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## FRANCE AND POLAND'S COMPLIANCE WITH EUROPEAN COMMITMENTS REGARDING FISCAL RULES

### Abstract

#### Abstract

This contribution deals with fiscal sustainability understood as “avoiding an excessive increase in government liabilities – a burden on future generations – while ensuring that the government can deliver the necessary public services, including the necessary safety net in times of hardship, and to adjust policy in response to new challenges”. The article aims the analysis of the legal framework for fiscal rules at the level of the EU and the national level in France and Poland. The research problem is to answer the question of how and whether the French and Polish regulations meet the international regulations in the field of fiscal sustainability. According to the research hypothesis, both countries only partially meet the EU requirements. The article is based on the detailed desk research method requiring analysis of the literature, statistical data, and EU and national legal regulations. The general conclusion is that both countries do not fully comply with EU commitments regarding fiscal rules.

**Keywords:** fiscal rules, sustainability, public debt, deficit

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## 1. Introduction

The issue of controlling the level of public debt and deficit is of great importance, as it is one of the pillars of the stability of public finances, and thus the entire state [Lotko, Zawadzka-Pąk 2016: 51]. The level of public debt is one of the crucial, even if not the only one, determinants of fiscal sustainability, understood as “avoiding an excessive increase in government liabilities – a burden on future generations – while ensuring that the government can deliver the necessary public services, including the necessary safety net in times of hardship, and to adjust policy in response to new challenges” [European Commission 2012: 1]. There is no defined upper limit to sustainable debt levels. The capacity to run high debts depends inter alia on the degree of development of financial markets, perceived risks, and trust in the capacity of a government to implement structural reforms and consolidate deficits. However, countries with high debt ratios are particularly exposed to market turbulences, such as changes in interest rates during times of large changes in economic prospects [European Commission 2012: 1].

Even if current generations of citizens may be pleased by the public debt accumulation used to finance public services, the excessive indebtedness may be dangerous for future generations. In extreme cases the excessive level of public debt decides about the undisturbed existence of states; significant public debt was one of the reasons for the bankruptcy of e.g. Argentina, and the problems thereof are being compared with the current situation of Greece [Zawadzka-Pąk 2018: 314]. The problem becomes more significant in the period of economic or, as recent events show, the epidemic crisis.

Due to the dangers resulting from excessive indebtedness, instruments for reducing the public debt and deficit are introduced both at the international and national levels. They take the form of so-called fiscal rules that are procedural or numerical. Procedural rules shape the rights and mutual relations of the participants of the budgetary procedure, while numerical rules, constituting a numerical limitation of the fiscal policy of the state, set the limit of the balance and budgetary (or more broadly, public) expenses, of the limit of public debt, or setting the minimum level of income [Kopits, Symansky 1998: 15; Corbacho, Ter-Minssian 2013: 40-41]. As results from the research conducted by the International Monetary Fund, the majority of countries in the world has introduced some kind of fiscal rules. As of end-2021, about 105 economies have adopted at least one fiscal rule. About 70 percent of countries with fiscal rules have a debt rule combined with operational limits on annual budget aggregates [Davoodi et al. 2022: 6-7]. Literature is reasonably positive about the fact

that rules are effective to enforce fiscal discipline [Afonso, Jalles 2019: 71]. There is a positive and significant effect of fiscal rules on sovereign countries' ratings [Fernández, Parro 2019: 588]. Moreover, fiscal rules reduce government borrowing costs [Thornton, Vasilakis 2018, 446]. In addition to the fiscal rules, some countries have established independent bodies to monitor the implementation of these rules, the so-called fiscal institutions (fiscal councils) that strengthen financial responsibility and discipline [Hagemann 2011: 76; OECD 2015: 38].

The increase in the number of fiscal rules came in a succession of waves, driven largely by the inclusion of supranational rules. For example, the large increase in the early 1990s reflected the signature Maastricht Treaty in 1992, which established the debt and deficit criteria for participation in the European Economic and Monetary Union (Eurozone) [Davoodi et al. 2022: 6; Buti, Giudice 2002, 823]. Within the European Union (EU) there are two groups of requirements regarding assuring fiscal sustainability related to membership in the Economic and Monetary Union. The current research concentrates on the legal framework of the examples of countries belonging to two distinct groups. France, being in European Union till 1958, adopted the common currency of the euro in 1999. In turn, Poland has been a member of the EU since 2004 and is not a member of the Economic and Monetary Union. The situation of public finance in both countries is differentiated. The following tables describe the state of French and Polish public finance using the data of general government gross debt, general government balance, and structural budget balance.

