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Rise of Non-Standard Policy Instruments: Can Budgeting Catch Up?

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For implementing their economic and social policies, governments have traditionally relied on direct spending but increasingly use “non-standard” policy instruments, such as loans and guarantees, which have become many governments’ tools-of-choice for crisis response. Further, loans and guarantees are increasingly considered as potential instruments for delivering new policy priorities, such as the green transition. However, in many OECD countries, loans and guarantees are not yet submitted to the same scrutiny than direct spending as part of the budget process, and future costs associated with the use of these policy instruments are often not estimated, nor provisioned, making them appear initially costless. In turn, this generates risks of potentially biased budgetary decision making, deviations from medium-term spending plans and limited transparency. Considering experiences of OECD countries that have sought to improve their budgeting practices for loans and guarantees, this paper summarises key considerations for adapting budget systems to this new paradigm. It advises mainly that budget offices take a leading role in proposing budgetary treatments for loans and guarantees that ensure an even-level playing field with traditional spending and put considerations of efficiency of spending above optimization of short-term fiscal outcomes. In line with the OECD Spending Better Framework, it suggests that costs of standardized loans and guarantees be measured based on estimates of the net present value of all expected cash-flows and deposit accounts be used to record provisions for future losses separately from actual cash-flows.

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1. Introduction

1.1. The rise of non-standard policy instruments

1. Governments have relied traditionally on direct spending, and more specifically on subsidies, for implementing their economic and social policies. However, other policy instruments have been developed over time to implement these policies, which are non-standard in that they do not rely on direct spending. They can take various forms, such as loans, guarantees, equity injections or tax expenditures. These non-standard policy instruments, which are a heterogenous group, do not have yet a well-defined name. They have been branded different names, such as “alternative policy instruments” (Parliamentary Budget Office, Commonwealth of Australia, 2020^[1]), “balance sheet-based policies” (Moretti, Braendle and Leroy, 2021^[2]) or “financial support measures” (Battersby et al., 2022^[3]).

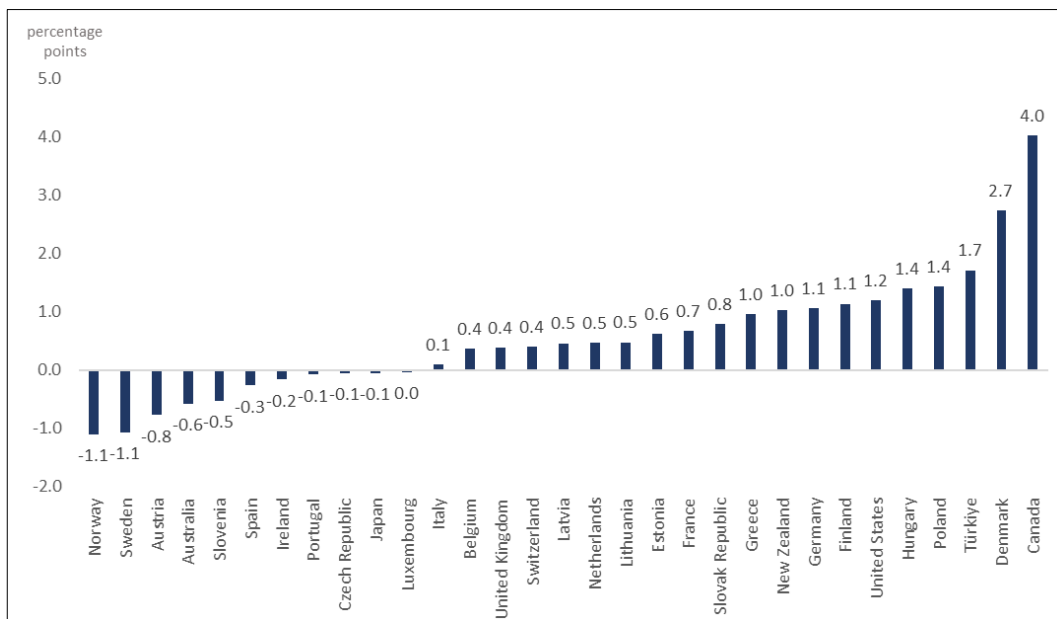
¹ This discussion paper was prepared by Delphine Moretti, Senior Policy Analyst in the Public Management and Budgeting division of the OECD’s Public Governance Directorate. Anne Keller, Policy Analyst, prepared Figure 1.1, with the assistance of Titouan Chassagne and Laurence Dynes. The author thanks David Torregrosa and Marvin Phaup, current and former staff of the United States Congressional Budget Office, for providing comments on this paper, as well as Ross Smith and Edwin Ng, both International Public Sector Accounting Standards Board staff, and delegates to the Working Party on Finance Management and Reporting.

