

Can Mongolia's Fiscal Stability Council Improve Fiscal Discipline?

Munkhsoyol Baatarjav

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Executive summary

Mongolia is one of the most mining-dependent countries in the world. According to the Ministry of Finance and other main statistics, in 2016, the mining sector accounted for 21 percent of the country's GDP, 85 percent of its exports, over 30 percent of the national budget revenue and over 70 percent of foreign direct investment.

In addition to economic growth, jobs and government revenue, mining also brought challenges to Mongolia. Resource revenues are volatile, which can lead to boom-bust cycles. Populist politics oftentimes incentivizes politicians to use finite resource revenue for immediate consumption rather than investing in long-term projects or a sovereign wealth fund. Addressing the challenges of volatility and exhaustibility requires a long-term policy to decide how much revenue to invest for the future, how much to spend on development projects and how much to disperse through other mechanisms.

Mongolia has developed a number of policies to manage resource revenues, including multiple fiscal rules and sovereign wealth funds, as well as distribution of resource revenues via direct cash transfers to citizens. In practice, the effectiveness of these tools has been weak. As a cornerstone of its revenue management policy, Mongolia adopted the Fiscal Stability Law in 2010, specifying multiple fiscal rules, including explicit debt, budget balance and expenditure growth limits. However, the government has modified these fiscal rules multiple times. Most recently, in 2016, it adjusted rules to accommodate its failure to meet its original budget targets. To date, there is no independent agency tasked with monitoring the rules or evaluating the sustainability of fiscal policy. A low score on the revenue management measure of the 2017 Resource Governance Index highlights the weaknesses of the fiscal rules and sovereign wealth fund governance.¹ This contributed to the country being largely unprepared for the recent fall of commodity prices, which ultimately pushed the country into a debt crisis.

Last December, the Mongolian parliament adopted a resolution to establish the Fiscal Stability Council (FSC) and approved its bylaws. The establishment of the FSC is an important step toward enhanced oversight. However, comparing the Mongolian bylaws to international standards reveals a number of shortcomings in the functions, transparency and safeguards of independence of the proposed FSC. I hence make the following main recommendations along the key considerations in the design and implementation of the FSC:

1 Dorjdari Namkhajantsan. "Resource Governance Index Points to state-owned Enterprises as Key Mongolia Reform Target" (Natural Resource Governance Institute, 2017), www.resourcegovernance.org/blog/resource-governance-index-points-state-owned-enterprises-key-mongolia-reform-target.

REMIT

- The current FSC bylaws list a number of government policy documents that the FSC should analyze and review. It is important to set one core assessment of fiscal rule compliance per year and to link that to the budget process (as in the case of Austria).
- The FSC should scrutinize and evaluate government forecasts, particularly mining revenue forecasts, to discourage over-optimism, which often leads to *ex ante* compliance, but evasion of responsibility for *ex post* deviations.
- The FSC's should support the Extractive Industries Transparency Initiative (EITI) in its effort to increase the transparency of the mineral sector .
- The FSC should establish a mechanism for coordination with existing agencies such as the Ministry of Finance, National Audit Office and National Development Agency, especially at the technical level on issues such as revenue forecasting and budget preparation.
- If the government modifies fiscal rules in the Fiscal Stability Law or evokes an escape clause, the FSC should review and evaluate these actions. Over time, the FSC can facilitate sensible amendments to fiscal rules without fearing excessive damage to credibility. For example, the FSC could provide medium-term reviews of fiscal rules and proposed amendments to it.
- The FSC should take on an increased role gradually; its remit should be refined to set list of tasks for the first year of operation.

INDEPENDENCE

- In order to strengthen the FSC's independence, government should only be able to abolish its existence through parliamentary resolution. Appointment of its members should be for fixed terms and non-renewable.
- To build public trust around the FSC, government should seek to elect the chairperson and members of the council with bipartisan support.
- The FSC should have sufficient staff (more than the two employees envisioned under the current bylaws) and have freedom in hiring them.
- Government should allocate sufficient resources to the FSC so that it may fulfill its tasks independently.
- Government should conduct the FSC nomination and selection process publicly and allocate no more than two seats to former politicians or high-level officials.
- Government should make a widespread public announcement seeking nominations for FSC appointments, giving sufficient amount of time. The selection process should be fair and competitive.

TRANSPARENCY AND ACCOUNTABILITY

- Government should define an appropriate communication and dissemination strategy that includes consultations and public hearings. The FSC can increase its role and reputation through communication and information dissemination to the public using different mechanisms such as organizing discussions and producing policy briefs.
- The FSC should have access to all relevant budget data and documents that significantly impact public finances. This may include mining contracts, annual accounts of key state owned enterprises, the balances of natural resource funds and off-budget entities.
- There should be a requirement for government or politicians to respond to recommendations made by the FSC on budget proposals, medium-term fiscal framework and budget laws.

CAPACITY

- The FSC should have mixed membership: some members with extensive government experience and others with more technical skills. Members should have diverse profiles but should all meet the basic criterion of being knowledgeable, skilled and having good reputations in order to gain the public's trust.
- The FSC should allow other existing watchdogs and civil society organizations in Mongolia, whose work focuses on budget transparency, accountability and citizen participation, to monitor the work of the FSC.

Introduction

The Mongolian economy is highly dependent on its mining sector. However, the volatile nature of the sector and frequent political upheaval are challenges to managing the economy. The government has struggled to ensure stable and sustainable growth amid such volatility despite many new policies and instruments it introduced throughout the past decade. This is in part a reflection of the government's weak commitment to follow through on the policies it has implemented and its lack of fiscal discipline. Ultimately, this led to high government expenditures, which have largely been financed by increasing and unsustainable levels of public debt. As a result, Mongolia had to resort to an International Monetary Fund (IMF) Extended Fund Facility (EFF) program in 2017 to access concessionary loans and to avoid defaulting on its sovereign debts. A condition tied to the bailout package was that Mongolia agreed to commit to reform its fiscal policy planning and implementation processes in order to improve fiscal discipline.

As envisioned by the government and the IMF, one of the main tools for fiscal reform would be the FSC. The IMF Article IV report detailing the EFF program for Mongolia states that “an independent fiscal council comprising from former prime ministers, ministers of finance, governors of the Bank of Mongolia, and other high-positioned individuals” will be established to provide “independent budget forecasts and macro projections. The council will prepare independent budget forecasts and costing of members of parliament's policy proposals, seek to enforce that off-budget vehicles are not being used to circumvent budget limits and monitor compliance with the Fiscal Stability Law.”²

A fiscal council can become a key entity to ensure reliable and unbiased forecasts of government revenue, including those from extractives. It can also determine whether government's policies follow fiscal rules and ensure long term sustainability. The IMF EFF requires that the Mongolian government prepare draft legislation to establish a fiscal council by the end of 2017. In line with this requirement, the Ministry of Finance proposed to amend the Integrated Budget Law to create the legal foundation for a fiscal council. However, the proposal was not supported by the parliament. Instead, a parliamentary resolution was approved setting out fiscal council bylaws. This document states that Mongolia's parliament, the State Great Hural (SGH), will establish a nine-member FSC under its budget committee. The FSC will aim to ensure the implementation of budget and fiscal stability laws, provide independent monitoring and evaluation of the potential impact of draft laws on the government budget and present their findings to the standing committee of parliament. It should be noted that the actual FSC has not been established as of July 2018, and the planning process for the government's budget for 2019 has started without FSC involvement.

2 International Monetary Fund (IMF), Country Report No. 17/140: *Staff Report For The 2017 Article IV Consultation And Request For An Extended Arrangement Under The Extended Fund Facility* (2017), 63.

Whether the FSC will improve budget planning, approval processes and fiscal discipline in Mongolia will likely depend on a number of factors, including proper implementation that reflects best practices from around the world, political will to ensure independence of the council, and technical expertise and leadership that provides credible and independent analysis of budget decision making. In this policy brief, I aim to provide analysis of the functions of fiscal councils around the world and draw conclusions relevant to the early plans for such an institution in Mongolia.

Fiscal council definition

A fiscal council is a permanent agency with a statutory or executive mandate to assess publicly and independently from partisan influence government's fiscal policies, plans and performance against macroeconomic objectives related to the long-term sustainability of public finances, short- to medium-term macroeconomic stability, and other official objectives. In addition, a fiscal council can perform one or several of the following functions: (i) contribute to the use of unbiased macroeconomic and budgetary forecasts in budget preparation (through preparing forecasts, or proposing prudent levels for key parameters), (ii) identify sensible fiscal policy options, and possibly, formulate recommendations, (iii) facilitate the implementation of fiscal policy rules, and (iv) cost new policy initiatives.³

This report is organized as follows. In Section 1, I will argue that a fiscal council can help Mongolia improve its fiscal discipline and ensure that recent woes of high deficits, mounting debt, and pro-cyclical spending are curtailed in the future, but that achieving these goals would require more ambitious reforms and political will to ensure the nascent fiscal council actually lives up to expectations. In Section 2, I discuss international experience of establishing and maintaining fiscal councils to provide analysis of how the proposed fiscal council in Mongolia compares with such institutions in other countries. Lastly, I provide conclusions and recommendations for the Mongolian government on how the bylaws can be amended to ensure the FSC is well-positioned to achieve its goals and fill in the existing gaps in prudent fiscal management. The report concludes with annexes providing the text of the FSC bylaws and common features of fiscal councils in different countries.

3 Lars Calmfors and Simon Wren-Lewis, "What should fiscal councils do?" *Economic Policy* 26, no. 68 (Mar 2011): 649-695.

I. How a fiscal council can help Mongolia

In Mongolia, the government's budget preparation, implementation and oversight processes are well established. However, research suggests that there is a room for further improvement, especially in terms of avoiding overoptimistic estimations of revenue and filling in the gap between laws and regulations and their implementation.⁴ In this section, I review the key laws and institutions Mongolia currently has in place for setting the fiscal policy, the rationale for establishing a fiscal council and the challenges that it may face, and the key attributes of the proposed FSC.

CURRENT INSTITUTIONAL ARRANGEMENT FOR FISCAL POLICY IN MONGOLIA

The laws currently in place to govern Mongolia's fiscal management of its resource revenue include the Budget Law, the Fiscal Stability Law, the Glass Accounts Law and the Parliament Procedures Law. The key institutions currently tasked with implementing these laws are the Ministry of Finance, the National Development Agency, the SGH and its secretariat, the National Audit Office, the Fiscal Stability Fund and Future Heritage Fund.

Despite having these laws and institutions in place, politicians have the power to change fiscal laws and rules relatively easily, and have exercised this power repeatedly in recent years.

The laws are described below and are listed in order of approval year.

Integrated Budget Law of Mongolia (2011)

In 2011, the SGH approved a revised edition of the Integrated Budget Law in order to improve the legal framework of budgeting, budget relations and fiscal management by merging the now defunct General Budget Law with the Public Sector Management and Finance Law.

