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INTERNATIONAL PERSPECTIVES ON COMMON FISCAL ISSUES

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HOUSE OF REPRESENTATIVES

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INTERNATIONAL PERSPECTIVES ON COMMON FISCAL ISSUES

WEDNESDAY, JUNE 5, 2002

HOUSE OF REPRESENTATIVES,
COMMITTEE ON THE BUDGET,
Washington, DC.

The committee met, pursuant to call, at 10:45 a.m. in room 210, Cannon House Office Building, Hon. Jim Nussle (chairman of the committee) presiding.

Members present: Representatives Nussle, Gutknecht, Watkins, Culberson, Brown, Putnam, Kirk, Spratt, McDermott, and Moore.

Chairman NUSSLE. Good morning.

Today we are holding a hearing entitled, "International Perspectives on Common Fiscal Issues" to discuss how different countries conduct the budget process and their approaches to solving some of the budgetary issues that, as countries, we all face.

We are looking forward to today's testimony to find different ways to address a number of issues. We will be looking at budgeting for emergencies, an issue that in fact just hit me as the chairman. Just yesterday, my district experienced, in some parts as many as 10 inches of rain and, as a result, quite a bit of local flooding which obviously, in some instances, requires the Federal government to be involved. How do we budget for these kinds of emergencies that come up from time to time?

Entitlement reform, as you may have—as our witnesses, you may have watched with some interest our battles that go on with regard to providing health care for seniors, as well as retirement security for seniors in what we call Social Security and Medicare as examples.

Performance budgeting, which I know a number of our witnesses have some experience with, and have some expertise to share with us—and for that matter, accrual accounting—issues that may be mundane and seemingly what we might call a budget wonk over here in the United States; these are issues that are important as we look at many different outcomes.

It is important for the United States to look at how other countries conduct their budget process so we may learn some ways to strengthen and improve our own budget. I have taken a personal interest in these particular budget issues that we are talking about today. I look forward to gaining personally some new insight on how to approach them from an international perspective.

This hearing is part of a larger effort this week to do just that. Tomorrow, I am honored to be co-hosting an international conference of budget chairpersons from around the world organized by

the Organization for Economic Cooperation and Development, commonly referred to as the OECD. We will cover some of the topics that we have talked about here today in more detail, and we will be discussing them with chairpersons of the parliamentary budget committees from around the world.

In addition, earlier this week, the Director of the Office of Management and Budget, Mitch Daniels, hosted a similar conference for his international counterparts, also organized by the OECD.

Today's hearing is intended to give you a preview of discussions we will be having at the conference. We are extremely pleased to have several of those international budget officials with us today to testify and give us their perspectives on these common fiscal issues.

Today, with us we have—and in advance I apologize for any mispronunciations:

Mr. Phil Bowen from Australia. Welcome. He is the General Manager, Budget Group, Department of Finance and Administration in Australia;

Mr. Peter Saurers, I believe from Switzerland, who is the Deputy Director, Administration of Federal Finances; and Mr. Mats Odell. Did I get that right?

Mr. ODELL. That is right.

Chairman NUSSLE. Who is the vice chairman of the Finance Committee of the Swedish Parliament.

I know that Ranking Member Spratt and the other members of the committee join me in welcoming you not only to our committee, but to the United States. We are very honored to have you and we look forward to a very informative discussion.

Mr. Spratt.

Mr. SPRATT. Quickly, let me echo what the chairman just said and extend to all of you a warm welcome.

We have some common problems, procedural and substantive, whether it is budget process, how to do it or whether it is entitlements, a problem that concerns us all. There is a lot that we can learn from your experience and, frankly, I think we should acknowledge we don't do enough in the way of comparative government in our government. We have such a big government that we are sort of satisfied that the whole universe is right here in our laps when in truth, you probably invented and devised some solutions that we would be well advised to take a look at.

So we are glad to have the opportunity to look at your lessons learned, to hear the problems that you are still coping with. We appreciate the fact that you are here and willing to testify.

Thank you very much for coming. We look forward for the next couple of days together.

Chairman NUSSLE. Just for the members present, we have a number of conference agenda items over the next 2 days, sponsored by the OECD and the Budget Committee. Members of Congress are welcome to attend any or all of these sessions and participate, and so we would welcome you to the committee for that purpose.

[The prepared statement of Mr. Putnam follows:]

PREPARED STATEMENT OF ADAM PUTNAM, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF FLORIDA

Thank you Mr. Chairman for convening this hearing. I would also like to thank our distinguished guests that have come from across the globe to be with us today to examine common fiscal issues.

My main objective here today is to understand how other governments conduct their budget processes. I believe that this conference provides a valuable platform for the Budget Committee in the U.S. and its equivalent counterpart abroad, to scrutinize one anothers efforts and achievements, as well as less successful initiatives. This conference affords us the opportunity to learn from one another, to gain the knowledge of experience by sharing practices, procedures and examining case studies.

There are three issues on the agenda that are of particular interest to me: budgeting for emergencies, entitlement reform, and accrual accounting. However, I would like to address only one of these issues at this juncture: accrual accounting.

Accrual budgeting is a method of financial planning that realizes expected long-term costs at the time that the assurances to incur those costs are made. There are three recognized benefits from the implementation of such an accrual accounting method. First, it encourages more efficient and effective resources management by recognizing costs. Second, it supports more decentralized and performance-focused management systems. Lastly, it provides better budgetary recognition of assets and liabilities.

Accrual budgeting, when used by other countries, has usually been adopted as part of broader reform efforts. The general consensus is that these reforms have been very positive. About half of the OECD countries use accruals in one form or another, usually to aid in financial management. However, under current U.S. law, most Federal programs use cash-based budgeting, leaving room for greater reform in the years ahead. Reform efforts in the U.S. could benefit a great deal from instituting accrual accounting standardization for some of our entitlement programs, such as Social Security and Medicare.

Spending on entitlement programs accounts for nearly two-thirds of the total Federal budget in the United States yearly. These expenditures are largely exempt from annual budget controls. They are effectively on cruise control. Long-term Social Security and Medicare reforms must be considered to ensure that Social Security will be solvent and relevant to current retirees as well as future generations of Americans. The objective must make Social Security sound for the next 50 years, not just the next fiscal year. These entitlement programs should start to use accrual budgeting to more accurately reflect their cost to taxpayers.

I want to especially thank our three witnesses: Mr. Bowen from Australia; Mr. Saurers from Switzerland; and Mr. Odell from Sweden. Thank you for your insights and participation. I believe that today we have an opportunity to examine this issue in further detail and perhaps learn about other examples in which accrual accounting has brought about real reform and positive change.

Let's begin today with Mr. Phil Bowen from Australia, General Manager of the Budget Group, Department of Finance and Administration.

Welcome. We are pleased to accept your testimony.

STATEMENT OF PHIL BOWEN, GENERAL MANAGER, BUDGET GROUP, DEPARTMENT OF FINANCE AND ADMINISTRATION, AUSTRALIA

Mr. BOWEN. Thank you, Mr. Chairman. Thank you for the opportunity to share with you the experience of the Australian Government over recent years in the development of its budgeting and reporting frameworks. My remarks relate to the implementation of the framework at the Federal government level.

Is that better?

Chairman NUSSLE. That is better.

Mr. BOWEN. OK. Sorry.

There are three key features of the Australian Government's budgeting and reporting framework, all of which are interrelated. These are budgeting on an accrual basis, budgeting and reporting

on outcomes and outputs, and devolution of management responsibility. Australia has been operating under this new budgeting framework since 1999.

The first element, budgeting on an accrual basis:

Prior to 1999 the Australian Government's budget was prepared on a cash basis only. Annual accrual reporting had been required for government agencies for a number of years, so the concept of annual accounting within government was not of itself new. However, preparation of budget estimates on an accrual basis required a new approach and made changes to the financial management systems of central and line agencies.

The induction of accrual information has added a new dimension to budget estimates. In addition to the important role that cash information provides, accrual information enables the full cast of government programs to be identified, along with the recognition of the impact that current decisions have on future budgets.