2. Within non-standard policy instruments, loans and guarantees deserve special attention. For several decades already, governments have carried out significant activity through loans and guarantees. These policy instruments were initially restricted to a few well-delineated areas, and mainly aimed to addressing market failures. During the global financial crisis and COVID-19 pandemic, however, they became many governments’ tools-of-choice for crisis response (Moretti, Boucher and Giannini, 2021^[4]; Battersby et al., 2022^[3]), evolving in the process into common policy instruments for counter-cyclical fiscal policies during economic downturns. This was illustrated recently by the energy crisis, during which governments made significant use of loans to support utilities in meeting their liquidity needs (Sgaravatti et al., 2021^[5]). Further, loans and guarantees are increasingly considered as potential instruments for new policy priorities, such as the green transition (e.g., concessional loans for building climate-resilient infrastructure).

3. Specifically, during the global financial crisis (GFC), some countries increased their loans and equity purchases by more than 4 percent of GDP and contingent liabilities, mainly guarantees, by more than 10 percent of GDP (Battersby et al., 2022^[3]). In most OECD countries, stocks of loans and guarantees were not brought back to their pre-GFC levels after the crisis. Further, during the COVID-19 pandemic, stock of loans increased again in several OECD countries, by more than 1 percentage point in terms of GDP for 10 OECD countries (Figure 1.1, a.). In addition, 13 OECD countries increased their stocks of guarantees by more than 1 percentage point in terms of GDP (Figure 1.1, b.).

Figure 1.1. Selected OECD countries: Change in stocks of loans and guarantees (2019-2021)

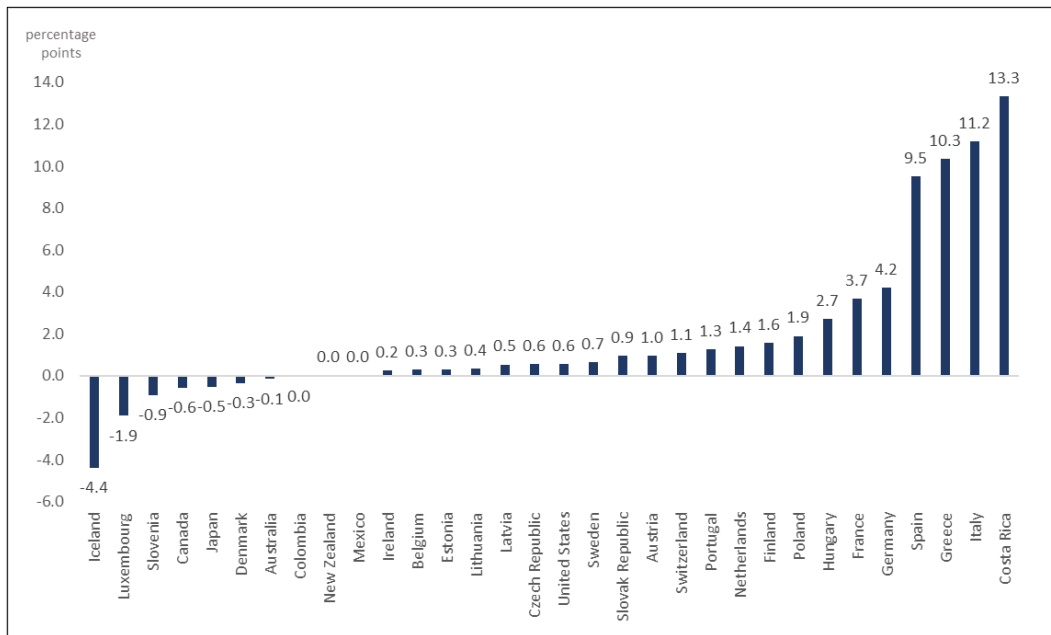
a. Change in government loans in terms of GDP, between 2019 and 2021



Note: Data for 31 OECD countries based on OECD statistics on loans for general government (710. Financial balance sheets – consolidated -SNA 2008, Transaction: loans). OECD countries not represented in this graph are those for which loans or GDP data was not available for 2019 or 2021.

Source: OECD staff estimates based on [OECD.Stat](#)

b. Change in government guarantees in terms of GDP, between 2019 and 2021



Note: Note: The figure is showing the difference between 2019 government guarantees as a percentage of GDP and 2021 government guarantees as a percentage of GDP. Direct comparisons can only be made between EU countries. For other OECD countries, the data is based on national definitions and methodologies, which may vary significantly from one country to another. The government guarantees data for EU countries refers to general government, data for Australia, Canada, Mexico, Switzerland and the United States refer to federal government and data for New Zealand refer to central government. OECD countries not represented in this graph are those for which loans or GDP data was not available for 2019 or 2021.

Source: OECD staff estimates based on government guarantees in national currency: Eurostat for EU member-states, national sources for other OECD countries; for GDP in national currency: OECD National Accounts Statistics (database) on 2 May 2023.

4. The rise of loans and guarantees as policy instruments is not always backed by strong evidence on their effectiveness vs. subsidies. For instance, a recent study recognizes their usefulness in crisis episodes, but less so in economic downturns (Battersby et al., 2022^[3]). Some OECD countries have therefore sought to prevent their excessive use. The Netherlands, for instance, has had for several years a “no, unless” policy which requires that new proposals for guarantees be underpinned by a strong rationale (Hofmans and van de Coevering, 2014^[6]). Recently, the United Kingdom also sought to better regulate possibilities for using guarantee schemes (HM Treasury, 2020^[7]).

