

In spring 2024, the Commission will recommend the Council open excessive deficit procedures based on an overshoot of the 3% reference value in 2023.³⁵ With an EMU balance of -0.3% of GDP in 2023, the Netherlands maintains sufficient distance from this reference value and, based on the 2023 figures, no excessive deficit procedure will be opened for the Netherlands. Furthermore, in their 2024 Stability Programme Member States are asked to justify how the budget deficit will remain below the 3% deficit rule and the 60% debt criterion in the medium term, or move sufficiently fast enough towards it.

2024 is a transition year from the old to the new European budgetary framework. Reference values of the corrective arm also play a key role in the new framework. Indeed, an overshoot of the 3% reference value and/or an overshoot of the expenditure path, which takes into account the distance from the reference values of the corrective arm, may constitute grounds for opening an excessive deficit procedure and imposing a corrective expenditure path (see Section B2).

3.3 *Possible budgetary implications of the new preventive arm*

In 2024, the European Commission will no longer perform an assessment in relation to the rules of the old preventive arm, as they will be dropped in the revised framework (see also Section B3.1). The Commission asks Member States to provide justification in their Stability Programme of how the budget deficit will remain below the 3% deficit rule and the 60% debt criterion in the medium term, or move sufficiently fast towards it. The Commission recommended that the Netherlands pursue fiscal policies beyond 2024 that focus on prudent public finances in the medium term.³⁶

Following the formal entry into force of the new European budgetary rules, Member States must submit a medium-term fiscal-structural plan by 20

³⁵ European Commission (2023). Communication on fiscal policy guidance for 2024, COM(2023) 141 final.

³⁶ European Commission (2023). Recommendation for a Council Recommendation on the 2023 National Reform Programme of the Netherlands and delivering a Council opinion on the 2023 Stability Programme of the Netherlands. COM(2023) 141 final.

September 2024. Since the submission of this plan coincides with the 2025 Budget Memorandum process, the Advisory Division considers it important to look ahead in this budgetary report at the potential budgetary implications of the new rules of the preventive arm.

As part of the medium-term fiscal-structural plan, Member States must include a medium-term expenditure path. The expenditure path, which prescribes maximum annual growth of net primary expenditure, will be derived from the structural primary balance. The structural primary balance is the structural balance, that is, the budget balance adjusted for temporary measures and cyclical effects, adjusted for interest rates (see also Box 2 in Section B.2).

In the rule for the structural primary balance, the Commission recalculates the structural primary budget balance needed at the end of the adjustment period of four, or seven years in the case of an extension, to bring or keep government debt on a credible declining path or at prudent levels below 60% of GDP in the medium term, and to bring or keep the budget deficit below 3% of GDP in the medium term.

The basic principle in this regard is that costs related to the ageing population in the years thereafter can also be adequately absorbed without additional policies. In addition, the fiscal adjustment must be linear and at least proportional during the adjustment period. Thus, the new framework adopts a country-specific approach: the worse the initial budgetary position and medium-term forecasts, the more stringent the expenditure path.

In June 2024, the Commission will issue Member States with a reference path if they have a deficit above 3% of GDP and/or debt of (more than) 60% of GDP at that time. If Member States have a deficit below 3% of GDP and a debt below 60% of GDP, they will have the opportunity to request technical information about the expenditure path. The reference paths and technical information will be based on figures from the Commission's spring forecast, which is published in May or June 2024. These figures determine the difference between the expected and target structural primary balance, and thus also the budgetary task for a Member State to meet the regulation's requirements for the expenditure path.

The expenditure path submitted by the Netherlands, as part of the medium-term fiscal-structural plan, will have to meet the conditions described in Section B2. If the Netherlands submits a plan that does not comply with the expenditure path requirements, the Council cannot impose an alternative expenditure path as long as the budget deficit is below 3% of GDP and debt is below 60% of GDP.

Since the Commission's spring forecast, which serves as the basis for assessing expenditure paths in Member States' medium-term fiscal-structural plans, will not be published until May or June 2024, at the moment it is only possible to provide a preliminary estimate of the fiscal efforts resulting from an expenditure path that complies with the conditions of the new preventive arm. The Commission shared

updated, preliminary indicative calculations of expenditure paths with Member States a few weeks ago.

In answering parliamentary questions, the Ministry of Finance shared the information that, based on the Commission's preliminary calculations, the Netherlands needs to move toward a target structural primary budget balance of 0.3% of GDP in 2028 (without an extension of the adjustment period) or 0.2% of GDP in 2031 (with an extension).³⁷ Based on the recent CEP forecast and the calculation of the Spring Memorandum, both by the CPB, Table 8 shows an indicative calculation for the structural primary balance in 2028. An update of the table will only be possible in May or June, based on the Commission's forecast, in which the target for the structural balance for the Netherlands in 2028 will also be adjusted.

Table 8: Indicative calculations for the structural primary balance

		As a percentage of GDP
A	Preliminary Commission calculation of the target for the structural primary balance for the Netherlands in 2028	0.3%
B	Structural balance in 2028 based on the CPB's Spring Memorandum calculation	-2.6%
C	Forecast of the Netherlands' interest expenditure in 2028 based on the CPB's CEP forecast	1.0%
D	Indicative structural primary balance in 2028 (B + C)	-1.6%
E	Indication of the extent of possible readjustments in 2028 (A-D)	-1.9%

Based on the indicative calculation of the structural primary balance resulting from the new European fiscal rules, if the Netherlands submits a plan that complies with the Commission's requirements for the deficit and debt in the medium term, it should achieve a fiscal adjustment that amounts to an improvement in the structural primary balance of 1.9% of GDP by 2028. No recent figures are available for an indicative calculation of the seven-year adjustment period.

The purpose of the preventive arm, in both the old and the new framework, is to prevent Member States from facing excessive deficits by maintaining a safe margin from the maximum budget deficit of 3% of GDP, so that Member States have a budgetary margin to pursue stabilising fiscal policy. The new framework also takes into account the distance from the 60% of GDP reference value. Moreover, this framework focuses more on the medium-term sustainability of public finances, as the fiscal adjustment should ensure that government finances remain on or reach a prudent path in a ten-year period following the adjustment period.

³⁷ Parliamentary Documents II 2023/24. No. 1448

If the Netherlands compiles a plan in line with the medium-term deficit and debt requirements of the new framework, it may require substantial fiscal efforts, to be achieved over a period of four, at most seven years.

4. Assessment under national fiscal rules

4.1 *Budgetary process*

During this government term, greater emphasis has been placed on the spring in the budgetary process. On the advice of the 16th Study Group on Fiscal Policy, since the 2022 Spring Memorandum, the government has aimed to not only decide on the main points of the expenditure side of the budget for the following year, but also those on the revenue side.³⁸ In response to the Advisory Division's advice on the 2022 Budget Memorandum,³⁹ the government decided to adjust the budgetary process, with the aim of giving parliament more time to reflect on the budget and the Tax Plan and to align it more effectively with the European Semester.⁴⁰

By opting for a single integral decision-making moment in the spring for the main points of both the expenditure and revenue side of the budget, various political aspirations, issues, windfalls and setbacks can be weighed up in an integral manner. This creates stability and calm in the political decision-making process, because integral considerations of different policy objectives can be performed at fixed times. It optimises adherence to the basic principles of Dutch fiscal policy, namely the efficient allocation of public resources, managing public finances and contributing to economic stability. Decision-making in August can then be limited to necessary adjustments and any additional purchasing power measures based on the latest insights.

In the past, the main decision-making moment, which focused solely on the expenditure side of the budget in the spring, was considered an internal cabinet meeting. This meant that parliament only obtained an insight into the budgetary decision-making process for subsequent fiscal years on Budget Day. Since the review of the budgetary process in 2022, the Spring Memorandum not only addresses budgetary changes in the current year in relation to the Budget Memorandum, but also includes the main points of the decisions related to the budget of the following year and outlines a multi-year scenario of expenditure as

³⁸ Parliamentary Documents II 2022/23, 36200, No. 6.