For the Australian Government, this is of particular importance in areas such as longer-term government employee entitlements, including employee pensions. Under cash budgeting, only the emerging cash impact of these entitlements was budgeted for. There was no recognition of the full cost of meeting the accruing liability for future employee pension payments, which is currently substantially greater than the annual cash outlay required to meet present employee pension payments.

These full costs are now recognized and budgeted for, along with the emerging cash requirements.

The move to accruals has not made cash measures irrelevant, and this is an important point. Cash and accrual measures complement each other in the information they provide. Cash information is important for measuring liquidity and the impact of government activity on the economy; accrual information better measures the sustainability of the government's financial position, in particular by identifying its emerging liabilities. This focus on longer-term issues has been strengthened by the publication in our most recent budget of an intergenerational report. This report looks at the impact of demographic factors on the Federal budget over the next 40 years.

The Australian Government is bound by legislation to prepare its budget in accordance with external standards. Accordingly, the Australian Government prepares the budget under the Australian accounting standards and also in conformity with the International Monetary Fund's Government Finance Statistics Convention.

The extent of financial information available under the new framework is greater than under the old and, thus, the level of transparency in budgeting and reporting has increased. The increasing harmonization of generally accepted accounting practices with the Government Finance Statistics Convention should help to lead to more simplified financial information in the future being presented for users.

The second feature of the Australian framework is that budgeting and reporting is conducted under an outcomes/outputs model. The resources made available to the government by the Parliament are appropriated to fund specific outcomes. Ministers have considerable flexibility in the deployment of these resources. Outcomes

may encompass a number of government programs that, taken together, are expected to have a particular impact on the Australian community.

Each portfolio minister is required to specify the outputs that will contribute to the outcomes of the portfolio. Portfolio ministers are also required to assign indicators of efficiency and effectiveness to their outcomes and outputs. These performance measures are reported publicly in the portfolio budget statements and annual reports of government agencies.

This model has been adopted to strengthen transparency in the reporting of government activities and to ensure that there is an accountability regime that focuses on results. The intention is that the Parliament and the community can assess what it is that the government and its agencies are achieving, the price at which the government's outputs are delivered, and the effectiveness with which these outputs are contributing to outcomes for the community. The auditor general and parliamentary committees play an important role in assessing the performance of agencies in the delivery of government programs.

However, the move to outcome/output budgeting and reporting has, in practice, also resulted in budgetary information being provided on a higher, more summarized level than previously when funds were appropriated at a lower program level. This has meant that some of the more detailed financial information associated with programs is no longer available to users of budget information. This is an area of the framework that is currently under review with the objective of restoring some of this information without increasing the complexity of the current budgeting and reporting arrangements.

The final future of the Australian budgeting and reporting framework is the increased level of management responsibility that has been devolved to chief executives of government agencies. Chief executives are responsible and are delegated authority from the minister for finance administration for the efficient, effective and ethical use of resources within their agencies. A number of powers previously held centrally have been devolved to agency chief executives. These include powers in relation to the remuneration of staff, the management of cash, and the preparation of budget estimates and financial statements.

Agencies have full responsibility for their own banking arrangements and earn interest on their cash holdings. These moneys are held within the official public account with the Reserve Bank of Australia and are monitored by the Department of Finance on a daily basis. Agencies provide the Department of Finance with summary financial data on a monthly basis. This enables the government to publish monthly financial statements and the Department of Finance to monitor agencies' financial performance.

The ability of the Department of Finance to have more timely access to agencies' financial performance information is currently subject to review with the objective of improving the quality and timeliness of advice to the government on budget estimates and program performance.

Performance reporting under the outcomes/outputs framework is an important accountability tool for agency chief executives, par-

ticularly in the highly devolved environment of the Australian system.

In conclusion, Mr. Chairman, at a time when there is increasing pressure for government agencies to perform and for the public sector to justify its share of the nation's resources, better measures of resource usage and performance have been welcomed by our government and the Parliament. Nonetheless, it will be important that the framework continue to evolve to provide a more robust budgeting and performance reporting system that supports sound resource allocation decisions and promotes transparency and accountability for achieving results.

Thank you.

Chairman NUSSLE. Thank you for your testimony.

Next we will hear from Mr. Peter Saurers from Switzerland, the Deputy Director of the Administration of Federal Finances.

Welcome. And we are pleased to accept your testimony.

STATEMENT OF PETER SAURERS, DEPUTY DIRECTOR, ADMINISTRATION OF FEDERAL FINANCES, SWITZERLAND

Mr. SAURERS. Well, thank you, Mr. Chairman. And I would like to start by saying how pleased I am and honored to appear before your distinguished committee.

The next remark would refer to the introductory remarks by Mr. Spratt when he said what can we learn from each other. One of the facts, that is, one of the main interests when I go to OECD, and the main results, is to take back information how other countries monitor and manage their affairs. When I give my testimony, I don't do it in a sense of, "look how you should do it," but rather just offering some information. And you will see to what extent you will derive something which is of value for you.

We talked about yesterday the political economy from reforms. When you talk about political economy, you already know what you ought to do, but you don't know how to implement it; and that is where I may give some contribution from our own country's experiences.

As you might know, we are a country with a long history of direct democracy. Direct democracy means you do more than just elect the Parliament. You can vote on issues; and the people, by and large, have two instruments at their hands.

First of all, 100,000 people can initiate a discussion, a vote, and a change in the constitution. And 50,000 people can at any time challenge a new law that has been adopted by Parliament. Those are the two main instruments.

And to what extent do they influence fiscal policy and to what extent, for instance, do we see some conclusions and draw some conclusions, how they affect political economy of implementing changes? In fiscal policy, our system foresees the tax rates are laid down in the constitution. The Parliament may not increase tax rates; they have to be approved by the people, and as a consequence, the budget basically at the Federal level is a discussion on the expenditure side.

Hardly ever do we vote on general tax increases. I believe the chances would be very small. They are bigger if they are earmarked like, for instance, in the old age security fund.

A couple of years ago we obtained a majority by the people to increase VAT to finance higher existing entitlements. So there is a great acceptance by the people to vote for higher taxes if they can see what use is made of them.

When we look at the issue now of reforms, of entitlement reforms—and let me say in our country right at the moment it goes far beyond simple Social Security and health insurance; we are a federalist state—we have a tight web between transfers between the Federal and state level, and they are as much of concern as Social Security.

In this context of direct democracy and entitlement reforms, I believe there are two things to be distinguished. First of all, does this direct democracy lead to better decisions? Second, will direct democracy react faster than another system of Parliament?

Regarding the first question: Is the outcome different than in a normal parliamentary agreement setting? I don't think it is very much different. People, by and large, vote along the same lines as Parliament. First of all, we elect members of Parliament and they should represent them; by and large, they should decide what we want them to decide. So I don't think that there is a big difference in outcome by the end of the day.

But on the other hand, I do believe that the system of democracy increases a faster awareness of problems. And if I recall, Mitch Daniels in his opening remarks at the OECD conference, he applauded in the way that, by and large, the general public does not care that much and how can we pass the message on to them.

I do believe the system of initiative, 100,000 people, 100,000 signatures, that is quite easy to come by in the first place, although we are a much smaller country. But it is easy to come by; and therefore, you get it on the floor of Parliament, and government is obliged to address the issue. They can't postpone it and put it in a drawer. They have to discuss it and to submit it for a vote of the people. And in the forefront of these votes there is a debate, particularly on TV, as well.

I do believe the awareness is created through that system. There I think you get a faster response by the general public, and maybe it will also influence afterwards the results.

The sign just lit on saying "stop." I don't know if you want me to carry on. I would just use another 2 minutes on emergencies.

How do we deal with emergencies? We decide on a budget and we have got mechanisms which allow either the government or a selected number of members of Parliament to decide on additional expenditures throughout the year. By and large, government never makes use of this right because government is aware of the fact that the budget, as such, is a matter of the Parliament. But however it can occur, it hardly ever does.

And the next step is that 6 out of 246 members of Parliament—we have got a coalition government—may make decisions. We had such a case last year in the context of the rescue of Swiss Airlines where an injection of about 1 billion Swiss francs had to be approved. And these six members, they decided and Parliament afterward approved their decision, acknowledged their decision.

