

# **Monocular Accounting and its Discontents: The case of the stability and growth pact**

**Leonhard Dobusch  
Jakob Kapeller  
Sabine Wandl**

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### **Abstract**

This paper addresses the issue of unanticipated incentives and related unintended consequences of monocular accounting as practiced in the context of the European Union's stability and growth pact. Specifically, the Maastricht treaty establishes criteria and rules to ensure budgetary discipline by regulating public debt without taking into account corresponding public assets. In a comparative empirical study of two political reactions to the Maastricht treaty we find that the latter imposes an ambivalent incentive structure, which produces unintended consequences in cases of rule-following as well as in cases of rule-evasion. In effect, monocular accounting fosters privatization and a reduction in public engagement in the case of rule-following as well as creative accounting practices and changes of public policy goals in the case of rule-evasion.

### **1. Introduction**

The introduction of the stability and growth pact (SGP) as a main by-law to the European Monetary Union (EMU) is unique insofar as it provides a legally binding international convention on public accounting and the organization of governmental budgeting. The scope of this convention does not only specify a series of operative accounting rules, but also includes a strategic dimension by imposing specific budgetary aims and restrictions on member states' fiscal proliferation. Hence, the SGP can be understood as a set of public accounting rules, which serve as a control device operating through formally binding rules to enforce cautious financial management throughout the EMU.

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\* Leonhard Dobusch, Freie Universität Berlin, Management Department, [leonhard.dobusch@fu-berlin.de](mailto:leonhard.dobusch@fu-berlin.de)

Jakob Kapeller, Johannes Kepler University Linz, Department of Philosophy and Theory of Science and Institute for Comprehensive Analysis of the Economy, [jakob.kapeller@jku.at](mailto:jakob.kapeller@jku.at)

Sabine Wandl, Johannes Kepler University Linz, Department of Philosophy and Theory of Science, [sabine.wandl@gmx.at](mailto:sabine.wandl@gmx.at)

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In spite of its contested origins (Segers & van Esch, 2007) and effectivity (Heipertz & Verdun, 2004), the SGP is often successful in imposing restrictions on member states' fiscal policy. However, in this paper we aim to look beyond the simple imperative for 'budgetary discipline' and focus on two specific applications of the rule-set embodied in the SGP to get a better understanding of the implementation strategies and follow-up effects related to this imperative. In doing so, we show that conforming to the imperatives of budgetary discipline expressed by the SGP can imply very different things when it comes to its practical implementation. Specifically, we argue that the imperative for 'budgetary discipline' triggers a series of – anticipated as well as unanticipated – effects, which do not depend chiefly on the imposed accounting rules themselves but rather on the specific handling of these rules by national governments. Hence, similar outcomes in terms of the criteria of the SGP may be achieved by quite different policies. In this context, we argue that different policies are eventually based on different application-contexts and interpretations of the accounting rules imposed by the SGP.

From this it follows that our main research question is of an exploratory nature, asking about differences in the interpretation and implementation of the accounting rules imposed by the SGP across different cases. In order to provide a first assessment of this question this paper provides a comparative discussion of two extreme, that is, particularly revealing cases (Flyvbjerg, 2006), which differ strongly with regard to the content, effects and motives of implemented policies, but achieve rather similar outcomes in terms of the SGP. As we will show, a key element for explaining the differences across these cases is thereby related to the 'monocular nature' of the SGP, which focuses solely on gross debt and budgetary deficits, but does not take into account the assets corresponding to these debts. In assessing this monocular nature we draw on both actual accounting practices and the underlying statistical framework guiding public accounting in the EU.

The remainder of the paper is organized as follows: First, we provide a historical discussion of the SGP in section 2 in order to substantiate our claim that the SGP serves as a control device aiming to coordinate fiscal policy across the EMU. In section 3 we provide a theoretical discussion on the inherent uncertainty of rule-following and try to delineate possible consequences of this account for the implementation of transnational public accounting standards in section 4. In sections 5 and 6 we discuss two specific cases in applied policy, where the rules imposed by the SGP served as the main rationale in motivating and justifying fundamental reforms. The purpose of these cases is to show that different interpretations and application-contexts of a given rule might lead to very different concrete policies, but similar outcomes in terms of the underlying framework of rules.

