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Options for Budget Consolidation on the Expenditure Side

A detailed analysis of Austrian public expenditures reveal both large efficiency reserves and savings potentials especially in the areas public administration, direct business subsidies, health care and pension systems. While the resulting short-term savings potentials can be implemented simply and fast relative to tapping the full potential of long-term savings – the latter imply far reaching institutional reforms.

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Empirical studies show the unequivocal importance of reducing expenditure for a sustainable and successful consolidation. Total government expenditure (according to the categorisation of the government sector under ESA 95) was € 137.9 billion in 2008 or 48.9 percent of GDP. Amongst the other countries in the EU 15 only Sweden, Denmark, France, Finland and Belgium had higher expenditure ratios than Austria (46.3 percent)¹. Against this background Austria clearly has, in principle, substantial potential for an expenditure based consolidation.

In a comparison of economic expenditure structure of 36 OECD countries (Table 1) relatively low production and investment spending in Austria is accompanied by noticeably higher transfer payments to private households and businesses (market producers). Part of this difference can be explained by the creation of extra budgetary units. Here, by international comparison, business subsidies and grants tend to be depicted too high, and state investment and production expenditure too low (Pitlik *et al.*, 2008). If investment of these extra budgetary units, which used to be part of the state sector, is included, the amount of public investment is 2.1 percent of GDP and thus twice as high, even though still small in international comparisons.

Using the functional expenditure structure Austria differentiates from other countries² in the categories defence, environmental protection, as well as housing and com-

Expenditure structure in an international comparison

¹ Government expenditure ratios are also influenced by institutional and accounting rules. Therefore any international comparison should, in principle, take account of these country specific differences (e.g., Joumard *et al.*, 2003). As a result of this, government expenditure in Austria tends to be underestimated due to budgetary classifications. In Italy and in Scandinavia social security payments are taxed in pretty much the same way as earned income whereas in Austria they are tax free. As a result social security expenditure and the total government expenditure (and tax revenues) in the former countries end up being *ceteris paribus* higher. The contrary is true of the Swiss pensions system which like the Austrian system works with compulsory contributions. In Switzerland, however, the pension system is run by private insurance companies with capital cover but regulated by the government. According to the ESA 95 this does not fall within the government sector. As a result when compared with Switzerland Austria's share of government expenditure tends to be much higher.

² Classification according to COFOG (Classification of the Functions of Government), without interest payments, which are mostly booked to the category of general public administration according to the COFOG classification. The most recent data for a larger group of countries refers to the year 2007. The information from other OECD countries (USA, Switzerland, and Japan) partly uses a different classification method and is often incomplete. We decided not to present that information here.

munity amenities. Austria spends much less in these areas than the international average. In Austria in 2007 spending in the areas "economic affairs" (+0.6 percentage points as compared to the average of the EU 15), health care (+1 percentage point) and "social security" (+2.6 percentage points; +4.1 percentage points as compared with the EU-27 average and Norway, without Bulgaria, Lithuania and Rumania; Table 2) is far above the average of those countries used for comparison³.

Table 1: Economic expenditure structure

2008

	OECD countries ¹	EU 15 ² As a percentage of GDP	Austria
Production expenditure	17.1	17.8	13.7
Personnel costs	10.8	11.4	9.2
Intermediate consumption	6.3	6.4	4.6
Transfers to private households	18.1	20.8	25.7
Benefits in kind	2.9	3.8	5.5
Monetary social transfers	12.7	14.8	18.1
Other transfers	2.5	2.2	2.1
Transfers to businesses	2.3	2.4	5.5
Subsidies	1.3	1.2	3.5
Capital transfers	1.0	1.2	2.0
Gross investment	3.3	2.8	1.1
Primary expenditure	40.7	44.0	46.3
Interest payments	2.1	2.4	2.6
Total government expenditure	42.8	46.4	48.9

Source: OECD, Eurostat (latest data available for comparison September 2009), WIFO calculations, Total Austrian expenditure: Eurostat, as of November. – ¹ Unweighted average for EU 27 (without Romania and Bulgaria), Australia, Iceland, Japan, New Zealand, Norway, Switzerland, South Korea, USA. – ² Unweighted average EU 15 without Austria.

Table 2: Functional expenditure structure

2007

	OECD countries ¹	EU 15 ² As a percentage of GDP	Austria
General public services	3.9	3.8	4.0
Defence	1.3	1.3	0.9
Public order and security	1.7	1.5	1.4
Economic affairs	4.4	4.0	4.6
Environmental protection	0.7	0.7	0.5
Housing, community amenities	0.9	0.9	0.6
Health care	6.0	6.5	7.5
Recreation, culture, sport, religion,	1.2	1.1	1.0
Education	5.4	5.2	5.2
Social protection	15.8	17.3	19.9
Interest payments (capital income)	2.2	2.4	2.9
Total	43.6	44.8	48.4

Source: Eurostat, WIFO calculations. – ¹ Unweighted average for EU 27 (without Bulgaria, Lithuania and Romania), Norway. – ² Unweighted average EU 15 without Austria.

³ The below average expenditure on the environment and on housing and communal amenities result mostly from the formal privatisation of the public utilities. As regards housing, the main part of expenditure on building subsidies is not included in the figures because loans within the definitions for the national accounts are financial transactions and therefore are not part of state expenditure.

When we talk about the presumed potential for savings in the area of public administration in Austria it is often argued that the government bureaucracy is too large and too expensive. However, considering international comparisons to find where savings can be made, it must be kept in mind that the size of the administration is dependent on the definition of the government sector and on the level of state involvement in production and the provision of public services (Pitlik *et al.*, 2008, p. 108ff). In addition when looking at the efficiency of public spending the actual quality of the services provided must be considered.

Public services can be carried out by state run corporations or non-state providers. However, the purchase of privately produced services still comes out of the general public finances (Naschold, 1995, Schedler – Proeller, 2006). As a result of this international comparisons can show large differences in personnel and intermediate consumption (material costs) which are actually due to purely organisational factors. Thus, the personnel and material costs of the Austrian state sector at 13.7 percent are lower than the average of the other EU 15 (at 17.8 percent see Table 1). However, these differences can partly be traced back to the different classifications of the government sector and variations in how the costs are statistically recorded (also Pilichowski – Turkisch, 2008). The personnel costs declared for Austria (9.2 percent of GDP) do not include the expenditure for numerous formally privatised units (hospitals, public utilities); intermediate consumption spending does not include any payments for services which are purchased from extra budgetary hospitals which used to be part of the state sector. Thus, the personnel and material costs for the general government sector systematically underestimate the running costs for public administration in Austria and therefore should only be used for international comparisons with some caution.

Savings potential

Public administration

Table 3: Definition of administrative terms

Total administration

Lifelong employed civil servants or contract staffs which work in a unit which is categorised as belonging to the government sector according to the ESA 95. Thus in Austria the employees of the ÖBB (rail), ASFINAG (roads), BIG (public real estate), most hospitals and numerous communal utilities are not actually included under the heading "total administration". Despite the formal outsourcing of the universities they do still fall under "total administration", because they are apportioned to the government sector.

Core administration

This includes all employees who fall into the NACE Classification "L" and perform "core public services". Public order and security (police, justice), defence and the administrative tasks associated with social insurance all fall into this category. What is not included are those employees providing services in the education system (e.g., teachers in schools and universities), health care (e.g., doctors and nurses), waste disposal or social care (e.g., social work). However, the administration of these services does fall within core administration.