They didn't really decide to sign off on it. But in the matter of that decision, we had the argument, is it correct that six members

of Parliament may take such decisions of a far-reaching consequence, 1 billion Swiss francs. That, out of a budget of 50 billion, is quite a huge amount of money.

We had a discussion going on, not yet decided, but I believe by the end of the day we shall leave that system as it is. That means we don't put emergency money in the budget as items, but rather have mechanisms where either government or a selected number of members of Parliament may decide on additional expenditures.

Thank you.

Chairman NUSSLE. Thank you for your testimony.

Our final speaker on this panel is Mr. Mats Odell from Sweden, vice chairman of the Finance Committee for the Swedish Parliament.

You are welcome. We are pleased to receive your testimony.

STATEMENT OF MATS ODELL, VICE CHAIRMAN, FINANCE COMMITTEE, SWEDISH PARLIAMENT

Mr. ODELL. Thank you, Mr. Chairman. Well, first of all, I am also very grateful to have had opportunity to take part in this meeting.

I would like to focus on two things: first of all, the big Swedish budget reform after the disastrous beginning of the 1990s, where we created very, very big deficits in our budget. Secondly, I would like to focus on our experiences in performance budgeting, especially in evaluation and follow up of goals and results in the budget process.

But I must say that the Swiss system is as far as you can come from the Swedish system. We have a tax rate of 54 percent of GDP, and I don't know what the people would have voted if they had the possibility to take steps by step. Perhaps we would have been where we are, but I am not quite sure.

And this high exposure to the budget cycle is, of course, one of our big problems. During the 1990s, Sweden experienced a spectacular deterioration and then recovery of its budget balance. From substantial surpluses in the late 1980s, the budget went into a deficit that reached more than 10 percent of GDP. And the budget for 1993 had a deficit of almost 14 percent of GDP.

Well, when we looked upon this status, it indicated that one of the structure reasons for the crisis was what you would call lax budget process. It was noted that in the 1970s, the preparation phases, as well as in the processing of the budget bill by the Riksdag, the Parliament, were skewed toward adding expenditure.

I think you are well aware of this tendency in the United States. Most of that growth was in social welfare, transfer programs sensitive to general developments in the economy, of course, which increased the volatility of the budget.

Well, then we decided to make reform and to bring the Swedish budget back into balance in the short term and to end this structure tendency toward expenditure growth. A system of top-down associating of budget constraints was introduced in 1996. And overall ceiling on total centrally financed expenditure is now set for 3 coming fiscal years. The 3 coming fiscal years are set in advance, and the ceiling is broken down into ceilings for 27 expenditure

areas. The latter ceilings form the framework of the preparation of the actual budget bill tabled in September.

When the Riksdag processes the budget bill, voting is done in two stages, first on the expenditure area envelope and only subsequently on the appropriations. The consequence is that a motion or an amendment to increase a particular appropriation must be accompanied by a proposal for how to increase it to be financed; that is, what other appropriation or appropriations within the expenditure area should be reduced. And this is, of course, a big problem.

Secondly, I can tell you there is no longer a possibility to pick the most interesting things for the opposition; the entire opposition must have a complete alternative to the government's budget bill if they want to. Or if we want—since I belong to the opposition, if we want to change any detail, we have to present a total covering to the government's budget from the Left Party to the Conservative Party; and you can imagine that is not very likely to happen.

So our system is also prepared for minority government's possibility to survive and to present responsible budgets.

The second thing I would like to say is about this Swedish Parliament how we try to integrate evaluation and follow-up of goals result in the budget process. Well, evaluation and scrutiny are important tools in any budget system, but with performance budgeting it is indeed necessary that the Parliament receives good information by the government. The Swedish budget act states in general terms that the government should provide the Parliament with information about targets, outcomes and performance.

The government provides much of its information in the budget bill, but there are also other channels as well. The Swedish budget is as I mentioned, divided in 27 expenditure areas. The government has asked to submit reports focusing more exclusively on performance information for all expenditure areas from next year, year 2003; and these reports are not supposed to cover everything within the expenditure area, but rather focus on some activities.

Well, the government submitted two reports with performance information only a week ago and we read them with great interest. One report is about the goal for culture policy. This goal concerns equality.

I don't know if you have goals like that in your budget process—equality, in the sense that all citizens should have the access and make use of various culture activities such as theaters, libraries and art exhibitions. According to the report, the efforts made by the state have contributed to equality in this sense, while we would have been surprised if it hadn't. That is fine.

But the conclusion in the report indicates the problem with governing by objectives and results; the conclusion is that in order to keep the high levels of culture activity and to improve culture activity further, the state's effort should continue to improve. While who can say anything against that, I can assure you that the political opposition will not say that the state efforts will not improve. We may disagree with the government on the level of expenditure for public culture, for instance, but the efforts can always be improved.

The other report submitted to the government concerns matters that are politically contested, more contested. And this report gives

an account for Sweden's implementation of the European Union's employment strategy. I will not go into any detail, but the European Union, as well as the OECD, has stated several times over the years that Sweden should lower its taxes on labor and deregulate its labor markets. As I indicated above, these matters are central to the political debate, and performance information may indeed create interest among the parliamentarians.

Well, Mr. Chairman, I could give you briefly or so what we have said in the finance committee, and also the Parliament has decided that we ask the government to be more precise about the goals. The goals and the objectives should be formulated in a way that makes it possible to follow up, for example.

The performance information must be relevant in relation to the objectives. Results should, to a larger extent, be given in quantitative terms, and the information should make it possible for the Parliament to assess the fulfillment of the goals. That is not always the case. The information should, to a larger extent, focus on outcome and performance and less on specific measures and so on. And we have listed what we want and what we expect from the government.

Well, Mr. Chairman, these are some of our experiences, and thank you for your attention.

Chairman NUSSLE. Thank you.

[The prepared statement of Mats Odell follows:]

PREPARED STATEMENT OF MATS ODELL, DEPUTY CHAIR, COMMITTEE ON FINANCE OF THE SWEDISH RIKSDAG

Mr. Chairman, dear participants, in the annotated agenda for the OECD Symposium for Chairpersons of Parliamentary Budget Committees, it was suggested that parliamentarians do not really use the result information that is submitted to them. This implies that valid information is not taken into account when decisions are made. It is also a waste of resources to produce information that is not used. This is probably a fairly common problem.

I will make a few remarks on this problem, relating from my experience in the Swedish Parliament. I have to admit that we also suffer from this problem, but sometimes the political interest for goals and results is high.

Let me start with the goals themselves. One reason for the apparent lack of interest may be that the goals and targets often are fairly technical. If the goals are more political, the parliamentarians will also be more interested.

But how should we know if the goals are politically interesting? One test can be to ask whether the different political parties can agree on the goals. If both the government and the opposition think that the goals are fine, there is actually a risk that nobody cares about the goals. It is hard to disagree on goals such as "the financial system should be stable and in order". Most goals are probably not very contested. For instance, most parliamentarians want sustainable economic development or, at another level, safe roads.

But it is possible to set up goals that encourage political debate.

I belong to the Christian Democrats, one of the opposition parties in the Swedish Parliament. We, the opposition parties, have set up a goal that Sweden should achieve 3 percent growth in the Gross National Product (GNP) every year. Our policies in various areas have to contribute to this goal. For instance, the labor market must function well if this goal should be achieved. There must also be more and freer competition in some areas where the public sector now is the only employer or at least a very dominant employer.

My point here is that goals and objectives may indeed be relevant for the political debate and may show the differences between the various political alternatives.

We have also had a political debate about another goal. The social democratic government set up a goal a few years ago that the open unemployment should decrease by half, from 8 percent to 4 percent. We, in the opposition, have been critical because we think that this goal has led to a focus on wrong matters. Simply put, it

has been more important for the government to put people in labor market measures than to create conditions in order to get what you may call real jobs.

These two examples show that goals—and results—may indeed cause political interest. These goals show the differences in the political debate.