## **2. The origins of monocular accounting: the history of the Stability and Growth Pact**

The Maastricht Treaty (1992) introduced, among others, convergence criteria for fiscal policy as a condition of eligibility for membership in the EMU. These requirements were spelled out in terms of reference values for the deficit-to-GDP ratio (3 per cent of GDP) and the debt-to-GDP ratio (60 per

cent of GDP) (Artis & Buti, 2000, p. 564).<sup>1</sup> Hence, the Maastricht Treaty is designed as an incomplete contract, insofar as these requirements only apply for candidates wanting to join the EMU, whereas it relies essentially on voluntary arrangements as soon as a country is part of the EMU. One option to resolve this issue of contractual incompleteness was to impose explicit rules on fiscal governance for EMU member states; an idea particularly favored by Germany and the Netherlands. Following this approach, a rule-based system to restrict budgetary deficits was implemented in 1997 in the form of the Stability and Growth Pact (SGP), which aims at making budgetary prudence as defined in the Maastricht criteria a permanent feature of the new currency region (Buti & Giudice, 2002; Heipertz & Verdun, 2004). More recently, the global financial crisis provided a completely new challenge for the EU (Heipertz & Verdun, 2010), which was, among other measures, confronted by the introduction of the Fiscal Compact in 2012, which further strengthened the role of the Maastricht criteria within the EU.

In turn many participating countries failed to meet the dictum that called for countries to strive for underlying fiscal balance. As early as in 2002, Buti and Giudice note that “several countries in the Euro area, including the largest ones, have not kept the spirit of the pact” (2002, p. 839; see also Annett, 2006). This observation was primarily related to Germany, France and Italy, where Germany was one of the countries supporting the idea of more strict and explicit rules, while France and Italy originally opposed the introduction of the stability and growth pact and partially tried to subvert its implementation as a control device (Segers & van Esch, 2007).

According to Heipertz and Verdun (2004), the most prominent pre-crisis reasons for the introduction of more stringent fiscal rules in the form of the Stability and Growth Pact are the following: first, many countries faced a real or alleged *need for consolidation* induced by the expansionary fiscal stance and the welfare-state expansion in most of the OECD countries. *Concerns about externalities and central bank independence* probably came second, and point to possible negative spill-overs from fiscal policy. Specifically, the loss of autonomy due to the abandoning of national exchange rates was related to the fact that the profligacy of single member states might turn into a problem for the whole currency zone and affect the exchange rate of its common currency.<sup>2</sup> In other words, strict rules on budgetary deficits were deemed necessary to prevent member states from free-riding by overspending on their budgets.<sup>3</sup>

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<sup>1</sup> These well-known fiscal criteria are complemented by a monetary rule stating that consumer prices shall not rise faster than average inflation in those three member states with the lowest inflation plus a slack of 1.5%.

<sup>2</sup> These arguments basically reflected simple (but contested) economic textbook-models, i.e. it was argued that an increase in government spending would lead to higher interest rates (either directly as in the Mundell-Fleming Model or via an increase of interest rates by the ECB to counter inflationary pressures). This increase in interest rates was assumed to cause an increase of the common currency's value due to capital inflows, which would lead to a deterioration of the trade balance. Thus, the economics behind the SGP suggested that the disciplinary effect on the ‘budgetary sinners’ is indeed decisive (Buti & van den Noord, 2004).