General public services

All employees which fall within the COFOG division "General public administration". These are the legislative and executive organs, financial and fiscal affairs, external affairs, foreign economic aid and general services (personnel services, statistical services). This means that general public administration primarily includes those services necessary for the organisation of the state and which do not serve a particular socio-economic or political function.

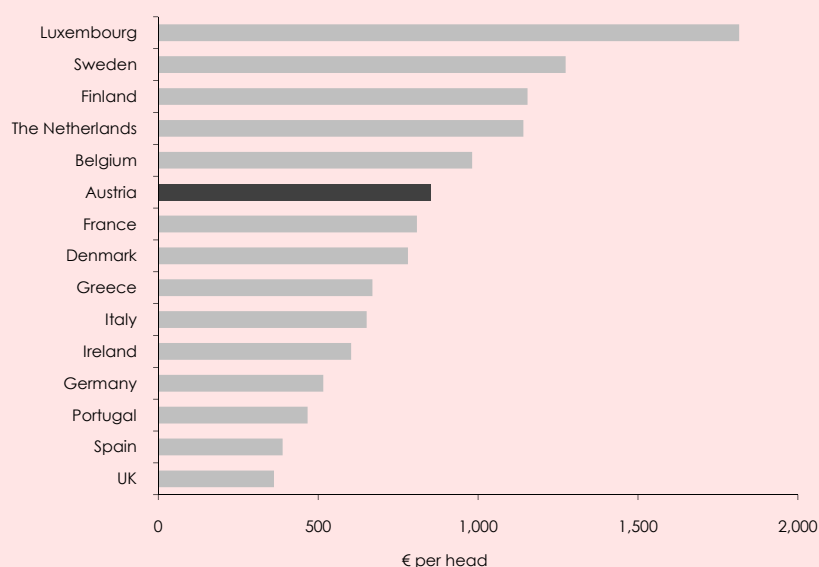
Source: Statistics Austria, WIFO. For the categorisation of the state sector. http://www.statistik.at/web_de/statistiken/oeffentliche_finanzen_und_steuern/oeffentliche_finanzen/oeffentlicher_sektor/index.html.

Therefore due to differences in classification for international comparisons it makes more sense to compare those costs which fall into administrative areas that usually carried out by the government (core services, see Table 3). Outlays on cores government services in Austria rose between 1976 and 1999 from 6.1 percent to 7.8 percent of GDP but could then be reduced to 6.9 percent of GDP by 2007 (€ 18.7 billion). The personnel and material costs of the core services as a proportion of GDP in Austria lie well below the EU-15 average. This is mainly due to the fact that the current costs for public security, law and order, and defence are well below average (1.3 percent and 0.8 percent of GDP respectively). If calculated per capita (population) the personnel and material costs falling under general administrative services in Austria take place 6 with € 852 within the EU 15 (Figure 1).

As shown by WIFO studies (Pitlik *et al.*, 2008, Pasterniak – Pitlik, 2008) economies of scale are especially relevant in the category of general public services which is

even more narrowly defined. Per capita expenditures of the government decline with an increasing size of the population. The costs in Austria for employees compensation and intermediate consumption do correspond to the international average, if you take into account other potential structural determinants (living standards, federal structure of the state, level of regulation), as compared with countries of a similar size such as Denmark or Ireland. However, there is still a theoretical potential to improve efficiency by € 0.75 to 2.5 billion. These potential savings would be equivalent to one third of the expenses. It is very difficult to measure the quality of the general public services and this is made even more difficult due to the macro political perspective which leads to aggregation and information problems. Nevertheless, empirical evidence in economic studies does point towards the fact that higher spending does lead to improved performance as in the comparable countries. In international comparisons the performance of the Austrian administration is good but it remains weaker than the performance of public administration in comparable countries (Denmark, Switzerland).

Figure 1: Current personnel and material costs for general public services in 2007



Source: Eurostat, OECD, Statistics Austria, WIFO.

The considerable savings potential can only be realised in the short term to a rather small extent, since structural reforms would be a pre-requisite in most cases. Civil servants have a comprehensive employment protection so that staff cutbacks are actually only partially possible by gradually not filling posts when they become vacant (attrition)⁴. The "natural turnover rate" of civil servants leaving public service on a yearly basis is about 3 percent (Hartmann, 2009). On the basis of this figure and the salaries in the public sector (according to the national accounts) which amounted to € 25.9 billion in 2008, the savings potential from not refilling posts as they become free would amount to € 775 million p.a. (Table 4). It must be noted that this calculation includes all public servants (e.g., police, justice, defence, welfare and education). The savings potential is considerably smaller if you exclude cut backs in education due to the incredible importance of education to the growth potential of Austria (€ 465 million).

In order to be able to exploit the short-term savings potential from an abdication of re-occupation, civil servant employment laws would have to become much more flexible. To facilitate the exchange of personnel between different areas of public

⁴ The method often used in Austria to make cut backs using early retirement does reduce the actual running costs but simply increases pension costs.

services, the restrictions on the placement and deployment of personnel need to be abolished as comprehensively and as quickly as possible.

Table 4: Short-term savings potential in the administration

	Savings potential by not refilling posts from natural turnover and cutting back material costs	
	Natural turnover of 3 percent	Natural turnover of 1,5 percent
	Million €	
Personnel costs		
General public administration	150	75
Core administration	375	185
Total administration without education	465	230
Total administration	775	390
Intermediate consumption		
General public administration	70	35
Core administration	235	120
Total administration without education	300	150
Total administration	370	185
Total personnel and material costs		
General public administration	220	110
Core administration	610	305
Total administration without education	765	380
Total administration	1,145	575

Source: WIFO calculations. The potential is not additive. The more narrowly a cutback is defined the smaller the resulting savings potential. Total administration: in 2008, material costs without disposing of the fighter jets. Education. Core administration and general public administration: in 2007. In order to make the data comparable the personnel and material costs from core administration were extrapolated using the growth rate of expenditure in the general public administration; education expenditure using the growth rate of total education expenditure according to COFOG. Expenditure in general public service was not extrapolated.

In the short term intermediate consumption can be reduced through a variety of measures, but in total only a rather limited overall saving can be achieved. Among these measures is an intensified co-operation in the production and provision of public services (shared services) which can be used in a repeated and standardised form for several units and barely need any specific local knowledge (Wegener, 2007). This means that legal provisions which currently prevent such cooperation need, as far as possible, to be abolished (Pitlik *et al.*, 2010). This is dependent above all on the willingness of decision makers in politics and administration to cooperate. If a benchmark a saving of 3 percent⁵ of administrative material costs is assumed, there could be a total saving in public administration cost in the short term of € 370 million (Table 4).

If this calculation is applied to the entire personnel and material costs there is a short-term maximum savings potential in public administration (at 2008 prices) of up to € 1.1 billion (Table 4). However, you can only achieve sustainable savings in the medium and long term if far reaching institutional reforms are implemented. This would mean that the actual institutional framework for public administration would have to change fundamentally. However, the potential savings from single reforms can almost not be quantified in a serious way. Only if these reforms are taken as a whole they can work as incentives for politics and administration to apply taxpayers' money more efficiently. Furthermore reforming institutional arrangements can very rarely be implemented without causing friction and therefore such reforms are often accompanied by initial re-organisational costs.