**Table 1. The situation of French public finance (data in relation to GDP)**

	<b>General government gross debt</b>	<b>General government balance</b>	<b>Structural budget balance</b>
<b>2011</b>	87.8	- 5.1	-5.0
<b>2012</b>	90.6	- 4.8	-4.2
<b>2013</b>	93.4	- 4.0	-3.3
<b>2014</b>	94.9	- 3.9	-3.0
<b>2015</b>	95.6	- 3.6	-2.7
<b>2016</b>	98.0	- 3.5	-2.7
<b>2017</b>	98.1	- 3.0	-3.1
<b>2018</b>	97.8	- 2.3	-3.1
<b>2019</b>	97.4	- 3.1	-3.5
<b>2020</b>	115.0	- 9.0	-4,8
<b>2021</b>	112.8	- 6.5	-5.7

Source: Eurostat and European Commission.

**Table 2. The situation of Polish public finance (data in relation to GDP)**

	<b>General government gross debt</b>	<b>General government balance</b>	<b>Structural budget balance</b>
<b>2011</b>	54.7	- 4.9	-5.9
<b>2012</b>	54.4	- 3.7	-3.9
<b>2013</b>	56.5	- 4.1	-3.3
<b>2014</b>	51.1	-3.6	-2.2
<b>2015</b>	51.3	- 2.7	-2.2
<b>2016</b>	54.2	- 2.2	-1.9
<b>2017</b>	50.6	- 1.5	-2.0
<b>2018</b>	48.8	- 0.2	-1.8
<b>2019</b>	45.7	- 0.7	-2.3
<b>2020</b>	57.2	- 6.9	-6.0
<b>2021</b>	53.8	- 1.8	-2.5

Source: Eurostat and European Commission.

The article aims the analysis of the legal framework for fiscal rules at the level of the European Union and the national level in France and Poland. The research problem is to answer the question of how and whether the French and Polish regulations meet the international regulations in the field of fiscal sustainability. According to the research hypothesis, both countries only partially meet the EU requirements. The article is based on the detailed desk research method requiring analysis of the literature, statistical data, and EU and national legal regulations.

## **2. Fiscal Sustainability Protection in European Union**

The EU legislator tries to protect the fiscal sustainability of the Member States using various types of institutional solutions. Numerical fiscal rules play a key role here. These rules were introduced in the EU in the 1990s, at the stage of building the legal framework of the Economic and Monetary Union. They are intended to prevent Member States from applying an excessively expansive model of fiscal policy. The use of this model harms the situation of all EU countries. The Economic and Monetary Union is a single financial market with free movement of capital. A state characterized by a high budget deficit may therefore reach for savings accumulated in other Member States. This contributes to an increase in long-term interest rates in the Economic and Monetary Union and a reduction in private-sector

investment (Panfil 2017: 117). Expansionary fiscal policy is also a significant threat to the monetary integration process. As many models of interaction between the government and the central bank suggest (review of these models in: Marszałek 2009: 121-133), the lack of budgetary discipline undermines the effectiveness of monetary authorities. In the long term, it is impossible to maintain the expansive fiscal policy and restrictive monetary policy. Such a situation may therefore become an obstacle to the achievement of the basic objective of the European Central Bank. This hypothesis seems to be confirmed by the experience gained during the debt crisis in the Eurozone.

The EU legislative solutions, which aim to protect the fiscal sustainability of the Member States, are based on Article 126 of the Treaty on the Functioning of the European Union (consolidated version Official Journal of the EU C 202 of 7.6.2016, p. 47; hereinafter: TFEU). It obliges all EU Members to avoid excessive deficits and creates a framework for the excessive deficit procedure. General provisions of Article 126 of the TFEU is clarified in Protocol No 12 attached to the TFEU. It introduces the reference value of the deficit and debt of the general government sector. These values are respectively 3% and 60% of GDP. Thus, the TFEU establishes two supranational fiscal rules applicable to all Member States. However, these rules are fulfilled by the provisions of Regulation (EU) No 549/2013 of the European Parliament and of the Council of 21 May 2013 on the European system of national and regional accounts in the European Union (Official Journal of the EU L 174 of 26 June, 2013, p. 1, as amended; hereinafter: ESA 2010) and Council Regulation (EC) No 479/2009 of 25 May, 2009 on the application of the Protocol on the excessive deficit procedure annexed to the Treaty establishing the European Community (Official Journal of EU L 145 of 10 June, 2009, p. 1, as amended).

The introduction of two numerical fiscal rules by the TFEU did not complete the process of building the legal framework for protecting the fiscal sustainability of the Member States. The next step was the adoption of the Stability and Growth Pact (hereinafter: SGP) in June 1997. It consists of three elements: Resolution of the European Council of 17 June 1997 on the Stability and Growth Pact (Official Journal of the EC C 236 of 2 August, 1997, p. 1), Council Regulation (EC) No 1466/1997 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies (Official Journal of the EC L 209 of 2 August, 1997, p. 1 as amended; hereinafter: Regulation No 1466/97), as well as Council Regulation (EC) No 1467/1997 of 7 July, 1997 on accelerating and clarifying the excessive deficit procedure (Official Journal of the EC L 209 of 2 August, 1997, p. 6, as amended). The Council Regulations included in the SGP constitute its preventive and repressive arm. Regulation No 1466/1997 requires Member

States to draw up stabilization or convergence programs, and Regulation No 1467/1997 supplements the excessive deficit procedure with a system of sanctions.