<sup>3</sup> Interestingly, while free-riding by deficit-spending was the primary concern, free-riding by depressing wages to boost exports was never an issue when discussing the SGP criteria. A more coherent framework of economic policy coordination would also look at the economic divergence

A third concern relates to the issue of economic coordination within a monetary union, which combines a centralized monetary policy with country-specific fiscal policies. In this context it was not only questioned whether a single and unified monetary policy would allow for country-specific economic policy strategies, but also whether inflexible coordination of fiscal policies might inhibit anti-cyclical policies in case of an economic crisis. Economic models referring to the general ineffectiveness of fiscal policy<sup>4</sup> as well as the possibility of political business cycles (Beetsma and Uhlig 1999) provided additional support for the demand for a “rule-based fiscal policy” (Buti & van den Noord, 2004, p. 7).

The SGP, introduced in 1998 and revised in 2005<sup>5</sup>, fleshes out such a “rule-based fiscal policy”. In general the SGP is seen as a “discipline device” (Buti & van den Noord 2004, p. 9) and its “goal is to ensure that fiscal discipline is maintained while creating room for automatic stabilizers to work. [... The pact is a] blueprint for running fiscal policies in the EMU” (Buti & Giudice, 2002, p. 838). The SGP can be seen as “the most stringent ‘commitment technology’ ever adopted by sovereign governments” (Buti & van den Noord 2004, p. 1) aiming for the budgetary positions of EMU-member states to be close-to-balance or in surplus. The regulatory objective of the SGP is to ensure the compliance of the individual countries’ fiscal authorities to the Maastricht criteria (Artis & Buti, 2000, p. 564). However, the enforcement of these rules is what has already, in the early years, been the Achilles’ heel of SGP (Annett, 2006, p. 3). While the main aim of the pact is budgetary discipline, a permanent feature of the EMU, the formal enforcement of the respective rules, has eventually been rather weak. As a consequence the SGP has been considered as a “dog that would never bite” (Heipertz and Verdun 2004, p. 576). In contrast, this paper will argue that the dog has bitten more often than one might think at first, although into unexpected targets. However, before laying out this argument in greater detail, we first need to introduce the organizational apparatus and regulatory instruments developed to monitor individual member states’ policies.

The SGP provides a two-pronged fiscal framework: the *preventive arm* – focusing on multilateral surveillance and the avoidance of excessive deficits, and the *dissuasive arm* – addressing gross policy mistakes (Annett, 2006, p. 3). The preventive arm aims to strengthen the surveillance of budgetary positions and co-ordination of economic policies. The dissuasive arm aims to accelerate and clarify the excessive deficit procedure of the Treaty (Buti & Giudice, 2002, p. 830). The essential tools of the preventive arm are country-specific and annually updated medium-term budgetary objectives (MTOs). Countries were urged to attain a “close-to-balance or in surplus” position (Artis & Buti, 2000, p. 563), interpreted as a deficit beneath ½% of GDP over the cycle, to provide a sufficient cyclical safety margin to allow full operation of automatic stabilizers during downturns without breaching the 3 %

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among the participating economies, which might lead to structural imbalances in terms of trade and capital flows.

<sup>4</sup> See, for example, Barro’s ‘Ricardian Equivalence’ (Barro, 1974) or Blinder & Solow’s (1973) argument on the instability of bond-financed expansions, potentially forcing central banks to eventually cover the resulting debt burden.

<sup>5</sup> In short, the reform of 2005 increased the amount of flexibility in a number of different ways, such as losing the escape clauses for participating countries, worded out at the outset of the Treaty, lengthening deadlines for taking action, and expanding the possibility to achieve longer adjustment periods.

reference value. The dissuasive arm, or Excessive Deficit Procedure (EDP), is charged with ensuring that countries respect the limits on deficits (3 percent of GDP) and debt (60 percent of GDP; cf. Annett, 2006, p. 3). Non-compliance with either the preventive or the dissuasive arm of the SGP can lead to the imposition of sanctions. In case of the dissuasive arm, this can involve annual fines for the euro area countries, and for all countries possible suspension of Cohesion Fund<sup>6</sup> financing until the excessive deficit is corrected.