The law introduced new provisions to ensure fiscal stability and transparency, to enhance the efficiency and predictability of resource allocation and to increase citizens' participation in the budgeting process. For example, under the new law, citizens play an active role in allocating and monitoring local development funds.

Article 10.2 of the Integrated Budget Law provides for the establishment of non-permanent National Budget, Financial and Economic Council comprised of representatives of non-government organizations, professional associations and scholars. This council was established in 2011 under the Prime Minister with the purpose of improving fiscal and economic policy planning, ensuring government fiscal transparency and exercising public oversight. The council has not functioned in practice due to lack of its power and capacity. The law also calls for the

4 NRG's 2017 report "Fiscal Sustainability in Mongolia" suggests that poor planning practices lead to systematic breaches of fiscal rules, and NRG's "Resource Governance Index" shows a big gap between existing rules and their implementation, including rules related to fiscal policy.

establishment of an independent research and analytical center to aid development of economic and fiscal policies under the auspices of the Ministry of Finance, but this center has not been established. If properly implemented, these institutions could have performed some functions now assigned to the FSC.

Fiscal Stability Law (2010)

The Fiscal Stability Law is the key mechanism for addressing challenges related to the extractives-based economy. The law was passed in 2010 and most parts of it came into effect in 2013. It set principles on the macro-fiscal management framework, created special fiscal requirements (rules), established a Fiscal Stability Fund, and put certain limits on the power of the SGH with regard to budget approval.

The Fiscal Stability Law established three explicit fiscal rules and a fund. In resource-rich countries, the design of appropriate fiscal rules is more challenging than in other countries. The characteristics of resource revenue, such as high volatility and uncertainty and dependency on exhaustible resources and mostly external markets greatly complicate the process. Therefore, some types of fiscal rules found in other countries are not applicable in resource-rich countries such as Mongolia. Fiscal rules are less common than resource funds as tools for fiscal management in resource-rich countries. However, they can play a critical role since, unlike resource funds, they are intended to constrain fiscal policies directly.

Mongolia introduced ceilings on the structural budget deficit, expenditure growth and public debt ratio as fiscal rules. The rules came to effect in 2013 and can be recalibrated every four years. The Mongolian government has not enforced the Fiscal Stability Law and circumvented the initial rules including raising the ceilings on the budget deficit and debt.

Fiscal Stability Fund (2010)

One of the by-products of the Fiscal Stability Law was the creation of the Fiscal Stability Fund to manage the volatility of mining revenues. Its main aim is to improve fiscal stability and discipline by providing safeguards against mineral price shocks. It is designed so that the government will accumulate savings during commodity price hikes and use them during economic downturns to sustain its expenditures.

The Fiscal Stability Fund receives transfers from the budget when actual revenues from mining exceed government estimates. In practice, however, when the Fund accumulated a modest amount in savings, the government relaxed withdrawal rules to address its large debt burden. As a result, no net financial wealth was accumulated and government incurred additional interest costs.⁵ Getting back on track with rigorous implementation of the Fund's deposit and withdrawal rules is an important component of strengthening overall fiscal discipline, and monitoring the Fiscal Stability Fund could be one of the main functions of the new fiscal council.

5 Andrew Bauer and David Mihalyi, *Premature Funds: How Overenthusiasm and Bad Advice Can Leave Countries Poorer* (Natural Resource Governance Institute, 2018), 3.

Glass Accounts Law (2014)

Transparency of fiscal policies is paramount to ensuring that fiscal rules are actually implemented in practice. For this purpose, the SGH adopted the Glass Accounts Law in 2014 to disclose the budget management processes and decisions through an information system (“glass accounts”) so that the public can monitor government spending.

All organizations funded by state and local budgets must dedicate a “Glass Accounts” corner on their website where the following information is required to be disclosed:

- Annual budgets, procurement plans and local development fund plans
- Semi-annual and annual budget performance
- Bid documents, bid procedures, tender/bid invitations, criteria for bidders, bid amount of grants and aids, and their allocation/expenditure

As concluded by the National Audit Office and a group of civil society organizations, the enforcement of this law has been insufficient.⁶ The new fiscal council can play an important role in monitoring the implementation of this law and, through its own disclosures, increasing fiscal transparency.

Law on State Great Hural Procedures (2007)

First adopted in 2007, this law regulates discussions on key policy documents such as government action plans, directives, monetary policy, budget law and execution of budgets at the SGH level. According to this law, budget proposals submitted by the executive should be discussed in four rounds so that recommendations from the standing committees including Budget Standing Committee and members of parliament and party caucuses, as well as institutions outside the parliament such as National Audit Office, can be incorporated and voted into the final budget document prior to receiving parliamentary approval. The FSC’s work should be integrated into the processes established by this law.

Future Heritage Fund (2016)

The Future Heritage Fund Law establishing a sovereign wealth fund was passed in 2016 and came to effect in 2017. The purpose of the fund is to create savings from mineral revenues and provide financial returns in the future when minerals are depleted. It is designed as a saving fund to accumulate funds for future generations and ease burden on budgets when mineral revenues subside. In addition, the fund is supposed to help avoid “Dutch disease” effects, as the investments of the fund will be exclusively in foreign assets. The fund will comprise of 65 percent of all royalty payments, dividends paid to state-owned enterprises by extraction companies and 50 percent of any potential new taxes on minerals. Beginning in 2030, 10 percent of the Future Heritage Fund’s net investment income will be transferred to the state budget annually.

6 National Audit Office of Mongolia, *Audit Report on Enforcement of Glass Account* (2017).

The IMF advised that the law on Future Heritage Fund should emphasize the importance of saving, but it should also be flexible enough to be realistic and not require savings in times of economic difficulty.⁷ Currently, the Future Heritage Fund's revenues will be fully used to retire liabilities of the Human Development Fund, which is projected by the government to be paid off in 2022. The timely establishment and performance of the Future Heritage Fund and implementation of its savings and withdrawal rules can be a part of the fiscal council's portfolio once the fund is established and operational.

Law on State Audit (2003)

The National Audit Office plays an important role in the budgeting process in Mongolia the Law on State Audit (2003) primarily regulates the work of this institution. Under this law, the National Audit Office performs financial audit of all state entities and the general government budget performance and provides a proposal on the executive's draft budget submitted to the parliament. Therefore, the National Audit Office currently comments on key aspects of fiscal policies including the executive's adherence to fiscal rules both in government budget plans and their actual implementation. This is a role that needs to be coordinated with the new fiscal council.

Given the mandates under these laws, functions usually performed by fiscal councils globally (discussed in Section 4) are currently shared by a number of institutions in Mongolia. Additionally, the Parliamentary Secretariat's budget analysis service provides technical support to members of parliament, standing committees and the SGH. Gaps and overlaps of responsibility existed prior to the decision to establish a fiscal council, the government would benefit from another look at the FSC bylaws to ensure its design addresses these gaps and overlaps and coordinates its functions with those of current institutions. The extant institutions are perceived to lack independence, the legal mandate and the technical expertise to act as a transparent and non-partisan monitor, succumbing to pressure of Mongolia's hierarchical political structure. This could be addressed by the new FSC.

KEY CHALLENGES AND RATIONALE FOR A FISCAL COUNCIL

Over the past decade, boom-bust commodity cycles have increased Mongolia's exposure to commodity exports. High commodity prices encouraged the government to spend excessively prior to the market downturn in 2008. Instead of cutting spending to reflect the economic reality, the government borrowed heavily, causing an economic crisis. In 2009, Mongolia received its first IMF bailout in the form of a USD 229.2 million loan.⁸ Not having learned its lesson from this earlier boom-bust cycle the government correspondingly raised spending by 56 percent from 2010 to 2011 up to 44 percent of its GDP, on the tide of exuberance brought by the Oyu Tolgoi copper-gold mining project and a rebound in commodity prices.

⁷ IMF, *Country Report No. 17/140*.

⁸ IMF, Press Release: *IMF Executive Board Approves US \$229.2 Million Stand-By Arrangement for Mongolia* (2009).

Since 2012, government debt has increased significantly because of politically-motivated spending despite stagnant budget revenues. Moreover, the government has been consistently overly optimistic about its revenue projections (by about MNT 1 trillion each year, equivalent to USD 406 million) leading to higher budget deficits. Parliamentary elections in June 2012 exacerbated the budget deficit because incumbent politicians spent funds to pander to voters. The Development Bank of Mongolia also engaged in significant off-budget spending that increased government debt. Domestic currency depreciation necessitated increased borrowing. These factors contributed to a public debt increase to over 80 percent of GDP in 2016. By 2017 it seemed likely that Mongolia was in danger of sovereign default.⁹

A set of fiscal rules and sovereign wealth funds modeled to respond to exactly such situations by reducing the pro-cyclicality of fiscal policy in the face of volatile resource revenues and promoting savings and sustainability did not work because the Fiscal Stability Law had been amended multiple times to increase debt and deficit limits.

The 2017 Resource Governance Index (RGI) reveals a large implementation gap—Mongolia has many fiscal laws, but has not been diligent about enforcing and adhering to its rules.¹⁰ Enforcement of laws and regulations related to transparency and accountability is especially weak. The Glass Accounts Law and the Open Government Partnership are examples of two institutions that the government created but failed to provide with adequate resources or authority. For example, necessary budget-related information is not fully available in the websites of budget entities and there is no regular monitoring as required by the Glass Accounts Law. The National Audit Office recommended that this be amended and that the information standardization be developed and applied.¹¹ The government should still significantly improve transparency and accountability of the sector through EITI and other instruments.

Revenue management should be further improved via prudent budget spending, adherence to fiscal rules, and better management of nascent sovereign wealth funds. The government devised the Fiscal Stability Fund and the Future Heritage Fund for this very purpose, but both bodies largely exist only on paper. As indicated by high deficits and the threat of defaults, the government budget remains unstable. Mongolia has not managed to conserve portions of its mining revenue for future generations, which is a result of politically-motivated spending and shrinking revenues. Rules governing these funds change often, and there is little publicly available information or scrutiny of these funds' policies.¹²

9 Andrew Bauer, Ragchaasuren Galindev, Munkh-Orgil Lkhagvajav, David Mihalyi and Nomuuntugs Tuvaan, *Fiscal Sustainability in Mongolia*, (Natural Resource Governance Institute, 2017).

10 Natural Resource Governance Institute (NRGI), *2017 Resource Governance Index, Mongolia Country Report* (2017).

11 National Audit Office of Mongolia, *Audit Report on Enforcement of Glass Account*, 20.

12 Dorjdari Namkhajantsan. "Resource Governance Index Points to State-Owned Enterprises as Key Mongolia Reform Target."

Consequently, Mongolia should benefit tremendously from a fiscal council, which scrutinizes and curtails excessive government spending and optimizes savings through austerity, rules adherence and more accurate revenue projection. Moreover, this council could play a coordinating role among the National Development Agency, Ministry of Finance, National Audit Office and the State Great Hural to improve transparency, limit off-budget and quasi-fiscal spending, reverse short- to medium-term pro-cyclical fiscal policy and avoid long-run boom and bust cycles.

