

Policies of Grants to Subcentral Governments

General grants vs. earmarked grants: theory and practice”

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“Intergovernmental Transfers in a Federal Context - the Case of Austria”

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Abstract

As a federal country Austria has three levels of governments, the federal government, the regional or *Länder* governments, and local governments. The transfer system between these levels of government is not designed according to a master plan with defined goals. Instead, it has evolved over decades of periodic negotiations between federal and subnational authorities on the one hand and between *Länder* and local governments on the other hand.

The transfer system's main goal is to equalize fiscal capacity of governments and to harmonize it with their respective functions. As a result of recent intergovernmental negotiations many federal transfers were changed from (often) earmarked grants into tax shares, free to be spent by the *Länder*.

Coordination of budgetary policies and obligatory negotiations on compensation for new functions support sustainability of subnational finances.

Efficiency is not a primary goal of intergovernmental fiscal relations, but remains in the responsibility of each government. Recently the federal government moved to a more program oriented budgeting system, a reform effort which should have a positive impact on the efficiency orientation of intergovernmental fiscal relations.

I. State Organization and Fiscal Federalism in Austria

1. Some Facts and Figures

Austria is a small federal country in central Europe. Its area comprises about 84.000 km² and its population is close to 8,3 million of which 1,7 mio live in Austria's capital Vienna. Austria is a member of the European Union as are all of its neighbours, with the exception of Switzerland and the principality of Lichtenstein.

GDP per head is well above the average of the Union and amounts in 2008 to about 123 % of EU27 average. In 2008 that's the fourth rank of EU27 countries behind Luxembourg, Ireland and the Netherlands.

Table 1: Austria - GDP

Year	GDP, bio.€	GDP, per capita in PPS, EU27=100
2000	207.5	131,4
2001	212.5	125,1
2002	218.8	126,2
2003	223.3	126,8
2004	232.8	126,7
2005	244.5	124,3
2006	257.3	123,7
2007	270.8	123,8
2008-	282.2	123,1

Source: STATÖ, WIFO: GDP, March 2009 notification; Eurostat: GDP per head

2. Budgetary policy

All Austrian governments of the last decenniums shared a similar budgetary policy. The policy was based on a moderate attempt to maintain sustainable public finances, that is an attempt to achieve a balanced budget over the economic cycle and to follow the Maastricht-criteria, resp. the criteria of the European Stability and Growth Pact. Additionally during most of that period the federal government, the main stakeholder in tax matters, tried to ease the tax burden as there was concern that Austria's relatively high tax quota could have a negative impact on economic development and growth.

Table 2: Austria - Main indicators of public finances, general government, % of GDP

	Public Expenditure	Tax quota	Public Deficit (Maastricht)	General Gov Debt
2000	52.1	43.2	-1.7	66.5
2001	51.6	45.3	0.0	67.1
2002	51.0	43.9	-0.7	66.5
2003	51.5	43.8	-1.4	65.5
2004	54.0	43.4	-4.4	64.8
2005	49.9	42.2	-1.6	63.7
2006	49.4	41.7	-1.6	62.0
2007	48.7	42.2	-0.5	59.4
2008	48.7	42.8	-0.4	62.5
2009	51.1	42.0	-3.5	68.5

Source: STATÖ, (until 2007), BMF (2008; 2009: forecast)

3 Governments and functions

The Austrian public sector includes the federal sector, the 9 *Länder* (regional government), 2,357 local governments and autonomous social security authorities (not being partner in intergovernmental fiscal relations, being federal government responsibility).

Table 3: Austria - public expenditure, 2008

	Bio. €	% of GDP	% of public exp.
Federal Government	52,5	18,6	38,2
<i>Länder</i>	22,8	8,1	16,6
Local governments	19,0	6,7	13,9
Social security authorities	43,0	15,2	31,3
General government	137,4	48,7	100,0

Source: STATÖ

Although there are consensus based instruments to coordinate budgetary policies (see below), all governments are independent and are constitutionally granted autonomy with respect to their budgets. Local governments are supervised by the *Länder* and have their budgets approbated - according to fixed rules laid down in advance by *Länder* laws and the possibility of appeal at the Supreme Administrative Court in case of conflicts

The federal level is responsible for the bulk of legislation. Most federal laws are implemented by *Länder* authorities with an easy-handed supervision by the respective federal line ministries. A notable exception is fiscal administration, where the revenue offices are federal government agencies.