The legal framework for protecting the fiscal sustainability of the EU Member States has evolved under the influence of the experience gained during its period of validity. Particularly significant modifications took place in 2005, 2011 (the so-called six-pack), and 2013 (the so-called two-pack). However, changes in the legal status of the EU did not remove all the problems that arose in the practice of applying numerical fiscal rules. It was necessary to increase the automatism of certain stages of the excessive deficit procedure, strengthen the position of the European Commission and transfer the power to impose financial sanctions to the Court of Justice of the EU. In pursuit of these goals, on 2 March 2012, representatives of 25 EU Member States, including France and Poland, signed the Treaty on Stability, Coordination, and Governance in the Economic and Monetary Union in Brussels (Journal of Laws of 2013, item 1258; hereinafter: TSCG).

In almost 30 years of being in force, the EU fiscal rules have come a long way: from two relatively simple rules of the first generation to four more or less complicated rules of the second generation. This path leads from pro-cyclical regulation to solutions characterized by a high degree of flexibility, taking into account both exceptional circumstances and structural reforms. Together, EU regulations form a set of mutually complementary elements. The two oldest solutions – the debt rule and the general balance rule – set the boundary conditions for fiscal policy. Exceeding these boundaries is possible only as a result of extraordinary circumstances described by exit clauses. On the other hand, two newer solutions – the structural balance rule and the expenditure rule – build an appropriate fiscal space between the current fiscal indicators and the reference values set by the TFEU.

The basis of the structural balance rule can be found in the provisions of the resolution on the Stability and Growth Pact. According to it, Member States should keep the medium-term budgetary objective close to balance or in surplus. This obligation is specified in Regulation No 1466/97, which identifies the medium-term budgetary objective as the structural balance of the general government. At the same time, it sets the reference value of this balance for Eurozone Member States and those participating in the Exchange Rate Mechanism II. In their case, this value cannot be lower than -1% of GDP. These provisions are further tightened by the TSCG, according to which the floor of the structural balance is, as a rule, -0.5% of GDP. Setting the reference value at -1% of GDP is possible only for countries that meet two conditions. Firstly, their level of the general government has to stay well below 60% of the GDP. Secondly, these countries have to be characterized by a low risk of losing long-term fiscal sustainability. Unfortunately, these solutions are also binding,

in principle, only on the Eurozone countries. Other EU Member States are bound by the aforementioned provisions of the TSCG only if they so decide<sup>1</sup>. Unfortunately, Poland has not decided to take such a step so far, and consequently, it can independently decide on the reference value of the binding fiscal rule<sup>2</sup>.

The construction of the expenditure rule introduced by Regulation No 1466/97 is much simpler. For countries that have reached their medium-term budgetary objective, annual expenditure growth doesn't exceed a reference medium-term rate of potential GDP growth, unless the excess is matched by discretionary revenue measures. However, for countries that have not yet reached this target, the annual growth rate of expenditure must be lower than the mentioned growth rate of GDP.

The EU legislator did not stop at building supranational fiscal rules. It also forced an increase in the restrictiveness of the national budgetary frameworks of the Member States. This is achieved by the provisions of the Council Directive No 2011/85/EU of 8 November, 2011 on requirements for budgetary frameworks of the Member States (Official Journal of the EU L 140 of 27 May, 2013, p. 1; hereinafter: Directive 2011/85), and in particular its Article 5. This provision obliges all Member States to have national fiscal rules. In the long-term perspective, their goal is to support the implementation of the obligations imposed on the Member States by the TFEU in the area of budgetary policy. National fiscal rules should primarily support compliance with the general balance and debt benchmarks. From a legal point of view, the entry into force of Directive 2011/85 started the process of harmonization of the provisions regulating the budgetary framework of the EU Member States (Panfil 2021: 328). The legal basis for issuing this act was Article 126 sec. 4 of the TFEU. It is worth emphasizing that directives, which are a two-stage law-making instrument (Bartosiewicz 2009: 112), enable the approximation of the legal provisions of the EU Member States, and thus the achievement of common goals, while maintaining the separateness of national legal orders and respecting the legal institutions developed in them, which often have a long tradition (Biernat 2006: 204).

It seems that the EU Member States, wishing to fulfill the obligation resulting from Article 5 of Directive 2011/85, must choose one of two ways to achieve this goal. Firstly, they may decide to create original national rules which, at the level of reference values, will be at least as restrictive as EU rules. Secondly, it is possible to link national rules to supranational rules. This task can also be accomplished in two different ways. Firstly, solutions identical to

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<sup>1</sup> Bulgaria, Denmark, and Romania have so far adopted this solution.

<sup>2</sup> Currently, this value is -1% of GDP.

supranational solutions can be introduced into the national legal order. The first way is to introduce into national law solutions identical to those in force at the EU level. The second way is the full transposition of EU rules into national law through the use of references to supranational solutions (Panfil 2021: 343-344).