1.2. A new paradigm for budget systems

5. As loans and guarantees’ effectiveness as policy instruments is not easy to demonstrate, this raises the question: why are they increasingly used? Part of the answer might lie in the fact that they “evade” the standard budget process and scrutiny. This is because, in essence, most OECD countries’ budget systems have been designed to manage the standard policy instrument of governments – that is direct spending. When a new subsidy is voted for the next fiscal year, the budgetary implication is clear: cash outflows

will incur over that fiscal year. This will be easily captured in a cash-basis budget, which is largely prevalent for managing appropriations in OECD countries.²

6. However, with non-standard policy instruments, things are more complex. Firstly, budgetary implications of new economic and social policies are more difficult to measure: guarantees and equity injections may generate delayed cash outflows (calls on guarantee and recapitalisations), loans may generate indirect cash outflows (difference between concessional interest rate and government's own financing rate), loans and tax expenditures may reduce cash inflows (payment defaults and revenue losses). Secondly, these budgetary implications are impossible to trace in a cash budget, making them initially, and mistakenly, appear as costless.

7. Budgetary issues associated with non-standard policy instruments are well known. Their increasing use across OECD countries and through successive crises however make these issues more acute and urgent to address. For instance, in Australia, the Parliamentary Budget Office recently called attention to the fact that “if the use of alternative financing arrangements continues to grow without a change to reporting practices, a larger share of government spending would be difficult to scrutinise, which could pose risks to the Commonwealth Government's fiscal position over the longer term.” (Parliamentary Budget Office, Commonwealth of Australia, 2020_[11]).

1.3. Objective of the paper

8. Against this background, this paper aims to provide an update on the OECD Secretariat's work on good practices for budgeting for government loans and guarantees, the groundwork for which was laid first in the OECD's 2015 *Recommendation of the Council on Budgetary Governance* (OECD, 2015_[8]) and subsequently developed in the OECD *Spending Better Framework*, presented at last year's SBO meeting.³

9. This paper does not aim to discuss policy rationales and outcomes of government decisions to use loans or guarantees but to summarize key considerations for making loans and guarantees more legitimate as policy instruments from a budgeting perspective and advocates a stronger role for central budgetary authorities (CBAs) in this area. In doing so, it serves to as a basis for discussion among Senior Budget Officials on the way forward for strengthening budgeting practices for loans and guarantees.

10. This paper mainly draws on OECD Secretariat's analytical work, as well as discussions in recent meetings of the SBO's Working Party on Finance Management and Reporting supported by specific country examples, including the United States experience with the implementation of the Federal Credit reform Act (Anderson and Burke, 2021_[9]) and the United Kingdom *Government as Insurer of Last Resort* report (HM Treasury, 2020_[7]).

² Spending limits are presented on cash and/or commitment bases by 16 countries, on both cash (or commitment) and accrual bases by 10 countries and on accrual basis by only 6 countries (OECD, 2019_[14])

³ These documents are all part of ongoing efforts by the Committee of Senior Budget Officials (SBO) to define features that constitute quality budget institutions and identify good practices that can support their effective implementation in OECD countries.

2. Principles of budgeting for loans and guarantees

1. In budgeting for loans guarantee, and more generally for any non-standard policy instrument, the Spending Better Framework advises that budgetary implications be made explicit in the budget documentation, with i) costs estimated for the full life of the policy and ii) fully funded in the budget. This aims to represent the “real” nature of the policy in the budget, which is to provide subsidy, rather than its form, which is a loan or a guarantee. It has been branded as budgeting “for subsidy cost” (Anderson and Burke, 2021^[9]), “for grant-equivalence” (Hong and Lucas, 2023^[10]) or “on a like-for-like basis” (Saxena, 2017^[11]).
2. This impacts budgetary decision making in three beneficial ways:
 - First, the estimation of costs for the full life of the policy supports *informed* budgetary decision-making by showing the real financial impact of policy instruments that would otherwise appear initially costless.
 - Second, the recording of an appropriation to cover costs for the full life of the policy forces *responsible* budgetary decision-making that considers trade-offs and priorities against a background of limited resources.
 - Third, the recording of an appropriation, similarly to what would be done for a subsidy, creates a “level playing field” between policy instruments and allows *neutral* budgetary decision making where efficiency considerations are put above short-term optimization of fiscal outcomes.
3. Although several OECD countries have sought to improve their budgeting approach for loans and guarantees, few are fully complying with the principles stated above. Some countries estimate costs for the full life of their loans and guarantees programmes, and record these in the government balance sheet as liabilities, but they do not record an appropriation for the corresponding amount. Rather, it is the estimated amount of cash outflows for the next fiscal year that is appropriated. Such an approach has obvious merits from an informed budgetary decision-making and transparency perspectives. However, it does not create a level playing field with subsidies and is likely to perpetuate decision-making bias in favour of non-standard policy instruments. Therefore, it does not fully prop up responsible and neutral budgetary decision-making.