Law making competencies at the federal level dwarf those of *Länder* parliaments, some exceptions being f.e. municipal laws, construction laws and sports. Instead, *Länder* strength is in the executive sector. Besides implementing their own laws, they are responsible for executing federal laws, as mentioned above, for example industrial and trade laws, water and riparian legislation, or laws pertaining to non-nationals, to forestry, and mining.

Municipalities have important tasks in organising services of local interest and local infrastructure. These tasks are granted to them by the constitution.

4. Stakeholders political influence

From a legal point of view, *Länder* position within the federation is weak since the federal constitution assigns ultimate decision making authority regarding federal-*Länder* relations to the federal parliament. But from political point of view the *Länder* enjoy considerable power, especially the *Landeshauptleute* – *Länder* governors whose office combines three functions. Not only are they the heads of the *Länder* government, but they also represent federal administration within their region and they head their respective regional party organizations. Given their politically powerful positions, federal politicians need the support of *Länder*. Additionally *Länder* governors have organized themselves as a Committee of *Länder* governors (*Landeshauptleutekonferenz*), and form a powerful pressure group to support their interests against the federal government.

Compared with regional governments dominating position behind the scene, municipalities have a weaker stance. They are organized voluntarily in two associations: the Association of Austrian Cities and Towns (*Österreichischer Städtebund*), representing the larger, more urban municipalities, and the Association of Austrian Municipalities, (*Österreichischer Gemeindebund*), representing smaller, rural municipalities. Often these two organisations hold conflicting views, especially in financial affairs.

5. Fiscal Federalism

5.1 Laws on fiscal federalism

The constitution authorizes the federal parliament to decide by single vote majority on all matters concerning taxes and revenue sharing, cost bearing rules and fiscal transfers given to subnational governments. Residual legal competencies remain with the *Länder* parliaments notably their fiscal relations with municipalities.

Intergovernmental fiscal relations between the federal government, *Länder* and local governments are laid down in a federal Intergovernmental Fiscal Relations Act (**Finanzausgleichsgesetz** – FAG). Although the *Länder* and municipalities have no veto concerning this FAG, they can address the Constitutional Court to review its fairness and equity. The Court can then declare the Act as null and

void. Relations between *Länder* and municipalities are fine-tuned at the *Länder* level, in some areas by *Länder* law, in other through direct decisions by the regional government.

5.2 Consensus oriented intergovernmental fiscal relations

The federal FAG' is close-ended, it's validity is limited in time – four to six years, according to political preference. Before being phased out, the federal finance minister, the *Länder* finance ministers and political appointees of the two municipal organizations enter into negotiations on intergovernmental fiscal relations for the next period.

Due to the strong political position of the *Länder* and the fact that Austria is a very consensus oriented society, the practice of fiscal federalism in Austria has moved away from the fiscal federal top down approach envisaged by the constitution. Instead subnational governments (SNGs) a strong say in intergovernmental fiscal relations. As a result the outcome of all FAG negotiations until now has been based on unanimously agreement. Furthermore, throughout the FAG's time period there is the possibility of changes via renegotiations due to actual developments or new government programs.

5.3 Main features of the fiscal federal system

Three pillars are at the core of the federal FAG:

- rules on tax allocation and collection (most taxes allocated to and levied by the federal revenue offices),
- rules on revenue sharing and
- rules on transfers from the federal level to the *Länder* (regional) level and to a minor extent to the local level.

Each *Land* complements the federal system through rules that regulate fiscal equalization between the municipalities within each region without interference of the federal government. Additionally each *Land* requires that municipalities cover a portion of the costs incurred by the *Länder* (for example hospital financing), the size of the contribution for their budgets from municipalities, its size being limited by federal law. Unlike the federal FAG, *Länder* regulations usually are not limited in time.