The situation has changed due to the outbreak of the COVID-19 pandemic. In the first quarter of 2020, the European Commission announced a communication on the activation of the general exit clause under the Stability and Growth Pact (Commission Communication of March 20, 2020), enabling the exclusion of the application of national fiscal rules in 2020. The Commission made such a decision taking into account the projected severe economic downturn as a result of the COVID-19 pandemic. Considering the development of the epidemiological situation, the Commission extended the application of the general exit clause also to 2021 (Commission Communication of September 17, 2020) and to 2022 (Commission Communication of March 3, 2021). The Commission did the same for 2023 (Commission Communication of May 23, 2022), due to Russia's invasion of Ukraine, high energy prices, disruption of supply chains, and the deteriorating economic situation of Member States.

### **3. Instruments Ensuring Fiscal Sustainability in France**

#### **3.1. Introduction**

The instrument ensuring the sustainability of public finances in France containing fiscal rules are the acts on public finance programming and financial (budget) acts. Acts on public finance programming constitute a special category of laws introduced into the French legal order by the revision of the Constitution of the Republic of October 4, 1958 (Official Journal of the French Republic of October 5, 1958). To this aim, the constitution was significantly modified by the constitutional law of July 23, 2008, on the modernization of the institutions of the Fifth Republic (Official Journal of the French Republic 24 July, 2008). As a result of this revision, around 30 provisions of the constitution were amended, in particular strengthening the role of the parliament and parliamentary committees. The current wording of Article 34 provides for the existence of a special category of acts, i.e. the acts on programming, which “set the objectives of the state’s activity and the long-term directions of public finance. The acts on programming are part of the objective of balancing the accounts of public administrations”.

The constitutional provisions, therefore, affirm that the acts on public finance programming target a goal, a direction to be achieved over several years, and that the concern for



respecting the financial balance of public administrations guides them [Querol 2018: 76]. These laws contain norms of a financial nature, but they do not have the character of a budget act, referred to in the French legal system as financial acts (fr. loi de finance). Financial acts define i.e. the level of public revenues, expenditures, and deficit.

The doctrine expresses the views according to which the acts on public finance programming should become what they seem to be, i.e. long-term financial acts containing binding norms for expenditure and public deficit [Querol 2018: 67]. However, the jurisprudence of the Constitutional Council does not confirm these expectations. The act on programming public finances does not infringe the prerogatives of Parliament when examining and voting on financial acts [Decision of the French Constitutional Council No 2012-658 DC of 13 December, 2012].

Based on the general constitutional authorization, three acts on public finance programming were issued covering the following periods:

- Act No 2009-135 of February 9, 2009 on the programming of public finances for the years 2009 to 2012 (Official Journal of the French Republic No 35 of 11 February 2009),
- Act No 2010-1645 of December 28, 2010 on the programming of public finances for the years 2011 to 2014 (Official Journal of the French Republic No 301 of 29 December, 2010),
- Act No 2012-1558 of December 31, 2012 on the programming of public finances for the years 2012 to 2017 (Official Journal of the French Republic No 1 of 1 January, 2013).

### **3.2. Acts on Public Finance Programming**

In the French legal order, there is a special category of acts, i.e. organic acts (fr. lois organiques), that aim at detailing constitutional provisions.

The first organic act regulating the content of acts on public finance programming was organic act No 2012-1403 of December 17, 2012 on the programming of public finance and governance (hereinafter: act No 2012-1403). Its issuing is strictly related to entering into force of Fiscal Compact. Based on the organic act No 2012-1403, two acts on public finance programming were issued covering the years 2014-2019 (Act No 2014-1653 of December 29, 2014 on the programming of public finances for the years 2014 to 2019) and 2018-2022 (Act No 2018-32 of January 22, 2018, on the programming of public finances for the years

2018 to 2022). Currently, till entering into force the organic act No 2021-1836 of December 28, 2021 on the modernization of public finance management, the content of acts on public finance programming is regulated by the amended organic act No 2001-692 of August 1, 2001 relating to finance acts (hereinafter: organic act No 2001-692). Currently, organic law No 2001-692 regulates comprehensively questions of public finance from annual and multiannual perspectives. However, based on the act 2001-692 in the current wording, no act on programming public finances has been implemented so far. The project of the act on programming public finances for 2023-2027 was submitted to French Parliament in September 2022. However, at first reading, the text was rejected in the National Assembly, while the Senate adopted a largely modified text. Meeting on December 15, the joint committee failed to adopt a common text. Consequently, the text remains under discussion in Parliament for a new reading, according to a timetable yet to be defined (Joder 2023). Hence, the subject of the analysis in the paper will be the act on public finance programming for 2018-2022 issued based on the organic act No 2012-1403 and the financial acts for the same period.