I would now like to say a few words about another aspect. In the Swedish Parliament, we try to integrate evaluation and follow-up of goals and results in the budget process. Evaluation and scrutiny are important tools in any budget system, but with performance budgeting it is indeed necessary that the Parliament receive good information ex post by the government.

The Swedish budget act states, in general terms that the government should provide the Parliament with information about target, outcomes, and performance. The government provides much of this information in the budget bill but there are other channels as well.

The Swedish budget is divided into 27 expenditure areas. The government has been asked to submit reports focussing more exclusively on performance information for all expenditure areas from the year 2003. The reports are not supposed to cover everything within each expenditure area, but rather to focus on some activities.

The government submitted two reports with performance information only a week ago. One report is about a goal for culture policy. This goals concerns equality, in the sense that all citizens should have access and make use of various culture activities, such as theaters, libraries, and art exhibitions. According to the report, the efforts made by the state have contributed to more equality, in this sense.

That's fine, but the conclusion in the report indicates a problem with governing by objectives and results. The conclusion is that in order to keep the high levels of cultural activity and to improve cultural equality further, the state efforts should continue to improve.

Who can say against that? I can assure you that the political opposition will not say that the state efforts should not improve. We may disagree with the government on the level of expenditure for public culture policy, for instance, but the efforts can always be improved.

The other report submitted by the government concerns matters that are politically more contested. This report gives an account for Sweden's implementation of the European Union's employment strategy. I will not go in to any detail, but the European Union, as well as the OECD, has stated several times over the years that Sweden should lower its taxes on labor and deregulate its labor market. As I have indicated above, these matters are central to the political debate and performance information may indeed create interest among parliamentarians.

Finally, I would like to mention that the Swedish Finance Committee has demanded certain kinds of performance information and also put more general demands on the government:

1. The goals and objectives should be formulated in a way that makes them possible to follow up.
2. The performance information must be relevant in relation to the objectives. Results should to a larger extent be given in quantitative terms.
3. The information should make it possible for the Parliament to assess the fulfillment of the goals.
4. The information should to a larger extent focus on outcome and performance, and less on specific measures.
5. The information should focus more on cross-sector activities and less on specific authorities.
6. The relation between performance and the new appropriation should be improved. The calculation of the appropriation should be made clearer.
7. The analysis of the performance should be based on facts. A clear distinction should be made between performance information and analysis on one hand, and the government's assessment on the other hand.
8. The motives for the government's assessment and the government's conclusions should be clear in order to improve the connection between performance and draft budget.
9. The volume of information should be better adjusted to the size of public spending and to the political relevance of the policy areas. The volume of the budget bill may therefore increase; and
10. The dialogue between Parliament and government on performance information should continue. It should be a common ambition for Parliament and government to further develop performance budgeting.

These demands also put demands on the Parliament itself to make use of the hopefully improved performance information. If the information is politically relevant, I do think that Parliament will make use of the information in the general public debate.

Thank you for your attention.

Chairman NUSSLE. And we could—well, I will speak for myself. I think could listen to all of you all day describe your process, because it is very interesting, what we have heard so far, just in comparison to our own system. In some ways, it is very similar in the challenges, and in other ways, you have blazed new trails. You have gone in different directions than even we have.

Let me begin with the question on accrual accounting for Mr. Bowen.

In particular, what was the reason that Australia went to an accrual accounting system from a cash accounting system, No. 1; and No. 2, how difficult was that transition? How difficult? Because obviously, from a budgetary standpoint, there is a huge difference in the ramifications, particularly in the years to come as you make that transition.

So why did you make the change and how difficult was the transition?

Mr. BOWEN. Mr. Chairman, one reason for the change: essentially it was to provide a full perspective on the government's financial position.

It is very difficult to gain a full perspective by simply looking at cash flows. Cash flows do not tell you about the accruing liabilities for the future. They do not tell you where you stand in terms of your total assets/liability position, the level of debt, et cetera, that you need to fund.

The intention was also to provide a better basis for the managers within agencies to manage their full resources, rather than simply focus on the amount of cash that pass through their hands.

Allied with the introduction of accruals, I mean, the bottom line, I suppose you might say, is, we were looking to be able to identify for managers the total cost of—the full cost of their activities, including the costs of what previously had been hidden expenses, such as employee entitlements, the costs using capital, et cetera.

Having said that, I wouldn't want to oversell the concept of accruals in budgeting. We think it is important, but we equally think that maintaining good cash information is just as important. So it is not accruals replacing cash; it is accruals complementing cash to give a balanced perspective on the totality of not only the impact of the government activity on the economy, which cash gives you, but the financial position of the government as an entity, which accruals help you see better.

There is no perfect tool from our experience. And I don't say or sit here today, Mr. Chairman, and suggest that this is the answer to our prayers, let alone yours. But we believe that it has helped and, hopefully, will help us in the future.

On the issue of how difficult was it, with hindsight, it could perhaps have been implemented in a somewhat more measured manner. In Australia, it was done—as I say, we had been reporting on an accrual basis for a number of years in our annual financial statements.

Chairman NUSSLE. When you say "a number," 5 years or how long were you reporting?

Mr. BOWEN. Well, I think it would have been somewhere closer to six. Yes. I think we have been doing that now for about 10 years,

and we have been budgeting for 4. We have just had our fourth accrual budget. So I think within the civil service that there was a reasonable understanding of accruals.

I am not so sure that there was at the political level. And we have not done enough to sell it effectively at the political level today. But it is increasingly gaining acceptance, I guess is what I can say.

It was somewhat difficult to implement because we tried to do it so quickly, and we tried to ally the induction of accruals with other reforms, such as a focus on outcomes and outputs, rather than the inputs that go to make up those products. So I guess one of our learnings certainly has been that it might be better to do an initiative—to undertake an initiative of that nature in a slightly slower, more measured way.

Chairman NUSSLE. Thank you.

Mr. Odell, on the issue of setting ceilings, we have what we call "caps," a similar type of concept it sounds like. And have you a 3-year cap, or 3-year ceiling, as you indicated; is that how you do it?

Mr. ODELL. That is right.

Chairman NUSSLE. How closely do you adhere to that for 1 year? Throughout the 3 years, for that matter, how closely do you hit those ceilings?

Mr. ODELL. The government is extremely clever in hitting them exactly, I can tell you. And——

Chairman NUSSLE. We hit them, but we run right past them sometimes.

Mr. ODELL [continuing]. Our budget act states that if and when the government gets indications that it will be—the budget—the expenditure will go through the ceilings, they are entitled to come up with measures to stop that. So far and, I must say, with some creative measures, they have managed, even though I think last year there were tendencies to exceed the ceilings by 10 billion Swedish kroner; that is about $1 billion. But they managed by postponing some expenditures, et cetera—but also not very much real cutting in expenditure, I must say, but they managed to keep them.

Chairman NUSSLE. You have 27, you said, different ceilings?

Mr. ODELL. Twenty-seven, like one for defense, one for health care, et cetera.

Chairman NUSSLE. And you also indicated, I believe, about emergencies. What happens if there is a legitimate emergency in Sweden when it comes to those caps? Is there a separate fund for emergencies, or how do you deal with that?

Mr. ODELL. Yes, there is a separate fund, but that is really a midget. It is only less than $1 million in this fund.

You can imagine, we have very few, so far, emergencies in our country. We had some heavy rain last summer that caused some damage that was paid by the state. But we have—for real emergencies, the Parliament gives the government the right to use nearly 4 billion U.S. dollars in case of war, danger of war, or other exceptional circumstances. And this is given by a yearly base.

But we try to solve our emergencies in other ways. One emergency is, of course, the experience from the early 1990s when we had these huge deficits. I think we have tried to find our process

with these expenditure ceilings. But the kind of emergency that you experienced and that you have tried to find ways to solve is not—we have not experienced anything like that.

Chairman NUSSLE. We have three—as I look around, three hurricane experts on this committee alone here today. So we would love to get your advice on how to deal with those disasters.

I have a number of other questions, but I will share the time with other members who I know are interested as well.

Mr. Spratt, one of our hurricane experts, by the way, too.