³⁹ Parliamentary Documents II 2021/22, 35925, No. 3. In its opinion on the 2022 Budget Memorandum, the Advisory Division provided recommendations to parliament for reinforcing its rights associated with the budget. The Advisory Division proposed, among other things, that from now on, the Budget Memorandum be submitted in the spring, so that the Dutch budgetary process is aligned more effectively with the European Semester, and the House of Representatives and the Senate are better placed to act in a more timely manner.

⁴⁰ Parliamentary Documents II 2021/22, Letter to Parliament on the Budgetary Process, April 2022.

well as the main points associated with revenue.⁴¹ As a result, parliament is involved earlier in multi-year budgetary decision-making, allowing it to exercise its parliamentary rights associated with the budget more effectively.

A multi-year budget must be submitted to the European Commission in the spring as part of the European Semester (the European budgetary process). Currently, this is the Stability Programme, which must be submitted annually by 30 April. In the new European budgetary framework, a multi-year plan will have to be submitted every four to seven years, with an annual progress report that follows the same time frame as the current Stability Programme (for more details, see Section B2). The deadline for submitting the Spring Memorandum is 1 June, which means the annual multi-year budgets in the context of the European Semester have until now, not contained the latest budgetary decisions. Consequently, the Stability Programmes were already obsolete when published.

Since the 2022 review of the budgetary process, the Advisory Division has expressed its appreciation for the changes already made by the government. At the same time, the Advisory Division has noted several times that the adjustments to the Spring Memorandum are a good step towards a new budgetary process, but that the process is not yet complete.⁴² For example, in both 2022 and 2023, there was no main decision-making moment and thus integral decision-making in the spring, because part of the budgetary decision-making process was postponed to the Budget Memorandum.

Moreover, not all budget documents, such as the supplementary budgets, the contents of the Tax Plan Package and the Advisory Division's independent budgetary advice, were sent to the House of Representatives at the same time as the Spring Memorandum, which meant the House of Representatives did not have a complete overview. Also, in both years, the Spring Memorandum was not aligned with the European Semester. In 2023, the government noted in a review on the budgetary process that there are starting points for improvement with regard to the development of the budgetary process.⁴³

Moreover, in the 2023 Spring Report the Advisory Division noted that, in addition to the opinion on the 2022 Budget Memorandum, one possible solution for creating greater clarity, predictability and calm in the spring budgetary process is to opt for a fixed moment for halting decision-making and a fixed moment for publishing the Spring Memorandum. This creates clarity for all parties involved, which will benefit the preparation of and debate on the Spring Memorandum. Such moments already exist in the August decision-making process. Furthermore, the Advisory Division recommended that the spring decisions be calculated by the CPB so that an independent calculation of the budgetary consequences of the

⁴¹ Parliamentary Documents II 2022/23, 36200, No. 6.

⁴² 2022 June Report, Parliamentary Documents II 36120, No. 3 W06.22.0084/111/B. p.m. reference Spring Report and September Report 2023

⁴³ Parliamentary Documents II 2022/23, 36120, No. C.

spring decisions is available for the budgetary assessment in the spring and for the purpose of parliamentary debate.

With the 2024 Spring Memorandum, the government has taken new steps towards an integral, orderly and transparent spring decision-making process. The introduction of a fixed moment for halting decision-making for the Spring Memorandum brings calm to the process. It also provided the opportunity for the CPB to perform a calculation of the spring decisions, after which, for the purpose of this Spring Report, the Advisory Division was able, for the first time, to assess compliance with national and European fiscal rules based on an independent calculation by the CPB. In addition, this year the national budgetary process has been brought forward enough to align it with the European Semester, so that the 2024 Stability Programme will contain the most recent budgetary information.

This year, at the last minute, the publication date of the Spring Memorandum was brought forward by more than a week to 15 April. The new government's informateurs asked the current government to share a draft of the spring decisions. In response, the cabinet decided to share the Spring Memorandum early with both the informateurs and the government. Thus, the Spring Memorandum was published earlier than the Stability Programme, the CPB's calculation and the Advisory Division's opinion. In a letter accompanying the Spring Memorandum, the government expressed its ambition to aim to provide the documents at the same time in the future.⁴⁴

With these new steps the government has laid a solid foundation for a new, improved budgetary process. Early decision-making allows for transparent and comprehensive political consideration of the use of resources and gives implementing organisations more time to prepare for policy changes and new policies. Moreover, citizens and businesses find out about the focus of government policy earlier on in the year. The Advisory Division recommends the incoming government, in association with parliament, continue on this path.

4.2 *Assessment under national fiscal rules*

National fiscal rules

In the Initial Policy Memorandum to the Coalition Agreement the government established the fiscal rules for the upcoming government term and confirmed that it would pursue trend-based fiscal policy. On the expenditure side, four multi-year expenditure frameworks (State Budget, Social Security, Healthcare and the new Investment Framework) were established, each with an annual expenditure ceiling that may not be exceeded.⁴⁵ However, the individual expenditure frameworks are indexed annually in relation to wage and price development.

⁴⁴ Accompanying letter to Parliamentary Documents II 2023/24, 36550, No. 1.

⁴⁵ For investments covered by the relevant expenditure ceiling, control of the total amount is more relevant than the amount per year and shifts over time are allowed, provided European fiscal rules allow for it.

A revenue framework applies on the revenue side with automatic stabilisation: revenue windfalls benefit the government balance, revenue shortfalls burden the government balance. In this way, revenue moves in conjunction, as it were, with the business cycle. In principle, the expenditure ceiling and revenue framework are not adjusted during the government term, which means that the frameworks set de facto policy-based upper limits for public finances.

In the frameworks revenue and expenditure are separate. This means that windfalls on the revenue side may not be used for additional expenditure, but also that revenue setbacks do not have to be offset by cuts on the expenditure side. Moreover, setbacks on the expenditure side must be compensated in the expenditure framework and must not lead to new measures on the revenue side. This provides maximum scope for automatic stabilisation and avoids pro-cyclical fiscal policy.

Basic principles

The current government's Initial Policy Memorandum set the expenditure ceilings and revenue framework ex ante for this government term. They were finalised in the 2022 Spring Memorandum, partly after incorporating the CPB's macroeconomic outlooks. In the same Spring Memorandum the government stated that the established revenue and expenditure frameworks thus serve as an anchor for this government term's budgetary policy. The purpose of enforcing national fiscal rules is to ensure that public finances remain within the limits of what the government deems acceptable. The decision to establish the level of the revenue and expenditure budgetary frameworks at the beginning of a government term is also a political choice.

The 2024 Spring Memorandum contains a first update of the State Budget for 2024 and an outline of the main decisions related to revenue and expenditure for the coming years, namely up to and including 2028. In the Spring Memorandum, the government provides an update on expenditure trends with regard to the ceilings and on the revenue framework. This includes both new policies and changes due to shifts in expenditure over time (movements of funds), progressive insights and windfalls and setbacks. Adopting a single decision-making moment allows policy aspirations to be weighed up against each other and, along with the changes, to be integrated in the budgetary frameworks for revenue and expenditure.

In the Spring Memorandum the government states that it has opted for restraint with regard to new policies, but to act on a number of urgent cases, namely damage repair and reinforcement in Groningen, the benefits recovery operation, the reception of displaced Ukrainians and support to Ukraine. Additional attention has also been devoted to realistic forecasts, namely, establishing a more realistic cash flow for expenditure due to the high level of underspending (see also Section B1.2).

Outcomes of the spring decisions

On the expenditure side, the government has provided additional funds for damage repair and reinforcement in Groningen, for Ukraine and the benefits recovery operation. In addition, the government opted for investment in the Dutch semiconductor sector (microchip sector), largely from the National Growth Fund, and additional investment in defence.