Fundamentally what needs to be checked comprehensively is whether government (co-)responsibility for the provision of particular goods and services is actually necessary and economically sensible. In other words: some services currently produced or financed by the government might be produced more cheaply and efficiently by the private sector, and it would be appropriate to reduce government intervention to a public guarantee function. Therefore it is primarily about "shortening" the list of

⁵ The material cost of disposing of the fighter jets is not accounted for.

government tasks⁶. As a particular task is abandoned (deregulation) the existence and organisation of the agency that was previously responsible should also be addressed. Reducing bureaucratic regulation cannot be separated from modernising administration in general. They both need to be subject to a common system of monitoring and control. However, the issue that remains open is whether savings can really be made by formal privatisation of organisations (so that they become extra budgetary) or whether the savings remain purely of an accounting nature in the budget.

As regards the employment of civil servants the most important issue is increasing their flexibility and mobility (both regional and professional). As it is actually impossible to make staff cut backs by terminating employment contracts it is even more important that available staff resources are used efficiently. This requires both that staff has a high level of qualification as well as that restrictions on mobility are abolished so that the civil servants can be deployed more flexibly. The pension system for public employees in the Länder and local authorities (Städte, Gemeinden) and in extra budgetary units which have been sourced out of the state sector should be aligned with those of the federal level so that barriers to mobility can be abolished when moving between public employers or to the private sector.

Modern employment and salary laws which, with only a few exceptions, no longer protect against dismissal or location changes and have no premiums for specific job tasks are also a key component of any reforms. By levelling out the salary scheme (higher starting salaries with less increase according to age) and placing a stronger focus on rewarding performance, significant savings could also be made (depending on how it is organised).

An important issue as regards administrative reform is the consolidation of which governmental level carries out which tasks and who is responsible for expenditure and revenue (Pitlik et al., 2010). Pivotal to the discussion is how various governmental tasks are allocated amongst the authorities. Currently the assignment of tax and expenditure responsibilities in Austria can be described as non-transparent, fragmented and inefficient (e.g., Schroeder – Weber, 2006). The political responsibilities in many fields (health care, schools, social care and economic development, etc.) are barely understandable. The entire system is riddled with an "organised lack of responsibility". Disentangling responsibility for particular tasks should be ranked high on the list of reform priorities. The number of policy areas where responsibility are shared between the federal and regional level (and if applicable, local authorities) should not be extended but rather kept to a minimum. This is in contrast to the "three pillar model" of the expert group for government and administrative reform.

The fragmentation of responsibilities brings with it its own set of problems. Austria's revenue sharing system does not actually allow for any institutional congruency (apart from in few insignificant circumstances). The almost complete separation of spending responsibilities from decisions regarding their financing is one of the main causes for the growth of public expenditures (e.g., Pitlik, 2007, Matzinger, 2008). The system of shared revenues (Finanzausgleich) has shown itself to be a fundamental obstacle for a consolidation of responsibilities for tasks, expenses and revenues at all levels of government. Achieving institutional congruence does not only mean taking responsibility for tasks and spending at the various levels of the federal state but also having some (limited) responsibility for your own finances. This would also mean allowing the regions and local authorities to have some say about levying taxes.

As compared to other countries with a federal government fiscal decisions in Austria are mostly made at a central level. The share of expenditures and revenues occurring purely at the local authority level is more similar to the average for centralised states rather than that of other federal states. This is reflected in particular in the financial interrelation between the central and sub-centrals of government which are

⁶ As highlighted by the tasks reform commission (Raschauer, 2001) whether or not a task is defined as a core state task depends on temporal and socio-political circumstances.

dominated by transfers and which places little importance on the tax autonomy of the Länder and communities. Between 2004 and 2008 intergovernmental transfer flows, that means payments between different levels of the government increased by 3.2 percent p.a. (*Government Debt Committee, 2009*). This does not even include payments within sub-sectors (e.g., transfers to extra budgetary units). The entire fiscal transfer system should be reformed, based on a clear and verifiable output goals (e.g., *Handler – Schratzenstaller, 2005*). In order to re-vitalise federalism it would be worth placing more importance on the principle of subsidiarity. Furthermore elements of competition should also become more pronounced in Austrian fiscal federalism.

The dominant principle of a cooperative federalism in Austria causes organisational and monitoring problems which mean that authorities at the federal, regional and local level have to co-ordinate their policies to fulfil their obligations. The main focus of any reforms should always be placed on trying to re-align the spending and financing powers, so that the responsibility for particular policy areas are consolidated for a single governmental task at a single level. For those political areas which are of a multi level character (e.g., education, environment and transport) a performance based control system could combine the advantages of a decentralised provision with centralised control elements. The main elements of such a system could be as follows (*Pitlik et al., 2010*):

- The assignment of responsibilities between the federal level and the regional level should try to orientate itself towards a performance related relationship defined in advance. The federal level should take on the role of the contracting body which sets the strategic goals and the regions should be the units which carry out the tasks to achieve these goals⁷.
- The federal level and the regions could agree on performance goals for political areas using a coordination process and could cement these in a quantitative performance measurement system.
- The regions should have a high degree of autonomy when choosing which instruments to use to fulfil their tasks so that the responsibility for both results and resources are combined. In this way the regions executing the tasks would also be responsible for the result of their administrative activities.
- The allocation of costs could be fixed within a framework of performance contracts. The most preferable system would be one with flat rate payments which could be developed not as payments to cover costs but as a reward for performance. An adequate incentive scheme would combine the factors of rewarding performance and covering costs.
- The effects of any monitoring and control would improve if Länder and communities were obliged to take part in institutionalised benchmarking.
- In order to increase transparency and improve comparability the budget and accounting system should be harmonised across all administrative levels.

The criticism directed at Austria's system of subsidies and capital transfers relates on the one hand to the level and efficiency of expenditures and on the other hand to the administration of the subsidies. In international comparisons direct business subsidies and grants in Austria (according to the national accounts) are exceedingly high⁸. The total amount of subsidies lies constantly well above 4 percent of GDP since the mid-1970s and since 1997 it has not even fallen below 5 percent⁹.

Direct business subsidies and grants

⁷ A similar system of administrative control has been put in place in the northern EU countries Denmark, Finland and Sweden. However, both countries do not have a regional level only a unitary constitution. According to the agency model ministries are purely responsible for strategic tasks whilst functional "agents" are responsible for the actual administrative tasks with a high level of autonomy and customer orientation. A model for cross level control could also be the "New Finanzausgleich" in Switzerland (e.g., *Frey – Wettstein, 2008*).

⁸ Here the data from the national accounts for the whole of the government sector ("general government") include not only direct business subsidies but also "subsidies" as defined in the national accounts as well as

Subsidies are increasingly viewed with scepticism because of their common side effect of preserving structures, for the corresponding lack of incentives they produce and for their distorting effect on the market (deadweight loss, permanent subsidies, moral hazard, etc.). Therefore if subsidies were cut back there could well be a significant consolidation effect which could also have positive effects on economic efficiency.