Articles 1-7 of the act on public finance programming for the years 2018-2022 set out the general directions of public finances of the French Republic. They contain, in particular, the values of the balance, debt, and public expenditure for individual programming years. Table 3 below presents data on the balances and public debt from this act.

**Table 3. Balances and public debt (in relation to GDP)**

	2017	2018	2019	2020	2021	2022
<b>Structural balance (1)</b>	-2,2	-2,1	-1,9	-1,6	-1,2	-0,8
<b>Cyclical balance (2)</b>	-0,6	-0,4	-0,1	-0,1	0,3	0,6
<b>Single and temporary measures (3)</b>	-0,1	-0,2	-0,9	0,0	0,0	0,0
<b>Actual balance (1+2+3)</b>	-2,9	-2,8	-2,9	-1,5	-0,9	-0,3
<b>Public debt</b>	<b>96,7</b>	<b>96,9</b>	<b>97,1</b>	<b>96,1</b>	<b>94,2</b>	<b>91,4</b>

Source: Article 2. of the Act on Public Finance Programming for the years 2018-2022.

The act on public finance programming also includes forecasts of the real balance for particular sub-sectors of the public sector, i.e. central, local, and social security. It also contains target values of public expenditure in relation to GDP (table 4). Such a solution is regarded as a fiscal expenditure rule.

**Table 4. Target values of public expenditure (in relation to GDP)**

	2017	2018	2019	2020	2021	2022
<b>Public expenditures, excluding tax benefits</b>	54,7	54,0	53,4	52,6	51,9	51,1
<b>Public expenditures, including tax benefits</b>	56,1	55,7	54,9	53,3	52,5	51,6

Source: Article 5 of the Act on Public Finance Programming for years 2018-2022.

### 3.3. Financial Acts

The act on public finance programming for 2018-2022 was the basis for deficit forecasts set out in financial acts for subsequent budget years. However, since the acts on public finance programming are not binding from the financial point of view, discrepancies between the deficit values adopted in the act on programming and those resulting from the financial act for a given year are possible. Moreover, the deficit values planned in the financial act may not be met either. The degree of implementation of the fiscal rule can be assessed through the comparative analysis of financial acts (fr. loi de finances) and approving financial acts (fr. loi de régleme) informing about the execution of financial acts.

The fiscal rules inscribed in the financial acts in France are budget balance rules. Their structure is not based on complex mathematical formulas, as in the case of the expenditure rule in Poland. The simplicity of the adopted solution lies in the fact that the structural balance (1), cyclical balance (2), single and temporary measures resulting in particular from the sanitary crisis (3), and the actual balance (1+2+3) are planned to be achieved. Details are provided in the tables below. The amounts presented in the tables are rounded to the nearest tenth, therefore the rounded amount of the actual balance may not be equal to the sum of the amounts used for its calculation.

**Table 5. Public administration balances in France realized in 2018 (data in relation to GDP)**

	Execution in 2018 resulting from the approving financial act	Financial act for 2018		Act on public finance programming for 2018-2022	
		Projected balance for 2018	Difference between projection and execution	Projected balance for 2018	Difference between projection and execution
Structural balance	-2,3	-2,1	-0,1	-2,1	-0,1
Cyclical balance	0,0	-0,4	0,3	-0,4	0,3
Single and temporary measures	-0,2	-0,2	0,0	-0,2	0,0
<b>Actual balance</b>	<b>-2,5</b>	<b>-2,8</b>	<b>0,2</b>	<b>-2,8</b>	<b>0,2</b>

Source: Approving financial act No 2019-811 of August 1, 2019.

**Table 6. Public administration balances in France realized in 2019 (data in relation to GDP)**

	Execution in 2019 resulting from the approving financial act	Financial act for 2019		Act on public finance programming for 2018-2022	
		Projected balance for 2019	Difference between projection and execution	Projected balance for 2019	Difference between projection and execution
Structural balance	-2,2	-2,3	0,1	-1,9	-0,3
Cyclical balance	0,2	0,1	0,1	-0,1	0,3
Single and temporary measures	-1,0	-0,9	-0,1	-0,9	0,0
<b>Actual balance</b>	<b>-3,0</b>	<b>-3,2</b>	<b>0,2</b>	<b>-2,9</b>	<b>-0,1</b>

Source: Approving financial act No 2020-937 of July 30, 2020.

Among all programming years (data for 2022 are not yet available), the largest deviations between the forecast resulting from the act on public finance programming for 2018-2022 and the implementation were recorded in 2020. Details are presented in table 7.

**Table 7. Public administration balances in France realized in 2020 (data in relation to GDP)**

	Execution in 2020 resulting from the approving financial act	Financial act for 2020		Act on public finance programming for 2018-2022	
		Projected balance for 2020	Difference between projection and execution	Projected balance for 2020	Difference between projection and execution
Structural balance	-1,3	-2,2	0,9	-1,6	0,3
Cyclical balance	-5,0	0,1	-5,1	0,1	-5,1
Single and temporary measures	-2,9	-0,1	-2,9	0,0	-2,9
<b>Actual balance</b>	<b>-9,2</b>	<b>-2,2</b>	<b>-7,0</b>	<b>-1,5</b>	<b>-7,7</b>

Source: Approving financial act No 2021-1039 of August 5, 2021.