KEY ATTRIBUTES OF THE PROPOSED FISCAL STABILITY COUNCIL

In late 2017, the State Great Hural adopted the bylaws of the Fiscal Stability Council. This legislation established the legal foundation for the FSC and regulates relations pertaining to the oversight of budget execution under the Fiscal Stability Law and ensuring fiscal sustainability. The following are the main remit of the FSC:

- Review and analyze the executive's proposals of annual budgets, medium-term fiscal frameworks and socio-economic development guidelines and draft laws pertaining to the budget and finance submitted to the parliament.
- Check compliance with the Fiscal Stability Law and fiscal sustainability of the above documents, and estimate the impact and burden on the state budget.
- Issue conclusions and recommendations with regard to the budgets.
- Provide information on fiscal issues to the public and ensure government's public financial transparency and disclosure.
- Upon request by the Budget Standing Committee, carry out studies of specific issues and provide recommendations.
- Disclose its reports to the public within three days of delivering them to the Budget Standing Committee.

The council would furnish its reviews, analyses, conclusions, recommendations, and other relevant information to the Budget Standing Committee and report on the implementation of the Fiscal Stability Law and its activities to the Budget Standing Committee on a semi-annual basis.

For the purpose of overseeing the implementation of the Fiscal Stability Law, ensuring fiscal and financial sustainability and conducting fiscal policy studies and analyses, the council will cooperate and exchange information with the Bank of Mongolia and Ministry of Finance.

The FSC will consist of a chair and eight members. The Budget Standing Committee, the Cabinet and the Bank of Mongolia will nominate two members each to the council. The Budget Standing Committee's secretariat will recruit three independent members through an open selection process. If the Budget Standing Committee does not accept a nominee, the same nominating body should propose another person within 14 working days. The FSC members will elect a chair by a simple majority vote.

The bylaws state that the FSC will be supported by a two-person staff to provide assistance to its members in fulfilling their functions, ensure normal operations of the council and furnish the council members with information necessary for making decisions.

The FSC is indeed designed to carry out important functions as one can see from the remit. However, given the history of independent oversight actors in Mongolia and elsewhere, the proposed setup for the FSC in Mongolia raises several issues related to the guarantee of operational independence, its ability to influence on the budgeting process, the quality of work that the FSC will be able to provide given limited resources and staff, and the political context related to gaps and overlaps in the work of the FSC and other existing institutions. Of key concern will be the FSC's ability to champion transparency and promote public engagement in budget policy debates. These issues are considered in more detail below in the light of international experience.

II. Fiscal council practices globally and their relevance to Mongolia

The purpose of fiscal councils, which are often referred to as “independent watchdogs,” is to promote sound fiscal policies. In evaluating fiscal councils globally and their relevance to the case of Mongolia, I consider the following questions:

- What is the rationale for fiscal councils?
- Do they complement or substitute fiscal policy rules?
- What are common features of effective fiscal councils?
- What are channels through which they can encourage sound policies?

As previously discussed, fiscal councils' main aims are to promote sound fiscal policy and long-term sustainability of public finances. Fiscal councils generally conduct forecasts, provide inputs into the planning and policy formulation processes (for example, by estimating costs of measures) and often make explicit recommendations on fiscal sustainability. In recent years, with the increase of quantitative macroeconomic targets, fiscal councils have increasingly been mandated to monitor compliance with such fiscal rules.¹³

Role of fiscal councils in Europe

Benoît Cœuré, member of the executive board of the European Central Bank, focuses on the requirements that national fiscal councils and the European Fiscal Board (EFB) should meet to be fully effective. He emphasizes the importance of fiscal councils being independent from government at both the national and European levels. The EFB is also charged with the important task of coordinating fiscal policy in the euro area to avoid pro-cyclical fiscal policies. “At this juncture using fiscal space would speed up the euro area’s return to growth and support the European Central Bank’s objective of medium-term price stability,” he explains. “But,” he says, “In many countries, such fiscal space simply does not exist, because rules have not been enforced in the past. Setting up independent institutions such as the fiscal councils at the national level and the EFB at the European level could prove to be a decisive step in this direction.”¹⁴

Countries adopt different forms of fiscal councils and they perform many different functions depending on history, context and reform needs. The IMF database of fiscal councils includes information of 39 member countries.¹⁵ There is also an Organization for Economic Co-operation and Development (OECD) database, which includes information on the fiscal councils of 21 countries (which are all in the IMF database as well).¹⁶ Information presented here comes mostly from the analysis of these two datasets.

13 IMF, *The Functions and Impact of Fiscal Councils*, (2013), 15.

14 Mario Draghi, President of the ECB, Vítor Constâncio, Vice-President of the ECB, *Frankfurt am Main*, 25 January 2018

15 IMF, *Fiscal Council Dataset*, (2016), <http://www.imf.org/external/np/fad/council/>.

16 Organization for Economic Co-operation and Development (OECD), *OECD Network of Parliamentary Budget Officials and Independent Fiscal Institutions (PBO)*, <http://www.oecd.org/gov/budgeting/oecdnetworkofparliamentarybudgetofficialspbo.htm>.

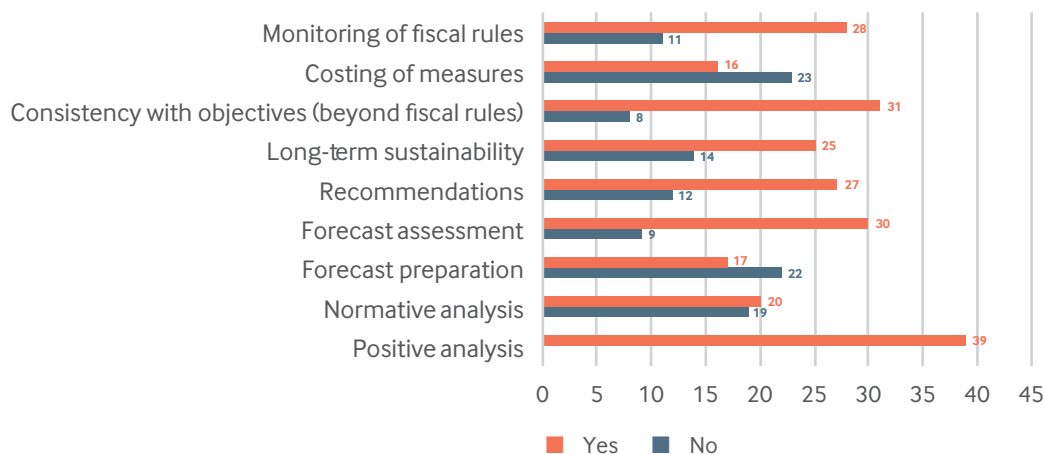
Fiscal councils were generally created as a response to economic downturn and/or financial crises or at times of structural reforms (such as in preparation for European Union membership). However, the root cause for considering and establishing fiscal councils most often has been the rise in public indebtedness and loss of fiscal discipline. The immediate and long-term implications of high public indebtedness can make social programs ineffective, and constrain growth and employment.

SPECIFIC ATTRIBUTES OF FISCAL COUNCILS

Mandate and key functions

Most fiscal councils have a mandate for restoring fiscal and debt sustainability along with increased fiscal discipline. Assessing forecasts prepared by the government, consistency of budgets with government's objectives, and monitoring of fiscal rules are popular functions that fiscal councils perform. In fulfilling this mandate, as shown in Figure 1, all fiscal councils concentrate on objective and fact-based positive analysis in budget formulation and implementation, whereas only half of the councils also engage in value and opinion-based (subjective thus cannot be proved or disproved) normative analysis.

Figure 1. Functions fiscal councils perform¹⁷



In the United Kingdom, for example, the Office for Budget Responsibility evaluates performance against targets by using the public finance forecasts to judge the government's performance against its targets for fiscal and welfare spending. For example, in January 2017 the government set itself two new medium-term fiscal targets: the structural deficit (cyclically adjusted public sector net borrowing) to be below two percent of GDP and public sector net debt to fall as a share of GDP by 2020-21. In its economic and fiscal outlook, the Office assesses whether it has a greater than 50 percent chance of hitting these targets under current policy.

In another example, Ireland's fiscal council assesses official forecasts produced by the Department of Finance. These are the macroeconomic and budgetary forecasts published by the department twice a year—in the "Stability Program Update" in the spring and in the budget in the autumn.

17 IMF, *Fiscal Councils Dataset* and author's calculation.

Most of the interventions by the fiscal councils naturally occur during the budget preparation and planning, i.e., by default they are engaged in *ex ante* analysis of fiscal policies. However, a majority of fiscal councils also performs *ex post* analysis of budget policies. (See Figure 2.) Roles such as fiscal policy coordination and other mandates beyond fiscal policies are rarely a priority.

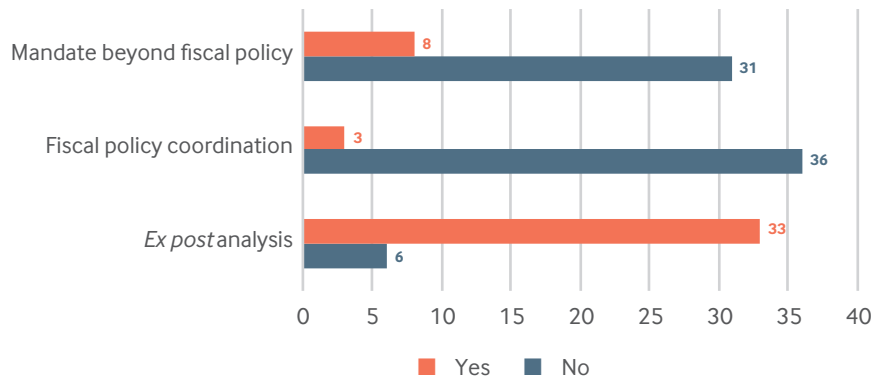


Figure 2. Functions of fiscal councils beyond *ex ante* analysis¹⁸

In most countries, fiscal councils have limited power in influencing the budgeting process. Fiscal councils, with the exception of Hungary's, cannot stall the budget process. Their forecasts are usually not binding and are not used in budget formulation. In eight countries, the government has to comply with fiscal council's recommendations or otherwise provide explanations. About half of councils organize formal consultations and hearings during budget debates. (See Figure 3.)