3. Scope of budgeting for loans and guarantees

4. In the Spending Better Framework and in this paper, the generic terms “loans” and “guarantees” refer to i) individual loans or guarantees granted to one third-party and ii) standardized programmes extended to a group of individuals or businesses. In providing individual or standardized loans and guarantees, governments may take over or mitigate credit risks, insurance risks or other types of risks, such as demand risks.
5. Terminology used for designating loans and guarantees may differ across countries. For instance, in the United States, legislation uses the terms credit programs to refer to both direct loans and loan guarantees aimed at aiding borrowers and insurance programs to refer to insurance of deposits in financial institutions and pension guarantees.⁴ Other countries

⁴ Direct loans are a disbursement of funds by the government to a non-Federal borrower under a loan agreement that requires repayment with or without interest. Loan guarantees include any guarantee, insurance, or other pledge of payment any portion of principal or interest on any debt obligation of a non-Federal borrower to a non-Federal lender.

may use the vocabulary of international accounting standards (International Financial Reporting Standards, or IFRS and International Public Sector Standards Board, or IPSAS). In these standards, loans and guarantees are referred to as financial instruments, loan commitments, insurance schemes, provisions, and contingent liabilities (Annex 1).

6. Irrespective of the terminology favoured, it is important that fiscal legislation includes a taxonomy of loans and guarantees used by a government, describe the budgetary implications of each main category of loans and guarantees, and explain the corresponding budgetary treatment. For instance, in the United States and Sweden, legislation has been passed that explains the nature and scope of federal/government loans and guarantee and legislates the associated budgetary treatment. In Australia, government loans and guarantees' taxonomy (e.g., the standards differentiate guarantees arising from legislative vs. contractual obligations) and their accounting treatment is determined in Australian Accounting Standards.

7. In principle, loans and guarantees should all follow similar budgetary treatment. However, in practice, government may provide for exceptions, which should be explained in legislation. Again, the United States provides a good example of this, as the exclusion of the deposit insurance programme as well as pension, crop, and flood insurance from the budgetary treatment applied to other credit programmes has been explained at the time of the Credit Reform Act's adoption (Anderson and Burke, 2021^[9]).⁵

8. A key issue with regards to budgeting for loans and guarantees is in relation to the institutional scope of OECD countries' budgets. This institutional scope varies significantly. This means that some countries will consider the budgetary implications of loans and guarantees schemes administered by state-owned corporations in their fiscal documentation (e.g., Australia), while others will not (e.g., the United States). This creates a risk that loans and guarantees be deliberately placed under the management of entities outside of the budget for fiscal rather than efficiency reasons (Heald, 2023^[12]).

9. Another issue is in relation to "implicit contingent liabilities". These are obligations that a government may feel obliged to fulfil for political or moral reasons in the absence of any contractual or legal obligation to do so. By virtue of being implicit and revealed only at the time when some crisis unfolds, these contingent liabilities are unbounded, imprecise, and therefore particularly difficult to identify and measure (Lindwall, 2013^[13]) However, they regularly crystallize. For instance, when the stability of a country's financial system is at risk, governments will likely feel obliged to provide financial support to banking institutions that far exceeds their legal obligation as evidenced by recent bailouts.

10. Whether financial implications of i) loans and guarantees administered by non-budgetary entities and ii) government implicit guarantees should be estimated and funded in the budget is not a settled question. In the case of implicit guarantees, the sheer scale of the financial sector in some OECD countries would make such an approach difficult to justify and even more difficult to implement, in addition to creating substantial moral hazard.

11. Therefore, a large majority of OECD countries prefer to quantify and report implicit contingent liabilities and other fiscal risks, such as those generated by non-budgetary entities, in a statement of fiscal risks (OECD, 2019^[14]). Good practices in OECD countries

⁵ Rationale for excluding deposit insurance programmes from the Credit Reform Act includes the fact that the goal of these programmes is to maintain stability and public confidence in the US financial system, which is monetary policy rather than fiscal policy.

with fiscal risks management have been discussed in a recent OECD Secretariat report (Moretti, Boucher and Giannini, 2021^[4])

4. Estimating costs of government loans and guarantees

4.1. Approaches for measuring the cost of loans and guarantees

12. There is no one-fits-all approach to estimating costs of loans and guarantees. Standardised loans and guarantees involve a pooling of risks and are very likely to generate cash outflows as it can be expected that in most cases some of the multiple beneficiaries will default on their loan payment or call guarantees. Accordingly, it is often possible to estimate reliably a future average loss by considering historical data. One-off loans or guarantees are, by nature, individual and credit risk analysis also needs to be done on standalone basis, with relatively less certainty on whether losses will be ultimately incurred or not.

13. In choosing an approach for estimating costs of loans and guarantees over their full lifetime, IPSASs are a useful reference to consider. IPSASs have been revised in 2018 to adopt new “forward-looking” evaluation principles, under which expected credit losses are considered for the initial evaluation of financial instruments, when they are first recorded in the balance sheet (IPSASB, 2018^[15]). Therefore, international accounting principles “match” to some extent the recommended approach for budgeting neutrally for loans and guarantees.