The government also decided to bring forward the new financing system for local and regional authorities and scrap the increase in the scaling-up rebate in exchange for a limited indexation of funds in 2025. In addition to the decision-making process, budgets were adjusted based on the latest implementation-related information and government forecasts, including a higher asylum estimate, and budgeted funds were carried forward to later years if they were not expected to be spent this year (see Table 9).

Table 9: Movements of funds

+ is higher spending in billions of euros	2024	2025	2026	2027	2028
Movements of funds Defence	-2.1	-0.9	1.4	0.6	0.5
Movements of funds Infrastructure & Water Management	-1.3	-1.0	0.1	0.3	0.1
Movements of funds Climate Fund	-0.2	-0.7	1.1	-0.2	-0.5
Other movements of funds	-0.3	-2.5	0.7	0.6	0.3
Total movements of funds	-3.9	-5.1	3.3	1.3	0.4

Source: 2024 Spring Memorandum

On top of the €2 billion announced in the 2024 Budget Memorandum allocated for military support for Ukraine in 2024, in the Spring Memorandum the government decided to make an additional €4 billion available for Ukraine for the period 2024-2026, about three-quarters of which will go to military support. The military funds for Ukraine are in addition to the €5 billion structural investment in defence in the Coalition Agreement and the 2022 Spring Memorandum.

With a tense defence market, a tight labour market and the Defence Department's efforts to support Ukraine militarily, the pace of Defence's planned investments is under pressure. Therefore, in this Spring Memorandum, the government has decided to alter the pace of defence investment. This is a first step to position the structurally allocated funds on a more realistic growth path.

With recent defence investment, the NATO target of defence spending worth 2% of GDP, excluding Ukraine aid, will only be met in 2026 (see Table 10). The Advisory Division stresses the importance of investing in defence and meeting NATO's 2% of GDP target, given geopolitical developments. It remains important to closely monitor depletion and ensure investments are made at a realistic pace so that the 2% of GDP target can be effectively achieved.

Table 10: Projected medium-term defence expenditure

Expenditure as a % of GDP	2024	2025	2026	2027	2028	2029

Defence expenditure (excluding Ukraine)	1.84%	1.85%	2.00%	1.87%	1.85%	1.79%
Defence expenditure (including Ukraine)	2.16%	2.05%	2.22%	1.90%	1.90%	1.80%

Source: 2024 Spring Memorandum

In the 2023 Spring Memorandum, the government outlined the new financing system for local and regional authorities that will apply as of 2026. From then on, the accrual system will be abandoned and an additional €1.1 billion will be structurally available (of which €1 billion for municipalities and €0.1 billion for provinces). As of 2027, the municipal and provincial funds will be indexed based on changes in nominal GDP. This system is more closely linked to the broad expenditure development of local and regional authorities than the current accrual system. The development of the volume of funds will be based on a historical average of the development of GDP, which is expected to reduce the extent to which the funds fluctuate. Indexation for inflation follows that of the current year, keeping the funds level in real terms.

In the 2024 Spring Memorandum, the government has decided to scrap the increase in the scaling-up rebate and to implement the new financing system early in 2024, in line with the Advisory Division's advice in the 2024 September Report.⁴⁶ This affords municipalities and provinces greater clarity with regard to the development of the municipal and provincial funds. In exchange, municipalities and provinces will receive a limited indexation in 2025, cumulatively €837 million instead of €1.55 billion (a difference of €689 million), allowing the government to bridge a gap in the 2025 budget.

Additional agreements were also reached with the Association of Netherlands Municipalities (VNG) and the Association of the Provinces of the Netherlands (IPO). It has been agreed with the VNG that in the future (target 2026) part of the WMO (Social Support Act) will come from separate funding, so that a more realistic indexation of budgets can be applied. It has been agreed with the IPO that in the short term, research is needed to determine whether the new financing system for municipalities and provinces develops proportionately with the development of costs in the areas of public transport, infrastructure and nature, in order to safeguard the balance between ambition, tasks, resources and implementation capacity. A budget of €528 million has been set aside to compensate for the lower surcharges for provinces due to the 30% reduction in the motor vehicle tax rate for emission-free passenger cars announced in the Spring Memorandum. Finally, it was agreed that agreements be made on the reduction of specific payments before the summer so that local and regional authorities will have increased freedom of spending and a reduced burden in terms of accountability and control.

⁴⁶ In the 2024 September Report, as part of its independent budgetary monitoring, the Advisory Division recommended that the establishment of the new financing system for local and regional authorities be brought forward to when the new government took office. At that time, clarity should also be provided on the increase of the scaling-up rebate that has been scrapped up to and including 2025, but is budgeted at €675 million as of 2026.

On the tax side, in the 2024 Spring Memorandum, the government balanced the revenue framework, which means the budgetary changes of additional policy measures are zero. A loss has been incurred since the 2024 Budget Memorandum, mainly due to the Industry and Electricity Bill failing to pass and the retention of the netting arrangement as a result of votes in the Senate. The government decided not to provide substantive content for the coverage, but to include technical content. To this end, the government is increasing the higher brackets of the energy tax for measures in industry. To retain the netting arrangement, the starting point for the top rate of Box 1 income tax is subject to a lower increase than intended and the SME profit exemption is reduced. There will be a second point of consideration in the upcoming August decision-making process, when coverage may be replaced by another source.

The revenue framework also includes some purchasing power reparations from the 2024 Budget Memorandum, measures arising from this spring's climate decision-making (including a rate cut for motor vehicle tax for zero-emission passenger cars and a reduced rate for hydrogen in the energy tax), and measures with budgetary implications that may be included in the Tax Plan. In addition, there are regular revenue changes, including the budgetary impact of reviews and the effects of healthcare expenditure via premiums.

Table 11: 2024 spring decision-making summary

+ is higher expenditure/revenue in billions of euros	2024	2025	2026	2027	2028
Total expenditure trends on the ceilings	-4.0	-5.5	-1.0	-4.6	-7.1
Ukraine expenditure outside the ceiling	2.1	4.5	2.7	0.0	0.1
Decision-making related to tax and premium revenue	0.0	0.2	0.0	0.0	0.1

Source: 2024 Spring Memorandum

Assessment under national fiscal rules

The outcome of the spring decision-making process shows an annual undershoot of the expenditure framework and a balanced revenue framework (see Table 11). The undershoot of the expenditure framework in 2024 and 2025 is largely due to movements of funds resulting from underspending (see Table 9). Expenditure on Ukraine is not included in the regular expenditure framework. The 2023 Spring Memorandum stated that until the end of 2024, the government can make additional budget available from the general funds for international requests for support from Ukraine (the Ukraine Scheme). Any additional Ukrainian support follows the regular budgetary system, which the current government is leaving to a subsequent government. This ends the Ukraine Scheme from the 2023 Spring Memorandum.

With the spring decision-making of the main points of both revenue and expenditure and the balancing of the revenue framework, the government succeeded in organising the integral main decision-making moment in the spring,

cf. previous agreements (see also Section B4.1). However, another round of decision-making on both the expenditure and revenue sides of the budget cannot be ruled out in August, due to a new government possibly taking office and the potential budgetary implications of the new EU fiscal rules (see Section B2).

The separation of revenue and expenditure is not respected by the government in various areas in the Spring Memorandum. For example, the increase in the Statutory Minimum Wage (Wml) as of 1 July 2024, which leads to an increase in expenditure for a large number of schemes linked to the Wml, is covered on the revenue side. The additional increase in the maximum hourly rates of the childcare allowance from 2024 and the increase in child benefit are also covered on the revenue side. In addition, the €66 million increase in housing benefit from 2025 will be covered on the revenue side through an increase in the rate of the first bracket.