The SGP, thus, is an instrument tailored to *coordinate economic development between different countries* based on *the implementation of a specific set of formally binding rules* to enforce *cautious financial management*. By transforming the Maastricht criteria, which were originally framed as conditions only for gaining membership in the EMU, into policy rules of permanent importance “the SGP put flesh on the bones of the Treaty, leading to better rules and procedures, although at the cost of somewhat more complexity” (Buti & Giudice, 2002, p. 839). However, since these rules and procedures were laid out in terms of accounting criteria, its specific implementation depended not only on the diligence of politicians, but also on accounting standards and practices prevailing in the individual countries’ public sector. This aspect is of particular importance, since the rules not only cover public households but also publicly owned corporations such as banks, hospitals or transportation operators.

At the same time, these accounting provisions introduce a second regulatory component beside the SGP, which allowed individual countries to extend their scope of action by adapting their accounting practices. In this context “experts [like Ministries of Finance, Monetary Committees] are in a strong position to influence politicians, since they possess intimate knowledge of the relevant issues and have detailed information on the bargaining positions of the others. They can indicate potential solutions and hence possibly prevent the discussion from being deadlocked” (Heipertz & Verdun, 2004, p. 773). Since these experts have a focal position in interpreting rules and putting them into practice, they may also change or modify accounting standards and practices and the associated organizational routines to anticipate the effect of the SGP. Such a “change of accounting technologies and practices in organizations” may in turn “establish another form of cognition” (Ezzamel et al., 2012, p. 285), which may then serve as an entry route for unintended effects of the SGP. For Buti and Giudice (2002, p. 839), such an effect is evident, since “the focus remains on short-term deficit commitments, thereby providing incentives for creative accounting and one-off measures.”

In this paper we argue that it is not only the short-term orientation of the SGP but also its monocular focus on debts that leads to unintended consequences with regard to the organization of public sector services. Before presenting some empirical examples of such unintended consequences, we strive to show how the implementation of rules to enforce cooperation creates novel questions and problems in

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<sup>6</sup> The Cohesion Fund, along with Structural Funds, is a financial instrument of the EU for regional policy, intended to narrow down the regional disparities among the Member States. The co-financed project must comply with EU legislation, particularly in matters of competition, the environment and public procurement (EU 2013).

the context of already existing institutional setups and routines. In turn, these problems and questions become a prime source of unintended behaviors and outcomes.

### 3. Regulatory Uncertainty and Unintended Consequences

The introduction of rules always implies transforming the fundamental uncertainty about the actions of other agents into regulatory uncertainty, which basically asks whether and how individuals follow, interpret and apply rule-based instructions (Dequech 2000). The main rationale for doing so is to facilitate cooperative action and efficient coordination in cases of a division of labor or the management of shared concerns. In this context, rules are found to be inherently ambiguous (Black 2002), at least to a certain extent, which is the reason why all kinds of rule-based frameworks are subject to regulatory uncertainty. In management and accounting research, this regulatory uncertainty and its consequences are often associated with some kind of dysfunctional coordination (e.g. Engau & Hoffmann, 2011; Andrew & Cortese, 2013). In line with Ortmann (2010), however, we interpret regulatory uncertainty more generally as the room for maneuver left to the individual rule-follower arising from the fact that no set of rules is ever going to be a complete guide for action. Rather, individuals have to apply the rules to specific situations, which forces rule-followers to make a series of deliberate decisions in order to apply the rule.

“There is a gulf between an order and its execution. It has to be filled by the act of understanding” Wittgenstein (1953, p. 128e, § 431)

In line with this definition of fundamental and regulatory uncertainty, the exercise of organized control by means of rule- and standard-setting intends to coordinate the actions of different actors, to make the actions of those actors calculable, and one’s own expectations more reliable (Botzem & Dobusch, 2012; Mattli & Bühe, 2005). In this sense, the justification for the SGP described in the previous section mirrors classic arguments on rule-setting and rule-following. The perspective of control inscribed in the SGP is typically also inherent in accounting(-based) rules and explicitly addressed in the respective literature as one of the main organizational functions of accounting as such (see, for example, Miller & Power, 2013). Accordingly, accounting rules are also subject to regulatory uncertainty, where the implemented rules might give rise to consequences unintended by the rule-setter (e.g. Laux & Leuz, 2009). Inherent in such a perspective is also an “active role” played by institutional actors “in the construction, challenge and deployment of budgets” (Covalevski et al., 2013, p. 333) and budgetary policies. This aspect does not come as a surprise, since any “theory that combines fundamental uncertainty and institutions should emphasize not only the existence of behavior in accordance with institutions, but also the possibility of creative, bold, unconventional behavior” (Dequech, 2003, p. 509).