14. IPSAS principles applicable to loans and guarantees can be summarized as follows:

- For loans and guarantees falling under the category “financial instruments”⁶, IPSASs prescribe mainly recording a liability representing the net present value of expected cash-flows for the scheme, using a so-called “dual measurement approach.”^{7, 8} IPSASs also prescribe market discount rates be used for measuring the present value of expected cash flows. The operating statement records the corresponding net benefit or loss. This represents the cost of the scheme for the government and should be treated as expenses in appropriations.
- For a concessionary loan, IPSASs require that the market value of the loan be determined with so-called “day one” losses generated by the concessionary interest

⁶ Financial instruments are defined in international accounting standards as contracts that give rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

⁷ For loans, these cash flows may include initial disbursements, repayments of principal and payments of interest and fees, estimated defaults, payments of penalties and other payments to the Government over the life of the loan, and recoveries or proceeds of asset sales in case of default, etc. For guarantees, these cash-flows may include payments of premiums, estimated calls, revenues from collaterals, etc. It.

⁸ The dual measurement approach authorises to estimate expected losses from financial instruments over 12-months or their lifetime. The determination of which expected losses to consider depends on whether there has been a significant increase in credit risk since the inception of the financial instrument: if there has not been a significant increase (typically the “normal” scenario), only the 12-month expected credit losses are factored into the loss allowance for the instrument; and if there had been a significant increase, the loss allowance needs to consider the lifetime expected credit losses of the instrument (which is often a higher amount than its 12-month expected losses). Whether a significant increase in credit risk has occurred depends on an assessment of any changes to the probability of default over the life of the instrument, and not changes to the expected loss itself.

rate measured at the time when a loan is granted. The operating statement records these losses. These represent the cost of the concessionary loan for the government and should be treated as expenses in appropriations.

- For guarantees that do not fall under the category “financial instruments”, IPSASs prescribe that a provision should be recorded on the government’s balance sheet if there is a higher than 50% chance that this guarantee will be called. The operating statement records the corresponding loss. This represents the cost of the guarantee for the government and should be treated as an expense in appropriations.

15. In defining a budgetary treatment for loans and guarantees, governments should avoid to the extent possible discretion and aim for prudence. Therefore, where IPSASs offer options or rely heavily on judgement, countries may want to use simpler and/or more prudent principles for budgeting. For instance, concerning guarantees that are not financial instruments, the accounting treatment prescribed by IPSAS relies heavily on judgement and may understate expected costs: a tail event that is unlikely to occur could still have major budgetary implications. Some countries, such as the United States, have therefore adopted a more prudent budgetary treatment, which consists in reporting the possible effects of “unlikely events” in the budget using an expected value approach that considers the full range of outcomes, irrespective of any “50 percent threshold”.

4.2. Implementation

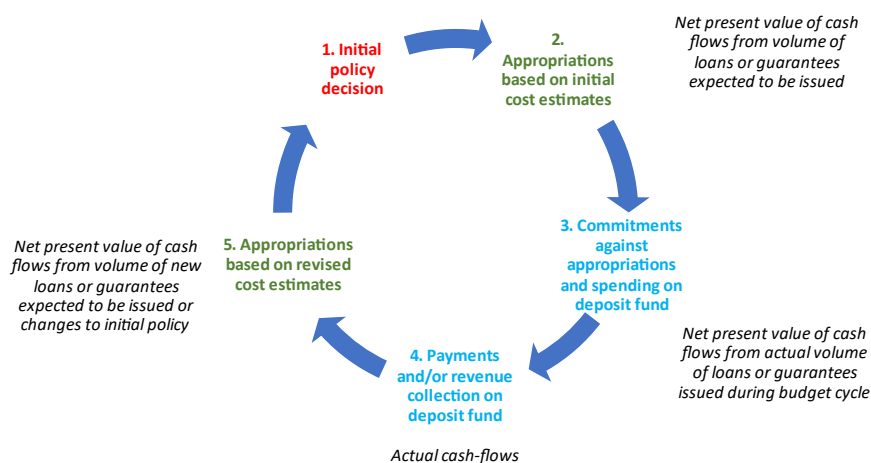
16. In implementing the measurement approach for standardized loans and guarantees, budgetary entities will be required to estimate all the estimated cash-flows for a given scheme, but also estimate how many loans or guarantees are expected to be granted over relevant budget periods (annual budget and/or medium-term fiscal plan). The appropriation allocated in the budget to the scheme, and resource envelope in the medium-term fiscal plan, will therefore cover costs from the successive cohorts of loans that governments will likely enter during each fiscal year covered by the budget and medium-term fiscal plan.

17. As part of each budget cycle, budgetary entities will be required to update these estimates, which may imply i) revising previous estimations of the number of loans and guarantees that will be entered into, ii) revising estimates of likely costs associated with each cohort of loans and guarantees, and iii) adding an outyear to the medium-term fiscal plan if additional obligations are expected to be incurred by government over that period (Figure 4.1).