In 2008, the total amount of subsidies and grants was around € 15.6 billion which corresponds to 5.5 percent of GDP or 11.9 percent of the primary expenditure of the general government. Subsidies and capital transfers in the remaining countries of the EU 15 reached on average only 2.2 percent of GDP. If Austria reduced its subsidies to the EU-15 average there could be a theoretical savings potential of € 9 billion.

Transfers to market producers include transfers to agriculture, trade and industry as well as railways, the postal service and hospitals. Subsidies and investment grants of around € 4.3 billion (in 2007) are due to the fact that some health care units became extra budgetary. Subsidies to cover losses in health care have developed somewhat dynamically since 1997. Without this position in the budget there are still subsidies in the amount of 4 percent of GDP, which is still far above average. More than half of the business subsidies in Austria are for grants to public enterprises such as for the railways, transport, hospitals and municipal utilities. The Federal Austrian Railways (ÖBB) are granted substantial subsidies for public services as well as to maintain and extend the rail infrastructure (the federal contribution in 2008 according to the annual report was around € 1.8 billion. Contributions from the Länder are in addition to this). Against this background the way subsidies are granted is a central aspect of efficiency problems in publicly owned corporations (*Fleischmann, 2009*).

In almost all COFOG categories Austria has higher subsidy expenditure than the majority of the other countries (*Pitlik et al., 2008*). In the functional classification 29.2 percent of the subsidies and capital transfers (in 2007) go towards health care (€ 4.3 billion, € 4.0 billion to hospitals) and 42.4 percent towards economic affairs (€ 1.7 billion in general subsidies for the economy and the labour market, € 3.0 billion in transport including € 1.8 billion in capital transfers). A large share of the subsidies amounting to € 700 million from the federal, regional and local authorities was given to agriculture, although this share has been decreasing for years (1995 it was around € 2 billion).

According to current WIFO estimates Austria spends 1.5 times the amount on business subsidies as would actually be required according to structural factors (*Pitlik et al., 2008*). Without the subsidies in the health care sector the ensuing reduction to the level of structurally expected spending would lead to a long-term potential increase in efficiency of € 3.5 to 5 billion p.a.¹⁰. On the one hand considerations regarding long-term savings tie in with the general necessity of and the efficiency with which subsidies are granted. On the other hand there is the question of how the institutional framework of the subsidy policy in Austria could be reformed in order to make it more efficient in the future.

From a fiscal point of view subsidies are predominantly discretionary expenses (expenditure without any compulsory legal obligation) so that they could be reduced quickly if the political will would exist¹¹. One strategy to reduce subsidies in the short

the transfer of assets (primary investment grants). Indirect subsidy measures via tax breaks are to be attributed to the income side of the state budget and therefore are not part of the current analysis.

⁹ The extraordinary level of expenditure in 2004 was due to the debt relief of € 6.1 billion which the state gave to the railways in the course of their restructuring. This amount was booked in the national accounts as an asset transfer causing a debt. In September 2008 Eurostat classified the capital injection of € 1.4 billion in the course of the rail restructuring as an investment grant. This means that the capital transfers to the railway increased to € 7.5 billion.

¹⁰ The entire volume of subsidies changes considerably if you look at the special grants supporting single companies (e.g., AUA – Austrian Airlines, the railway – ÖBB, and temporary investment incentive programmes). This is not only the case in Austria. However, the potential to increase efficiency cannot be clearly ascertained using international benchmark comparisons on a single base year.

¹¹ A rate of 10 percent is also politically not unrealistic since at the start of the negotiations for the federal budget for 2009-10 a reduction of discretionary expenses in this amount was advised.

term would be to reduce all subsidies across the board by the same percentage ("Lawn mower method"). This across the board method might be easier to implement politically but would be viewed critically from an economics point of view since some subsidies which are defensible because they correct market failures or have a desirable socio-political effect would also be reduced. What would be more advantageous from an economic point of view would be a sophisticated approach where the priorities for granting subsidies are set at a political level. In particular the area of R&D subsidies which received € 630 million according to the COFOG statistics 2007 should probably be excluded from any cuts. In the current crisis it is also difficult to argue for a blanket reduction in labour market subsidies and for transfers to non-governmental providers of social services (advisory and care facilities) where the government has withdrawn from providing these services. In the field of business subsidies a given efficiency saving across the board of 10 percent would in the short term save approximately € 850 million. Subsidies for health care, labour market policies and social services are not included in this calculation.

Table 5: Subsidy and capital transfers in functional classification

COFOG classification, 2007

	Subsidies	Capital transfers Million €	Total	
				Percentage shares
General public services	68.8	1,188.7	1,257.5	8.6
Defence	0.7	0.0	0.7	0.0
Public order and security	2.3	21.0	23.3	0.2
Economic affairs	3,818.6	2,350.9	6,169.5	42.4
General economic, commercial and labour affairs	1,424.5	242.2	1,666.7	11.5
Agriculture and forestry	555.7	144.9	700.6	4.8
Fuel and energy	20.5	21.0	41.5	0.3
Mining, manufacturing and construction	0.0	0.6	0.6	0.0
Transport	1,225.4	1,817.7	3,043.1	20.9
Communication	52.6	0.1	52.7	0.4
Other industries	67.3	66.0	133.3	0.9
R&D economic affairs	472.5	48.9	521.4	3.6
R&D economic affairs n.e.c.	0.1	9.7	9.8	0.1
Environment	36.4	504.5	540.9	3.7
Housing and communal amenities	123.1	683.5	806.6	5.5
Health care	3,913.2	334.5	4,247.7	29.2
Recreation, sport, culture, religion	295.0	215.8	510.8	3.5
Education	238.2	142.7	380.9	2.6
Social protection	464.7	141.0	605.7	4.2
Total	8,960.9	5,582.6	14,543.5	100.0

Source: Eurostat, WIFO calculations.

In general it is not advisable to shield single subsidy programmes ex ante completely from a savings discussion. Ideally deciding whether savings can be made should be unconditional and on the basis of generally valid objective criteria. The German "Stiftung Soziale Marktwirtschaft" advises a general "check list" for reducing subsidies (Donges et al., 2006). In principle the idea is a comprehensive evaluation of all subsidies and capital transfers including those which are generally seen as productive. A central issue in this context is the political definition of the targets the subsidies should (measurably) achieve. Following such a strategy, however, will lead to massive political opposition against the evaluation of every single subsidy programme. As a result a combination of selective cut backs and some reductions across the board seems the best way if you want to have a small level of success in this area.

As a rule, only those programmes in Austria which receive a high amount of funds are actually ever evaluated (Pitlik et al., 2010)¹². The results of evaluations which

¹² Programmes with a share of EU funds are, as a rule, compulsorily evaluated.

have been partly carried out by external agencies are sometimes drawn on when subsidy programmes are adjusted, but this is not compulsory. Programmes which receive fewer funds and numerous other cases of smaller subsidies are very rarely evaluated in practice. Indeed it is actually often only checked and documented whether the funds are used for the purpose for which they were intended.

Due to the alleged substantial efficiency gains which could be made and due to the windfall gain from many grants or subsidies it would be worth checking the following areas (Pitlik et al., 2008):

- (national) agriculture subsidies (in 2007 around € 700 million),
- general labour market and commercial subsidies as well as special sector based subsidies (in 2007 just short of € 1.9 billion),
- housing subsidies only have a limited effect towards reducing a deficit. Because of their character as a loan they are mostly "financial transactions". According to the COFOG classifications subsidies for housing which were viewed as expenditure totalled around € 360 million in 2007.
- culture grants (€ 360 million in 2007), recreation and sport grants (€ 120 million in 2007).