Mr. SPRATT. It is a little island, but nevertheless a hurricane would wipe out an emergency fund of a million dollars in about 1 minute.

I ask each of you: Your countries have some kind of a balanced budget requirement?

Mr. ODELL. Yes.

Mr. SAURERS. Yes.

Mr. BOWEN. Yes.

Mr. SPRATT. Is this a cash budget or accrual budget that has to be balanced?

Mr. BOWEN. We have managed to achieve that.

Chairman NUSSLE. Could you turn your microphone on, please.

Mr. SPRATT. So one of the first steps in the budget process is to determine what the economic cycle is likely to be. And over that cycle you have to balance the budget.

Mr. BOWEN. That is the commitment that our government has had. And, yes, as I say, they have maintained that.

Mr. SPRATT. Is there standing statutory law that requires to you balance the budget?

Mr. BOWEN. No, there isn't, Mr. Spratt.

Mr. SPRATT. And Switzerland?

Mr. SAURERS. Sixty percent of Parliament approved an expenditure rule and 80 percent of the people approved the amendment of the constitution. So there was, you may take it, a sense of more rationality by the people.

Our expenditure rule, which will be in place there next year onward, is based on a structurally balanced approach, and hence, we do have the problem of the cycle as well, yet we believe that empirically, that problem is not as big as the problem that we had when expenditures were exceeding revenues during the past years. So the error there might be marginal there, compared to problems we had in the past.

We deal with emergencies within that concept to the extent that whenever there is an emergency—and that is specified by law, that needs a qualified approval by Parliament—that these expenditures can be spent outside of the normal expenditure rule, and hence, will lead to an increase in indebtedness. We do not create the fund, but rather just to allow for additional expenditure.

Mr. SPRATT. Mr. Odell, over this 3-year period, does Sweden have the requirement that the budget be balanced, that the expenditures equal revenues?

Mr. ODELL. Yes, and even more.

We have a target of 2 percent surplus in the total national economic sector, which includes not only the state but also the common sector and the pension system. This should be 2 percent on

average over the cycle. And we have managed to have more, over 4 percent last year. This year, which is a weak year, and next year seems also to be a weak year.

Mr. SPRATT. Four percent of the budget, 2 percent of the budget?

Mr. ODELL. Two percent of the entire budget for the whole public sector. And this means this year will be 1.8 percent surplus and next year also a surplus of 1.8 percent.

But then the big surplus is in the pension system; and the state budget is—more or less—next year, will be a minus. But the target—and this is, I think, for the OECD countries and European Union countries should also include the system.

Mr. SPRATT. So you can use the surpluses in your pension system to consolidate with the operating budget and create a 2 percent or 4 percent surplus overall?

Mr. ODELL. I think it is the consensus method of measuring the national budgets.

I wonder whether someone from the OECD could—yeah, so I think this is not especially for Sweden. This was mainly, I think, created because many countries had state budgets that seemed to be rather sound, but they had pension systems that were absolutely black holes. And you had to take everything into consideration.

And we have, which we will talk about tomorrow; we have reformed also our pension system to a totally autonomous system with big buffer funds.

Mr. SPRATT. It is totally autonomous now? But nevertheless the two are consolidated, so you get the economic effect of government?

Mr. ODELL. Yes, but you cannot take money from the pension funds for the state. That is not possible.

Mr. SPRATT. What are the assets of the pension fund invested in then?

Mr. ODELL. The pension funds got new rules for organization and investments a few years ago, and they invest in shares and in bonds. Also internationally.

Mr. SPRATT. But not Swedish government bonds.

Mr. ODELL. Naturally, of course, they do.

Mr. SPRATT. They do?

Mr. ODELL. They do, yes.

Mr. SPRATT. In effect, we have this problem here, when the Social Security trustees buy government bonds, they are, in effect, funding government spending.

Mr. ODELL. If I am—if I remember right now, we have a system where people can choose how to invest their pension money when the money comes in. But those who don't choose anything, their moneys going into the so-called "seventh fund." This seventh fund, that is for people that should not be speculating and so on. They have 95 percent in shares. They have 4 percent of this 95 percent—65 percent are foreign shares, and 30 percent Swedish shares, and 4 percent in what we call Swedish state bonds, and 1 percent is cash. So it is not a big amount of Swedish state bonds in this portfolio.

Mr. SPRATT. Let me ask you a question about something you described as a parliamentary procedure in considering the budget on the floor of the Parliament, so I understand.

I understood that you said, in order for someone to add an expenditure, his motion had to include a provision for paying for that additional expenditure. We call that, around here, the pay-as-you-go rule. We have that rule.

Is it strictly enforced in Sweden? Is there any way around it?

Mr. ODELL. It is absolutely strictly enforced. On top of that, you have not to—I mean, you have to convince the rest of the opposition to find exactly the same, both appropriations but also the financing. And that will never happen. So there will be very, very few changes in the budget bills proposed by the government when the decision comes in Parliament.

Mr. SPRATT. Does the same rule apply to tax cuts, tax reduction?

Mr. ODELL. The income of the budget is not treated in the same way as the expenditures. So the income has—this makes also an opportunity, of course, for the government to convert new expenditure to less taxes. So this is one of the ways you can—because the expenditure, if you don't increase the expenditures, you can cut the taxes and reach exactly the same purpose.

Mr. SPRATT. In balancing the budget?

Mr. ODELL. And still balancing the budget.

Mr. SPRATT. Let me ask you, in each of your governments if the budget is defeated, is this still a cause for dissolution of the Parliament?

Mr. BOWEN. It can be in extreme circumstances. In the Australian system, the government would normally have a majority in the lower house; in the upper house, for many years that has rarely been the case.

But the Australian budget is passed in two different types of appropriation bills, one of which is for ordinary annual services of government and that is very—usually passed without major amendment. It can be rejected and sent back for reconsideration. The other one is for new items, capital expenditure, et cetera; but again, there is rarely a situation where there would be a total rejection of that bill.

Mr. SPRATT. Mr. Saurers.

Mr. SAURERS. We have a coalition government, and our procedures exclude that the budget could be defeated. And let me explain:

Parliament approves credit lines for different items, and of course, at the end, the total amount of expenditures. Now if there are differences between the houses, they are not on the budget as a whole, but maybe on a few items. Our procedures are three times, to and fro, between the houses. If there isn't an agreement by the end of the day, the lower amount will be inscribed in the budget, and as such, we always have a budget by the end of the year.

Mr. ODELL. We don't have that system, but we have a minority government which has two supporting parties, the Left Party and the Green Party. And they have a negotiation and they negotiate a budget. And in the extreme case of the budget would be defeated, there is one possibility, of course, and that is that the government itself calls for new elections. That could be a threat, of course, if the opposition is weak, if they have a strong opinion behind them.

But we don't have the possibility to just dissolve the Parliament, no.

Mr. SPRATT. Thank you all very much. We will talk further, but I want to give others an opportunity to ask questions as well.

Chairman NUSSLE. Mr. Gutknecht.

Mr. GUTKNECHT. Thank you, Mr. Chairman. On behalf of all the members of the committee we want to thank all of you for coming. This has been very interesting.

First of all, we have heard from Sweden on the idea of privatized and/or personalized retirement programs. I am wondering if your two colleagues from Australia and Switzerland would share what kind of retirement program you have, what we describe as Social Security. Has it become more privatized or personalized than we have in the United States?

Mr. SAURERS. We have what we call three-pillar approach. A first pillar is compulsory unfunded system—compulsory system, unfunded system, state pension; we have what we call a finance, basically by payroll taxes of employers and employees.

Mr. GUTKNECHT. So if I can be clear, you require that a certain percentage be taken out of people's paychecks and then is deposited in a private retirement account?

Mr. SAURERS. No, that is public. The first is public. The second pillar is a funded system with—we have got private funds; and again, it is compulsory to the extent that the employer and the employee have to contribute and money is invested in these funds.

Mr. GUTKNECHT. But that money is then invested in shares?

Mr. SAURERS. Shares and funds. Equities, yes; and real assets as well.

And the third pillar, that is what we call "private," to the extent that you as an individual can put money in a blocked account, and you receive some tax benefits while do you it.