Budgetary decision-making is subject to the revenue and expenditure ceilings agreed upon by this government until a new government takes office. Due to the government's caretaker status, the CPB did not provide an overview and analysis of all the ceiling adjustments and framework corrections in this August decision-making process.

4.3 *Quality and transparency of public finances*

Quality

High-quality public finances are essential for the effective and efficient deployment of public resources. Article 3.1 of the Government Accounts Act (CW) requires an ex ante explanation of the proposals, intentions and commitments of the pursuit of the objectives, effectiveness and efficiency, the use of the policy instruments and the financial consequences for the State and, where possible, for the social sectors. In its budgetary reports the Advisory Division thus reflects on the rationale for the choices in the budget memoranda. This serves to support the House of Representatives and the Senate in exercising their rights associated with the budget.

The CW 3.1 requirements are part of the government-wide evaluation system, which provides information on the effectiveness and efficiency of policies. Central government has a comprehensive evaluation system at various stages of policy and legislation. This means relevant reports are available at various decision-making moments, such as when a new government is formed and for the Spring Memorandum and the Budget Memorandum, which can facilitate efficient and effective decisions.

In the 2023 Spring Report, the Advisory Division noted that the government was deploying unmotivated and unfocused expenditure cuts for coverage, while the government has at its disposal a large number of reports and studies with well-considered policy options and alternatives, which can help to arrive at integrally considered choices and priorities. For example, additional expenditure cuts were

made in the 2023 Spring Memorandum by withholding part of the funds for the wage and price adjustment, and windfalls and incidental underspending were used for coverage.

In the 2024 Spring Memorandum, the government redirects part of the wage and price adjustment to the Health, Welfare and Sport (VWS) budget for the benefit of the latter's budgetary outlook. However, using funds for the wage and price adjustment for other purposes is not without consequences. The wage adjustment consists of an allowance for contract wage development and the development of social employer contributions and the price adjustment consists of an allowance for price increases. Thus, wage and price setting is an indexation needed for the continuation of policy processes. The use of these resources for other purposes affects these processes and thus indirectly has a negative impact on social objectives.

In recent years, the budget balance has consistently been more positive than previously estimated, in part due to the historically high level of budget underspending (see also Section B1.2). This underspending prompted the government to examine forecasts within the budgets in this Spring Memorandum and, where necessary, to establish a more realistic cash flow for the budgeted funds. As a result, investments have been pushed back in the areas of Defence, Infrastructure and Water Management and the Climate Fund, among others.

In addition to investments, regular expenditure from 2024 and 2025 has been postponed for several years. In total, €5.1 billion in 2024 and €3.9 billion in 2025 have been carried forward several years by means of movements of funds. The government is unsure, despite the substantial movements of funds, whether it will succeed in spending the earmarked funds this year and in coming years. Therefore, the government will review whether the current expenditure forecast needs adjustment in the upcoming Budget Memorandum.

On top of the movements of funds, the budget for 2024 and 2025 already takes into account additional underspending of €3.6 billion in 2024 and €2.3 billion in 2025. In addition, this Spring Memorandum includes €4.9 billion as the revenue and expenditure target for both 2024 and 2025.⁴⁷ As a result, the government demonstrates that underspending amounting to a total of €8.5 billion in the 2024 budget and a total of €7.3 billion in the 2025 budget must be achieved in order to fully meet the additional underspending and the revenue and expenditure target. Because of these choices made by the government, the underspending that has been booked but is not achieved at the end of the year will lead to a deterioration

⁴⁷ The revenue and expenditure target is the annual accounting equivalent of the year-end margin. To prevent the expenditure ceiling from being exceeded by the annual payment of the year-end margin, an equally sized target, known as the revenue and expenditure target, is booked at the same time. This means that carrying the year-end margin forward does not provide additional funds in the year to which it is carried forward. The revenue and expenditure target has no concrete implementation, but must be covered by underspending as the year progresses.

in the EMU balance. These amounts are higher than the underspending amounting to €7.2 billion achieved in 2023.

If underspending occurs, the government assumes that funds will be spent in the medium term, unless a decision is made to reduce the budget. This puts the EMU balance under pressure in later years. On several occasions in recent years, the government has booked additional expected underspending in advance.⁴⁸ Consequently, the government is taking an advance on the underspending expected to occur during the course of the year. The funds can subsequently be used for other priorities. Should the underspend be lower, it will lead to an overshoot of the expenditure ceiling and a deterioration in the EMU balance.

In its opinion on the 2024 Draft Budget Memorandum, the Advisory Division stressed that using underspending for other priorities does not, on balance, create scope in the budget, as the policy objectives must be achieved at a later date. In the 2023 Spring Report, the Advisory Division recommended that if underspending is used for coverage purposes, this should be accompanied by a downward revision of policy objectives, since, on balance, underspending does not create scope in the budget.⁴⁹

The government did not book any additional underspending in the 2024 Spring Memorandum. In doing so, the government recognises that booking additional underspending is not preferable and that it is better to ensure a realistic spending rhythm in the budgets or position underspending in the budget with concrete measures. Together with the total amount of underspending booked, the budget assumes €13.6 billion of projected underspending in 2024 and €11.1 billion in 2025.

The Advisory Division deems it positive that in this Spring Memorandum, the government has taken a critical look at the forecasts in the budget and tried to establish a more realistic cash flow for the budgeted funds. A more realistic forecast increases the predictability of policies and the credibility of forecasts.

At the same time, in the 2024 Spring Memorandum, the government states that policy ambitions for 2024 remain intact, despite uncertainty about whether it will succeed in spending the earmarked funds this year and in the coming years. The Advisory Division believes it is important to continue to critically assess the impact of underspending on the timely achievement of policy objectives. The Advisory Division recommends that this be addressed in more detail in the individual budgets.

Transparency

⁴⁸ Additional underspending was included for the first time in the 2019 Budget Memorandum; since then, the instrument has been used five more times.

⁴⁹ 2023 Spring Report, Parliamentary Documents II 2022/23, 36350, No. B

Transparent fiscal policy serves a democratic interest by providing insight into the decisions taken. It helps parliament form an informed opinion on government policy and helps create public support for policy. This is why the Advisory Division reflects on the degree of transparency of fiscal policy in its budgetary reports.

The Advisory Division noted in the 2023 Spring Report that the government had taken steps to increase the transparency of budget documents. The government has followed previous advice issued by the Advisory Division to, for example, make the multi-year horizontal (year-on-year) development of expenditure and taxes transparent. This provides insight into the total development of expenditure and taxes, including the development that was already included in the baseline.

At the same time, the Advisory Division noted that further improvements could still be made. The 2023 Spring Memorandum contained a large number of changes presented in tables at the macro level. However, it lacked an integral overview of the total coverage-related challenge, intensifications and spending cuts, making decision-making difficult to follow and fathom.⁵⁰

In response to the 2023 Spring Report, the government took steps by providing insight into the changes in the 2023 Spring Report compared to the 2023 Budget Memorandum, when answering parliamentary questions on the Spring Report.⁵¹ In the 2024 Budget Memorandum, the government included a vertical overview per chapter of the budget, showing the changes that have occurred in the budget since the 2023 Spring Memorandum.

The Advisory Division notes that the government has taken significant steps in improving the transparency of budgetary information in the 2024 Spring Memorandum. This concerns both the presentation of decision-making and the explanation of various technical terms and of the decisions taken. For example, the 2024 Spring Memorandum contains summary tables showing the outcomes of decisions related to revenue and expenditure.

These tables not only show policy changes, but also provide insights into movements of funds, departmental windfalls and setbacks, and a series illustrating overall expenditure trends for the ceilings. Below these tables is a brief explanation for each series with policy clarification and references are provided to the main text or appendix where a more detailed clarification can be found. In the 2024 Spring Memorandum, the government continued the method of vertical overviews per chapter of the budget provided in the 2024 Budget Memorandum. The government also devotes attention to explaining the budgetary decisions and technical changes in the Spring Memorandum.