To facilitate a more thorough analysis of regulatory uncertainty, we suggest identifying three general dimensions of regulatory uncertainty, which every rule and regulation is subject to. First, it is uncertain whether the rule is really accepted and obeyed, or if non-compliance may arise as an exception possibly (dis-)proving the rule or paving the way for a new rule. This first source of uncertainty is inherent to every rule, because rules and regulations only make sense somewhere in-between necessity and



impossibility. The second uncertainty is that rules cannot fully include the rules of their own application. This means that for the interpretation of a rule, more rules are needed and rule interpretation is vague and cannot be determined to the last detail, at least in some respects. But not only is there a need to interpret the rule as such, since it also needs to be applied in ever new contexts with a series of more or less unique situations. In turn, this uniqueness again requires interpretation. Hence, any rule inherently requires a double act of interpretation, since both rule and situation must be interpreted respectively. If we add the possibility of non-compliance with a rule, we end up with three inherent dimensions of uncertainty in the context of rule-based organizing (Dobusch & Kapeller, 2012).

Taken together, the main consequence of this regulatory uncertainty lies in recognizing the full scope of the “active role” taken even by those who intend to follow or conform to a given rule. Following Giddens (1984), we operationalize these three forms of regulatory uncertainty and their influence on actors who apply or even try to evade a rule by looking at unanticipated conditions of a given rule. These conditions may either refer to the actual obedience of the rule-follower (which cannot be guaranteed), the ambiguities inherent in a given rule (which cannot be eliminated) or the specific situation and context in which the rule is to be applied (which cannot be entirely anticipated). In turn, these unanticipated conditions can lead to unintended consequences (Hirschman, 1967), i.e. unexpected positive or negative effects arising in the application or the execution of a given rule. With respect to accounting and accounting practices, Roberts and Scapens (1985, p. 447) strongly emphasize this aspect when stating that any “accounting system” creates a “system of accountability”, where the former “will inevitably meet with unanticipated conditions and, through us, will generate unanticipated consequences” (see also: Hopwood 1972, 1974).

Such a perspective aligns well with current theoretical arguments on regulatory uncertainty, stating that “rules and standards enable and restrict” because they “enable through restriction” (Ortmann, 2010, p. 205). In other words, while rules and standards preclude some options and strategies and favor others, they also raise awareness for additional, not-yet uncovered routes of action, which are highlighted only because of some specific properties of the underlying rule. In the same vein, rules can be used to legitimate any course of action, which seems beneficial or necessary in the light of the given rule, but has not been considered as a suitable option beforehand. In this paper we apply such a theoretical perspective to specific empirical cases of unanticipated consequences induced by the accounting regulation implicit in the “rule-based fiscal policy” (Buti & van den Noord, 2004, p. 7) advocated by the SGP. In this context, the regulatory uncertainty associated with the SGP leads to unintended consequences for fiscal policy and publicly owned firms throughout the European Union. Thereby, unintended consequences are not limited to cases where actors try to evade the underlying rule, but also occur in cases of strong rule-commitment.