Mr. GUTKNECHT. What we would describe as an IRA in the United States.

Mr. Bowen.

Mr. BOWEN. In Australia, the government has traditionally funded old age pensions. Those pensions are not subject to any individual contribution; they are funded on a pay-as-you-go basis by the government. And the pensions are means tested and indexed by movements in average wages. But the pension is at a fairly low level. It is not a high level.

In addition to that, for some years, employers have been required to contribute to employee super annuated schemes. I think from the first of July this year, that contribution of the minimum guaranteed payment that will be 9 percent of an employee's salary. That money is required to be invested and approved, what we call super annuated funds, managed funds.

Mr. GUTKNECHT. What we would describe as mutual funds.

Mr. BOWEN. Mutual funds managed by the private sector, not part of the government sector at all. The impact of that is certainly starting to bear fruit, and in our long-term projections in our recent intergenerational report, it does suggest that this will have a major impact on holding down the government's future requirement to pay tax funded pensions.

Mr. GUTKNECHT. Mr. Odell, is there something else you wanted to add?

Mr. ODELL. The Swedish system is not purely a privatized system. It is not privatized at all, I must tell you. But it is like that. 18 percent of your salary——

Mr. GUTKNECHT. I know the terms are different, but here in the United States there is—at least we are having some discussion about having a system under the umbrella of Social Security in which employees could contribute a certain percentage of the taxes that go to Social Security into privatized accounts. It would still be under the umbrella of Social Security, but the money would not simply be an intergovernmental borrowing where it would ultimately into government bonds in the United States.

The average rate of return, for example, for a younger worker in America in the money they put in is something like 1 percent. And more and more younger workers are saying we can do much better putting money into banks.

Mr. ODELL. Our system is like the employer pays 18 percent of your salary to your pension. Two-and-a-half percent goes to a system where the individual can choose between, I think 4- or 500 different alternatives. And this is a state agency that is managing the whole system. The rest, 15.5 percent of your pension's money goes into a traditional pay-as-you-go system, which has five buffer funds to smooth the differences in the business cycle and also in the demography and so on.

I must tell you that we are very proud of our pension system. But one important element is that we manage to be—have a very big and broad consensus in Parliament. We have seven partisan in Parliament and five of this party's—the five biggest are totally behind. And doesn't matter if it is a socialist or a non-socialist government. We have like a coalition government around our pension reform. We have a governing group of people from five parties and irrespective of what kind of majority, these five parties stick to this pension reform and they are really taking care of the reform and it has been very successful so far.

Mr. GUTKNECHT. Can I switch direction just slightly on this? Maybe perhaps quickly, you can tell us what is roughly the economic growth rate currently in each of your countries and what is your unemployment rates? Australia?

Mr. BOWEN. Our economic growth is currently around 3¾ percent per annum and projected to go forward at least at that rate. Unemployment is running at around 6 percent.

Mr. SAURERS. Our real GDP growth rate is 1 percent. Our potential is below 2 percent by past experiences. And unemployment at the moment is slightly above 2 percent.

Mr. ODELL. Well, the Swedish present rate of growth is around 1.8 percent and that is unfortunately also the average of—from the year around 1970 to 2001. This is absolutely too low and the opposition has the target to reach potential of 3 percent. That calls for a lot of structural reforms. Our unemployment rate is what we call the open unemployment is around 4 percent. But if you take into account all people in different kind of labor market activities and so on, we have more than 13 percent, perhaps 14 percent.

Mr. GUTKNECHT. One of the issues we wrestle with here in the United States is what percentage of our budget we should spend on important issues like defense and health care. Can you give us—and I don't know if you brought these numbers with you—but roughly what percentage of your budget do you spend on defense and approximately what percentage do you spend on health care?

Mr. SAURERS. On defense it is below 10 percent. I am a representative for the Federal government, and particularly when it gets to health, it is blurred because states are spending much less on health as well. At the Federal level, we spend maybe about 2 billion. About 4 percent, Federal level only on health care.

Mr. GUTKNECHT. I know it is a tough question.

Mr. ODELL. Defense, around 5 percent, and that is rather much for a Scandinavian country. Health care is more difficult because most of the responsibility for the health care is on the communes, but I say around 25 percent.

Mr. BOWEN. I haven't got accurate figures here with me, but I think defense is around 8 percent and health would be around 15. Health in Australia—the health costs in Australia are growing at a very rapid rate, and that is one area of major concern for us over the next decade.

Mr. GUTKNECHT. The reason I raise the issue, particularly of defense, and it is a bit of a sore spot with us, when you compare us to the European Union, and we just recently passed another emergency supplemental which increased defense spending, we will spend about double what the European Union does, almost any way you measure it. And one of the things we are hoping is you take the message back to your colleagues in the European Union is that we in the Budget Committee would like the European Union to pick up a little more expenses in defending the planet.

It is becoming incredibly difficult for us to keep up with the requests from our own Pentagon. Right now we are in a circumstance—and the other issue that I am not sure the Europeans—my time is about up—is that we do regard ourselves at war right now. And as a result, we have been very generous with our defense expenditures. But long-term, we can't get up there around 20 percent of our total expenditures. With that, I yield back the balance of my time, Mr. Chairman.

Chairman NUSSLE. Mr. Watkins.

Mr. WATKINS. You are very generous, Mr. Chairman. Thank you for this opportunity, because I think it offers some very good insight. You were asking some of the same things in the budget. One of the things we have sometimes in our Ways and Means, which is taxation phases, is that we have to come up with offsets and talk about some gnashing of teeth when you are trying to find offsets.

I notice, Mr. Odell, it seems like you have less flexibility or elasticity to try to deal with certain things as you try to work through some of the budgets and all. But I will follow up with what my colleague from Minnesota asked about a couple of things. I would like to ask, all of you, in dealing with your budgets, what is the—and I guess you have debt—what is the percentage of your debt of your GDP?

Mr. ODELL. I think our debt is now around 40 percent of GDP. But then we also have assets. So if you take our net debt, I don't think we have a net debt.

Mr. WATKINS. Right. If you are allowed to put the assets——

Mr. ODELL. Forty percent of GDP. But if you have a balance sheet, we also have assets and we think in the opposition that we should sell more of state-owned companies and bring down our gross debt, of course.

Mr. WATKINS. Your overall costs are running around—budget—what percentage of GDP.

Mr. ODELL. The cost of running the budget?

Mr. WATKINS. How much is the overall—budget. The budget itself compared to the GDP. What percentage of the GDP?

Mr. SAURERS. I give you the figures for the Federal level, the debt of the percentage of GDP is now at 25 percent and it doubled over the last 10 years which explains that we have big problems. Our expenditures as a percentage of GDP are approximately 12 percent at the Federal level as well. And if you take that to the overall government debt, would be about 50 percent and expenditure as a percentage of GDP would be about 40 percent.

Mr. WATKINS. About 40 percent of the expenditures. What about Australia?

Mr. BOWEN. In Australia, the net debt is roughly a half of a percent of GDP. It is very low. And it is expected to fall to zero in the next 3 years. The budget, as a percentage of GDP, is roughly 25 percent.

Mr. ODELL. On the Swedish budget as percentage of GDP, is roughly 35 percent, 800 billion out of 2,000.

Mr. WATKINS. Any particular trends there that you see? Do you see any sizable trends? Overall, our expenditures are up, but as a percentage of GDP, we have——

Mr. ODELL. Our expenditure as percentage of GDP has been smaller over the time. But this year, it starts to grow again.

Mr. WATKINS. Mr. Chairman, I have one other question that I thought would be very, very important for all of us to find out what the meaning here is of this. There is a statement in here about in Australia, you have got something called a Charter of Budget Honesty Act. Tell me what that is. We might need that around here.

Mr. BOWEN. Broadly, Mr. Watkins, it is an act that specifies the requirements on government for the budget reporting. It requires the government to report or present its budget in accordance with external accounting standards. It requires the government to produce financial reports at certain times in the year and it requires the government to produce certain reports at certain times in the electoral cycle. In particular, when an election is called, the government is required and the heads of our treasury and finance departments are required, to sign off on the budgetary position under the terms of the Charter of Budget Honesty. There is an obvious reason for that, to ensure that there is a public statement of the budget position to inform the electorate prior to the polls.