The draft of approving financial act for 2021 was submitted to the French parliament on July 4, 2022. It is unprecedented that, as a result of the legislative procedure, the Parliament rejected this draft in its entirety on August 3, 2022. Therefore the act approving financial act for 2021 was not adopted. Thus, table 8 contains the data from the bill (draft) approving financial act for 2021.

**Table 8. Public administration balances in France realized in 2021 (data in relation to GDP)**

	Execution in 2020 resulting from the draft of approving financial act	Financial act for 2021		Act on public finance programming for 2018-2022	
		Projected balance for 2021.	Difference between projection and execution	Projected balance for 2021	Difference between projection and execution
Structural balance	-4,4	-3,8	-0,6	-1,2	-3,1
Cyclical balance	-2,0	-4,5	2,6	0,3	-2,3
Single and temporary measures	-0,1	-0,2	0,1	0,0	-0,1
<b>Actual balance</b>	<b>-6,4</b>	<b>-8,5</b>	<b>2,1</b>	<b>-0,9</b>	<b>-5,5</b>

Source: bill approving financial act for 2021.

The French Audit Court (fr. *Cour des Comptes*), assessing the 10 years of functioning of the acts on public finance programming, stated that the results are not satisfactory. Multiannual

programming is essential to strengthen the credibility and sustainability of public finances and to make the right public decisions. Public finance management has gradually received a constitutional and organic framework aimed at establishing and implementing a medium-term financial strategy for all public administration units [Audit Court 2020b, p. 26]. However, the objectives set out in the five acts on public finance programming adopted since the constitutional amendment in 2008 have rarely been achieved. While the financial crisis and recession of 2010 disrupted the first act, they do not explain the inability to follow the set trajectories thereafter, even though economic growth was close to potential. In practice, however, this mechanism remains ineffective in achieving the objective of balancing public accounts [Audit Court 2020a: 7]. The reason for the relatively high budget balance is the constant increase in public expenditure with a limited increase in public revenue. For instance, in 2019, public spending in France increased by 1.9% (Audit Court 2021: 49). A specific situation has taken place since 2020, which was caused by the Sars-Cov-2 virus epidemic. As a consequence, public spending in France increased by +6.5% in 2020 and +2.7% in 2021. However, as underlined by the Audit Court, without counting the funds allocated to reconstruction after the health crisis, expenditure has maintained sustainable growth (+1.1% in 2020 and +2.0% in 2021) (Audit Court 2022: 39).

#### **4. Instruments Ensuring Fiscal Sustainability in Poland**

##### **4.1. Introduction**

The fiscal sustainability protection system in Poland is based on original national solutions, which only in general terms refer to EU regulations. For over a quarter of a century, the most important element of this system has been the debt rule introduced by Article 216 sec. 5 of the Constitution of the Republic of Poland of 2 April, 1997 (Journal of Laws 1997, No 78, item 483 as amended; hereinafter: Polish Constitution). In the late 1990s, this rule was supplemented by a correction mechanism in the form of the so-called precautionary and remedial procedures. These procedures are now regulated in Article 86 of the Act of 27 August, 2009 on Public Finance (consolidated text Journal of Laws 2022, item 1634 as amended; hereinafter: PFA). For years, however, the Polish legislator did not attempt to supplement the fiscal sustainability protection system with other fiscal rules. This situation changed on 1 January 2011, when the so-called temporary spending rule came into rule. It was regulated in Articles 112a – 112d of the PFA. The temporary spending rule was the Polish legislator's response to the deteriorating condition of public finances. The sources of financial problems should be sought in the economic slowdown resulting from the global

financial crisis of 2007-2009. Unfortunately, the application of the temporary expenditure rule was suspended on 20 August, 2013, due to problems that arose during the implementation of the provisions of the 2013 Budget Act.

Another Polish expenditure rule (hereinafter: the stabilizing expenditure rule) was regulated by Article 112aa of the PFA, which entered into force on 28 December 2013. However, due to the shape of the budgetary procedure, the restrictions arising from this rule were applied for the first time during the work on the Budget Bill for 2015. Entry into force of Article 112aa of the PFA prompted the repeal of Articles 112a - 112c of the PFA and the amendment of the text of Article 112d of that Act. However, it should be emphasized that this step was already planned in the government's Plan for Development and Consolidation Finance 2010 - 2011 (Rada Ministrów 2009: 9-10). According to the drafters, the new stabilizing rule was to be counter-cyclical in nature and lead to the completion of the public finance consolidation process, including Poland's achievement of the medium-term budgetary objective set out in the Convergence Program. At the same time, the establishment of the stabilizing expenditure rule was supposed to be a form of fulfilling the obligations imposed on EU Member States by Directive 2011/85.