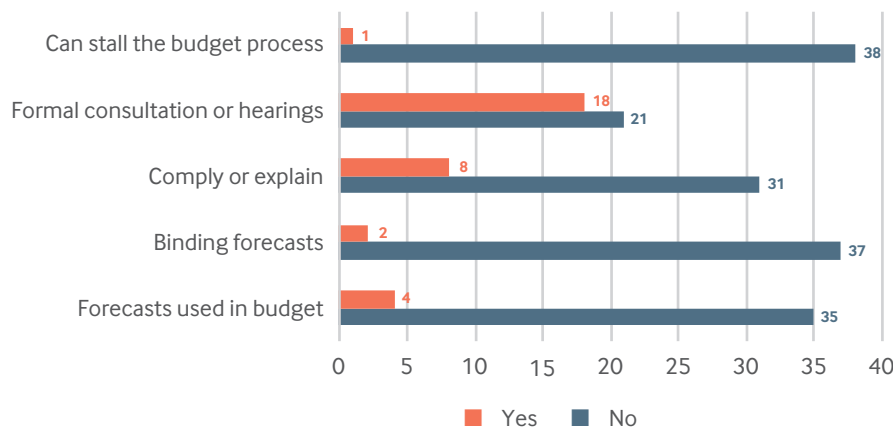


Figure 3. Powers of fiscal councils in budget process¹⁹

In terms of communicating their work, almost all of the fiscal councils in OECD countries (20) publish reports, but also send them to the legislature (19).²⁰ The exception is Chilean Advisory Fiscal Council, which actually does not produce any public reports. Two-thirds of fiscal councils engage in media publications, whereas seven of the councils do not have such engagement. To again use the example of the U.K., its Office for Budget Responsibility publishes briefing materials to inform people about its work, and provides a same-day briefing on the monthly public finances statistics in order to help the public interpret the data.

18 IMF, *Fiscal Councils Dataset* and author's calculation.

19 *Ibid.*

20 OECD, *OECD Network of Parliamentary Budget Officials and Independent Fiscal Institutions (PBO)*.

According to its bylaws, Mongolia's FSC will monitor fiscal rules, analyze consistency of budgets with government objectives, develop recommendations, focus on long term fiscal sustainability, and provide cost analysis for proposed projects. It appears that the FSC will review and offer analyses on most of the documents related to the state budget and fiscal policy and programs. One important aspect for Mongolia is adherence to fiscal rules and government objectives. Up until now, the National Audit Office has played a role of reviewing the compliance of budget laws with fiscal rules, but their findings and recommendations are non-binding. A few non-government organizations have tried to play a similar role, but do not have enough power to influence government decision-making. In order to monitor budget documents and policies, the FSC will need adequate resources and independence from government. It will also need valid data and timely information to perform its duties and tasks efficiently.

The bylaws of the FSC can be improved by defining a mechanism for coordination with existing agencies such as the Ministry of Finance, National Audit Office and National Development Agency, especially at the technical level on issues such as revenue forecasting, budget preparation, evaluation of fiscal rule violation or modification. The FSC should set one core assessment of fiscal rule compliance per year, and link that to the budget process. Over time, the FSC can help facilitate sensible amendments to fiscal rules so that the government can amend them responsibly and without excessive damage to its credibility. The FSC could be tasked with providing medium-term reviews of fiscal rules and proposed amendments.

There is no requirement for government to respond to the recommendations made by the FSC on budget proposals, approved medium-term fiscal framework or budget laws. The FSC could build partnerships with the public to increase the pressure on the government to respond to its recommendations, but this will require educating civil society and public on fiscal issues and involving them in the FSC activities. As of now, Mongolia's FSC is not designed to do formal consultations with non-government entities. The bylaws of the FSC state, "The communication and reporting of the FSC shall be only with/to the Budget Standing Committee."²¹ The Budget Law and the regulation of the Local Development Fund regulate public participation during budgeting, which is quite limited. Public participation has been low and the public does not possess sufficient information or power to influence the budgeting process. The bylaws of the FSC would do well to articulate a communications strategy that includes public hearings.

21 Government of Mongolia. *Bylaws of Fiscal Stability Council of Mongolia, Attachment to Parliament Resolution #83 (2017)*.

Functions performed by fiscal councils globally	Is Mongolia's FSC to perform this function?	Comments on FSC design
Macro-economic and fiscal forecasting/ assessing forecasts	Uncertain	Not explicitly mentioned in the bylaws, but in order to do analysis on fiscal sustainability, the FSC should do this at a certain level.
Evaluating performance against targets	Yes	The FSC will perform review and analysis of the executive's proposals of annual budgets, medium-term fiscal frameworks, and socio-economic development guidelines, and draft laws pertaining to the budget submitted to the parliament.
Sustainability and balance sheet analysis	Uncertain	Check compliance with the Fiscal Stability Law and fiscal sustainability of the above documents, and estimate the impact on the state budget. Issue recommendations with regard to the budgets.
Evaluation of fiscal risks	Yes	The FSC will provide independent evaluations and analysis of draft laws on government's budget, and provide recommendations to the Budget Standing Committee.
Scrutinizing tax and welfare policy costing	Uncertain	If required by the standing committee, the FSC can carry out studies of specific issues and provide recommendations to the standing committee.
Monitoring compliance with fiscal rules	Yes	Ensure the implementation of Budget and Fiscal Stability Laws.
Communication and reporting	Yes	The FSC is to provide information on fiscal issues to the public and ensure financial transparency in regards to the potential impact of fiscal policy decisions. It will disclose its reports and recommendations and provide explanations after three days of delivering them to the Budget Standing Committee.

Table 1. Key functions of Mongolia's fiscal council

Mongolia's FSC is not designed to conduct *ex post* analysis, which might be important given the absence of an efficient system of accountability and fiscal discipline. This role is currently assigned to the National Audit Office. While its conclusions and recommendations are discussed by the parliament, usually there are no mandatory follow up actions by ministries, agencies or public, which ensure accountability. Additional concrete provisions can be added in the bylaws of the council where it organizes public hearings on whether budgets achieved their objectives and met fiscal rules, *ex ante* analysis was taken into account and any follow up actions were taken.

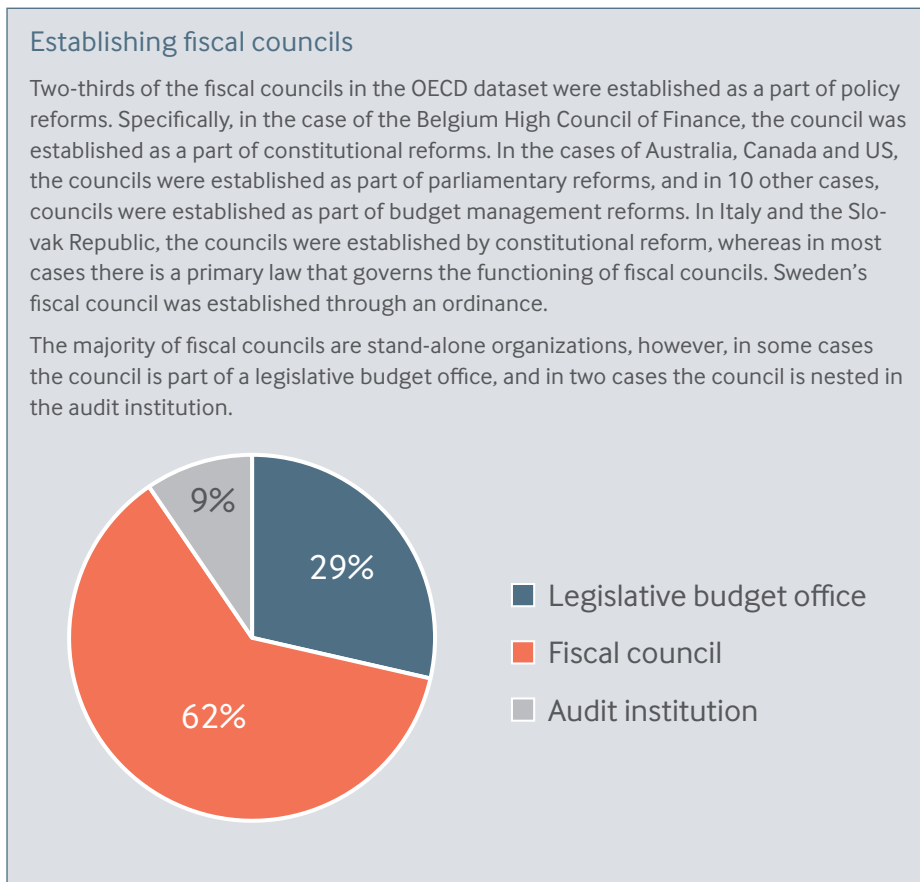


Figure 4. Institutional form of fiscal councils in OECD countries²²

Independence and institutional setup

Fiscal councils require a strong governance structure and independence from government in order to achieve their objectives. The notion of “independence” primarily refers to guarantees of non-partisanship in performing tasks—or operational independence—rather than the strict legal separation that the delegation of policy prerogatives requires. This explains the many forms that fiscal councils take and still qualify as “independent” institutions. In general, and without prejudice of its overarching objective to promote fiscal sustainability, the council would be expected to benchmark its assessments against official policy objectives, as using its own benchmarks could place it in the partisan fray and undermine its legitimacy.²³

Another characteristic of an independent fiscal council is the ability to openly present its analysis and conclusions without interference or fear of retribution from the executive or the legislature. Enshrining independence in legislation demonstrates political support for a fiscal council and a prerequisite for success. The following should also be considered for governance of fiscal councils:

- Appointment procedures that seek to guarantee professionalism, not political preferences;
- Long and non-renewable periods of office for the institution’s decision-making body;

²² OECD, *OECD Network of Parliamentary Budget Officials and Independent Fiscal Institutions (PBO)*.

²³ IMF, *Fiscal Councils Dataset* and author’s calculation.

- Restrictions on the government's freedom to fire the members of the institution's decision-making body;
- Outright prohibitions both against the government interfering with the institution's on-going work, and against the institution taking instructions from the government.

The choice of principal for a fiscal council can also influence its independence.²⁴

The examples of fiscal councils show that the governing body members are appointed either by the parliament (legislature) or the government (executive), but in about 21 percent of cases they are appointed by some other bodies as shown in the figure below. When it comes to the dismissal, in 15 cases it is the parliament's decision and in 10 the government's. In six cases other institutions have the right to dismiss the members of the fiscal council.

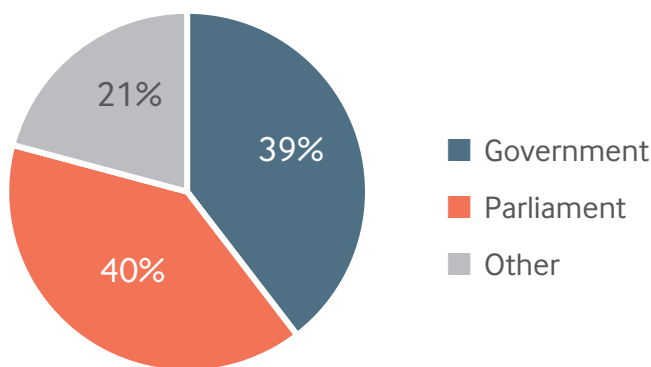


Figure 5. Institutions appointing members to the governing body²⁵

A key factor for independence from the political system is budgetary independence. A fiscal council should have a long-term budget, removing a temptation for governments to try and influence the council's work through the size of budget appropriations. Independence is also jeopardized if the council is not provided with sufficient resources but instead has to draw on the resources of a finance ministry or other institutions.