#### **4. Unintended Consequences of the Stability and Growth Pact due to Monocular Accounting?**

If we apply the gist of our theoretical argument – that the implementation of rules for public accounting and fiscal policy is not straightforward, but rather subject to several qualifications – to issues of transnational coordination of fiscal requirements and goals, we can draw a series of conclusions. For instance, in the course of implementing the SGP, a codified set of accounting rules and procedures emerged under the label European System of National and Regional Accounts or ESA 95, which aimed at reducing the scope of interpretation associated with the SGP-framework. Hence, ESA 95 serves as a main tool for harmonizing public accounting standards and procedures in order to ensure comparability between member states as well as the enforceability of fiscal rules (European Commission 2002).<sup>7</sup>

The three dimensions of uncertainty in rule-following emphasized in our theoretical argument is also clearly visible in the context of the SGP: fiscal rules and common accounting standards provide incentives for creative accounting (von Hagen & Wolff 2006) and have been circumvented in the past, e.g. in Germany when specific interpretations of accounting standards fostered risky speculation by publicly owned banks (Jungbluth 2011). Also, the ongoing relevance of aligning rigid rules with a volatile economic situation has contributed to the emergence of a series of economic models (hosted by the European Commission) trying to separate ‘structural’ and ‘cyclical’ components of GDP and unemployment (Havik et al. 2014). In a sense, these models allow for additional flexibility within the SGP framework by adapting the latter to the current economic situation in different member states. Hence, we not only observe conscious rule-deviation but also witness the emergence of a certain technical tool-kit – incorporating statistical and model-based frameworks – to facilitate the interpretation of current economic conditions across member states in the context of applying the SGP.

Aside from these specific examples, the implementation of accounting rules as well as fiscal guidelines brings excess baggage with it, in the form of implicit or explicit incentives. While the facilitation of a strong and publicly visible commitment to balanced budgets or the implementation of restrictive fiscal policies count among the explicit incentives, a series of implicit incentives arise from the monocular orientation of the SGP: the sole focus on accumulated debts without juxtaposition of the relevant assets imposes restrictions on the financing of public services in transportation, health or child-care, as any additional debts incurred in these contexts are – strictly speaking – part of the debt burden relevant with respect to the Maastricht-criteria. Hence, there is an overarching rationale for the privatization of public infrastructure, as long as the latter relies at least partly on external financing. Similarly, publicly owned firms are confronted with these restrictions and, hence, have to modify their strategic orientation accordingly when SGP-induced financing criteria gain importance.

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<sup>7</sup> ESA 95 has been updated only recently to ESA 2010 (<http://ec.europa.eu/eurostat/web/esa-2010>, accessed: 16.12.15).

In the following two sub-chapters we aim to provide a stronger empirical foundation to these theoretical considerations by means of two in-depth case studies. In the first case – the privatization of the Berliner Wasserbetriebe (Berlin water supplier, BWB) – the SGP was framed as a main rationale for undertaking and justifying the privatization against the backdrop of the tense financial situation of the municipality of Berlin. In the second case we look at the organization and financing of motorway construction in Austria and trace the emergence of a specific institutional setup influenced by the introduction of the SGP. In both these cases we will find unanticipated conditions leading to unintended consequences related to the monocular orientation of the SGP, which eventually have a strong impact on the final outcomes.

### **5. The perils of conformity: the case of the Berlin waterworks**

The Berliner Wasserbetriebe (BWB) sees itself as a company with tradition, taking care of water and sanitation in and around Berlin as a public utility for over 150 years until it was partly sold to plug a hole in Berlin's municipal budget in the mid-1990s. While Berlin's municipal context was special insofar as its elected officials had to cope with the reunification of two equally overfed public administrations, the way they took on this challenge was not. Privatizing public corporations in general and public utilities in particular was an overall trend in Europe during the 1990s, not least due to the expansion of European competition law in the field of public services (Deckwirth, 2008). At the end of this decade, however, resistance against privatization strategies began to emerge, since promises of increased efficiency and investments had rarely been met.