18. The recording of the appropriations for the costs of loans and guarantees should be done on the most appropriate budget line. As the purpose of this budgetary treatment is to allocate resources to cover for the subsidy element of government loans or guarantees, a classification under the “transfer” or “subsidy” chapter of the budget would be justified. This is for instance the approach followed in Sweden, in cases when there is a “substantial subsidy element” in loans or guarantees.

19. In implementing what can be considered as a complex budgetary treatment, judgement can be applied. For instance, in the case of Switzerland, appropriations are recorded only significant schemes and those that are not considered significant in terms of their gross amount may not be budgeted for. In parallel fashion, in the United States, the Congressional Budget Office uses its own subsidy estimates for student loans and the various mortgage finance credits, which are large programs. For smaller programs, it uses Office of Management and Budget’s estimates.

Figure 4.1. Steps of appropriating resources for loans and guarantees' costs



Source: Author

20. Concerning one-off guarantees, it will be often the case that a guarantee will be granted initially on the assumption of a low probability of it being called, but subsequently the financial situation of the beneficiary might be deteriorates to the point where a call on the guarantee seems to be more likely than not. Therefore, budgetary entities should be required to monitor at least annually their portfolio of one-off guarantees to identify any such situation and allocate appropriate resources in their budget envelope to cover corresponding losses.

4.3. Methodological issues

21. In estimating the costs of loans and guarantees, OECD countries experience show that there are key methodological issues with estimating default and calls risks; choosing a discount rate; and treatment of administrative costs in estimates of future cash flows. Each one of these factors can significantly influence the outcome of the costing and have an even more significant impact taken all together.

22. On estimating risks of defaults and calls, a range of approaches are used by OECD countries. For one-off loans and guarantees, credit ratings are most used. For standardized loans and guarantees possible approaches include credit ratings (e.g., Australia, Sweden, and Switzerland), statistical models (e.g., Republic of Türkiye) and stochastic simulations (e.g., Sweden). The choice of an approach is highly context-specific, with “key differentiating factors [including] characteristics of the guarantee and on-lending portfolio, the sovereign’s specific risk exposure, the availability of market information and data, and resources and capacity in the public sector” (Bachmair, 2016^[16])

23. On the setting of a public sector discount rate, OECD countries follow a range of approaches. Some OECD countries (e.g., Australia, New Zealand, and Switzerland) use market rates as prescribed by IPSAS. The United States’ Office for Management and Budget uses the government’s own borrowing rate. The United Kingdom uses “the higher of the rate intrinsic to the financial instrument and the real financial instrument discount

rate set by HM Treasury”.⁹ The choice of market or government own borrowing rates can have significant impact on the measurement of costs of loans and guarantees. For instance, in the United States, the Congressional Budget Office estimated that for new loans and loan guarantees issued in 2023, depending on the borrowing rate used, the policy would be estimated to carry a significant subsidy cost vs. generating significant savings.¹⁰

24. Pros and cons of using market or government own borrowing rates have been discussed in several recent publications (Hong and Lucas, 2023^[10]; Anderson and Burke, 2021^[9]). Debates are on-going and can be very briefly summarized as follows:

- The logic of using government own borrowing rates is that government loans and guarantees’ costs should be measured based on the actual financing conditions for the government.
- The logic of using market rates is that government loans and guarantees’ costs should be determined irrespective of them being financed by government, which benefits from more favourable financing conditions than the private sector due to taxpayers’ acting as risk-absorber and therefore implicitly are bearing that cost, even if not measured in the budget. It is to be noted that the use of market rates can convey practical challenges as these rates may not be publicly available as was highlighted in a recent presentation by Switzerland (Walker and Matter, 2023^[17]).

25. The United States’ experience shows that integrating or not administrative costs – that is the costs to manage a loan or guarantee programme (including salaries of staff) - can have substantial impact on the estimated subsidy cost for loans and guarantees programmes, and therefore influence decision-making on most appropriate financing model for a policy (Anderson and Burke, 2021^[9]).

26. It is undisputable that integrating administrative expenses in the costing of loans and guarantees schemes is the appropriate way to inform on their full cost, but such a costing is also not consistent the objective of creating a level playing field with direct spending as grants, transfers and benefits-related appropriations does not include administrative costs. Therefore, countries may consider providing activity-based costings for loans and guarantees that include administrative costs, programmes in the budget documentation but recording allocating resources in appropriations that do not include administrative costs.¹¹ In such a case, budget instructions should require that administration costs of these schemes be properly accounted for in baselines provided by budgetary entities as part of the budget formulation process.

⁹ See [Government Financial reporting Manual](#). The real financial instrument discount rate set by HM Treasury is recalculated annually and is made up of two components. Firstly, the nominal rate is based on yields on UK government bonds as published by the Bank of England. Secondly, the rate of inflation, which in practise may be RPI or CPI or perhaps a similar rate depending on the individual loan or guarantee. The Office of Budget Responsibility produce a forecast for various inflation rates biannually as part of their Economic and Fiscal Outlook publication that is used for the purpose of defining the rate of inflation when calculating a real discount rate.