Another crucial factor for independence is accountability. When a fiscal council gets into conflict with the government, the latter may want to restrict its independence or reformulate its tasks. The best protection against this could be transparency of the work of the council so that the public can see the logic behind council's positions and regular peer evaluations of the quality of the council's work by councils in other countries or by international organizations such as the IMF and the OECD.²⁶

24 Calmfors and Wren-Lewis, *What should fiscal councils do?*, 17-18.

25 IMF, *Fiscal Council Dataset* and author's calculation.

26 Calmfors and Wren-Lewis, 18.

Figure 6 below shows that most of the fiscal councils have legal and operational independence from the government. Additionally, most fiscal councils have significant access to information, have their own staffs who possess enough expertise to perform functions prescribed to the fiscal council, and have the right to select staff on merit and without influence. There is however less insurance that fiscal councils' budgets will be sufficient to perform their duties—in half of the countries studied, fiscal councils have no right to determine their own budgets.

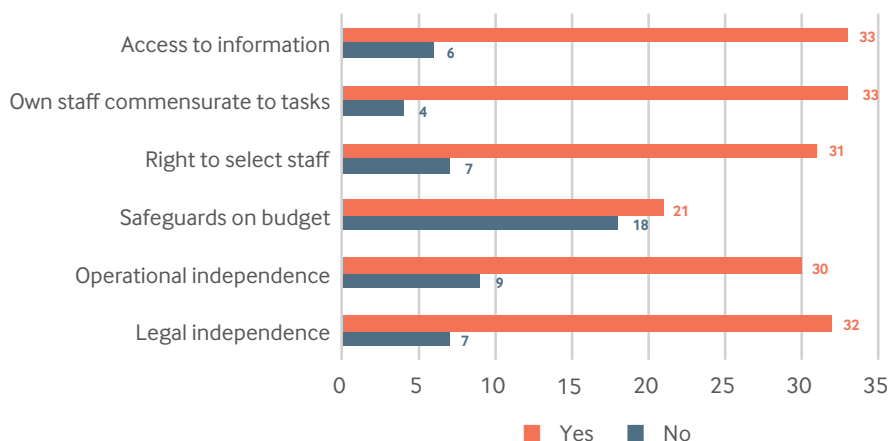


Figure 6. Independence of fiscal councils²⁷

In Mongolia, the risk of being dependent on government will be higher because the parliament is relatively small (76 members), and almost all cabinet members are also members of the parliament. The Budget Standing Committee, the Cabinet and the Bank of Mongolia are to nominate the majority of FSC members. While three of nine members will be openly selected, the Budget Standing Committee must approve them. FSC members have some protection in that its members cannot be dismissed for circumstances other than those explicitly states in the bylaws. The FSC chairperson will receive a salary and FSC members will be provided bonuses for their work—these financial incentives are intended to make them less susceptible to corrupting influence. The Fiscal Analytical Unit under the Budget Standing Committee will support the FSC's work and provide it with necessary information. The FSC will cooperate with the Bank of Mongolia and the Ministry of Finance to ensure that they provide it with necessary information.

27 IMF, *Fiscal Council Dataset* and author's calculation.

The FSC nomination and selection process should be conducted publicly and the appointment of former politicians should be limited. Only parliament should be able to abolish the council and the appointments should be for fixed, non-renewable terms. Building public trust around the FSC is key and could be done by seeking to elect the chairperson and members with bipartisan support. The FSC should have more than just two staff and have freedom in hiring them. To ensure its independence, sufficient resources should be allocated to fulfill its tasks.

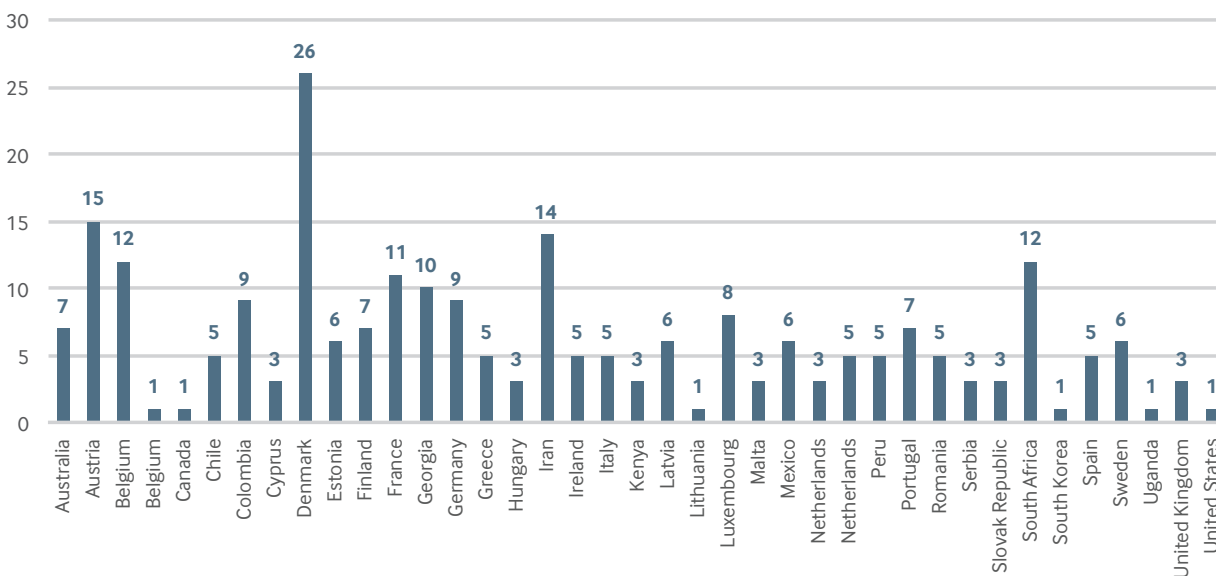
Key independence indicators from fiscal councils globally	Is Mongolia's FSC designed to ensure independence?	Comments on the FSC's design
Institutional independence <ul style="list-style-type: none"> • Legal independence • Timely access to information including detailed budgetary data 	Not definitive	There is only a statement for FSC to be independent and transparent. It is uncertain how these principles will be implemented.
Functional independence <ul style="list-style-type: none"> • Free to choose how to assess fiscal policy • Free to choose how to communicate with public 	Not definitive	The FSC bylaws need to be modified to add concrete communication mechanisms.
Personal independence <ul style="list-style-type: none"> • Appointments based on professional qualification • Fixed term 	Yes	Given the experience of functioning of other "independent" institutions in Mongolia, there is a high risk that the FSC will be politically affiliated since members are envisioned to be former politicians and/or high-level officials. Only three members out of nine will be openly selected, however, the Budget Standing Committee would still have to approve them.
Financial independence <ul style="list-style-type: none"> • Sufficient resources and budget to deliver their mandate • Should not be financed by the Ministry of Finance 	Yes	The FSC's own budget is to be discussed by the Budget Standing Committee as a part of the SGH's budget proposal.

Table 2. Key attributes to ensure Mongolia FSC's independence

Composition, leadership and resources

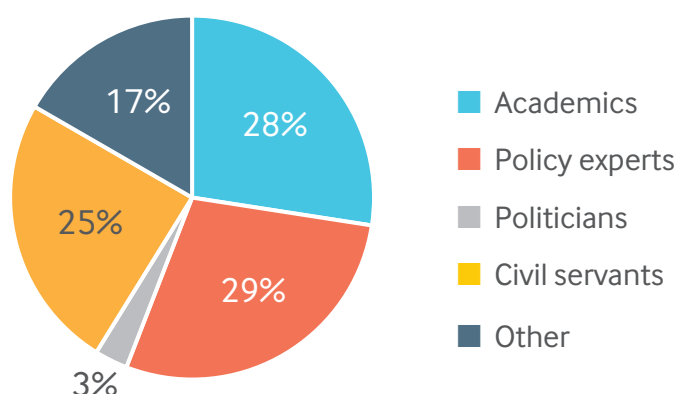
Figure 7 shows the composition of governing or high level management of fiscal councils in different countries. One can see that the numbers range from just one person in countries such as Belgium, Canada, Lithuania, South Korea, Uganda and the United States to up to 26 members in Denmark. The amount of paid staff also varies widely—from four to 236 with an average staff of 44. (See Table 3 in Annex 3.) On average, fiscal council staff contracts last 9.2 years (however, by removing the outliers of Netherlands (99 years) and Uganda (60 years), the average contract length is 5.2 years. Most countries allow the management to be reappointed. Half of the countries allow non-citizens to be appointed to their fiscal councils.

Figure 7. Number of members in governing bodies of various fiscal councils²⁸



There are at least four possible pools of people from which council members could be recruited: (i) academic researchers and civil society activists; (ii) public-finance experts from various parts of government administration; (iii) analysts in the financial sector; and (iv) former politicians. Globally, policy experts, academics and civil servants dominate governing bodies while politicians play a very limited role.

28 IMF, *Fiscal Council Dataset* and author's calculation.

Figure 8. Composition of fiscal councils²⁹

Academics' judgments are likely to be less affected by political concerns than those of most other groups because there is a high reputational cost in the academic sector for a researcher who is seen to be acting in a political way rather than making research-based judgments.³⁰ However, they may not have the expert knowledge necessary to make detailed assessments of budget bills. This is an argument for also including public finance experts with a background in government administration. There is a risk that public finance experts are more likely to be influenced by concerns over future career possibilities in government administration. Think tanks and non-government research institutions analysts present another possibility of less biased membership. Inclusion of former politicians with practical experience of economic policy making can lend legitimacy to a fiscal council. Since the work of fiscal councils is technically demanding, and capacity and political economy issues should be considered, the council must include people of strong standing and reputations who have skills and experience. Their work requires adequate technical support to produce broad fiscal policy assessments.³¹

In Ireland, for example, the fiscal council has a strong international dimension with three international members. Initial appointments to the council have been made on a staggered basis with terms of office ranging from two to four years. All detailed information of the meetings, along with the council's internal meetings and responses to the parliamentary questions relating to the fiscal council are publicly available and accessible on the Internet.

In another example, South Korea's National Assembly Budget Office (NABO) employs 135 people. The speaker of the national assembly appoints the chief of NABO in consultation with a steering committee. The term of office is not fixed and the speaker, with the consent of the steering committee, can remove the chief. The chief appoints staff based solely on competence without regard to political affiliation. Seventy percent of the staff is comprised of experts with advanced degrees in fields of fiscal policies, economics, public administration, statistics, accounting, law and public policy. The remaining workforce is responsible for its operations including human resources management, financing and information services.