Mr. WATKINS. It doesn't have anything to do with Arthur Andersen doing the accounting?

Mr. BOWEN. Very little to do with Arthur Andersen. This was introduced prior to the Enron issue.

Chairman NUSSLE. Mr. Kirk.

Mr. KIRK. Mr. Bowen, I am wondering, I reviewed your testimony very carefully and would just offer you a chance to immigrate to the United States and run our OMB. It is a considerable jump in the political process to move to accrual accounting. It requires political will to recognize that enormous debt and put it on the books. Can you describe the process by which that decision was made 5 or 6 years ago for a government to recognize that liability?

Mr. BOWEN. Mr. Kirk, I think the advantage that we had at the time was that on an annual basis in the accounts of the government, all of those accrual measures were recognized. That was purely on a ex post reporting basis. So it was publicly available information at a point in time looking backwards. The—and to be fair, the majority of the liabilities facing the government had previously been in clearly on budget paper but perhaps not in a systematic way or as systematic a way as you achieve under an accrual based budgeting regime.

So I think in the Australian experience, that by undertaking accrual reporting for a number of years, that did help to phase in a better understanding, but I would hasten to add that we still have a way to go for—before I think we present our budget in a very effective simple straightforward accrual way and a way in which all users of that information can understand it. One of our areas of concern is the fact that under our Charter of Budget Honesty, we report against external standards.

There happen to be two that apply. So within our budget papers, we do present the budget on two different bases. Now there are a lot of commonalities in those two approaches, but there are some differences. And that does mean that in our parliamentary committee hearings at budget time, there are some interesting questions that have to be answered.

Mr. KIRK. Imagine if we moved to accrual accounting; we would have mass unemployment on K Street because we would recognize such an enormous liability of the Federal government that the decision to create any new Federal program would be immediately laughed out of the halls of Congress. But you talked about external standards. The administration has moved to create a preponderance of private sector accounting entities to review the Federal accounting standards but has done so by executive order. I would hope we would do so by legislation. Regarding your independent standards for government accounting, how different are they than private accounting standards used to assess the value of a publicly traded company in Australia?

Mr. BOWEN. As I say, we have two sets of standards that we adhere to. One is the Australian accounting standards, but standards which are specifically written for the public sector. However, they are not substantively different to the standards that a public company would have to adhere to. And increasingly, they have become closer and closer. The accounting standards board that develops and sets the standards is a board established on the legislation, and it establishes the standards for the public and private sectors. The other standard that we adhere to is the International Monetary Funds' government finance statistic standard. As I say, that has some different elements to it.

Mr. KIRK. If the Prime Minister is upset with the standard that is getting in the way of a policy direction, can he or his representatives on the board fudge the standard?

Mr. BOWEN. Well, it is far more likely that if the government feels that a presentation strictly in accordance with the standard would not reflect the government's policy intention, that they would change the presentation but make it explicit in the notes to that presentation that they have deviated from the standard. In fact, that happens.

Mr. KIRK. And they hope no one reads the footnote.

Mr. BOWEN. They may hope that, but in fact, people do and people on committees such as yours increasingly are looking at those footnotes, and people in my position have to answer those types of questions.

Mr. KIRK. When you moved to outcomes, and I looked at this particularly with our foreign assistance program, instead of measuring how much gas we allow to the foreign assistance agency or how many hours employees work, we just look at whether we increased female literacy in this region and measure it that way. But the question is who measures. Under the current—our Current Results Act, the agency running the program also measures the results. You can see the inherent conflict of interest. In Australia, who measures the outcome?

Mr. BOWEN. Look, we have a similar situation in that the primary center of the targets or proposer of the targets, the primary measurer is the agency concerned. However, that is done in the context of budget proposals and there is oversight by my department to a degree.

Also, I mentioned briefly that our auditor general and the parliamentary committees have the opportunity to scrutinize. I wouldn't like to suggest that this is done always or always in great detail, but the opportunity is there for parliamentary committees to scrutinize those targets and the results and to ask questions about them. The auditor general has a mandate to conduct what we call performance audits. And those audits can be quite broad in scope, looking at the actual performance and the effectiveness of program delivery.

Mr. KIRK. Thank you. Thank you, Mr. Chairman.

Chairman NUSSLE. Thank you.

Mr. Brown.

Mr. BROWN. Thank you Mr. Chairman. Mr. Bowen, I certainly appreciate you all coming and being a part of this discussion, and I am sorry I wasn't here for the presentation. Maybe I might be repeating what you have already discussed, but in relationship with the interest, the private interest earned, is that taxable in Australia?

Mr. BOWEN. Can I just get some clarification on your question, Mr. Brown?

Mr. BROWN. If you have a CD, a bank deposit or something that draws interest, does the government tax the proceeds?

Mr. BOWEN. If a private individual or a company has an interest earning deposit, yes, certainly, that is part of taxable income.

Mr. BROWN. And if you have a mortgage that you pay interest, is that tax deductible?

Mr. BOWEN. No, not if that mortgage is for private purposes. If the mortgage is associated with a business purpose, then yes, it would be.

Mr. BROWN. So a home mortgage is not deductible?

Mr. BOWEN. No.

Mr. BROWN. How does that work in Switzerland.

Mr. SAURERS. Interest income is taxable, and at the moment we have got a system where an imputed rent is taxed and mortgages are deductible, and there are discussions going on of change of the system.

Mr. BROWN. Mr. Odell.

Mr. ODELL. Well, the tax on this kind of income is 30 percent, and you can also deduct 30 percent, the entire—if you have borrowed, but not the mortgage is not at all deductible.

Mr. BROWN. But the interest on the mortgage is.

Mr. ODELL. The interest is deductible from your income, yes.

Mr. BROWN. In light of 9/11, the homeland security costs in America have been—you know, has gone up exponentially, and I am just wondering if that impacted your countries at all and if it did, to what degree?

Mr. BOWEN. In Australia, it certainly has impacted in this last budget. I don't have the figures with me, but it was a major factor in the increase in outlays, not only for our Defense Department, but also for our protective security agencies domestically.

Mr. SAURERS. It changed our efforts as well and has impacts in the government sector as well, but I couldn't give you the figures. But again, I would assume they are there, but they are not major concern.

Mr. ODELL. It had a very big political impact of course. Also, our government, prime minister and social democratic government skeptics of the United States have been 100 percent, and still 100 percent behind United States of America and its President in the war against terrorism. The budgetary consequences, I cannot tell you anything about it, but we have, of course, enhanced our security levels in several areas a lot.

Mr. BROWN. Thank you, Mr. Chairman.

Chairman NUSSLE. Thank you.

Mr. Culberson.

Mr. CULBERSON. Thank you, Mr. Chairman, for organizing this hearing. It is really interesting and informative and we are very grateful for you coming to join us today, and I simply wanted to ask about your tax systems and how the governments generate revenue. Do you have an income tax, and if so, what is the top rate of that income tax and do you tax capital gains and if so, at what rate? Australia, please, Mr. Bowen.

Mr. BOWEN. We have an income tax. We also have a goods and services tax and we do tax capital gains. The top income tax rate is around 48 cents on the dollar. The rate on goods and services is 10 percent. And we tax capital gains—we have taxed them at the marginal tax rate for individuals, but I think we have recently introduced some concessions there. We also have a company tax structure and the company tax rate I think now is down around 30 percent.

Mr. CULBERSON. Thirty percent on a company tax rate. How do you determine that? Is that a——

Mr. BOWEN. That is a flat rate based on net taxable income for a company.

Mr. CULBERSON. And you are not sure that the capital gains tax rate you say—the marginal rate is about——

Mr. BOWEN. Has been at the marginal tax rate—taxpayers—my tax expert has——

Mr. CULBERSON. Where would we be without them?

Mr. BOWEN. I am advised now and I recall that if you hold your assets now for in excess of 12 months, as an individual, your capital gains tax is half—is taxed half your marginal tax rate.