The granting of business subsidies is not limited to single local authorities in the federal system in Austria. Rather all levels of government participate. In 2008, 58.8 percent (around € 9 billion) of all subsidies and investment grants were granted by the federal government (as classified by the national accounts). The regional level (21.4 percent which is € 3.3 billion) and the local authorities (18.1 percent which is € 2.8 billion) were also active in granting subsidies, giving way together around 40 percent of the total subsidies, therefore also playing an important role; Grants from social security bodies only amounted to 1.7 percent of the total. At a regional level (including extra budgetary units) the largest proportion by far of subsidies and capital transfers in 2007 went to hospitals (63.9 percent from a total of € 4 billion). Above all the regions supported the area of economic affairs (around € 800 million, 20.3 percent). The local authorities (including Vienna and extra budgetary units) were involved in health care grants (in 2007 € 900 million, 27.4 percent) and labour market and economic subsidies (€ 1.04 billion, 31.8 percent). Environmental protection grants (especially to waste management companies, € 400 million) and culture and sports grants (€ 260 million, 8.1 percent) also played an important part.

There is no detailed summary, categorised according to the definitions in national accounts, of those private entities that receive grants or the purpose for which those subsidies or capital transfers were granted. Especially at a regional and municipal level the documentation of subsidies has until now been inadequate and very difficult to access. What is lacking is a list of all subsidies granted across all levels of government presented in one common "subsidies report". As a result it is not only difficult to carry out a detailed economic analysis of the costs and economic effects of grants to business in Austria, it is also difficult to monitor and control them politically.

Business subsidies are granted not only by sovereign state authorities but also by agencies or public funds which act like private business agents using a subsidies contract. As a result of this all local authorities are able to act outside their constitutionally assigned responsibilities. A total overview of the content and quantity of all subsidies is therefore impossible due to the differing reporting and budgetary duties of the federal government, regional and local authorities and extra budgetary units.

The result is a complete unmanageable muddle at the local authority level, although there are some focus points and actions regarding subsidies which are similar. Consultation between actors at various levels of government is mostly absent. This means that certain grants can possibly be made two or three times over. At the same time the administrative and information costs for the government and the business increase as a result of this fragmentation of responsibilities. If various providers co-operated and formed a one stop shop these costs could be reduced. It should be noted however, that the administrative savings hoped for by the politicians from more stringent demands in the application and evaluation process might not be all that large. Rather conversely a more simplified and non-bureaucratic ap-

proach might actually lead to more costs if the subsidies granted are then applied less efficiently.

Therefore, fundamentally all governmental layers should be constrained by the list of responsibilities laid down in the constitution as a guide when granting subsidies. Naturally this should also be the case for policy areas where governmental agencies act as "private" ("Privatwirtschaftsverwaltung"). Untangling the mishmash of the subsidy system is going to have little success if the way policy responsibilities are assigned to the governmental layers is not simplified.

In this context politicians usually do not announce a concrete formulation of the desired outcomes for any subsidy system. These could then be used as a benchmark for controlling how funds are allocated using performance against these outcomes as a measure. The process of setting goals and strategies for the monitoring process is also hindered by differing information when experts from extra budgetary units which deal with subsidies also influence how outcomes are defined and funds are distributed when they advise the government. Therefore politicians really need to ensure that before any subsidy agency is formed the qualitative and quantitative goals for subsidies are already laid down.

Total public expenditure allocated to health care in Austria (COFOG 7) amounted to € 21.8 billion in 2008. Thereof € 11.7 billion (53.7 percent) accounted for inpatient care, € 4.65 billion (21.3 percent) for outpatient services and € 3.4 billion (15.6 percent) for medical products, appliances and equipment (Table 6).

Health care

Table 6: Composition of expenditures in health care

COFOG classification

	2006	2007	2008	2006	2007	2008
	Million €			Percentage shares		
Medical products and equipment	2,904	3,132	3,396	15.0	15.2	15.6
Outpatient services	4,258	4,514	4,651	22.0	21.9	21.3
Hospital services	10,321	10,920	11,731	53.4	53.1	53.7
Public health services	500	554	528	2.6	2.7	2.4
R&D health	470	499	535	2.4	2.4	2.5
Health n.e.c.	866	945	984	4.5	4.6	4.5
Total	19,320	20,564	21,826	100.0	100.0	100.0

Source: Statistics Austria, WIFO calculations.

Amongst EU-15 countries Austria spends the largest share of GDP on its health care system. To assess whether these above average expenditures are related to above average quality of medical care the Data Envelopment Analysis, an internationally recognised benchmarking instrument for health care systems (Czypionka – Kraus – Röhring, 2008A), can be used. The degree of care quality is measured by health status indicators, e.g., life expectancy, healthy life expectancy, and infant mortality. Existing empirical efficiency studies show significant room for improvements¹³ in the Austrian health care system. According to these there is a large potential for reducing costs which does not decrease the quality of health care.

With a 7.5 percent share of GDP on public health expenditures the Austrian rate lies 1 percentage point above the (unweighted) average of the remaining EU-15 countries. A large part of this difference can be attributed to structural characteristics of the Austrian health care system. The ratio of expenditures on the (more expensive) inpatient services to outpatient services is 2.4 : 1 in Austria, whilst the average ratio for the remaining EU-15 countries¹⁴ is merely 2.0 : 1.

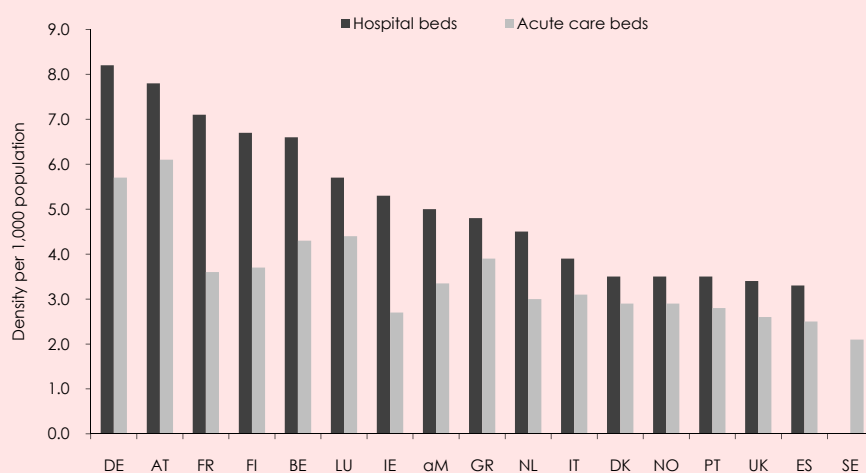
¹³ Concerning the efficiency of the Austrian health care system in international comparison see Afonso – St. Aubyn (2005A, 2005B, 2006), Rätty – Luoma (2005), Retzlaff-Roberts – Chang – Rubin (2004). An overview of the results provide Pihlik et al. (2008, pp. 246).

¹⁴ Detailed figures for all EU-15 countries are not available.