So when Berlin's municipal government suggested the privatization of the BWB in an attempt to balance municipal budgets, some scattered opposition emerged even among members of the social-democratic SPD, which was in a coalition with the conservative CDU at that time. Gerlinde Schermer, then a member of the Berlin state parliament, was one of the most vocal critics of the planned deal. She recalls that the Maastricht criteria served as a justification for privatization efforts even before the introduction of the SGP in the mid-1990s:

“I remember that in 1994 a debate began with regard to the question whether to transform the hitherto owner-operated municipal enterprise *Berliner Wasserbetriebe* into a public corporation. [...] a main issue was to gain financial autonomy so that decisions on incurring new debt could be made in-house. [...] In 1995 budgetary consolidation was framed as an additional concern in this context, mainly substantiated by the introduction of the Maastricht-criteria.” (Schermer, interview)

In 1996 Berlin's then new finance senator Annette Fugmann-Heesing published a paper on 'Privatization in Berlin'. The aim was to activate public assets of DM 10.3 billion (roughly 5 billion €) through privatization, thereby reducing the interest burden and increasing budgetary leeway (see Passadakis, 2005). While balancing the budget deficit was the main argument of privatization

advocates, the introduction of the SGP and its enforcement of Maastricht criteria, also on the state level, soon provided another, seemingly imperative rationale for privatizing public utilities.

To secure support from the social-democratic group in the Berlin state parliament, SPD chair Detlef Dzembitzki and head of the SPD faction Klaus Böger called for an extraordinary state party conference of the SPD with the main topic of budget consolidation in November 1997. At this party conference, Böger and Dzembitzki (1997) presented a paper entitled “Die Krise als Chance nutzen” (“Using the Crisis as an Opportunity”), which devoted a whole section to the SGP’s Maastricht criteria under the heading “Maastricht has consequences for Berlin”. In this section, the two politicians quoted articles 104c and 109 from the Maastricht treaty at length, pointing to the 3 percent deficit rule and the 60 percent debt-to-GDP rule. Böger and Dzembitzki (1997, p. 9) then summarized (emphasis in original):

“These scales show that there *is no alternative to consolidating the state budget also from the viewpoint of the establishment of the European Monetary Union.*”

The monocular focus of these two rules on the debt side of the municipal balance sheet made privatization particularly attractive for Berlin’s government officials. As state parliament member Gerlinde Schermer recalls:

“They thought, we will do this with our public utilities. When we take them out of our state budget, we are also getting rid of all their debt.” (Schermer, interview)

While Maastricht was only one of several reasons given for consolidation efforts, privatization measures were considered to be a particularly effective means to meet the SGP’s Maastricht criteria. Most other reasons given for consolidation, such as stopping the growth of debt, relief for future generations, or structural changes to improve efficiency lacked a similarly focused incentive for privatization.

In addition to arguments that private management would provide higher efficiency compared to a publicly owned utility, the clear and seemingly objective Maastricht criteria also helped to convince opponents of the privatization measure:

“It looked so scientific with this 3 percent criteria. And everything sounded so complicated, and when something sounds complicated, people tend to say ‘it’s got to be right that way’”. (Schermer, interview)

At the time of the debate on its privatization, the BWB gave over DM 300 million to the state budget as a dividend, adding another DM 230 million in refurbishment. In addition, the workforce was a public unit, with staff-renting-contracts costing value-added tax, bringing DM 65 million to the state budget.

Together with concession fees the amount transferred to the state was about 800 or 900 million DM per year (SPD Berlin, 1997, p. 69). Privatization, in turn, would be merely a one-off payment with shareholders absorbing the profits. In other words, privatization meant short-term improvement according to the SGP's Maastricht criteria at the cost of long-term losses of dividend payments.

Nevertheless, in 1997 the first offer for BWB became public, as well as the fact that negotiations about possible investments had already been running for months (Böger & Dzembitzki, 1997, p. 8). In the year 1999 the French utility Veolia Water and the German RWE Group became private partners. As "strategic investors" they held 49.9% (24.95% each) of the BWB (Berliner Wasserbetriebe, 2015). These private partners had secured guaranteed dividend payments for themselves through secret supplementary contracts until 2003. In effect, this led to a significant price increase for water and eventually the state of Berlin gave millions of its profit to the BWB's private co-owners to avoid further price hikes (Thomsen, 2013; Zawatka-Gerlach, 2013).