In the 2024 Spring Memorandum there is also a special focus on the forecasts used for the budget documents and decision-making process. Both the CPB and

⁵⁰ 2023 Spring Report, Parliamentary Documents II 2022/23, 36350, No. B

⁵¹ Parliamentary Documents II 2022/23, 36350, No. 2.

the government forecast the EMU balance and EMU debt. In recent years, the difference in the forecasts produced by the government and the CPB appeared to increase. In an explanatory paragraph, the government discusses its own forecast method and reason for the differences with the CPB; there are differences in both the macroeconomic assumptions used and the forecast method. For example, the CPB expects more underspending on the expenditure side than the government. On the revenue side, the government estimates higher revenues than the CPB until 2029. This difference is due to a difference in the tax revenue system.

The clear language, summary tables and vertical explanations provide insight into the overall multi-year development of revenue and expenditure in addition to the horizontal (year-on-year) development of expenditure and taxes. As a result, the government provides insight into the decisions taken. Illustrating the differences between the CPB forecast and the government forecast also increases the transparency of the budgetary information. The Advisory Division expresses its appreciation with regard to the significant steps the government has taken in improving the transparency of the budgetary information.

5. Recommendations for the budgetary policy of the incoming government

The incoming government will shape the budgetary policy to be implemented and formulate the budgetary anchors and fiscal rules during its term of office. To this end, developments in the economy and public finances in the medium and long term and the initial financial position are relevant, as well as recent insights and future developments with implications for public finances, including in the areas of defence, climate and the labour market.

Dutch budgetary policy aims to support the process of allocating financial resources to policy priorities and is founded on three basic principles.⁵² The first basic principle of Dutch budgetary policy is the efficient allocation of public resources. Since resources can only be spent once, public funds must be distributed as efficiently as possible between the different policy priorities. The second basic principle is the control of public finances. To avoid passing costs on to future generations, a government makes clear agreements at the beginning of a government term on what the maximum permitted expenditure is in one year (expenditure ceiling) and what the policy adjustments to taxes should be each year (revenue framework).

The third principle is macroeconomic stabilisation. Buffers are built up in favourable economic times to provide a budgetary margin in economic downturns and which means, in principle, no additional cuts are required. By pursuing trend-based fiscal policy, the revenue side of the budget basically moves in tandem with the economic cycle. The (non-cyclical) expenditure remains at the agreed level.

⁵² Ministry of Finance (2022). Fiscal Rules 2022-2025.

In order to implement fiscal policy during the upcoming government term in which the basic principles described above can be respected, and given the current economic and budgetary assumptions and recent insights and developments, the Advisory Division identifies the following areas of concern:

- I. *Pursue prudent budgetary policy and, when choosing a budgetary anchor, ensure there is sufficient budgetary margin so that the budget's automatic stabilisation function can do its job. This necessitates a medium-term budgetary task, taking into account the negative impact of spending cuts or tax increases on the economy and society.*

Since 1994, successive governments have opted for trend-based fiscal policy. Thus, fluctuations in revenue due to cyclical developments do not, in principle, lead to a policy adjustment. This creates automatic stabilisation in the budget system: the revenue side of the budget moves in tandem with the economic cycle so that trends in the economic cycle are automatically mitigated. In principle, the expenditure ceiling and the revenue framework will not be adjusted during the government term, which means that the frameworks set policy-based upper limits for public finances. If necessary, as during the Covid-19 crisis, discretionary policies can be implemented in addition to automatic stabilisation.

The incoming government will agree on a financial framework for its policy aspirations. The basic principle of this framework is to ensure that public finances remain within the limits of what the government deems acceptable. The decision to establish the level of the budgetary frameworks on the tax and expenditure side and a quantitative budgetary anchor at the beginning of a government term is a political choice. However, when establishing the financial framework, two relevant points should be taken into account, namely the relationship with European fiscal rules and the initial budgetary position.

In the 2023 Spring Report, the Advisory Division noted that the government was sailing close to the wind with a medium-term budget deficit of around 3% of GDP, the agreed limit for the maximum budget deficit within the corrective arm of the Stability and Growth Pact.⁵³ In the new European fiscal rules, politically agreed upon and expected to enter into force in May 2024, the operational indicator for Member States, the expenditure rule, includes a buffer in relation to the rules of the corrective arm to allow trend-based fiscal policy to be implemented. Steering in terms of this indicator should ensure that the estimated government debt and the estimated budget deficit remain below the reference values of 60% of GDP and 3% of GDP, respectively, in the medium term (i.e., fourteen to seventeen years) based on different scenarios (see also Section B2). The new government will have to take this into account.

⁵³ 2023 Spring Report, Parliamentary Documents II 2022/23, 36350, No. B. Partly because of the high level of underspending, the budget deficit has been below 3% of GDP in recent years (see also Table 3 in Section B1.2).

In the short term, the budget deficit will not be an issue, partly due to the high level of underspending and temporary windfalls on the revenue side (see Section B1.2). This will provide a temporary improvement in public finances but no extra scope in the budget in structural terms. In the medium term, Dutch public finances will deteriorate, in part due to an increase in population ageing-sensitive expenditure on healthcare and the state pension, among other things. Costs related to climate change are also expected to increase in the coming decades.

The budget deficit exceeds 3% of GDP in most forecast years; between 2029 and 2032, the deficit increases to an average of 4.6% of GDP (see also Section B1.2). Therefore, the 17th Study Group on Fiscal Policy recommends a change in direction for the next government term, to reduce the annual budget deficit. The Study Group on Fiscal Policy recommends a structural task of about €17 billion from 2028, resulting from an adjustment to an annual EMU balance of about -2% of GDP and a structural balance of about -1.6% of GDP.⁵⁴ Consequently, the initial budgetary position facing the incoming government is not particularly bright: in order to comply with European fiscal rules and maintain a margin for implementing trend-based fiscal policy, public finances must be structurally improved compared with the current level. This budgetary margin can be achieved through both higher taxes and lower expenditure.

Lessons from previous periods involving a budgetary task are relevant in fulfilling this budgetary task. For example, between 2009 and 2014, the Netherlands was in the corrective arm of the European budgetary framework as it exceeded the 3% of GDP deficit norm, necessitating very drastic budgetary measures in a short period of time. The emphasis to address the budget deficit at the time was on controlling public finances through extensive ad hoc spending cuts. While public finances improved due to the drastic cuts, this was at the expense of the basic principles of macroeconomic stabilisation and efficient allocation on certain points.⁵⁵

Research by the CPB shows that between 2011 and 2014, pro-cyclical fiscal policy was pursued, through spending cuts in a worse economic period. While austerity during a downturn has harmful economic consequences and should be avoided as much as possible.⁵⁶ Accordingly, the 17th Study Group on Fiscal Policy argues that when cutting certain areas of public expenditure, it is important that the extent of the cuts is right to avoid unnecessary economic and social damage in the short term and in the future. Short-term cuts must account for costs now and in the longer term.

⁵⁴ 17th Study Group on Fiscal Policy. (2023) Bijsturen met het oog op de toekomst. (Adjusting for the future.)

⁵⁵ 15th Study Group on Fiscal Policy. (2016) Van saldosturing naar stabilisatie. (From balance control to stabilisation). Appendix to the Fiscal Policy Audit.

⁵⁶ CPB Netherlands Bureau for Economic Policy Analysis (2023). Cyclisch begrotingsbeleid (Cyclical fiscal policy). CPB - September 2023

Conducting trend-based fiscal policy with a budgetary anchor that allows for this serves a democratic and social interest. If an expenditure ceiling and a revenue framework is established for the entire government term, it creates insight into and certainty about the level of public expenditure and the tax burden, and interim adjustments through spending cuts or tax increases can be avoided.