²⁹ IMF, *Fiscal Council Dataset* and author's calculation.

³⁰ Calmfors and Wren-Lewis, 19.

³¹ Teresa Dabán and Jean-Luc Hélys, *A Public Financial Management Framework for Resources-Producing Countries*, (IMF, 2010).

In the case of Mongolia, the FSC chair will be elected by a simple majority of its members. Current elected officials are barred from FSC membership. FSC members should meet the following criteria: i) hold a degree in economics or finance, have at least 15 years of work experience in the field; or be a former prime minister, minister of finance, or central bank governor; ii) have no overdue balances on loans, guarantees and security agreements; iii) be of personal ethical values and reputation which are not expected to adversely affect the council's work; and iv) have no criminal record. The term of office of the chair and members is four years, and a member may serve a maximum of two terms. The Budget Standing Committee can release the council chairperson and members on the following rationale: i) the term of office ends; ii) the member is not able to perform official duties due to health and other reasons; iii) If the standing committee, by majority of the committee meeting vote, considered the member not fulfilling his/her duty in a satisfactory manner; and iv) the member submits a request for resignation.

It is uncertain how the composition of the FSC and the nominations process would be shielded from political interference. As previously discussed, in order to improve independence of the FSC, its nomination and selection process should be public and former politicians should be limited to a maximum of two seats. The public announcement of three members to be selected publicly should be widely distributed and the process should ensure fair and competitive selection. Moreover, having only two staff will seriously impact the effectiveness of the FSC, so the parliament should increase the number of staff.

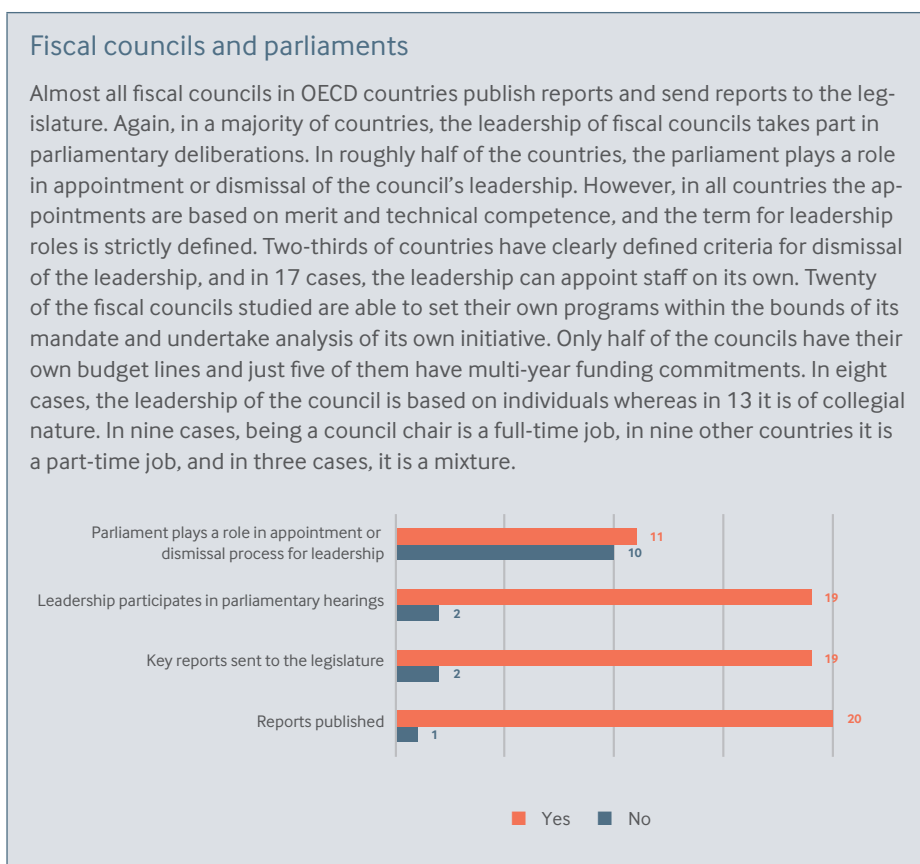


Figure 9. Relationship with legislature³²

32 OECD, *OECD dataset* and author's calculation.

THE FEATURES OF FISCAL COUNCILS IN RESOURCE-RICH COUNTRIES³³

Resource-rich developing countries, compared to others, may have more complex fiscal rules and policies as well as a higher need to improve fiscal discipline, but limited capacity to manage large inflows of revenue from the resource sector. Fiscal councils can therefore play an important role, but may also be taking up scarce human capital, so countries should ensure that they have an appropriate mandate and resources. In places with limited human resource capacity, fiscal councils can focus on the need for the advisory and auditing input that add value to what other institutions such as standing committees, audit offices and others already do, rather than performing overlapping roles or drawing on resources that may affect capacity in other institutions. Countries with limited capacity may benefit from setting relatively narrow remits for the council, at least in the initial stages. Once sufficient capacity and credibility have been attained and progress made, the functions of the council may be gradually expanded.

In Mauritania, the National Committee for the Monitoring of Hydrocarbon Revenue is composed of government officials and is chaired by its treasurer. Its responsibilities are limited: it publishes monthly information on daily oil production, sales, taxes collected and amounts placed in the petroleum fund and it estimates and monitors the transfers from the resource fund to the government.³⁴

The Petroleum Fund Consultative Council in Timor-Leste is an independent watchdog made up of former government officials. It comments on the annual transfer from the Petroleum Fund proposed in the budget. This transfer is a critical fiscal variable, as it relates to the estimated sustainable income from oil, and it finances the non-oil deficit in its entirety. Government savings for future generations are deposited and managed in the Petroleum Fund, and the transfer therefore reduces accumulated long-term savings held in the fund. The council can also advise Parliament on other matters relating to the performance and operation of the Petroleum Fund and on whether the appropriations of the Petroleum Fund are being “used effectively for the benefit of current and future generations.”

In Chad, the Petroleum Revenue Oversight and Monitoring Committee, a joint government–civil society entity (including representatives from the parliament and the supreme court), was given extraordinarily wide powers. Notably, expenditure commitments and payments from the oil budget (one of four separate budgets) required the prior authorization of the committee. In practice, this *ex ante* intervention in the expenditure circuit duplicated budget control mechanisms, delayed budget execution, and interfered with spending decisions. The committee also conducted *ex post* assessments of oil-financed expenditures, but weak technical capacity and resources severely hampered this function.³⁵

33 Rolando Ossowski and Håvard Halland, *Fiscal Management in Resource-Rich Countries: Essentials for Economists, Public Finance Professionals, and Policy Makers*, (World Bank Group, 2016).

34 Dabán and Héris, *A Public Financial Management Framework for Resources-Producing Countries*.

35 *Ibid.*

In São Tomé and Príncipe, the Petroleum Oversight Commission comprises of representatives appointed by the president, the National Assembly, local governments, business associations, and unions, and was granted wide powers of oversight of various oil accounts, as well as investigative and judicial powers. Besides issuing reports on topics subject to its oversight, the commission could initiate investigations of irregularities; carry out searches, inspections, and seizure of documents; and judge and enforce administrative proceedings of violations of the Oil Revenue Law.

In Mexico, the Center for the Study of Public Finances is a parliamentary entity. Its charge is the provision of objective, impartial, and timely analytical materials on public finances and technical support to the lower chamber and parliamentary commissions. The center analyzes and assesses fiscal plans; analyzes the fiscal impact of draft laws; reviews quarterly reports on the economic situation, public finances, and debt produced by the government; presents its own estimates and projections to congress; and reviews performance under the fiscal rule.

Colombia created a fiscal council in 2011 with a mandate to support the calculation of the cyclically adjusted balance as well as to oversee compliance with the fiscal rule. Peru also mandates the *Consejo Fiscal del Peru* to oversee compliance of fiscal rules, but only those that apply to states and local governments. The Brazilian Federal Court of Accounts only reviews compliance with fiscal rules *ex post*, however, in November 2016, the Federal Senate created the Independent Fiscal Institution which will act as a fiscal council, including overseeing and evaluating forecasts, assessing fiscal policy and overseeing the fiscal rules, but only for the federal government.³⁶ The U.K.'s Office for Budget Responsibility reviews compliance with fiscal rules, evaluates the impact of new policies by costing newly-announced tax and policy expenditures, as well as provides long-term projections of fiscal sustainability.³⁷

As also discussed before, Mongolia's fiscal rules are significantly related to its resource base, and the Fiscal Stability Fund is designed to respond to likely volatility of minerals revenues while the Future Heritage Fund is designed to generate savings. Strengthening overall budget processes is significant, but the new FSC can monitor the impact of mineral revenues on long-term budgets, the Fiscal Stability Fund, the Future Heritage Fund and fiscal rules. Moreover, reviewing Mongolia's annual EITI reports could be a part of FSC's remit. In order to do this, the FSC should have access to mining contracts, annual accounts of key state-owned enterprises, balances of natural resource funds and off-budget entities, which are all relevant data and documents impacting public finances significantly. The FSC in Mongolia should scrutinize and evaluate government forecasts, particularly mining revenue forecasts, which lead to *ex ante* compliance and evade responsibility for *ex post* deviations, to discourage over-optimism.

36 IMF. *Brazil Fiscal Transparency Evaluation*, May 2017, 7.

37 David Mihalyi and Liliana Fernandez, *How Did Fiscal Rules Hold Up in the Commodity Price Crash?*, (NRGI, 2018), 24.

III. Conclusions and recommendations

CONCLUSIONS

Mongolia continues to experience turbulent economic shocks caused by fluctuations of commodity markets. In response to these shocks, the country has devised a complex set of fiscal policies, which includes measures to promote countercyclical fiscal policy, comply with fiscal rules set out in the Fiscal Stability Law and accumulate reserves during commodity booms. These efforts were designed to help achieve sustainable growth in Mongolia's volatile environment, but results so far have not all been positive as the country continues to face a significant debt burden, run fiscal deficits, and struggle to fulfill fiscal rules. Much of this is related to the fact that politically-motivated decisions continue to override any attempts to improve fiscal discipline, and often-changing governments only exacerbate chances to effectively implement good fiscal policies. In this regard, establishing a fiscal council can improve budget planning, approval processes and fiscal discipline by providing independent monitoring of the Fiscal Stability Law and evaluating draft laws proposed.

But how effective it will be remains a question. Independent fiscal institutions vary between jurisdictions, and there is no single model suited to all political environments. Based on Mongolia's past experience with independent institutions and international practices, the FSC may benefit from further strengthening its status, role and responsibility along the lines of clarity of function, increased independence from the executive and legislature, and continuous capacity building. Without necessary credibility, independence and resources the FSC runs a risk that it will not be able to fulfill its roles, especially when some other institutions including parliamentary standing committees, the National Audit Office, the National Development Agency, the Ministry of Finance and other players have long established roles that may apparently be fulfilling the roles the FSC will perform. Further, politicians and the public may perceive the FSC as a temporary institution only to please the IMF as a part of a bailout package for Mongolia.