Table 4: Three pillars of fiscal federalism in Austria, percent of national tax revenue, 2007

	Federal Gov	<i>Länder</i> Govs	Vienna*)	Local Govs	EU
Tax collection	94,69	0,32	1,39	3,59	0,0
Revenue sharing	- 24,25	+ 9,05	+ 4,85	+ 7,38	+ 2,99
Transfer system	- 12,96	+ 11,69	+ 2,26	- 1,00	0,00
Sum	57,48	21,06	8,5	9,97	2,99

*) Vienna is both - Land and municipality

Source: BMF

II. General trends in grants policy

1. Concepts OECD and Austria

A discussion of general trends in Austria's grants policy first needs a clarification of what grants are. As it turns out this is not as clear-cut as one might think. Different international organisations use different criteria to define "tax sharing" and separate the term from "grants". The dividing line between tax sharing and grants was recently dealt with in an OECD paper¹. The OECD proposes the following four criteria test :

- *Risk sharing*: The amount of revenue allocated to the sub-central level strictly related to total tax revenue (*e.g.* as a given share of annual tax revenue), *i.e.* does the sub-central level of government fully bear the risk of tax revenue slack and fluctuations?
- *Un-conditionality*: Is sub-central government free to use the revenue allocated, *i.e.* are the revenues unconditional (non-earmarked)?
- *Formula stability*: Is the revenue share between the central and the sub-central government predetermined in advance and not changed in the course of a fiscal year?
- *Individual proportionality*: Is the revenue share of *each* sub-central government strictly related to what it generates on its own territory, *i.e.* is there no horizontal redistribution or fiscal equalisation across sub-central governments?

Arrangements that do not even meet the first three criteria, are referred to by the OECD as an *intergovernmental grant*.

Austria's system of defining grants and tax shares used to be a little bit blurry, based more on traditional classifications than on economic definitions. Of course the term grant in itself does not exist in Austria's German legal fiscal federal terminology. It comprises

- *Finanzzuweisungen*: *i.e.* , non-earmarked grants, mostly mandatory, as general purpose grants or as block grants;
- *Zweckzuschüsse*: earmarked grants, discretionary grants and mandatory matching and non matching grants²;
- *Kostentragungen*: cost transferring, *i.e.* spending by the *Länder* is covered directly by the federal budget, without advance payment from *Länder* budgets (you send the bill – we pay).

¹ COM/CTPA/ECO/GOV/WP(2009)10, Finding the dividing line between tax sharing and grants: a statistical investigation

² Taxonomy of grants: OECD, 2006, Network on Fiscal Relations Across Levels of Government, Working Paper No. 2, Fiscal Autonomy of Sub-central Governments

The first two types of transfers sometimes were allocated to SNGs partly according to a stable formula, mostly a fixed yearly amount, and partly according a risk sharing approach, using a certain percentage of a specified tax revenue. These latter parts of intergovernmental fiscal allocations used to be defined as grants, though the OECD test would refer these allocations as tax shares, given their formula stability and un-conditionality.

2. Recent reform of federal grant system

Inter alia the OECD recommended the reduction of earmarked transfers to lower levels of government. For example, federal government funding earmarked for residential construction subsidies and infrastructure spending by the *Länder* should be phased out³.

One of the goals of the Federal Ministry of Finance (MoF) at the last round of negotiations towards the next *FAG* was to comply with that recommendation. As a result, many former transfers were converted into (non-earmarked) tax shares with the effect of

- more accountability for meeting regional preferences at the *Länder* level (subsidiarity)
- risk sharing for formerly fixed amounts of transfers
- reduction of administrative burdens due to former information and oversight processes.
- improvement of transparency in fiscal federal relations.

Table 5: Austria – federal grants, in 2008 resp. 2009 converted into tax shares, Recipients: *Länder*

Purpose	Type of grant	Amount 2007, mio. €
housing subsidies, environment and infrastructure	earmarked, mandatory, non-matching	1,780.5
general improvement of budget situation	non earmarked, mandatory, general purpose	1.217,5
regional road construction and maintenance	earmarked, mandatory, non-matching	539.1
public transport	earmarked, mandatory, non-matching	167.9
convergence of fiscal capacity per head after revenue sharing	non-earmarked, mandatory, general purpose	104.6
environmental protection, saving energy	non-earmarked, mandatory, block grant	94.8
promotion of agriculture	earmarked, mandatory, non-matching	14.5
environmental protection	non-earmarked, mandatory, non matching	6.9
other		7,5
Sum		3,933.3

Recipients: local governments

³ OECD, 2005, Economic Review, Austria

general improvement of budget situation	non earmarked, mandatory, general purpose	116.6
other		5.3
Sum		121.9
Länder and local governments, sum		4,055.2
% of GDP 2007		appr. 1.5%

Source: BMF, Erläuterungen zu SchlüsselVO, 2008

A possible disadvantage of the new system might be, that *Länder* will lobby again for supplementing grants in the future for the same purposes as prior to the reform. At the federal level too, there too might be political interest to spend additional money for certain defined purposes well accepted by public opinion.

