Issue Brief: Reforms (Fiscal/Markets/Administrative) and Stimulus Measures March, 2019

In this brief, the writers intend to convey the best practice in structural financial reform based on the work of the EU to survey, analyze and report the effects of various strategies used across numerous economies, large and small, and suggest the best norms for reform. Further, the brief provides OECD policy recommendations regarding the guiding principles for designing and aligning stimulus measures for long term growth.

In each section, along with guiding principles, are examples of strategies and summaries of lessons learned.

Further, the writers have created a “briefing advice” to guide the review of a local plan.

The recommendations in this brief can be used by the VBC and other stakeholders to evaluate the local government strategies to address the mandates of the CFT for sustainable public administration of the public budget to see if they meet the EU and OECD best practice guidelines which lead to long term fiscal reform and economic stimulation.

Section 1: Core Principles of Public Administration Reform

A well-functioning public administration requires a professional civil service, efficient procedures for policy and legislative development, well-defined accountability arrangements between institutions and citizens as well as among institutions, ability of the administration to effectively/efficiently deliver services to citizens and businesses, and a sound public financial management system.

Since 2014, the European Commission has defined the scope of public administration reform as covering six principal/core areas (see recommended sources for details):

- the strategic framework for public administration reform
- policy development and co-ordination
- public service and human resource management
- accountability
- service delivery
- public financial management.

Briefing Advice:

Does the Government proposal to CFT?

Lay out a strategic framework for public administration reform?

Lay out a sound financial management system with check and balances?

Lay out a revenue and expenditure streaming program to reserve and earmark funds for investing in the administrative reform effort?

Lay out how, with guideline, the funds will be protected from unintended uses?

Without funds being reserved for investment in administrative reform, we will not only never be able to reduce administration cost structurally, but also not be able to deliver on economic/structural reforms.

The VBC must try to convince the CFT of this, since the usual cost-cutting measures will worsen the situation, as proven from past local experiences and international examples.

Section 2: Core Principles and Policy Recommendations for Stimulus Strategies

Without a stimulus package, there will be no public support for economic (fiscal/tax, factor markets, and administrative) reform.

OECD makes the following policy recommendations on the strategies for aligning stimulus measures with long term growth.

Guiding principles for designing and implementing stimulus packages

The need for additional discretionary fiscal stimulus varies across countries because automatic stabilizers operate more powerfully in some economies. In this differentiated context, the biggest constraint on introducing additional fiscal stimulus is the reaction of financial markets to greater government borrowing needs.

- Crisis measures should not be allowed to reduce competition.

  Coordinated action can create positive spillover effects as it results in a larger overall output effect than if any country acted alone.

  Looking further ahead, many of the emergency measures taken today could pose a threat to long-term growth and sustainability if not properly unwound. For this reason, *measures should be designed and implemented as temporary and in the least distortive manner, with a clear and credible plan and timeline for phasing out as recovery takes hold.* It is critical to consider these so-called "exit strategies" now, together with emergency measures, in order to prevent new risks down the road.

- The credibility of the medium-term fiscal framework needs to be strengthened through the announcement upfront of a clear commitment to long term fiscal sustainability.

- Credible fiscal consolidation plans may require tax reforms, including the broadening of tax bases and better tax compliance to ensure sustainable revenues.

  As economies emerge from recession, it is likely to be necessary to raise additional revenues. Unless permanent cuts in expenditure are implemented, it will not be sufficient to restore them to pre-crisis levels.

- Countries need to ensure that taxes that are properly due are assessed and collected.

  Globalization and the integration of financial markets have made it easier for taxpayers to engage in offshore tax evasion. This poses a threat to tax revenues and undermines the fairness of tax systems.
- The tax system has fairness.

  The OECD has developed standards of transparency and exchange of information that have been accepted as the international norm. The implementation of these standards by all countries will allow both developed and developing countries to not only protect the revenue base at a time when public finances are under pressure but also ensure citizens that the costs of dealing with the crisis are fairly shared.

Briefing Advice:

The VBC needs to convince the CFT of the importance of a detailed growth strategy that generates funds. There will be a need to have the ability to borrow money to create growth. The recommended OECD source document supports the growth strategies. The Guidelines in the following section serve as a frame of reference for the evaluation of the government's growth strategy agreement with Holland.