¹⁰ “Using Federal Credit Reform Act of 1990 procedures, CBO estimates that new loans and loan guarantees issued in 2023 would result in savings of \$41.1 billion. But using the fair-value approach [which measure the market value of the government’s obligations], CBO estimates that those loans and guarantees would have a lifetime cost of \$51.1 billion.” See <https://www.cbo.gov/publication/58031>

¹¹ Activity based costing identifies and assigns the cost of each activity or specific input that delivers a service or output.

4.4. Data challenges

27. Reliable estimation of costs associated with government loans and guarantees does not require only a sound measurement approach but also appropriate data to implement the methodology. Tellingly, at the outset of the COVID-19 pandemic, many OECD countries only disclosed in their budget documentation a figure on the maximum exposure on loans and guarantee schemes announced by governments, with the lack of historical data on new and emergency schemes announced by governments often cited as the main cause for not providing cost estimates (Moretti, Braendle and Leroy, 2021^[2]) Irrespective of constraints experienced during crisis situations, assembling data necessary to produce costs estimates is generally considered a challenging exercise (HM Treasury, 2020^[7])

28. In implementing budgeting for loans and guarantees, a key task for governments is to establish procedures in budgetary entities to ensure that relevant data on loans and guarantees administration are, first, collected and, second, properly maintained. In the case of the United States, data collected includes, among other things, historical data and trends, sensitivity analysis or actuarial analysis that identifies the critical factors in predicting cashflows, reports from accounting systems, documentation of program design factors relevant to the estimates including defined fees, grace periods, terms to maturity, borrower interest rates, legal definitions, and program eligibility requirements (Anderson and Burke, 2021^[9]).

29. In the case of new schemes with no historical data available, budgetary entities should be encouraged to i) use alternative data sources assuming these are considered reliable enough and ii) apply their best judgement in defining which external data sets or expert opinion to use. For instance, in 2020, Switzerland provided a new type of guarantee on more than 100,000 commercial bank loans as part of their response to the COVID-19 crisis and used external rating agencies' credit rating as an input to assess the average probability of default and record the corresponding liability on the government balance sheet (Walker and Matter, 2023^[17]).

5. Budgeting for loans and guarantees in cash budget systems

30. As noted above, appropriations are managed on cash-basis in the vast majority of OECD countries. This reflects the fact that cash appropriations allow more reliable and understandable setting of spending limits and better control over actual resources spent by ministries and departments, contrary to accruals-basis, which may generate volatility and discretion in spending limits estimates. Some countries have however moved away from "strict" cash-basis by introducing some accruals concepts where these were supporting better budgetary decision-making.

31. In budgeting for loans and guarantees on accruals basis in an otherwise cash-basis appropriations system, the successful experiences of the United States and Sweden in using notional reserve accounts for budgeting for standardized loans or guarantees programmes are noteworthy:

- In the United States, a system of "financing accounts" is used. The financing accounts are included in the budget totals but are treated as a "means of financing", defined by OMB as "...monies received or paid by the Government that are not counted in the budget totals as either collections (governmental receipts, offsetting collections, or offsetting receipts) or outgo (outlays)." (Anderson and Burke, 2021^[9]) For loans, financing account include i) appropriations (called "subsidy payment"), ii) borrowing from Treasury to finance the loans and iii) actual cash

flows from the loans (loan disbursements, default payments to lenders, loan repayments, interest payments, recoveries on defaulted loans, and fee collections). The financing account is used to repay Treasury with interest over time, using payments from the borrower. For guarantees, financing accounts hold i) appropriations, which serve as a reserve against default claims; ii) interest earnings on this reserve from Treasury, iii) and actual cash flows from default claims. This system also allows make sure the costs estimates and cash-flows line up.

- In Sweden, each responsible authority keeps a “notional reserve account” at the Swedish National Debt Office. Expected losses from lending and guarantees are credited to the notional reserve account. A call on state guarantee is booked against the applicable nominal reserve and the resulting payment is charged against the Treasury Single Account. Fees and recoveries are also recorded in these nominal accounts and transferred into the central government revenues to decrease the SNDO’s borrowing requirement.

32. The United Kingdom’s approach to budgeting for one-off guarantees is also noteworthy. Its newly approved Contingent liability approval framework mandates that when departments decide to enter into a new one-off guarantee, this guarantee must be affordable within their existing resource budgets, unless there is a bespoke agreement that extra resource will be provided. Therefore, expected losses are recorded as “non-cash costs” in the appropriations, under the category “annually managed expenditures”. This gives departments approval to spend, but do not entail a cash allocation, so if the guarantee crystallises, it is expected that resources will be reallocated from another budget line or from the contingency reserve managed centrally by the Treasury.