Mr. CULBERSON. So 24 percent?

Mr. BOWEN. If you are at the maximum rate.

Mr. CULBERSON. Thank you.

Mr. Saurers.

Mr. SAURERS. Again, we are a Federal state. We have income tax at three levels: Federal level, state level and the local level, which is just a percentage of the state level. Now I am talking about Federal level because I have got no expert behind me and I only have figures in my head. But those I have got at least. The flat rate at the Federal level for companies is 8.5 percent and the maximum rate for income tax, personal income taxes is about 13 percent. But don't let yourself impress by these low figures, because they come on top of the figures on of the state level.

Mr. CULBERSON. Thirteen or 30?

Mr. SAURERS. Thirteen. Last year in our system, we voted on an introduction of a capital gains tax at the Federal level. That initiative was declined by about 55 percent of the people. That does not mean that they are no capital gains taxed at all. First of all, on real property at the state level, there is a capital gains tax in the difference of value if you buy and sell your estate. And second, most state tax cost you a fortune at the flat rate. So you can consider that as a substitute of the capital gains tax that you pay irrespective if you make any gains or losses.

Mr. CULBERSON. That is your principal source of government revenue?

Mr. SAURERS. No. Again at the Federal level, the VAT brings in about 25 to 30 percent of revenue. And income tax at the Federal level, that is about 20 percent.

Mr. CULBERSON. And you also have a death tax. You have a death tax, when people die?

Mr. SAURERS. It is a bit complicated. At the state level, not at the Federal level. And quite a number of states are reducing one after the other, reducing their tax on what we call inheritage.

Mr. CULBERSON. Thank you. Mr. Odell.

Mr. ODELL. I think we are the world champions in taxing our citizens. We start by 25 percent VAT. There are some deductions for food, for example, 12 percent. Then we have 30 percent income tax. That is for the commoner level. Everybody has to pay 30 percent. And then for little bit higher incomes, 20 percent state. We are not a Federal state, so the state means the national level, at 20 percent. And for some higher incomes, even 25 percent.

Mr. CULBERSON. On top of the 30.

Mr. ODELL. On top of the 30. So this means the average income tax is around, I think, 40 percent. But some people pay 55 percent. Then comes the capital gains tax that is 30 percent on interest, or on what you get from your shares—what is the name of that—equity—that's right. Then we have a company tax and that is 28 percent. That is the lowest in European Union. Also Finland has 28 percent.

I would also like to mention our property tax, which is 1.5 percent on your taxed property, and that is all property more than—around $150,000. You can imagine in a globalized economy, when our citizens have to pay 1.5 percent in property tax and you can move your capital freely to other countries how this is hurting our economy. This is what we are trying to convince our socialist government about, because they think this is some kind of equality-making tax, but we think it is making us more poor instead. So this is about the Swedish tax structure.

Mr. CULBERSON. Mr. Chairman, may I ask one follow up to Mr. Bowen? On the goods and services tax, you mentioned Australia has 10 percent, is that a value added tax or a point of sale retail sales tax, consumption tax? What do you mean by goods and services tax of 10 percent?

Mr. BOWEN. It is effectively a consumption tax. I should add that the revenue raised from that tax is passed directly to our state government.

Mr. CULBERSON. And then finally to Switzerland, the capital gains tax was rejected by the voters. Under your system—the voters have a right to approve taxes?

Mr. SAURERS. There was an initiative of 100,000 or more people who submitted a proposal for the introduction of a capital gains tax. Parliament had to deal with it. Government had to produce a proposal and the people voted on that initiative last year and in the vote, itself, it was declined. So we won't have a capital gains tax.

Mr. CULBERSON. Fifty-five percent said no.

Mr. SAURERS. Forty-five yes, and 55, no.

Mr. CULBERSON. Zero capital gains tax in Switzerland?

Mr. SAURERS. Yes.

Chairman NUSSLE. I wasn't going to get into this line of questioning. We had some earlier good conversation about your budget procedures, but now my curiosity is peaked. Do all of your citizens pay taxes or do you exclude particular citizens from taxation? There were a couple of you that mentioned that everyone, I believe—Sweden, everyone pays 30 percent on their income.

Mr. ODELL. Even on Social Security. We pay—people who live on Social Security have to pay taxes on that.

Chairman NUSSLE. Is that true for the other countries involved?

Mr. SAURERS. At the Federal level, income tax, there is quite a large proportion of the population which will not pay any income tax at all. We are, at the moment, introducing a reform that will even increase that proportion. But this development has to be seen in the overall picture of taxation where Federal government historically had no income tax at all, and therefore, should be sort of reluctant of imposing its own income tax on top of the income taxes

of the states. So the reform goes in a way of the direction of further exempting part of the poor population from income taxation.

Mr. BOWEN. Mr. Chairman, in Australia, we have the progressive income tax scale. So there are people on very low incomes who would not be subject to tax, income tax or who would be subject to a very low rate of tax. However, there are, to my knowledge, no exemptions from consumers paying the goods and services tax.

Chairman NUSSLE. Are there any other questions that members have for this panel? If not, I would like to thank you for your testimony today and for being willing to answer a number of questions, even beyond what we asked you to come and talk about. We are very curious about how a number of different facets of your country operate, and I think you saw that with the questions today. Just for the information of the members and the audience that are here, tomorrow and Friday, we will continue with OECD conference on economic—excuse me, on budgeting. And tomorrow we will be considering fiscal rules and fiscal risks in the morning session as well as budgeting for emergencies and then in the afternoon entitlement spending will be considered.

Then on Friday, we will take on performance budgeting and accrual accounting. And members—all members are invited to participate in this conference. It will be here in this room and we will be happy to share with you a schedule about that. This is about the OECD conference for chairpersons and parliamentary budget committees and all members are invited to attend.

Mr. CULBERSON. If I could have one quick follow up. Can taxes be raised in your countries by simple majority votes of your legislatures or your Parliaments or does it require a super majority?

Mr. BOWEN. Simple majority.

Mr. SAURERS. Maximum rates are in the constitution for VAT and income tax and the people have to decide if the rates are increased.

Mr. ODELL. In Sweden, it is sufficient with a simple majority to increase taxes.

Mr. CULBERSON. I prefer learning more about how Switzerland handles its tax system.

Mr. BROWN. Mr. Saurers, have you—have the citizens had an opportunity to increase those limits? Have they taken a vote to address it and if they did, was it a positive vote?

Mr. SAURERS. When we changed to the system from a consumption tax to a VAT tax, we, at the same time, increased the tax rate and maybe that was a political move. Part of that increase was earmarked for old age pension. And at that time, that increase of tax rates was approved. And I recall a little more back, we increased a petrol tax in a vote as well, earmarked for the construction of motor ways and that was increased as well. Our taxes are—not only do we have the maximum rates in the constitution, but the right to raise taxes is limited in time and requires prolongation of about every 12 years.

And on these occasions, always the issue comes up, do we eliminate maximum tax rate from the constitution in order that Parliament could fix them? Do we eliminate limitation and time? In past experiences when government tried to do both in Parliament, the result was always negative. And what we do again right now,

we try to keep the maximum rates, but we flood with the idea do we eliminate the necessity to have a vote every 12 years to prolong taxation of the income and VAT, but we shall see if that will pass.

Mr. BROWN. Every 12 years you actually go back to the voters to approve the tax code?

Chairman NUSSLE. Not the tax code.

Mr. SAURERS. Not necessarily the code in details, which is afterwards decided by the Parliament with the possibility of a referendum, of course, since it is a law. But at that time you fix what taxes, Federal government is allowed to introduce. You fix on the maximum rates. Yes, that we do.

Mr. BROWN. What happens if they don't approve it?

Mr. SAURERS. We got wise in the past. The existing tax system lasts until the year 2006, and we intend to have the first vote in 2004 in order for us to have a second attempt.

Chairman NUSSLE. We really do appreciate your testimony today and for taking extra time to talk to us about a number of topics, and we look forward to your participation in the conference to come. Thank you very much. Committee is adjourned.

[Whereupon, at 12:30 p.m., the committee was adjourned.]

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