It is also worth noting that Poland is characterized by a very unusual choice of fiscal rules. From a theoretical point of view, the best complement to the debt rule seems to be the budget balance rule. In contrast, Poland is the only EU Member State that does not have such a rule at the national level. Consequently, it is only bound by two supranational budget balance rules. As can be seen from the data in Table 2 in the period preceding the outbreak of the Covid-19 pandemic, Poland had no problems meeting the constraints of the general balance rule. The high dynamics of GDP growth played an important role here. In contrast, Poland was unable to meet the constraints of the structural balance rule. The structural deficit exceeded the reference value of 1% of GDP throughout the research period. On the one hand, this circumstance explains why the Polish legislator has so far decided not to introduce the budget balance rule into the national legal order. On the other hand, it shows how important the right choice of fiscal rules is for the protection of fiscal sustainability.

#### **4.2. The Debt Rule**

According to Article 216 sec. 5 of the Polish Constitution, it is forbidden to take out loans or grant financial guarantees and sureties, as a result of which the national public debt will exceed 3/5 of the value of annual GDP. Thus, this provision constitutes a debt rule, which, however, is not suitable for operational use. The Polish Constitution does not provide any

guidelines on how the concept of public debt and annual GDP should be understood. It only requires that the method of calculating both of these values be specified in a legal act of statutory rank. In this way, it is the legislator who fills in the content of the constitutional debt rule, and thus influences the scope of restrictions imposed on public authorities. This situation, to some extent, contradicts the assumptions underlying the regulation of fiscal rules at the constitutional level (Skoczylas-Tylman 2010: 39).

While the methodology for calculating GDP in Poland is identical to that used at the EU level, the scope of national public debt differs significantly from the scope of general government debt. At the national level, the method of debt calculation is defined by Articles 72 and 73 of the PFA. Pursuant to these provisions, the national public debt is the consolidated debt of public finance sector entities derived from enumerated debt titles. At the same time, Article 9 of the PFA contains a closed catalogue of entities included in the public finance sector. This means that the debt of entities not listed in this catalogue does not affect the level of the national public debt. In this sense, the method of determining the subjective scope of the public finance sector in Poland is based on completely different principles than those adopted by the EU legislator in the ESA 2010. This circumstance creates a critical legal loophole, which has been used for years by the Polish public authorities to circumvent restrictions resulting from the national debt rule.

The level of national public debt can be adjusted to current political needs by transferring selected tasks of the state to entities located outside the public finance sector. An example here may be funds located in the state-owned Bank Gospodarstwa Krajowego (e.g. the National Road Fund, the Covid-19 Prevention Fund, the Armed Forces Support Fund), or the State Development Fund. On the one hand, these entities are not part of the public finance sector in Poland, on the other hand, they are part of the general government sector. As a consequence, the Polish and EU debt rules, despite their apparent similarity, refer to indicators describing different economic categories. The growing scale of this problem is evidenced by the statistical data contained in Table 9. As an aside, it should be emphasized that the decline in the debt-to-GDP ratio visible in recent years is not the result of a radical improvement in the condition of Polish public finances but has its source in dynamic inflationary processes.



**Table 9. National public debt and general government debt in relation to GDP (%) in Poland in 2017-2022**

	2017	2018	2019	2020	2021	2022
National public debt	48,3	46,4	43,6	47,8	43,8	39,4
General government debt	50,6	48,8	46,0	57,5	53,8	49,3

Source: GUS: <https://stat.gov.pl>; Eurostat: <https://ec.europa>.

A significant disadvantage of the Polish debt rule is the fact that it operates in a binary mode. Until the national public debt exceeds the debt limit, this rule does not impose any restrictions on the conduct of fiscal policy. Recognizing this fact, the Polish legislator supplemented the constitutional debt rule with a correction mechanism, i.e. prudential and remedial procedures. Along with the increase in the ratio of national public debt to GDP, these procedures impose increasingly far-reaching restrictions on state and local public authorities. A characteristic feature of the measures taken to protect the constitutional debt limit is their gradual gradation. They are intended to slow down the dynamics of the state's public debt (Ofiarski 2007: 40). Unfortunately, in practice, prudential and remedial procedures were changed each time they began to have a real impact on the way fiscal policy was conducted. As a result, they have been given a shape that is inadequate for the purpose that these procedures are intended to serve. It may turn out that the correction mechanism designed to protect the constitutional debt rule will be activated after the national public debt exceeds the reference value.