Will the government have the ability to borrow?

Does the proposal have a beginning phase that is designed to be implemented as temporary and in the least distortive manner, with a clear and credible plan and timeline for phasing out as recovery takes hold. (with so-called "exit strategies"). Does it then show the structural reform strategy that replaces the temporary strategy?

Does the plan include structural tax reform that will not devastate the consumer?

Are the structural reform cuts structured in such a way that they cannot be overturned easily?

Section 3: Guidelines for long term growth policies

The overall plan for structural reform and long-term growth are built around five areas that will strengthen the economy and will show the citizens that the short-term consequences will have positive long-term results.

Long term growth strategies include actions in the following six areas:

1.Tax measures

Growth-oriented tax reforms would generally involve shifting revenue from corporate and personal income taxation or social security contributions onto consumption and property taxes, including housing taxation.

At the same time, any tax policy proposal needs to take account of its effects on income distribution, and it is particularly important to consider the poor during an economic recession, as they tend to be badly affected by the crisis.

Tax cuts that are targeted at workers with modest incomes can improve living standards, both by directly increasing their disposable income and by giving them a greater incentive to work.

2.Labour, social and education measures

Subsidy schemes to expand labor demand should be temporary and well targeted. Introduction of early retirement options should be avoided.

Countries with weak unemployment benefit systems may wish to consider extending the coverage and, possibly, the maximum duration of their benefit schemes during the downturn.

Expanding effective active labor market programmed would be important to maintain the activation stance. But it may be difficult to match the rise in job seekers with greater resources for public employment services, not least because it takes time to recruit and train good case managers. Under the circumstances, there may be opportunities for effective co-operation between public and private employment agencies to provide a range of contracted-out activation services.

Support for education and training that enables the transition to new jobs and emerging opportunities should also remain prominent in the policy agenda, as well as policies to help youth in their transition from school to work.

Concerns in terms of the integration of immigrants should be fully integrated into the labor market components of stimulus packages.

3.Infrastructure investment

Focus on projects which are "shovel ready", notably those aimed at stated policy goals and advanced enough in planning to be implemented quickly and effectively. A period of crisis does not lend itself to complex investment projects which typically require careful and lengthy planning. To the extent possible, priority should be given to modern projects with a greater potential to raise the efficiency of energy and resource use, and which support long-term environmental sustainability.

Target expenses to idle resources, notably vulnerable groups such as low skilled youth, women and older workers, who are at greater risk of falling into unemployment trap (see above).

Use existing programs and agencies to distribute the spending but make sure that they are equipped for the task. Regional agencies can be used as a vehicle to reach actors that cannot be reached by national agencies and programs.

Governments can play an important role in stimulating the development of nationwide high-speed broadband networks, including through public-private partnerships. Investment in this area must be accompanied by regulatory frameworks which support open access and competition in the market. High speed broadband networks can underpin new economic activities, have widespread economic productivity benefits and facilitate many social goals.

Combine investments in physical infrastructure with the provision of soft infrastructure, such as skills and other innovation-related assets, to maximize the impact in terms of long-term productivity growth.

4.Green recovery

The economic slowdown should not be used as an excuse to weaken efforts to achieve long-term, low-carbon economic growth. It is important to ensure that economic stimulus packages do not lock-in inefficient or polluting energy technologies, or dirty modes of production and consumption, but instead promote clean alternatives. Priorities for investments might include energy efficiency in buildings, increased public transport and increased fuel efficiency, as well as upgraded and expanded water treatment, supply and sanitation systems.

The crisis offers opportunities to introduce win-win policies that remove expensive and environmentally-harmful policies, while also benefitting the environment and the economy as a whole – removing subsidies to fossil fuel-based energy production and consumption, cutting trade barriers to climate-friendly goods, addressing market failures and assessing policies to support renewables.

5.R&D and Innovation

Any additional horizontal supports to business innovation should be designed with a focus on measures that are counter-cyclical. If transitory, greater reliance on grants may be justified because they can be counter-cyclical, as opposed to tax incentives, which tend to be pro-cyclical. Nevertheless, overall consideration should be given to choosing policy interventions with least deadweight loss and risk of distortion.