3 Grant system after reform

Despite the reform some federal transfers remain and a lot of transfers which flow from land to local governments and vice versa.

Table 6: Austria – remaining federal grants after federal grants reform

Recipients: Länder

Purpose	Type of grant	Amount 2007, mio. €
salaries of <i>Länder</i> employed teachers	cost transferring	2,896.3
pensions of <i>Länder</i> employed teachers	cost transferring	973.1
hospital financing	earmarked, mandatory, non-matching	122.0
reconstruction of public infrastructure and assistance after natural disasters	earmarked, discretionary, capital and current expenditure	71.8
special housing subsidies	earmarked, mandatory, non-matching	17.0
theaters	earmarked, mainly mandatory, matching	12.8
Sum		4,093.0

Recipients: local governments

public transport	earmarked, mandatory, matching	71.8
convergence of fiscal capacity per head after revenue sharing	non-earmarked, mandatory, general purpose	98.0
special support for local governments in not self induced financial distress	non-earmarked, discretionary, general purpose,	1.2
theaters	earmarked, mainly mandatory, matching	8.8
reconstruction of public infrastructure after natural disasters	earmarked, discretionary, capital expenditure	28.2
other		2.0

Sum		210,0
Länder and local governments, sum		4,303.0
% of GDP 2007		appr. 1.6%

Table 7: Austria – Länder grants, recipients: local governments

Purpose	Type of grant	Amount 2007, mio. €
support of local governments real investment and of local governments in financial distress	earmarked, discretionary, capital grant	628,7
% of GDP 2007		appr. 0,2%

Table 8: Austria – Local government grants, recipients: Länder

Purpose	Type of grant	Amount 2007, mio. €
strengthening fiscal capacity of <i>Länder</i>	non-earmarked, mandatory, general purpose	312,0
hospital financing	earmarked, mandatory, non-matching	233,0
financing social services	earmarked, mandatory, matching	501,0
Sum		1,046.0
% of GDP 2007		appr. 0,4%

Table 9: Austria – Local government grants, recipients: Local governments

Purpose	Type of grant	Amount 2007, mio. €
municipal cofinancing of various social services	earmarked, mandatory	324,6
municipal cofinancing of school construction and maintenance	earmarked, mandatory	86
Sum		410,6
% of GDP		appr. 0,2%

Source: STATÖ, Gebärungen und Sektor Staat, Teil II, 2007

III. Mechanisms to compensate subnational governments given new functions

1. Traditional approach

The traditional approach of covering expenses in Austria's fiscal federal system is an own cost bearing rule: all governments have to pay the cost associated with executing functions allocated to them by the constitution or by law or taken over according to their own preferences. However, there are exceptions: cost transfers. The respective higher ranking government can carry over costs to lower

ranking ones or take over costs of lower ranking governments. for example, the Federal government pays the salaries of teachers of elementary school and of a certain type of secondary level schools, all employed by the *Länder*. The system has often been criticised of being inefficient: massive principal-agent problems arise, if one government pays while the other government hires and employs the teachers. It is no surprise therefore that Austria has one of the most expensive school systems in the world. Until now all efforts towards reform had only minor success, as for example implementation of firm staff planning to which *Länder* have to stick. Due to information problems federal enforcement is constrained.

Table 10: Costs of school education per head, (2005)

	elementary school (Volksschule)	secondary school I (Unterstufe)
Austria		
US \$	8.259	9.505
% of OECD*)	132	128
OECD		
US \$	6.252	7.437

*)OECD = 100

Source: OECD, Education at a glance, 2008

At the *Länder* level cost transfer to lower government levels is used: *Länder* governments require municipalities to bear some of the costs of the *Länder*, e.g. (partly) financing of public (*Länder*) hospitals (see Table 8).