Conversely, the economy and society benefit from stable budgetary policy in more favourable economic times. This can promote stable and predictable policies and implementation so that citizens and businesses, as well as local and regional authorities and implementing organisations, have relative certainty in the medium term. This is all the more important now that the implementation of important social challenges such as climate and housing is required by local and regional authorities and implementing organisations.⁵⁷

At the same time, the current initial budgetary position requires additional budgetary margin to be created. In doing so, it is important to take into account the economic and social effects of spending cuts and tax increases, to avoid a repetition of the negative effects of the round of cuts following the euro crisis (2011-2014).

- II. *Adopt an approach that focuses on broad prosperity when implementing fiscal policy and when elaborating the budgetary task. This promotes long-term thinking, which can facilitate efficient and effective decisions.*

The fiscal policy to be pursued and the fulfilment of the budgetary task require political decisions that not only focus on the short term, but also take the longer term into account. It is socially important to have policies that are effective, stable, predictable and feasible. With regard to the fiscal policy to be pursued, adopting an approach that integrates broad prosperity, rather than simply considering the economic consequences of policies, promotes long-term thinking.⁵⁸ Steering in terms of broad prosperity is more than steering in terms of one or a single indicator: the connection between dimensions of broad prosperity and the distribution between groups is important. Moreover, increasing broad prosperity, precisely because of the connection between social tasks, requires structural reforms and investment. Steering annually in terms of isolated indicators merely produces limited or temporary effects.

The feasibility of policy proposals should also be considered when taking political decisions with a longer-term view. This concerns budgetary feasibility, which includes a consideration of the policy instrument to be deployed, as well as feasibility in terms of implementation, taking into account the tightness of the labour market and nitrogen space, among other factors. Budgetary feasibility involves integral consideration of resource deployment, in which additional public

⁵⁷ Council of State (2023). Annual Report 2022.

⁵⁸ Netherlands Institute for Social Research (SCP) (2022). Reflection on the 2021-2025 coalition agreement from the citizen's perspective.

spending is not always the most efficient and effective approach. For example, pricing or standardisation may in some cases be a more effective incentive to achieve a specific policy objective. Feasibility in terms of implementation is important to ensure that social tasks are actually achieved.

If this is factored in, underspending is also expected to decrease. In the opinion on the 2023 Draft Budget Memorandum, the Advisory Division, following the lead of Drees sr., noted that “not everything is possible, and certainly not at the same time,” due to stalled implementing organisations and a long-term tight labour market. Prioritisation is inevitable when faced with a large number of social challenges in conjunction with major bottlenecks in implementation.⁵⁹

During the upcoming government term, it is important that fiscal policy can contribute to citizens’ confidence in the effective provision of public services and policy intentions. Unrealistic promises erode trust in the government. In view of the large number of interrelated and complex social challenges, in its opinion on the draft 2024 Budget Memorandum, the Advisory Division recommended that steps already taken in the field of broad prosperity be followed up by using the first Budget Memorandum of the incoming government for an Initial Policy Memorandum on Broad Prosperity, containing an analysis of the future Dutch economic, social, ecological and financial structure, linked to the objectives in the upcoming coalition agreement. This will allow integrally considered political priorities to be defined along with related objectives, which can then be monitored annually in budget documents.⁶⁰

III. *The quality of public finances is important for achieving societal goals. When justifying policy choices and elaborating budgetary tasks, consider not only the immediate consequence of the choices made, but also the consequences for the economy and society and the future impact of the proposal.*

High quality public finances are essential for the effective and efficient deployment of public resources. Therefore, the Advisory Division not only addresses the quantity of public finances in its budgetary reports, but also the quality. Several tools exist to evaluate policies ex ante, ex durante and ex post. For example, Interdepartmental Policy Reviews (IBOs) take place annually, examining alternatives to existing policies, and the Strategic Evaluation Agenda (SEA) ensures the continuous improvement of policy and implementation.⁶¹ Potential savings are periodically identified through reviews. Besides an extensive

⁵⁹ Opinion on the 2023 Draft Budget Memorandum and 22 September Report on Budgetary Monitoring, Parliamentary Documents II, 2022/23, 36200, No. 6.

⁶⁰ Opinion on the 2024 Draft Budget Memorandum and 2023 September Report on Budgetary Monitoring, Parliamentary Documents II, 2023/24, 36410, No. 4.

⁶¹ The SEA lists all planned policy audits by policy article once every four to seven years. The SEA also provides an overview of all other ex ante, ex durante and ex post studies of policy efficiency and effectiveness. This includes evaluations of grants and other instruments, agencies and autonomous administrative authorities (ZBOs).

evaluation system at various stages of policy and legislation, governments have at their disposal numerous (policy) opinions and reports from independent study groups, commissions, assessment agencies and advisory councils, among others.

Nonetheless, in the (recent) past, funding allocation has regularly been achieved using the 'cheese slicer method', by underspending or withholding funds for the wage and price adjustment.⁶² The use of such methods can be counterproductive, as they usually do not compel the adjustment of policy objectives to bring them in line with the spending cuts made. The original policy objectives remain undiminished, but must be achieved with fewer resources.

It is not rare for this to come at the expense of the quality of implementation or ultimately, for the budgeted spending cuts not to be achieved. Therefore, when identifying policy options, it is extremely important to take into account the effects of individual measures on the economy and society and the future effects of the proposal, the so-called second and third-order effects.⁶³ This is because societal challenges are complex and are often closely related.

The Advisory Division reiterates its advice from the 2023 September Report that policy choices should take sufficient account of the complexity of and connection between challenges, by integrally considering measures and identifying second and third-order effects where possible. In this regard it is important that the final policy choices are simple, do not make systems more complicated and that they improve implementation. That is why (policy) evaluations, interdepartmental policy reviews (IBOs), in addition to studies and reports by assessment agencies and advisory councils, are important to be able to weigh up substantiated policy options as effectively as possible.

IV. *Over the past few years a solid foundation has been laid for a new, improved budgetary process in the spring. Continue on this path, in association with parliament, during the upcoming government term.*

Since 2022, the current government has taken steps towards a multi-year, integral, orderly and transparent spring decision-making process, in part on the advice of the 16th Study Group on Fiscal Policy⁶⁴ and in response to successive

⁶² The cheese slicer method results in generic cuts scattered across ministries and other government organisations, with no substantiated reduction in specific policy objectives. Underspending does not only mean failure to spend the budgeted funds but also that in the medium term, this previously planned expenditure will still go ahead, possibly at higher prices, in order to achieve the intended policy objectives. The wage and price adjustment is an allowance for increased taxes and thus an indexation necessary for the continuation of existing policy processes.

⁶³ A first-order effect is the direct result of the proposal, in this case the direct savings anticipated. Second-order effects are the effects of the proposal on, for example, the economy and society. Third-order effects are the future consequences of the proposal.

⁶⁴ 16th Study Group on Fiscal Policy. (2020) Koers bepalen. Kiezen in tijden van budgettaire krapte. (Setting the course - Decisions in times of budgetary constraint.)

opinions issued by the Advisory Division since the 2022 Budget Memorandum.⁶⁵ The government strives for a single integral main decision-making moment in the spring for the main lines of both the expenditure and tax side of the budget for subsequent fiscal years. As a result, various political aspirations, problems, windfalls and setbacks can be weighed up in an integral manner.

Integrating this decision-making process in the Spring Memorandum, sending it to parliament in a timely manner, having it independently calculated by the CPB, and supplying all relevant budget documents at the same time, means parliament is involved in the multi-year budgetary decision-making process in a timely manner. As a result, parliament is able to exercise its rights associated with the budget more effectively. It also aligns the decision-making process more closely with the European Semester.