In comparison to the other EU-15 countries Austria exhibits the second highest number of hospital beds and the highest number of acute care beds per capita (Figure 2). The high density of beds creates incentives for excessive admissions as observed in Austria compared to the other member countries. Thus productivity in the inpatient sector is significantly lower than it could be (Czypionka – Kraus – Röhrling, 2008B, Hofmarcher – Lietz – Schnabl, 2005). Efficiency reserves in inpatient care could further be deployed by reducing repetitions in inpatient care, cutting back parallel structures, intensifying specialisation of hospitals¹⁵ and by partially substituting inpatient for outpatient treatment¹⁶.

Figure 2: Hospital beds and acute care beds

2007



Source: OECD Health Data 2009. Arithmetic mean (unweighted average) of the countries excluding Austria. Data for Greece are for 2006.

Ebner *et al.* (2003) and Roland Berger Strategy Consultants (2001) estimate savings potentials in Austria after addressing structural deficits and excess capacity ranging from € 1.7 billion (0.8 percent of GDP in 2000) to € 2.4 billion (0.9 percent of GDP in 2010) per year. The estimates of possible efficiency gains by Hofmarcher – Paterson – Riedel (2002) suggest a reduction in expenditure on inpatient care by 30 percent. If the savings potential is measured according to the difference of the Austrian health expenditure share of GDP to the EU-15 average share, € 2.8 billion (1 percent of GDP in 2010) p.a. could be consolidated.

It goes without saying that savings of this magnitude are only feasible if institutional reforms are designed, for the long run. The reforms should abolish the fragmentation of responsibilities for tasks, expenditures and revenues between the regional authorities and the Federation of Austrian Social Security Institutions (Czypionka *et al.*, 2008). Currently the responsibility for resource planning and ensuring inpatient capacities lies with the regional authority, which only finance about half of the running costs. The other half is financed by local authorities, the Federation of Austrian Social Security Institutions, private insurances and patients. In addition, the federal government contributes 1.4 percent of the VAT revenue and a fixed yearly sum. The outpatient sector is almost exclusively financed by the social health insurance.

¹⁵ With parallel structures not allowing to reach the mandatory minimum number of operations by far in some areas the surgical risks are increased. Intensifying the specialisation of hospitals would over an increase in the number of operative cases contribute to an improvement of the treatment quality (Upper Austrian Provincial Court of Audit, 2009).

¹⁶ The Austrian Court of Audit estimates for the province Carinthia alone a medium to long term savings potential of € 125 million p.a. without losses in the care quality by reducing the inpatient care capacities and the length of stay, by adjusting the excessive payments in comparison to the other provinces, and by optimizing the hospital size through concentrating on fewer locations (Court of Audit, 2006).

The dual tasks structure, the separated expenditure responsibility as well as the interwoven financial flows result in inefficiencies in the coordination of health care providers which causes substantial additional expenses and cost shifts. Because in contrast to the outpatient care the social security agency only provides around half of the costs for inpatient care, there exists an incentive to increase inpatient treatment as opposed to ambulatory treatment. Losses occurring in hospitals are covered by provinces (subsidised), which in turn balance their budgets via the fiscal equalisation scheme. Since provincial households are almost entirely financed by shared taxes and duties all Austrian tax payers bear the costs for the subsidisation of hospitals by regional authorities. Such a structure dampens the incentives for cost cutting and capacity reduction, e.g., through hospital mergers (*Fuentes – Wurzel – Wörgötter, 2006*). In order to adjust the inefficient institutional structure of the Austrian health care system the expenditure and revenue responsibility should be assigned to one public body only. Ideally the responsibility should lie with the social security agency (*Court of Audit, 2002*).

In the short run it should be possible to capitalise 10 percent of the long-term efficiency reserves through savings. Assuming a short to medium-term savings plan of around € 300 million a year from 2011, the budget in 2012 would be relieved of € 600 million, € 900 million in 2013, € 1.2 billion in 2014 and of € 1.5 billion in 2015. If this efficiency path is continued, the difference in health care expenditures between Austria and the European average could be saved by 2019.

One consolidation option which has until now not really been considered would be based on the revenue side of the statutory health insurance. Before the new regulation of 2001 an unconditional contribution-free co-insurance for relatives existed. Nevertheless, no additional contribution has to be payed as long as the family member lived in the same household with a child for a minimum of four years. From the 2,061,100 co-insured people in 2008 1,606,500 were children and 454,600 other family members (*Haydn, 2009, Federation of Austrian Social Security Institutions, 2009*). Assuming that only around half of the other family members are actually able to work¹⁷, a cautious estimate of the minimum increase in receipts as a result of abolishing this exceptionally rule amounts to yearly savings of € 141 million.

The labour market stabilisation measures implemented in response to the financial crisis comprise expenditures on short-time work and measures to improve qualifications. In addition, they envisage an extension of social benefits for older employees, such as old-age part-time work benefits and interim allowances, which are controversial both from a fiscal and labour market policy point of view. In light of the low labour market participation of the older population in comparison to international rates, continuing to finance these implicit early retirement benefits should be reconsidered.

As old-age part-time employment schemes in Belgium, Germany, Finland and Sweden showed, this labour market instrument is effectively equal to subsidising for older employees to leave the workforce early (*Lindecke – Voss-Dahm – Lehdorff, 2007*). An increase of employment is statistically barely visible¹⁸. *Graf et al. (2009)* actually indicate negative labour market effects for Austria. Therefore withdrawing old-age part-time work benefits for older employees (€ 358 million in 2008) could be considered. Abolishing it would not cause excessive hardship because the people affected are mostly employees with higher earnings and a continuous employment history (*Kaldybajewa, 2004, German Council of Economic Experts, 2007*). If old-age part-time work agreements were cancelled by 2011, a cautious estimate of possible savings until 2013 would amount to around € 65 million a year. In the medium to long term, i.e., from 2014 onwards, yearly savings of around € 130 million are possible.

¹⁷ Among those people who are co-insured, hence exempted from contributions since unable to work, are carers, people in need of care and people rearing a family.

¹⁸ Therefore the subsidising of part-time work for older employees was abolished in Sweden in 1999 and expired in Germany in 2009 (*Lindecke – Voss-Dahm – Lehdorff, 2007*).

Labour market subsidies

Interim allowances are available for the long-term unemployed until they reach pensionable age. These are 25 percent higher than unemployment benefits. Analogously to the old-age part-time work benefits for older employees they are an implicit form of early retirement which counteracts the economic intention of lengthening the employment history over the life cycle. Assuming inflows and expenditures as well as a cautiously calculated volume of savings consisting of the 25 percent unemployment benefits supplement € 18 million per year could be realised in the short run.

According to the classification of the European System of integrated Social Protection Statistics (ESSPROS) expenditure on pensions (cash benefits)¹⁹ amounted to 13.8 percent of GDP in Austria in 2007 (Table 7). Within the EU 15 this share was only exceeded by Italy (14.6 percent of GDP). Even when differentiating by the type of pension Austria still lies above EU-15 average in almost all categories (Table 7).