#### **4.3. The Stabilizing Expenditure Rule**

The constitutional debt limit is supplemented in the Polish legal order by a stabilizing expenditure rule. To put it simply, this rule links the permissible growth rate of expenditure of selected general government units with the medium-term dynamics of GDP and inflation. This solution is therefore to prevent excessive growth of public finances and stop politicians from abusing additional tax revenues that appear in times of good economic times. Unfortunately, these circumstances caused a temporary change in the shape of the stabilizing expenditure rule. At the end of 2015, the expenditure growth rate was linked to the central bank's inflation target, not the inflation rate. The existing structure of the stabilizing expenditure rule made it impossible for the ruling party to implement a new social program (the so-called 500+ program), the essence of which is the payment of benefits to

those raising children. It is worth emphasizing that in the middle of the second decade of the 21st century, inflation remained at a very low level or turned into deflation. Thus, replacing the inflation rate with the central bank's inflation target of 2.5% significantly increased the allowable level of spending. However, in 2022, the Polish legislator returned to the original structure of the stabilizing expenditure rule. So this time the central bank's inflation target has been replaced by the inflation rate. During the period of dynamic inflation processes, such a solution increased the spending limit. These circumstances illustrate the instrumental approach to fiscal rules by Polish public authorities.

Another problem with the stabilizing expenditure rule is that its constraints are very often circumvented by creative accounting. This type of action is facilitated primarily by the incorrectly constructed subjective scope of the rule. It covers selected units of the public finance sector, as well as funds deposited in Bank Gospodarstwa Krajowego. However, outside the subjective scope of the stabilizing expenditure rule is the majority of state special funds. This circumstance creates a critical loophole. Tasks traditionally financed from the state budget, which do not "fit" within the limitations resulting from the stabilizing expenditure rule, are simply transferred to newly created state special funds. This procedure leads to the "debudgetisation" of Polish public finances with all the negative consequences of this phenomenon. Limitations resulting from the stabilizing expenditure rule are also circumvented by substituting expenditures with other financial operations. For example, subsidies may be transferred not in the form of money but in the form of treasury securities. This solution allows public authorities to hide part of the state budget expenses.

The analysis of the application of the stabilizing expenditure rule in practice shows that its structure was adapted to current political needs. Moreover, the constraints of this rule have been circumvented by public authorities through the use of creative accounting. At the same time, in 2020 the stabilizing expenditure rule was temporarily suspended. This happened because the conditions triggering the rule's exit clause were met (announcement of an epidemic state on the entire territory of Poland and a simultaneous, significant decrease in GDP growth). In the following two years, public finances in Poland were on a legally defined path toward the target spending limit. Consequently, the stabilizing expenditure rule became fully applicable again from 2023 onwards.

## 5. Conclusion

The solutions discussed in this article adopted in France and Poland are guided by a common goal, which is to ensure the fiscal sustainability. EU regulations have a significant impact on

their shape. The solutions adopted in France and Poland differ significantly. The differences relate to the degree of complexity of the adopted solutions, content, and legal rank.

It is especially worth paying attention to the latter aspect because in France the effectiveness of fiscal rules and compliance with EU regulations were to be guaranteed by the constitutional rank of legal acts setting debt, expenditure, and public deficit limits. However, even though the acts on public finance programming are enshrined in the constitution, their provisions are often not applied in practice. As a consequence, both the first and second-generation EU fiscal rules are violated. Among the first-generation EU fiscal rules, there are debt rules (60% of GDP) and the public deficit rule (3% of GDP). France, with its debt approaching 100% of GDP, has not complied with the debt rule for many years. In turn, as regards the public deficit rule, only during the first two years of the Act on Public Finance Programming for 2018-2022 in force, the permissible level was not exceeded (data for 2022 will be known in mid-2023). On the other hand, when considering the EU fiscal rule of the second generation, i.e. the structural balance rule, in any year covered by the 2018-2021 programming period, France failed to achieve this indicator at the level of -1% of GDP, as it results from the Stability and Growth Pact, and even more at the level of -0.5% of GDP as it results from the Fiscal Compact. The main reason for France's non-compliance with EU regulations in the field of fiscal rules is the fact that the internally established national legal framework (Act on Public Finance Programming) is not respected. On the other hand, it should be positively assessed that in France the method of calculating the scope of the public finance sector is fully compliant with the principles adopted by the EU legislator in ESA 2010. Also, Polish experience related to the application of national fiscal rules does not inspire optimism. The constitutional debt limit is seeming of key importance for the protection of fiscal sustainability, but it is not suitable for operational use. Its content is fulfilled by the legislator, which undermines the importance of the fiscal rule included in the constitution. Another important problem is the clear lack of systemic assumptions underlying the Polish fiscal rules. Their different subjective scope means that they do not form a set of complementary elements. In addition, the credibility of Polish fiscal rules is undermined by frequent changes in their construction, as well as extensive circumvention of the resulting restrictions through the use of creative accounting and optimistic budget forecasting. Nevertheless, the situation of Polish public finances, assessed through the prism of the rules resulting from the TFEU, seems to be stable. Poland complies with the debt constraints and – at least temporarily – complies with the general balance requirements. It seems, however, that this state of affairs results rather from circumstances that are exogenous to fiscal policy, including the dynamics of GDP growth and inflationary processes. The actual situation of

Polish public finances is best evidenced by the fact that Poland has never managed to meet the requirements of the EU structural balance rule.

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