In the new European budgetary framework, which is expected to come into force during 2024, this remains as relevant as ever. Decision-making in August can then be limited to necessary adjustments and any additional purchasing power measures based on the latest insights.

The changes to the budgetary process serve a more predictable and stable budgetary decision-making process by making decisions on paper more structured than before. With the changes made the government has laid a solid foundation for a new, improved budgetary process. The Advisory Division recommends the incoming government, in association with parliament, continue on this path.

V. *Gradually make the budgetary framework climate-inclusive.*

Climate change will be one of the greatest social challenges in the coming decades. Preventing and adapting to climate change is an extensive structural task, affecting virtually all government policy areas. The composition and level of government revenue and expenditure will change structurally and significantly. Currently, the climate is not yet sufficiently incorporated in the considerations that apply to fiscal policy. Therefore, in its opinion on the 2024 Draft Budget Memorandum, the Advisory Division recommended creating a climate-inclusive budgetary framework so that considerations regarding climate adaptation, mitigation, and damage constitute an integral part of budgetary decision-making.⁶⁶

The new European budgetary framework also addresses fiscal risks posed by climate change. After the new framework enters into force in mid 2024, insofar as possible, in their national budgetary frameworks Member States must take into account fiscal risks posed by climate change and the impact of climate change on the environment and distribution of the burden. Member States must also devote attention to climate-related contingent liabilities, if possible (see also Section B2).

⁶⁵ Parliamentary Documents II 2021/22, 35925, No. 3.

⁶⁶ Opinion on the 2024 Draft Budget Memorandum and 2023 September Report on Budgetary Monitoring, Parliamentary Documents II, 2023/24, 36410, No. 4.

It is important to develop the climate-inclusive budgetary framework gradually; not everything is possible and certainly not at the same time. But a start must be made now. In the 2024 Budget Memorandum, the Advisory Division outlined the following elements for creating a climate-inclusive budgetary framework:

- Create greater understanding of the (future) fiscal implications of climate change. There is currently a lack of understanding due to limitations in available data. Understanding the intergenerational aspects of climate policy and incorporating them in the sustainability analyses of public finance will improve the ability to make integral considerations for resource allocation in fiscal policy.
- Develop broad definitions and a classification of climate-related expenditure and revenue consistent with European methods. It is important to be able to track and monitor mitigation and adaptation policy on both the revenue and expenditure side of the budget so that resources can be allocated efficiently and effectively and the effects of policy are understandable and transparent. By learning from the European taxonomy system, which also requires companies to report on the climate impact of their operations, it will not be necessary to reinvent the wheel.
- Create transparency in the budget, including for the purpose of exercising parliamentary rights associated with the budget. In order to make fiscal policy more climate-inclusive, independent, relevant and reliable, information must be available in a timely manner to make integral considerations in fiscal policy. This means effective alignment between the cycle of the Climate Act and the budget cycle is important.

C. RESPONSE FROM THE GOVERNMENT

The government would like to thank the Advisory Division of the Council of State (hereinafter: the Advisory Division) for its assessment of the 2024 Stability Programme (SP) and the 2024 Spring Memorandum. The Spring Memorandum contains an update of the State Budget for the coming years and the corresponding first supplementary budgets contain the concrete changes per chapter of the budget. The SP describes the development of Dutch public finances and the economic outlook with respect to the Stability and Growth Pact (SGP). Public finances in the SP were presented for the first time this year on the basis of an ex ante calculation of the spring decisions by the CPB Netherlands Bureau for Economic Policy Analysis, while the economic outlook is based on the Central Economic Plan (CEP). The Advisory Division has assessed the extent to which the development of public finances complies with the rules of the Stability and Growth Pact (SGP), taking into account the latter's reform.

The government thanks the Advisory Division for expressing its appreciation regarding the significant steps taken in improving the transparency of budgetary information. The government remains committed to further streamlining the budgetary process and improving the transparency of the documents.

For the past two years, a significant improvement has been made to the budgetary process with the multi-year Spring Memorandum. Bringing forward the decision-making process has provided scope for the CPB to perform a calculation, which can be included in the Stability Programme. The Council of State can also include this calculation in its opinion on the Spring Memorandum and the Stability Programme. Furthermore, this aligns the decision-making process more closely with the European Semester. It also means parliament has an insight into the spring decisions earlier along with an independent calculation by the CPB.

The government had planned to publish the Spring Memorandum at the same time as the CPB's calculation of the spring decisions, the Spring Report as part of the Council of State's budgetary monitoring and the Stability Programme (the annual report to the European Commission). However, given the informateurs' request to share the spring decisions, the government decided to bring the publication of the Spring Memorandum forward. At the same time, the ambition to further improve the budgetary process remains undiminished.

Assessment under European fiscal rules

In the Spring Report the Advisory Division assessed whether the budget complies with European fiscal rules in 2023, 2024 and 2025. In doing so, the Advisory Division examines figures from the Stability Programme, which incorporates CPB forecasts for public finances (including an ex ante calculation of the spring decisions). The Stability Programme in its current form will no longer exist in the revised SGP. Instead, Member States will submit a medium-term fiscal-structural

plan⁶⁷ to the European Commission. Subsequently, Member States must publish annual progress reports.

The Advisory Division concludes that based on both the Stability Programme and the Spring Memorandum, the Netherlands meets the requirements of the corrective arm of the Stability and Growth Pact (SGP) in all the years. For example, in 2023, the EMU balance is 0.3 of GDP and EMU debt is 46.5% of GDP. Also in the 2024 and 2025 forecasts, the EMU balance remains below 3% of GDP (2.0% of GDP and 2.1% of GDP, respectively) and EMU debt below 60% of GDP (46.8% of GDP and 48.1% of GDP, respectively). In 2024, the European Commission will no longer perform an assessment in relation to the rules of the old preventive arm of the SGP, as they will no longer apply in the revised framework. Therefore, in view of the medium-term fiscal-structural plan in the revised SGP, the Advisory Division looks ahead to the possible implications of the rules in the new preventive arm. The Advisory Division states that only a preliminary estimate of the multi-year fiscal efforts that would result from the new preventive arm can be provided at this time because the figures from the Commission's spring forecast are not yet available. The Advisory Division's preliminary estimate of the budgetary task amounts to a 1.9% improvement in the structural primary balance⁶⁸ in 2028. The new preventive arm comes into play if debt and the balance do not sustainably remain below 60% and 3%.

The government agrees with the Advisory Division's assessment regarding compliance with European fiscal rules. The government acknowledges that based on the most current estimates, the Netherlands faces a budgetary task in relation to the new rules of the preventive arm. However, at this time it is difficult to say how challenging this budgetary task will be, as it depends on the latest economic developments and macroeconomic assumptions and the decisions taken by a subsequent government, among other things. In addition, the Advisory Division rightly notes that preliminary figures from the European Commission are currently only indicative and that the European Union cannot recommend an alternative expenditure path as long as the budget deficit is less than 3% of GDP and debt is below 60% of GDP. This also applies if the Netherlands were to submit a plan that did not meet the expenditure path requirements under the regulation.⁶⁹

⁶⁷ As part of the preventive arm in the revised European budgetary framework, Member States submit medium-term fiscal-structural plans to the European Commission every four years. This plan includes an expenditure path, public investment and reforms.

⁶⁸ The structural primary balance is the EMU balance net of cyclical effects and interest expenditure.

⁶⁹ The expenditure path must ensure that debt remains at a prudent level (below 60%) or - if above 60% - credibly declines after the fiscal adjustment period, and the deficit is kept below 3% of GDP. The credibility of the decrease in debt after the expected fiscal adjustment is assessed by means of a debt sustainability analysis.