Pension system

Table 7: Pension benefits in EU-15 comparison

ESSPROS classification, 2007

	Total	Old-age pension	Early retirement pension	Disability pension	Early retirement benefit due to		Survivors' pension
					Reduced capacity to work	Labour market reasons	
As a percentage of GDP							
EU 15	12.0	8.8	0.4	0.9	0.2	0.1	1.6
Belgium	10.7	7.0	0.0	1.3	–	0.4	1.9
Denmark	10.8	7.5	1.5	1.8	0.0	–	0.0
Germany	12.4	8.7	0.6	0.2	0.8	0.1	2.0
Ireland	5.2	3.5	0.0	0.8	0.1	–	0.8
Greece	12.1	6.8	2.6	0.7	–	0.0	2.0
Spain	9.0	5.3	0.6	1.2	–	0.0	1.9
France	13.3	10.6	0.0	0.7	0.0	0.1	1.8
Italy	14.6	11.3	0.0	0.7	0.0	0.1	2.5
Luxembourg	8.2	3.7	1.4	1.0	0.0	0.2	1.9
The Netherlands	12.1	8.0	0.6	2.1	0.0	0.0	1.4
Austria	13.8	9.4	0.9	1.5	0.0	0.0	2.0
Portugal	13.1	9.0	0.3	2.1	0.0	0.1	1.5
Finland	10.8	6.9	0.5	1.9	0.0	0.4	0.8
Sweden	11.8	8.2	0.7	2.3	–	0.0	0.6
UK	10.5	8.8	–	1.0	–	–	0.7

Source: Eurostat, WIFO. Expenditures for partial pensions are zero except for Finland (0.1 percent of GDP) and therefore not expressed. ESSPROS European System of integrated Social Protection Statistics (*European Communities*, 2008). Old-age pension: available at legal/standard age. Invalidity pension: available due to impaired ability to work for mental or physical reasons. Early retirement: available before reaching legal/standard age (with or without deductions). Early retirement benefit due to reduced capacity to work or labour market reasons: available before reaching legal/standard age (with or without deductions) for the aforementioned reasons (early retirement benefits normally cease when the beneficiary becomes entitled to an old-age pension). Definitions of the types of pension and their availability can differ across the countries.

The GDP-share of expenditure on pensions in Austria is 1.4 percentage points higher than in Germany although the German old-age dependency ratio is 5 percentage points higher (Figure 3). Thus the high GDP expenditure share of pensions in Austria does not result from a disadvantageous population structure. The public expenditures on pensions are of course not only influenced by the age structure of the population but also by the spreading of private, public and publicly subsidised pensions.

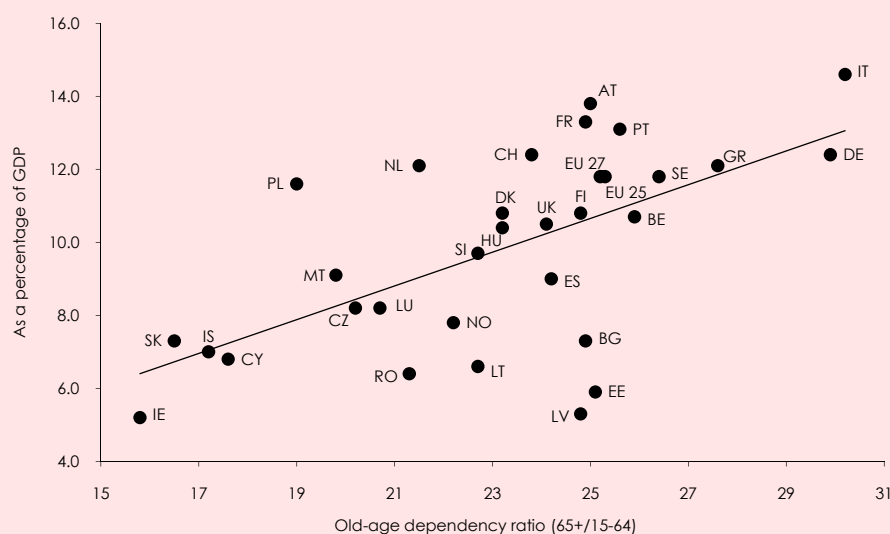
The above average pension expenditures in Austria relative to the other EU member countries are caused primarily by the comparatively longer duration of benefits re-

¹⁹ The category comprises old age pensions, early retirement pensions, disability pensions, early retirement pensions due to reduced ability to work and labour market reasons, partial pensions and survivors' pensions (Table 7).

ceipt which in turn stems from a low retirement age and by the relatively high compensation rate (OECD, 2009A)²⁰. In order to curb the expected long-term increase in pension expenditures earlier reforms envisaged phasing out early retirement pathways as well as raising the retirement age, the deductions and the period of assessment. However, any budgetary relief will arise very slowly and with considerable delays because of simultaneously implemented exemption rules regarding the transitions into retirement (Pensions Commission, 2009). In order to disburden public finances in the short to medium run the pension legislation could only be changed as regards the most recent extension of benefits since these are not protected for reliance on existing laws.

Figure 3: Pension expenditure and old-age dependency ratio in European comparison

ESSPROS classification, 2007



Source: Eurostat, WIFO calculations. Pensions (Cash benefits): old-age pension, early retirement pension, disability pension, early retirement pension due to reduced ability to work, partial pension, survivors' pension.

Withdrawing the recent extension of the deduction-free early retirement option for the long-term insured would remove a not justifiable special provision for particular groups. It would also have a desirable impact on employment policy. The recent prolongation undermines the budgetary indispensable increase in the labour market participation of the older workforce. Furthermore, well-paid employees with an uninterrupted employment biography are advantaged. Hence this extraordinary early retirement provision without deductions is redistributing to a group of insured with the highest pension benefits and is also a strain for the public budget. The possibility of "buying" pension-relevant periods for school and university attendance in order to qualify for pension benefits widens the circle of beneficiaries and favours graduates. Because this special option is deductible as an extraordinary expenditure from the personal income tax it reduces tax revenue²¹. Reversing the extension could save around € 250 million per year.

²⁰ The pension system for civil servants features a lower standard retirement age for men than ASVG (social insurance system for employees of the private sector). Moreover, the compensation rate is higher for both sexes than in ASVG because pension benefits are still predominantly assessed on the salary level before retirement (Grossmann –Hauth, 2007, Court of Audit, 2009B).

²¹ As a consequence of progressive income taxation the revenue shortfall respectively tax-reduction will be higher, the higher the income of the insured employee. The tax deductibility of contributions for pension-relevant periods for school and university attendance paid later is not conform to the tax system since the compulsory contributions during employment are liable to income tax.