6. Role for Budget Offices

33. Roles and responsibilities for the management of government loans and guarantees have been an area of attention since the global financial crisis, during which governments started making significant use of these mechanisms to support banks and corporations through the crisis. At that time, a more active engagement in the management of contingent liabilities of a number of stakeholders was called, including budget offices and debt management offices. Using debt management office’s expertise in areas such as producing guarantees issuance guidelines, estimating premiums to be charged on guarantees, managing of guarantees-related reserve funds was for instance highlighted as essential (Ülgentürk, 2017^[18]). Budget offices were expected to take a more active role in budgeting for loans and guarantees, along the two main lines discussed below.

34. First, they should play a role in highlighting budgetary issues with non-standard policy instruments such as loans and guarantees to the attention of policymakers. They should also take the lead in proposing new or improved approaches for budgeting for loans and guarantees, consistent with the principles stated in section 2 above. In doing so, budget offices fulfil their key role of achieving allocative efficiency.

35. Second, they have a crucial role to play in operationalizing this approach as part of their role of coordination of the budgets and appropriations’ formulation for completeness and accuracy. This involves at least:

- Defining rules and principles regarding data collection on loans and guarantees by budgetary entities, including which type of data to collect, time-periods to be covered, auditability requirements, etc.

- Defining requirements for all new policy proposals involving a guarantee or loan, including the production of an estimate of the full cost of the new policy as well as quantification of costs of delivering the same policy objectives through traditional financing.
- Providing methodological guidance on how to assess the costs of loans and guarantees, including designing appropriate calculation tools and updating these at least annually (e.g., with up-to-date discount rates).
- Reviewing new policy proposals, including assessing the clarity of the stated objectives, verifying costings, the soundness of criteria and rules for granting loans and guarantees, etc.
- Requesting that budgetary entities' multi-year baselines and annual budget submissions include costs for government and loans, as well as any increase in administrative, including legal, costs for the administration of these programmes.

36. Another important role for ministries of finance is to manage movements from or to any actual or notional deposit fund – that is recording and monitoring cash outflows (loan disbursements, pay-outs for guarantees, etc.) and cash inflows (reimbursements, interests, fees, etc.). This might be a function of the budget office or, alternatively, of the Treasury function within the ministry of finance.

37. An important decision to make in defining operational procedures for budgeting for loans and guarantees is whether to decentralise or centralize the measurement of their costs. Such a measurement may be difficult to produce by budgetary entities because it requires a range of technical skills, such as credit risks analysis for credit programmes, actuarial analysis for insurance programmes, as well as general commercial and legal expertise (HM Treasury, 2020^[7]). Centralization and decentralization have pros and cons as budgetary entities have first-hand knowledge of schemes and programmes, but the budget office and other specialized entities have most of the technical knowledge required for producing the costings.

38. If the decentralization approach is favoured, the budget office should ensure that budgetary entities are provided with all necessary guidance. In the case of Australia, for instance, the Department of Finance supports agencies through a team assigned with specific sectors and tools and guidance available on the department's website. In the case of the United States, however, fragmented responsibilities are considered to have caused inefficiencies (Anderson and Burke, 2021^[9]).

39. In any case, establishing a strong central capacity to directly produce costings or verify the costings produced by budgetary entities is generally considered a key success factor in managing risks associated with loans and guarantees (HM Treasury, 2020^[7]). Such a central capability should be in the budget office with the responsibility of coordinating with relevant specialised entities for expert knowledge or data, such as the debt management office and agencies specialized in credit or insurance programmes management.

7. Conclusion

40. This paper asked whether “budgeting can catch up with the rise of non-standard policy instruments”, and more specifically with the rise of loans and guarantees. The answer is clearly yes based on the experiences of the OECD countries presented in this paper. Budget systems will however need to adapt to this new paradigm.

41. Key considerations for successfully managing non-standard policy instruments include:

- Budget offices should have a leading role in proposing budgetary treatment for loans and guarantees that ensure an even-level playing field with traditional spending (*i.e.*, budget neutrality) and put considerations of efficiency of spending above optimization of short-term fiscal outcomes.
- Loans and guarantees used to fund government policies directly should be explained in legislation and/or budget documentation and the budgetary treatment applicable to each category defined. Any exception to the principle of budget neutrality should be identified and explained.
- For achieving budget neutrality, costs of standardized loans and guarantees should be measured based on estimates of the net present value of all expected cash-flows from them. In defining a measurement method, IPSASs can be used as reference and clarity is needed on approaches for evaluating risks of defaults and calls; discount rates to be used; and inclusion or not of administrative costs in costs evaluations.
- For one-off loans and guarantees, budgetary treatments should be prudent and avoid relying too heavily on discretion and judgement. Countries may consider the United States approach of recording possible effects of “unlikely events” in the budget using an expected value approach.
- When losses incurred from loans or guarantees are recorded on accrual-basis in an otherwise cash-basis appropriations system, an actual or notional deposit accounts should be used to record these accrual expenses separately from actual cash-flows.
- Data requirements for measuring costs of loans and guarantees should be specified in Budget Offices’ instructions to budgetary entities, with options and alternatives offered in case when historical data is lacking.
- Budget offices should establish a strong central capability with relevant expertise for producing directly or verifying costings of loans and guarantees and coordinating with agencies with specialized knowledge.

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