2. Intergovernmental negotiations

As was mentioned above, the federal FAG is in force for four to (presently) six years. At the end of its cycle the Federal Finance Minister invites colleagues from the *Länder* and political representatives of the two municipal associates to discuss and negotiate tax allocation, tax sharing and transfer rules for the next period. These negotiations require political investment from all sides: as the topic is money and therefore about power discussions usually are pretty tough and lengthy. Alliances usually are not formed according to party lines but according to government levels. Subnational governments, most importantly *Länder* governments try to find unanimous positions against the federal government.

Municipal associations are generally hampered during the negotiations by internal conflicts: According to the revenue sharing system larger municipalities (population) get more tax shares per head as smaller ones, due to the assumption that they have to bear higher costs per head (Brecht's

law⁴). More often than not, municipal associations try as far as possible to sail in the wake of the more powerful *Länder* governments..

Negotiations start based on the current situation. Subnational governments argue for change (= more money) in light of the rising cost of their existing functions as well as the cost of new functions they were assigned or had taken on.

The MoF advocates reform efforts by subnational governments towards more efficient governance and also requests SNGs to support of federal program.. The negotiations's end result is usually a trade off: the federal side agrees to increase SNGs income and in return gets some of the items on its reform agenda.

Table 11: Results of negotiations in 2007 for intergovernmental fiscal relations 2008-2013

Financial results*),	2008	2009	2010	2011	2012	2013
Federal Gov	- 346	- 346	- 346	- 538	- 538	- 538
<i>Länder</i> Gov	+ 293	+ 293	+ 293	+ 380	+ 380	+ 380
Local Gov	+ 53	+ 53	+ 53	+ 158	+ 158	+ 158
Efficient government reform results	Agreements on: staff reductions, implementation of SNG pension reforms according to the fed. reform, expanding tax base of payroll tax for family allowances to public employees (to avoid classification problems), uniform tax code, ...					
SNGs supporting federal programs	Improvements in nursing (promotion of 24-hours care for senior citizens), implementation of a means-tested minimum income, housing subsidies used for climate protection initiative, ...					
Intergovernmental fiscal relations reforms	reform of grant system, reform of financing small local governments, implementation of yearly population statistics for intergovernmental fiscal relation purposes, incentives for local government cooperation, additional support instrument for financially weak towns, ...					

*) Mio. € per year, compared to 2007

Source: BMF

3. Problems of the consensus oriented approach

A major problem of the negotiation process is the implicit expectation of all stakeholders that SNGs (esp. the *Länder*) will be bailed out in case of financial turmoil. In fact *Länder* strategy is based on that expectation. They see rising costs as an argument for more money from the federal government. This more or less successful strategy is an important negative incentive against efficiency enhancing efforts by SNGs. Cost reduction weakens the SNG's negotiating position and could dissatisfy regional and local constituencies. Given that negative incentive problem a big bang' reform of federal relations and of the constitution often is demanded, but until now never succeeded even though considerable effort was devoted to it.

⁴ Brecht, A. (1932). Internationaler Vergleich der öffentlichen Ausgaben, Leipzig/Berlin; Zimmermann,

4. Reform approach – consultation mechanism

In the '90s the traditional approach no longer satisfied the SNGs. They felt burdened by new functions and not being properly compensated during the period of the existing FAG. As a result SNGs used the internal Austrian bargaining processes triggered by the accession to the EU as leverage to get a new system: the consultation mechanism.

The consultation mechanism is a treaty between federal, *Länder* and local governments, ratified by all parliaments and having therefore the status of a law. The treaty stipulates that all parties are to be informed if new legislation is planned. Additionally, it is mandatory that a calculation of the new legislation's financial burden, according to agreed upon guidelines is disclosed in advance. Any party feeling financially stressed by the new legislation can demand negotiations in a high ranking political committee. Also, if the information and negotiation commitments are not met or the negotiations do not result in a satisfying solution, then due compensation can be demanded at the Constitutional Court.

The consultation mechanism has some exceptions (e.g. implementing EU law, tax laws, partly parliamentary initiatives) and is only on effect for the respective period of the FAG. However, it is assumed that compensations will become part of future FAG negotiations.

It must be noted that the consultation mechanism does not work as it was envisaged by its creators. High ranking politicians who were meant to be members of the committee did not engage in the process and SNGs never sued the federal government at the Constitutional Court. Nevertheless even according to the testimony of SNGs representatives the mechanism is seen as a significant improvement of intergovernmental relations. SNGs have more possibilities to express their concerns during the drafting phase of new laws while federal ministries take the concerns seriously and try to adapt their drafts to avoid possible future conflicts.