In the medium to long run several adjustments within the pension system under protection for reliance on existing laws could contribute to budgetary consolidation:

- Under the Pensions Harmonisation Law 2004 the decrement in the pension scheme of people insured with ASVG, GSVG and BSVG (covering all employee groups excluding civil servants) will be conferred for federal civil servants after a long transition phase. Regional civil servants are still not affected, although in the (vertical) Financial Equalisation Pact of 2008, the provinces committed to transposing financially equivalent reforms²². According to calculations by the Austrian Court of Audit, aligning the pension benefits of provincial civil servants between 2010 and 2049 would avoid future pension expenditures in the amount of € 445 million (*Court of Audit*, 2009B). A corresponding adjustment of the pension laws for local authority civil servants would allow further savings. But above all aligning pension laws is desirable with regards to the equal treatment of civil servants and other employees who have to additionally bear a risk of unemployment. Furthermore, overcoming job mobility barriers within the public sector would allow for staff adjustments leading to an increase in efficiency of the provision of public goods and services.
- Additionally special pension rights for civil servants of the Federal Austrian Railways (ÖBB), the Central Bank (OeNB) and the public television provider (ORF) exist²³. Their pension laws could be harmonised in accordance with the pension law of the federal civil servants. The Austrian Court of Audit expects additional cumulative expenditures in the height of € 1.2 billion from May 2002 until 2056 solely for the inclusion of notional fringe benefits in the assessment base of the ÖBB pensions (*Court of Audit*, 2004). Under the assumption of evenly distributed discharges, cutting back these notional fringe benefits would annually relieve the pension budget by € 26 million between 2011 and 2056.
- In order to enable women to rely more on an old-age income which is based on their own pension entitlements, an earlier and faster adjustment of their lower standard retirement age to the male level is necessary. From an economic point of view the investment in women's human capital – which is identical to that of men – should redeem itself in an equivalent employment period, i.e., tax and social insurance contributions. Correspondingly, a phasing out of survivors' pensions for wives and husbands respectively could be considered.
- Since the pension calculation according to the ASVG, GSVG and BSVG is already harmonised, their pension insurance agencies could be merged in order to reduce the size of the administrative apparatus. Making it more efficient and thereby saving administrative costs.

The presented short-term measures allow for a considerable contribution to consolidating the public budget in a relatively fast manner. The short-term savings potential for the administration is estimated to lie at € 0.2 to 1.1 billion a year. For subsidies at € 0.9 billion a year. Initial efficiency gains in the health care system would yield savings of € 0.3 billion per year (increasing yearly). Limiting the contribution-free co-insurance would generate yearly revenues of € 0.1 to 0.2 billion. Withdrawal of a few special arrangements in the unemployment insurance could save € 0.1 billion per year and in the pension system € 0.3 billion per year. Along the short-term consolidation path ranging from 2011 to 2013 these measures would add up to a total budget relief of € 1.9 to 2.9 billion p.a. (Table 8).

This short-term consolidation potential is feasible within a relatively narrow time frame of one to two years. In the end the speed at which these reforms could be imple-

Summary and the future

²² Whilst the reforms of pension rights for provincial civil servants in Lower Austria, Vorarlberg, Styria, Upper Austria and Burgenland should allow financially comparable reliefs, there are still no amendments enacted in Salzburg, Tyrol, Vienna and Carinthia.

²³ The OeNB and ORF are not attributed to the government sector. Any contributions to consolidation result from higher profit transfers or lower allocation of public funds.

mented depends on the legislators' willingness to perform. In particular cases (e.g., business subsidies) it has to be checked to what extent provisions as well as whether the subsidies could be apportioned to discretionary payments which are more flexible in the short term.

Exploiting any medium to long-term potential for savings and efficiency gains requires a fundamental reform of the institutional framework. A central point of reference and therefore an important first step in any reform would be a disentangling of policy responsibilities between the governmental levels and the consolidation of responsibility for tasks, expenditures and revenues (e.g., Pitlik, 2007). Such measures have been demanded for many years. The problem joint responsibilities are evident in every political field addressed here.

Table 8: Total consolidation potential

	Short term	Long term
	Billion €	
Administration	0.2 to 1.1	
General public administration	0.2	0.7 to 2.5
Core administration	0.6	
Total administration (without education)	0.8	
Total administration	1.1	
Business subsidies	0.9	3.5 to 5.0
Health care	0.3	2.0 to 2.8
Health insurance (co-insurance)	0.1 to 0.2	0.1 to 0.2
Unemployment insurance (old-age part-time work benefits, for older workers, interim allowances)	0.1	0.1
Pension system (long-term insured, ÖBB allowance)	0.3	0.1
Total	1.9 to 2.9	6.5 to 10.7

Source: WIFO.

The reorganisation of the institutional framework regarding the different political and administrative decision making levels would be of considerable importance to achieving and realising long-term savings potential. This is stressed in studies by the WIFO and the Court of Audit (Pitlik et al., 2008, Court of Audit, 2009A). There it is argued that savings can only be sustainable if institutional regulations actually create stronger incentives for politics and the bureaucracy to carry out the tasks delegated to them in a more efficient manner (see Pitlik et al., 2010):

- Responsibility for different policy tasks needs to be disentangled and clarified.
- Reforms of the assignment of taxing powers should strengthen the tax autonomy of sub-central levels.
- For those policy areas where a joint responsibility of several levels of government appears to be suitable (e.g., schools, transport and environment), cooperation between the federal, the regional and the local authorities to fulfil the tasks is necessary. This would allow the economic benefits of a decentralised administration to be exploited and would guard against an over-centralisation.
- The use of an effective governance strategy between the federal and the regional level means that strategic (choice of desired outcomes) and operative aspects of fulfilling tasks (autonomous choice of instrument to achieve goal) can be clearly separated.
- In order to increase the necessary autonomy of the sub-central government bodies, the financial means to fulfil any tasks need to be flexibly deployable within the framework of a global budget. The use of funds should not be regulated by strict detailed provisions.
- In order to increase the transparency of state actions the existing budget system and accounting system could be harmonised across local authorities.
- A generally institutionalised benchmarking system, which could allow for sensible comparisons, could be implemented for all performance relationships. Using

monetary incentive schemes, performance factors, cost covering aspects and budgeting could be connected to each other.

The goal of any long lasting consolidation of the public finances also implies that the long-term consequences of any government expenditure decisions have to be considered. Short-term savings in a particular expenditure category could lead to higher (budgetary) consequential costs in the medium to long term such that there would be no long-term savings effect. By the same token short-term increases of government expenditure in particular political areas could lead to long-term sustainable savings and efficiency. What is important is an intertemporal linking of particular expenditure decisions. However, in any case for successful cost savings it is necessary to make long-term plans which also extend beyond the next general election.

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Options for Budget Consolidation on the Expenditure Side – Summary

To curb the rise of government debt it is necessary to evaluate public expenditures and revenues in terms of their necessity and efficiency. Notwithstanding the potential to improve the balance by raising taxes or levying new ones this article concentrates on adjustment options on the expenditure side. Among the different expenditure items in Austria public administration, economic affairs (i.e., direct business subsidies) and health care offer the most extensive opportunities for expenditure cuts.

Although Austrian public administration spending is only slightly higher than the OECD average, there is still some scope for efficiency gains. Whereas short-term measures can be taken fast and easily (e.g., a recruitment freeze), long-term solutions require fundamental institutional reforms. One example is the reorganisation of the responsibilities and powers between the different levels of government in order to eliminate expensive overlaps. The combination of all such measures would facilitate economies of up to € 2.5 billion per year.

Furthermore, business subsidies in Austria are insufficiently targeted, which causes additional and unnecessary costs. There is also considerable potential to slash subsidies in agriculture, the labour market, housing and culture. Altogether up to € 5.0 billion could be saved per year.

Austria's health expenditures are above the international average. One of the reasons for this fact is that the rather expensive inpatient treatment is used much more often in Austria than in other countries. Besides the existing overlaps require institutional reforms. The combination of short-term and long-term measures permits savings of up to € 2.9 billion per year.

In addition to the measures mentioned above special arrangements in other fields such as unemployment and pension insurance could be scrapped to reduce early retirement. This would lead to total savings of up to € 2.9 billion per year in the short run and up to € 10.7 billion per year in the long run depending heavily on the political will to tackle institutional reforms.

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