Assessment under national fiscal rules

Budgetary process

With the 2024 Spring Memorandum, the Advisory Division notes that the government has taken new steps towards an integral, orderly and transparent spring decision-making process. The introduction of a fixed moment for halting decision-making for the Spring Memorandum will bring calm to the process. It also provided the opportunity for the CPB to perform a calculation of the spring decisions. As a result, the Advisory Division was able, for the purpose of this Spring Report, to assess compliance with national and European fiscal rules based on an independent calculation by the CPB for the first time. In addition, this year the national budgetary process was brought forward enough to align it with the European Semester, so that the 2024 Stability Programme contains the most recent budgetary information.

The government agrees with the importance of an orderly budgetary process. The government has started working on the recommendations and points of concern regarding the 2023 Spring Memorandum with the aim of presenting decision-making in a more transparent and comprehensible manner. Consequently, the government appreciates the Advisory Division's recognition of the steps taken in recent years to improve the budgetary process and to make the documents clearer and more comprehensible. The government continues to examine ways to further improve the budgetary process. The Advisory Division's opinions are of great value in this regard.

Assessment under national fiscal rules

The Advisory Division notes that this spring, the government succeeded in achieving an integral main decision-making moment; decisions were taken on the main revenue and expenditure lines, and the revenue framework was balanced. However, the Advisory Division did note that the government failed to respect the separation of revenue and expenditure in various areas in the Spring Memorandum. The Advisory Division also states that with the latest defence investments, the NATO target of defence spending worth 2% of GDP, excluding Ukraine aid, will only be met in 2026. The Advisory Division cites the importance of investment in defence and of achieving NATO's target of 2% of GDP and considers it important to closely monitor depletion and ensure investments are made at a realistic pace so that the target of 2% of GDP can be effectively achieved. The Advisory Division also notes, in line with its advice in the 2024 Spring Memorandum, that the government has decided to scrap the increase in the scaling-up rebate and to implement the new financing system early in 2024.

The government underlines the importance of an integral main decision-making moment. The government also endorses the importance of separating revenue and expenditure. However, fiscal rules dictate that this separation can be deviated from if it would lead to inefficiencies. In the case of the purchasing power reparation, this involved a relatively limited recovery in budgetary terms compared to the package presented in the 2024 Budget Memorandum. In this regard, housing benefit proved to be the most effective tool to achieve the reparation.

Consequently, this adjustment is consistent with regular purchasing power decisions. For this reason, the government opted to adjust the expenditure ceilings accordingly, with coverage provided on the revenue side. The government also adjusted the frameworks for the motions, amendments and commitments by the House, which collectively form a revenue and expenditure package. This includes the increase in the statutory minimum wage and maximum hourly rates for childcare, which were passed in the House of Representatives at the time, and the revenue measures that serve as coverage.

As for the NATO standard, last year in Vilnius the Netherlands committed to the Defence Investment Pledge to invest at least 2% of GDP in defence each year. Given geopolitical developments, the government recognises the importance of this international agreement.⁷⁰ In addition, the government agrees with the advice of the Council of State to continue monitoring the depletion of the Defence budget. Despite the challenges posed by a tight defence and labour market, the Department of Defence is making efforts to ensure that planned investment resources are actually spent. Should the current pace still prove too ambitious, the government will adjust the pace of funds in the defence budget at a subsequent budgetary moment. Of course, the earmarked funds remain available to Defence.

The government thanks the Advisory Division for its opinion on the new funding system, as this helped in reaching an agreement with the local and regional authorities. The new funding system provides municipalities and provinces with a stable source of revenue and clarity on how the Municipal and Provincial Fund will develop in the future.

Quality and transparency of public finances

In the 2024 Spring Memorandum, the Advisory Division notes that the government redirects part of the wage and price adjustment to the Health, Welfare and Sport (VWS) budget for the benefit of the latter's budgetary outlook. The wage and price adjustment is an indexation needed for the continuation of policy processes. Use of these resources for other purposes affects these processes and thus indirectly impacts social objectives. The Advisory Division deems it positive that in this Spring Memorandum, the government has taken a critical look at the forecasts in the budget and tried to establish a more realistic cash flow for the budgeted funds. The Advisory Division does believe it is important to continue to critically assess the impact of underspending on the timely achievement of policy objectives. The Advisory Division recommends that this be addressed in more detail in the individual budgets. Finally, the Advisory

⁷⁰ The percentages in the Spring Memorandum were calculated using the Dutch calculation method. As indicated in the 2024 Spring Memorandum, NATO uses a different nominal calculation method than the Netherlands. NATO reporting is used to compare allies in an international context. NATO calculates the figures provided by the Netherlands back to 2015 price levels, using a different adjustment for the numerator than for the denominator. This creates a different outcome than dividing the Dutch defence budget reported in the budget by Dutch GDP. In recent years, NATO reported a higher percentage than that calculated by the Netherlands. Based on NATO's calculation method, the Netherlands is again expected to exceed the national calculation method as of 2024. In addition, military support for Ukraine does not count towards the NATO target under the current directive (from 2018). Not all countries distinguish between these different expenditure in their budgets.

Division expresses its appreciation with regard to the significant steps the government has taken in improving the transparency of the budgetary information in recent years.

The government endorses the principle that funds for the wage and price adjustment should not be used for other purposes. Indeed, using wage and price adjustment funds for other purposes has consequences for policy processes. As such, the government considers this restructuring. In these specific cases, it was estimated that the same societal objectives could be achieved with fewer resources. The Advisory Division underlines the importance of continuing to critically assess the impact of underspending on the timely achievement of policy objectives. In the Spring Memorandum, budgeted expenditure was carried forward to later years if not expected to be spent this year. Thus, because funds are carried forward to later years, the underspending does not come at the expense of policy objectives, but possibly at the expense of when the objectives are achieved. The government continues to be mindful of the budget's realism and will thus revisit the issue of whether the current expenditure forecast needs adjusting in the Budget Memorandum. The departmental annual reports for 2023 will include a special 'underspending' appendix that will specifically address underspending in relation to achieving results at the request of the House. Furthermore, underspending is also the main topic of the 2023 Annual Financial Report of the Kingdom.

The new government's fiscal policy

The Advisory Division outlines five points of concern for the incoming government's fiscal policy. Firstly, the Advisory Division states that the current medium-term initial budgetary position requires additional budgetary margin to be created, taking into account the negative impact of spending cuts or tax increases on the economy and society. The Advisory Division also advises the new government to adopt an approach that focuses on broad prosperity when implementing fiscal policy and when elaborating the budgetary task by means of, for example, an Initial Policy Memorandum on Broad Prosperity. In order to ensure the quality of public finances, the Advisory Division advises the new government consider not only the immediate consequences of the decisions taken, but also the consequences for the economy and society and the future impact of the proposal, when justifying policy choices and elaborating budgetary tasks. The Advisory Division also notes that over the past few years a solid foundation has been laid for a new, improved budgetary process in the spring. The Advisory Division recommends the incoming government, in association with parliament, continue on this path. Finally, the Advisory Division recommends gradually making the budgetary framework climate-inclusive.

The government thanks the Advisory Division for its opinions regarding the new government's fiscal policy. Given its caretaker status, this spring the government does not consider it appropriate to include a spending cut task. However, in the Spring Memorandum, the government did adhere to the budgetary frameworks as agreed in the Coalition Agreement by balancing both the revenue and expenditure

frameworks in 2024 and 2025. Furthermore, steps have been taken in recent years to integrate broad prosperity in the budget system and budget cycle and to make the budget climate-inclusive. This government has benefited from the Advisory Division's recommendations. It is up to a subsequent government to further shape fiscal policy, taking the Advisory Division's opinions into account.

Yours sincerely,
the Minister of Finance,

S.P.R.A van Weyenberg

The response from the government has not prompted the Advisory Division to change its assessment. In the September Report, the Advisory Division will discuss the implementation of the commitments.

The Vice-President of the Council of State,

Mr Th. C. de Graaf