IV. Supporting sustainable subnational spending via the design of conditional grants?

1. EU accession triggered reform of budgetary coordination

Since Austria's EU-accession in 1995 all federal government programs regards stable finances as the basis for a functioning public sector. federal governments committed themselves to a balanced budget across the economic cycle.

Despite its commitment the federal governments never had direct control of local or regional spending. Instruments to coordinate budget policies across all levels were needed.

The federal governments could stick with existing practices given the FAG's limited time and the fact that negotiations between levels of government provide for sufficient opportunity to check the sustainability of SNGs finances. Nevertheless there was and still is a serious flaw in that approach: SNGs use the possibility of an unsustainable fiscal position to argue for more federal funds. Though not always and seldom to a large extent successful, this method might look meaningful from a narrow SNG position, but is not sustainable from a general government point of view. Besides it is far removed from any criteria of efficiency.

After EU accession the federal government looked for more promising examples to coordinate diverging budgetary policies and found an example in the EU itself. The European Stability and Growth Pact envisages fiscal stability for the members of the union, despite substantially different initial positions and untouched budgetary sovereignty of member states. Austria's federal government could not enforce a stability pact on SNGs, due to their constitutional autonomy. But the shared goal of participating in the first round of Monetary Union and the wish of SNGs to ratify the too treaty-based consultation mechanism supported the federal government's position.

2. Austria's system of Internal Stability pacts

In 1997 the first of a series of Internal Stability pacts was ratified by parliaments.

Austria's Internal Stability Pact (*Österreichischer Stabilitätspakt - ÖStP*). The *ÖStP* is usually negotiated for a period of 4 years interlinked with the Intergovernmental Fiscal Relations Act -FAG. Its present period therefore is 6 years – until 2013.

The *ÖStP's* goal generally is to coordinate budgetary policies according to federally set targets. Among them the most important goal is a balanced budget over the economic cycle. Federal government adjusted its focus in later years and accepted temporary deficits to allow for reductions of the high tax quota, but aims at a balanced general government position at the end of the stability pact period.

The method of the pact was to designate a common budgetary goal and to require all governments to achieve well defined budgetary outcomes. Federal government had to reduce its initial deficit, *Länder* governments had to produce a budgetary surplus and groups of local governments within each *Land* were bound to balanced budgets.

3. Accounting problems

The ESA-European System of National Accounts, - the method EUROSTAT uses to compute the deficits and surpluses of member states – was chosen as the accounting method to monitor outcomes. However, in the beginning, *Länder* were unwilling to accept the redefinitions of ESA rules by EUROSTAT for Austria's internal processes. As EUROSTAT developed new ESA interpretations to deal with creative accounting of some member states Austria's *Länder* too were affected, having used such methods. A growing wedge between the outcomes according to Austria's internal accounting method and the Maastricht method had to be covered by the federal government. It was only in 2006 after a renegotiation of the ÖStP, when this attitude was overcome and all parties agreed on the pure ESA methods.

4. Governments supporting dedication of their partners

To give SNGs an incentive to accept the pact, the federal government took precautions. If a *Land* did not ratify the treaty it lost part of its shared taxes. Although a very controversial method, this provision came into effect, was executed and helped SNGs to join the stability efforts of federal government in their internal decision processes.

Within each *Land* a committee coordinates the inter-budgetary policy of municipalities and their relationship to the *Land*. Though local governments are free by constitution in their decisions, they are subject to oversight by the *Länder* and have to adhere to the municipal laws of their respective *Land*. Additionally, *Länder* are allowed to allocate 12,7 percent of the local government share of federal taxes according to their own criteria (see Table 7).. *Länder* use these options to encourage local governments to stick to the goals of the ÖStP as well as other *Länder* set goals.