For the FSC to be successful, it is important that it adequately responds to the economic, political and public finance challenges Mongolia is facing, which are:

- Vulnerable economy and strong dependence on mining sector;
- “Boom and bust cycle”: Big budget deficit, high public indebtedness, and poor fiscal discipline
- Lack of compliance with fiscal rules as a result of frequent and ad-hoc amendments
- Weak track record and over-optimism in macro-economic forecasts
- Lack of oversight of resource revenues and sovereign wealth funds (the Fiscal Stability Fund and the Future Heritage Fund)

- Perceived lack of political will to reform current public finance management, especially in terms of limiting politically-motivated decision making that can stress fiscal sustainability
- Excessive parliamentary powers to make changes in proposed budgets, which often results in suboptimal spending and short-term prioritization
- Lack of transparency and accountability mechanisms and platforms for meaningful public discussions
- Capacity issues across the key government institutions and especially those relating to the planning and implementation of government budgets

A serious constraint on establishing an independent fiscal watchdog in Mongolia will be the issue of capacity and lack of political legitimacy to monitor and question the executive branch. Ideally, the FSC could play an important role in building awareness among legislators about the need for fiscal responsibility, especially where the parliaments has increased its checks on the executive.³⁸

The approved bylaws of the FSC are relatively vague on the issue of how the council will operate and fulfill its roles and responsibilities. The following are the main weaknesses of the FSC as currently envisioned:

- The provisions on its transparency and independence are quite weak.
- It is regulated by the parliamentary resolution, not by a law, which may lead to easy changes in the regulation and can lead to an unstable remit, political pressures, and difficulty in tracking impacts and thus lack of accountability.
- There are no established communication mechanisms with other institutions and the public, such as organizing consultations, public hearings and others.
- It is unclear what will happen if decision makers and politicians do not follow the Budget and Fiscal Stability Laws and recommendations made by council in submitted budget proposals, approved MTF, budget laws and fiscal policies.
- There is a risk that the institution is perceived as having only been established because of the IMF demand in the framework of the EFF program and may not stay permanently.

38 Stuart Webster, *Fiscal Councils, International Experience and Lessons for Mongolia* (The European Union's Economic Governance for Equitable Growth (EG4EG) Project for Mongolia, 2017).

RECOMMENDATIONS

In order to clarify the remit, protect independence, and ensure transparency and accountability as well as proper capacity, I recommend the following changes to the bylaws and the design of the FSC:

Remit

- The current bylaws list a number of government policy documents that the FSC should analyze and review. It is important to set one core assessment of fiscal rule compliance per year and to link that to the budget process (as in the case of Austria).
- The FSC should scrutinize and evaluate government forecasts, particularly mining revenue forecasts, to discourage over-optimism, which often leads to *ex ante* compliance, but evasion of responsibility for *ex post* deviations.
- The FSC's should support the EITI in its effort to increase the transparency of the mineral sector.
- The FSC should establish a mechanism for coordination with existing agencies such as the Ministry of Finance, National Audit Office and National Development Agency, especially at the technical level on issues such as revenue forecasting and budget preparation.
- If the government modifies fiscal rules in the Fiscal Stability Law or evokes an escape clause, the FSC should review and evaluate these actions. Over time, the FSC can facilitate sensible amendments to fiscal rules without fearing excessive damage to credibility. For example, the FSC could provide medium-term reviews of fiscal rules and amendments proposed to it.
- The FSC should take on an increased role gradually; its remit could be refined to set list of tasks for the first year of operation.

Independence

- In order to strengthen the FSC's independence, the government should only be able to abolish its existence through parliamentary resolution. Appointment of its members should be for fixed terms and non-renewable.
- To build public trust around the FSC, the government should seek to elect the chairperson and members of the council with bipartisan support.
- The FSC should have sufficient staff (more than the two employees envisioned under the current bylaws) and have freedom in hiring them.
- The government should allocate sufficient resources to the FSC so that it may fulfill its tasks independently.
- The government should conduct the FSC nomination and selection process publicly and allocate no more than two seats to former politicians or high-level officials.
- The government should make a widespread public announcement seeking nominations for FSC appointments giving sufficient amount of time. The selection process should be fair and competitive.

Transparency and accountability

- The government should define an appropriate communication and dissemination strategy that includes consultations and public hearings. The FSC can increase its role and reputation through communication and information dissemination to the public using different mechanisms such as organizing discussions and producing policy briefs.
- The FSC should have access to all relevant budget data and documents that significantly impact public finances. This may include mining contracts, annual accounts of key state owned enterprises, the balances of natural resource funds and off-budget entities.
- There should be a requirement for the government or politicians to respond to recommendations made by the FSC on budget proposals, medium-term fiscal framework and budget laws.

Capacity

- The FSC should include mixed membership: some with extensive government experience and others with more technical skills. Members should have diverse profiles but should all meet the basic criterion of being knowledgeable, skilled and having good reputations in order to gain the public's trust.
- The FSC should allow other existing watchdogs and civil society organizations in Mongolia, whose work focuses on budget transparency, accountability and citizens' participation, monitor the work of the FSC.

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Annex 1. Bylaws of Fiscal Stability Council of Mongolia

ATTACHMENT TO PARLIAMENT RESOLUTION #83 OF 2017

BYLAWS OF THE FISCAL STABILITY COUNCIL

One. General provisions

1.1. The purpose of these bylaws is to establish the legal foundation of activities of the Fiscal Stability Council (hereinafter referred to as the Council) and to regulate relations pertaining to oversight of the budget execution under the Fiscal Stability Law and ensuring fiscal sustainability.

1.2. The Council shall conduct an independent technical review of fiscal policy, issue conclusions and recommendations, and support activities of the Budget Standing Committee of parliament.

1.3. For the purpose of explaining the potential impact of the fiscal and financial policy decisions to the public, the Council shall provide information on fiscal issues to the public and ensure fiscal and financial transparency.

1.4. The Council may have an emblem expressing specifics of issues under its jurisdiction and shall use a stamp and letterhead printed in accordance with the set rules.

Two. Operating principles of the Council

2.1. The Council shall be guided by the principles of independence, non-partisanship, ensuring fiscal sustainability, protection of common and legitimate interests, free discussion of issues, and decision-making by majority vote in its activities.

Three. Areas of jurisdiction of the Council

3.1. The Council shall carry out the following functions:

3.1.1. Do a review and analysis of proposals of the annual budget, medium-term fiscal framework, and socio-economic development guidelines, and draft laws pertaining to the budget and finance submitted to parliament, check their compliance with the Fiscal Stability Law and fiscal sustainability, estimate the impact and burden on the state budget, and issue conclusions and recommendations.

3.1.2. Upon request from the Budget Standing Committee, carry out a study of specific issues and issue recommendations.

3.2. The Council shall disclose its report and recommendations and provide explanations after three days of delivering them to the Budget Standing Committee.

Four. Council meeting

- 4.1. The Council's main form of operations shall be a meeting.
- 4.2. The Council meeting's quorum deemed to be met if the majority of members arrived to the meeting.
- 4.3. If necessary, external experts and professionals can be invited to attend the Council meeting.
- 4.4. The Council meeting minutes shall be kept in detail.

Five. Council decisions

- 5.1. The Council shall make its decisions by majority vote, with the Council Chairperson signing them off to authenticate.
- 5.2. The Council's decisions made within its mandate shall be in the form of conclusions and recommendations.
- 5.3. The Council shall do a review and analysis, and prepare its conclusions and recommendations within 15 days after drafts of legal document specified in 3.1.1 of these bylaws were submitted to parliament, and deliver to the Budget Standing Committee.
- 5.4. For the purpose of implementing its mandate, the Council may contract out works to external and professional non-government organizations.

Six. The Council's relations with the Budget Standing Committee

- 6.1. The Council shall furnish its reviews, analyses, conclusions, recommendations, and other relevant information to the Budget Standing Committee.
- 6.2. The Council shall report on the implementation of the Fiscal Stability Law and its activities to the Budget Standing Committee on a semi-annual basis.
- 6.3. The Budget Standing Committee, if necessary, shall enquire the cabinet to provide relevant explanations regarding the Council's conclusions and recommendations.
- 6.4. The Fiscal Analytical Unit under the Budget Standing Committee shall support the Council's work and provide necessary information.

Seven. Council's relations with the Bank of Mongolia and Cabinet

- 7.1. For the purpose of overseeing the implementation of the Fiscal Stability Law, ensuring fiscal and financial sustainability, and conducting fiscal policy studies and analyses, the Council shall enter into a Memorandum of Understanding (MOU) on cooperation with the Bank of Mongolia and the Ministry of Finance.
- 7.2. The MOU shall cover such issues as obligations of and information exchange between the Bank of Mongolia, the Ministry of Finance, and the Council for the purpose of ensuring fiscal sustainability.
- 7.3. The Council shall be guided by the MOU specified in 7.1 of these bylaws in its relations with the Bank of Mongolia and the Ministry of Finance.

Eight. Council Chairperson and members, their appointment

8.1. The Council shall consist of a chairperson and eight executive members.

8.2. The Budget Standing Committee shall nominate two, the cabinet two, and the Bank of Mongolia two members to the Council. The Budget Standing Committee's Secretariat shall recruit three independent members through open selection process.

8.3. If the Budget Standing Committee did not accept the nominee, the authorized body specified in 8.2 of these bylaws shall nominate another person within 14 business days and present to the Budget Standing Committee's consideration.

8.4. The Council chairperson shall be elected from its members; the member who gets the largest number of votes will be appointed as chairperson.

8.5. The servant currently in political public position cannot be nominated and appointed as the Council chairperson and member:

8.6. The Council chairperson and members shall satisfy the following qualification criteria:

8.6.1. Hold a degree in economics or finance, have at least 15 years of work experience in the field; or former Prime Minister, cabinet member, Minister of Finance, or Central Bank governor

8.6.2. Have no overdue debt under loan, guarantee and security agreements;

8.6.3. Personal ethics and reputation are not expected to adversely affect the Council's work;

8.6.4. Have no criminal record.

8.7. Member of the council shall be obliged to attend the meeting at the time the meeting is announced at.

Nine. Term of office of the Council Chairperson and members

9.1. Term of office of the chairperson and members of the Council shall be four years and may be re-appointed once.

9.2. The Budget Standing Committee shall release the Council chairperson and members on the following rationale:

9.2.1. The term of office ended;

9.2.2. The member is not able to perform official duties due to health reasons and other excuses;

9.2.3. If the standing committee, by majority of the committee meeting vote, considered the member not fulfilling his/her duty in satisfactory manner

9.2.4. The member submitted a request for resignation.

9.3. The request for a release of the Council Chairperson and/or member from duties on the reasons specified in 9.2 of these bylaws shall be presented to the Budget Standing Committee by the body that nominated him/her.