Financing for well-designed public-private partnerships for research and innovation can help ensuring fruitful interactions across segments of the innovation system.

Governments will also have to focus on risk sharing policies with the private sector, particularly with regard to new technologies.

6. SMEs and entrepreneurship

A straightforward way to ease the current constraints of notably small businesses is to allow tax payments to be deferred and paid back over a period of time.

Building on the immediate stabilizing effects of public capital injection and tax reliefs, governments could take steps to encourage private-sector capital injections. One option to consider could be creating risk-sharing schemes that would reduce the risk associated with investment by SMEs and especially innovative potentially high growth start-ups.

The creation of new business opportunities and the reallocation of resources from declining activities towards emerging ones should support a sustainable recovery. Government plans should not hamper this reallocation process and facilitate structural change.

Briefing Advice:

The VBC needs to convince the CFT that:

- Direct taxes and premiums already create a heavy burden of the cost of business and living. Increasing taxes and premiums even further will be more detrimental to the competitive position of the country and will contribute to more poverty/less purchasing power. The path to follow is rather what the IMF recommendation has been: shift to indirect taxation.
- To see the results of structural reform takes time. In the mean time we need to find a way to get the economy going, otherwise, the situation will worsen. The fastest way to do that is through
  - needed investment in infrastructure.
  - The economic structure of this nation needs to change. We cannot continue banking on industries that on the longer term are unsustainable or have reached their growth plateau or are even descending. We need to shift to new industries, and investing in infrastructure that would help that development is imperative. A state of the art 'digital highway' is just one example, whereby we can combine investment in infrastructure with the need for structural economic reform.
- Maybe we should consider retweeking our investment tax incentives regime, to make that possible. For example, It is our understanding that the recent search for interested parties to invest in a solar energy park was abandoned, because of the poor ROI
- Getting big business to establish on the island is likely a thing of the past. We rather have to focus on SME's development which seek to get into new markets and products. We need to have infrastructure in place that allows and stimulate them look for innovation and help them to export. Maybe a bold idea is to promote the island as an innovation lab, where AI entrepreneurs can come to try out their new ideas. The benefit would be jobs, technology transfer, and creation of expertise *that can be exported.*
- As far as labor market measures are concerned, see the 2014 IMF article iv consultation report, and various labor force development structural reform plans that reside in the national development plan but remain undeveloped.

Systemic strategy:

Sovereign Wealth Fund/ Economic Stimulus Fund

- Set up a sovereign wealth fund with specific guidelines for the use of the funds with accountability standards, checks and balance systems and targeted uses for the funds.

  Example: Norway is an example of how to do it well. It's sovereign-wealth fund raked in a return of round 1.028 trillion kroner, or $131 billion, in 2017 thanks to global stock market rallies, which let its profits swell to around one-third of its home-country's gross domestic product in 2017. The focus of the fund is to sustain, what is now, a very wealthy, resilient society with high quality living standards, world-class health care, education, and retirement systems.

Summary

IF these guidelines are followed in the evaluation of the local government proposal to the CFT, structural edits, revisions and adaptations can strengthen the proposal which will lead to the kind of structural reforms and economic stimulus which VBC wants and the community at large needs. Revisions following these guidelines will create a convincing proposal for CFT to accept.

Sources:
EU: Methodological Framework for the Principles of Public Administration, November 2017
OECD: Strategies for Aligning Stimulus Measures with Long Term Growth 2013
Full versions are available on line for download.

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Think Different; DO Change!

Issue Briefing Advices (Listed and numbered for easy discussion/reference: (Prepared for VBC Board Meeting: March 11, 2019

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7. Does the proposal have a beginning phase that is designed to be implemented as temporary and in the least distortive manner, with a clear and credible plan and timeline for phasing out as recovery takes hold. (with so-called "exit strategies"). Does it then show the structural reform strategy that replaces the temporary strategy?
8. Does the plan include structural tax reform that will not devastate the consumer?
9. Are the structural reform cuts structured in such a way that they cannot be overturned easily?

Section 3: **Guidelines for long term growth policies**

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