Table 12: Austria – Sustainable spending - ÖStP – stability targets
% of GDP

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Central government		-2,1	-0,8	-0,8	-0,8	-2,4	-2,2	-1,4	-1,3	-0,7	-0,14
State government		0,60	0,60	0,60	0,60	0,48	0,48	0,56	0,36	0,39	0,42
Local government		0,15	0,15	0,15	0,15	0,12	0,12	0,14	0,09	0,10	0,10
Social security funds											
General government		-1,30	0,00	0,00	0,00	-1,80	-1,60	-0,70	-0,88	-0,19	0,38

Procedure: 2001-2006: ESA, Austrian interpretation, status 2000; 2007 et seqq.: ESA;
Source: ÖStP 2001,2005,2008

Table 13: Austria – Sustainable spending - results,
% of GDP

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Central government	-1,70	-0,73	-1,17	-1,63	-4,60	-1,78	-1,58	-0,64	-0,58		
State government	0,10	0,46	0,29	0,10	0,14	0,10	-0,16	0,09	0,12		

Local government	0,04	0,26	0,25	0,17	0,16	0,14	0,13	0,11	0,09		
Social security funds	-0,13	0,00	-0,04	-0,06	-0,09	-0,02	0,00	-0,09	-0,02		
General government	-1,69	-0,01	-0,67	-1,42	-4,40	-1,57	-1,61	-0,53	-0,39		

Procedure: ESA

Source: STATÖ, notification;

5. New challenges

The *ÖStPs* were largely effective throughout most of the time they were in effect, even though discipline deteriorated over time. The self-set goals for general government were met each year - at least according to Austria's internal accounting method – usually due to overperformance of the federal budget and better than expected results at the local level. At the *Länder* level outcomes were mixed, but deficits were more than offset by the performance of the other two government levels.

The sharp and severe economic downturn in 2008 shattered that system of stability efforts.

Governments all over the world implemented stimulus programs, deficits being of lesser importance at the moment. Austria's government too, tried to stabilize its economy by reducing taxes and implementing various stimulus programs. These measures seem to have had some success, with economic prospects somewhat improved compared to earlier in the year. However, this advantage was gained at the price of high deficits and surging debts.

Table 14: Austria – new budgetary plans

Stability program 2008-2013	2008	2009	2010	2011	2012	2013
General government	-0,4	-3,5	-4,7	-4,7	-4,7	-3,9

Procedure: ESA

Source: Austrian Stability Program 2008-2013

The present *ÖStP* planned for a moderate general government surplus for 2010 and beyond. This plan had to be abandoned in the light of the financial crisis. An understanding exists with the SNGs that in autumn 2009, a new strategy on how to deal with the *ÖStP* has to be negotiated.

V. Results towards economic efficiency of local public services?

1. Efficiency a priority – but not in intergovernmental relations

As was shown above, Austria's system of intergovernmental fiscal relations and as a part of it, the transfer system, is not focused on the economic efficiency of local or regional public services. Instead, it is aimed at fiscal equity - balancing the fiscal strength of governments by equalising a large portion of tax revenues across all governments. It does so by using various instruments (tax allocation, tax

sharing, transfers, cost bearing) while keeping in mind the burden of varying functions of the respective governments.

However, efficiency considerations are not disregarded in Austria's public sector. Constitutionally efficiency is a goal for public sector entities – the constitution defines it even as a mandatory criterion in the Court of Audit's public sector auditing. But - as a consequence of Austria's federal system - efficiency is left to the respective governments and to checks and balances within a specific government – from government efforts to parliamentary control to federal, local or regional auditing authorities. Especially at the interface of the federation –*Länder* relations there is an increasingly urgent need for efficiency reform. To solve the problem, a discussion on a complete reform of the federal constitution has begun, but all efforts toward reform have failed until now.

2. Performance oriented budget reform

In another area MoF developed a more promising approach: Until recently public sector budgeting was focused solely on providing a detailed description of appropriations that are input based. Correspondingly, legislation focused on parliamentary control of inputs as opposed to budgetary appropriations on a program or activity basis. A MoF-initiated federal budget law reform reoriented the federal budget system to focus on results: In exchange for more flexibility in budget management, in this approach decentralised managers will have greater responsibility for achieving results from a relatively small number of government programmes.

A similar system is considered for the still hesitate *Länder* and local governments. Therefore, federal government set this approach on the schedule of a special working group, including representatives of the federal states. This group should develop proposals for a large scale reform of the public administration on the basis of work undertaken by the Court of Audit and the board of national debt surveillance. Among these proposals the working plan aims at a reform of subnational budget laws, to be implemented by *Länder* parliaments.

In this system of performance-oriented public finances intergovernmental fiscal relations will have to change too and have to develop – in addition to their current focus on fiscal strength and equalisation - a new pillar with greater emphasis on output/outcome and resulting efficiency.