Ten. Guarantee for the Council chairperson and members to perform their activities

10.1. It shall be prohibited to release and dismiss the Council chairperson and members except for the circumstances set forth in 9.2 of these bylaws.

10.2. The chairperson shall be provided with a salary and members, for the work they performed, will be provided with bonuses.

10.3. The Council's budget proposal shall be discussed by the Budget Standing Committee as a part of the parliament's budget proposal.

Eleven. Council Secretariat

11.1. The Council shall have a secretariat to provide assistance to its members in fulfilling their functions, to ensure normal operations of the Council and to furnish the council members with information necessary for making decisions.

11.2. The secretariat shall have up to two staff.

11.3. The secretariat of the Budget Standing Committee shall transform the Council's decisions and meeting minutes into an archive unit, and submit to the State Great Hural's archives.

Twelve. Confidentiality of internal information of the Council

12.1. It shall be prohibited for the Council member and secretariat staff to disseminate, share or use for personal purposes the information classified as internal information of the Council and not designated for the public, except for the circumstances set forth in the bylaws.

Annex 2. OECD Countries Fiscal Councils Dataset

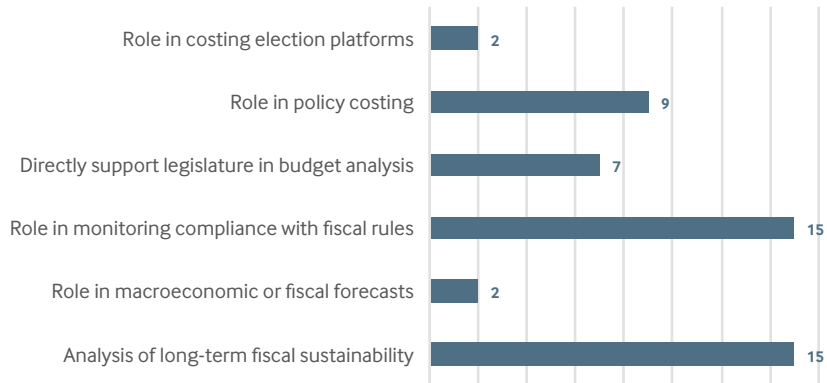


Figure 10. Functions fiscal councils perform

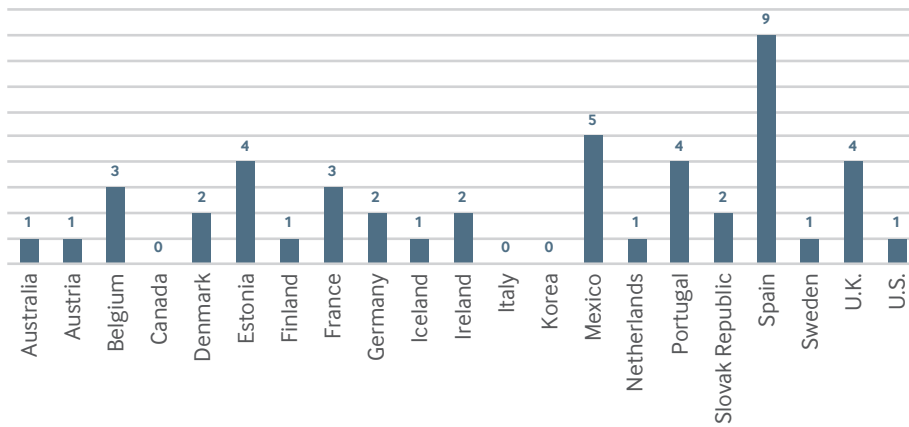


Figure 11. Number of reports required in legislation each year

Country	Who makes the final appointment of leadership?			
	Government only	Parliament only	Other institution	A range of stakeholders
Australia	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>
Austria	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>
Belgium	<input type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>
Canada	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Denmark	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Estonia	<input type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>
Finland	<input type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>
France	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>
Germany	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>
Iceland	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input checked="" type="radio"/>
Ireland	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Italy	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>
Korea	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>
Mexico	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>
Netherlands	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Portugal	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Slovak Republic	<input type="radio"/>	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>
Spain	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
Sweden	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
U.K.	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
U.S.	<input checked="" type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

Table 1. Appointment of leadership

Country	Institution name	Year	Budget
Australia	Parliamentary Budget Office (PBO)	2014	AUD 7 million
Austria	Fiscal Advisory Council (FISK)	n/a	Not disclosed
Belgium	High Council of Finance (HRF/CSF)	n/a	Not disclosed
Canada	Parliamentary Budget Office (PBO)	2014	CAD 2.8 million
Denmark	Danish Economic Council	2014	DKK 27.4 million
Estonia	Fiscal Council of Estonia	2017	EUR 0.07 million
Finland	Independent Monitoring and Evaluation of Fiscal Policy Function - National Audit Office of Finland	2015	EUR 0.7 million
France	High Council of Public Finance (HCFP)	2014	EUR 0.8 million
Germany	Independent Advisory Board to the Stability Council	2017	EUR 0.1 million
Iceland	Icelandic Fiscal Council	2017	EUR 0.3 million
Ireland	Irish Fiscal Advisory Council (IFAC)	2013	EUR 0.8 million
Italy	Parliamentary Budget Office (PBO)	2014	EUR 6 million
Korea	National Assembly Budget Office (NABO)	2013	USD 13.6 million
Mexico	Center for Public Finance Studies (CEFP)	2009	MXN 50.9 million
Netherlands	Netherlands Bureau for Economic Policy Analysis (CPB)	2011	EUR 13 million
Portugal	Portuguese Public Finance Council (CFP)	2014	EUR 2.53 million
Slovak Republic	Council for Budget Responsibility (CBR)	2015	EUR 1.3 million
Spain	Independent Authority of Fiscal Responsibility (AIReF)	2015	EUR 4.48 million
Sweden	Swedish Fiscal Policy Council (FPC)	2012	SEK 8.931 million
U.K.	Office for Budget Responsibility (OBR)	2014	GBP 2.075 million
US	Congressional Budget Office (CBO)	2011	USD 46.8 million

Table 2. Resources available to fiscal councils

Country	Staffing (full-time)			
	Staff	Chairs	Council/Board	Total
Australia	38			38
Austria	6		15	21
Belgium	14	3	24	41
Canada	17			17
Denmark	30	4	21	55
Estonia	1.5	1	5	7.5
Finland	4			4
France	2.5		11	13.5
Germany	1	1	8	10
Iceland	0	2	2	6
Ireland	5		5	10
Italy	30		3	33
Korea	138			138
Mexico	59			59
Netherlands	117			117
Portugal	15-20		5	22.5
Slovak Republic	15-20		3	20.5
Spain	35			35
Sweden	5		6	11
U.K.	17	3	2	22
U.S.	246			246

Table 3. Staffing of fiscal councils in OECD countries

Table 4. Tasks of fiscal councils³⁹

	Forecasting	Costing of policy initiatives	Evaluation of fiscal transparency	Ex post evaluation of fiscal policy	Ex ante evaluation of fiscal policy	Complement to fiscal rules	Evaluation of fiscal sustainability	Normative recommendations	Analysis of broader issues
Austria (Government Debt Committee 1997)	●	○	○	●	●	●	●	●	○
Belgium (Public Sector Borrowing Requirement Section of the High Council of Finance 1989)	○	○	○	●	●	●	●	●	○
Canada (Parliamentary Budget Office 2008)	●	●	●	●	●	●	●	○	○
Denmark (Economic Council 1962)	●	○	○	●	●	○	●	●	●
Germany (Council of Economic Experts 1963)	●	○	●	●	●	●	●	●	●
Hungary (Fiscal Council 2008)	●	●	●	●	●	●	●	○	○
Netherlands (Central Planning Bureau 1947)	●	●	●	●	●	●	●	○	●
Slovenia (Fiscal Council 2010)	●	○	●	●	●	●	●	○	●
Sweden (Fiscal Policy Council 2007)	●	○	●	●	●	●	●	●	●
U.K. (Office for Budget Responsibility 2010)	●	○	○	●	●	●	●	○	○
US (Congressional Budget Office 1975)	●	●	○	●	●	○	●	○	●

39 Lars Calmfors and Simon Wren-Lewis, *What should fiscal councils do?*, 24

Table 5. Members, independence and resources of fiscal councils⁴⁰

	Staff	Number of (full) members	Composition (multiple expertise areas possible)	Principal
Austria	N/A	14	Academics: 3 Government administration experts: 10 Financial analysts: 2	
Belgium	14	12	Academics: 4 Government administration experts: 5 Financial analysts: 2 Ex-politicians: 2	Government
Canada	14	1	Government administration experts: 1	Parliament
Denmark	35	4	Academics: 4	Government
Germany	20	5	Academics: 5	Government
Hungary	37	3	Academics: 2 Government administration experts: 1 Financial analysts: 1	Parliament
Netherlands	>170	1 (3) 4)	Academics: 1 (3) Government administration experts: 0 (1)	Government
Slovenia	0	7	Academics: 4 Government administration experts: Financial analysts: 2	Government
Sweden	4	8	Academics: 6 Ex-politicians: 2	Government
UK	?	3	Academics: 2 Government administration experts: 1	Government but parliamentary oversight
US	250	19)	Academics: 1 Government administration experts: 1	Congress

40 *Ibid.*, 26

Appointment by	Periods of office (years)	Renewability	Relationship to Ministry of Finance and central bank
Government: 6, Chamber of Commerce: 3 Federal Chamber of Labor: 3	4	Yes	Staff and funding provided by the central bank
Government (Royal Decree) ¹	5	Yes	Staff provided by the Ministry of Finance. Minister of Finance chairs the High Council of Finance, which the Public Sector Borrowing Requirement Section is a part of.
Government (in council) after submission of three names from review committee formed and chaired by the Parliamentary Librarian through the Leader of the Government of the House of Commons	5	Yes	Independent
Government after proposal from council itself	3	Yes	Independent
President on nomination by Government	5	Yes	Independent
Parliament on nomination by President, Governor of central bank and Head of National Audit Office	9	No	Independent
Minister of Economic Affairs	7	Yes	CPB is formally a branch of the civil service within the Ministry of Economic Affairs, formal meeting with Government before publication of annual report on fiscal policy
Government after proposal by Minister of Finance	5	No	Operating, administrative and technical tasks performed by the General Secretariat of the Government
Government after proposal from council itself	3 (1)	Yes	Independent
Chancellor, veto right for Treasury Select Committee in the Parliament	5	Yes	Semi-independent
Speaker of the House of Representatives and the President pro tempore of the Senate after recommendations from the two budget committees in Congress	4	Yes	Independent

Munkhsoyol Baatarjav is a consultant to the Natural Resource Governance Institute (NRGI).

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