In 2005 journalist Jörg Böwe made a request for access to the contracts. His application was rejected by the Senate Department of Finance on the grounds that an economic disadvantage to private companies could result from disclosure. A referendum on the disclosure of contracts followed in 2007. The Citizens' Initiative "Berlin Water Table" along with "Berlin Alliance against privatization" initiated a petition entitled: "No more secret treaties – Berlin, we want our water". The contracts were finally published in October 2010 by the left daily "die tageszeitung", followed by a successful referendum demanding re-municipalisation. Thereafter, the Senate continued with repurchasing efforts (Rau, 2013; Nürnberger, 2013).

## **6. The hidden treasures of rule-evasion: the case of Austrian motorways**

The ASFINAG<sup>8</sup> is a publicly owned stock corporation, which was founded in 1982 with the intention of providing a central financing company for Austria's highly segmented motorway-construction sector. Hence, in its first fifteen years of existence the ASFINAG was mainly a vehicle for fostering a coordinated and balanced expansion of traffic networks. In this period ASFINAG's main aim was one of supraregional coordination in the context of financing motorway construction projects to increase allocative efficiency and to administer a variety of mostly state-owned, but formally outsourced motorway-construction agencies.

The introduction of the Stability and Growth Pact in 1997 led to a profound change in this situation, since the prevailing mode of financing the construction of motorways throughout the country involved loans taken up by the ASFINAG. At the same time the ASFINAG was not allowed to collect any tolls. Hence, the ASFINAG was – according to ESA 95 – to be seen as a part of the general government sector. Therefore, its liabilities had to be counted as public debt when evaluating Austria's budgetary

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<sup>8</sup> The acronym ASFINAG stands for *Autobahn- und Schnellstraßen-Finanzierungs-Aktiengesellschaft* (stock corporation for financing highways and motorways).

situation with respect to the Maastricht-criteria. A first assessment of the situation clearly pointed to a relative increase in public debt with respect to the Maastricht criteria, since the ASFINAG had built up significant liabilities reaching about 6 billion € or more than 3% of the Austrian GDP at that time.

While one might assume that officials and politicians directly confronted the budgetary role of the ASFINAG as well as the respective routines of financing the construction of motorways, the mere existence of the ASFINAG as an external financing vehicle came into political focus for quite different reasons. While the introduction of the Stability and Growth Pact was met by significant efforts by the Austrian government to consolidate its budget, representatives of Austrian unions demanded the introduction of some expansionary measures to partially counteract the macroeconomic effects of a general contraction of the governmental sector. These two factors – the existence of the ASFINAG as well as the demand for expansionary countermeasures – can be considered as unanticipated conditions, which facilitated the emergence of a second possibility: redesigning the ASFINAG in a way suitable to evade the impending increase in public debt according to the Maastricht-criteria and, moreover, creating an option to circumvent the Maastricht-criteria in the future so as to facilitate the financing of additional public construction investment. As a former government consultant involved in the redesign of ASFINAG recalls:

“The aim was, the ASFINAG was designed to, I mean, the political backdrop was that the unions said they would only agree to a series of consolidation measures already planned, if some expansive countermeasure was taken. So he went to the Chancellor, and Klima [then the social-democratic chancellor of Austria] said ‘We have to do something, although it should not cost anything, because we have to conform to the Maastricht criteria. So, please come up with something!’ And, well, as a response we suggested [redesigning] ASFINAG and said, we could do something there.” (interview with a Ministry of Transportation official)

And indeed, an organizational revision of ASFINAG soon followed, with the main aim being to circumvent the Maastricht criteria in order to increase budgetary leeway. This revision was implemented in July 1997 (retroactively in January 1997) under the label of the *Infrastrukturfinanzierungsgesetz* (“Financing Infrastructure Act”).

Thereby, the aim to exempt some part of Austria’s public debt from the Maastricht criteria was offered as the main justification and legitimation of the *Infrastrukturfinanzierungsgesetz*, which revised ASFINAG’s purpose and organization. The official document even gives a nod to the monocular nature of the subverted rules by officially noting that

“the aim of this act is to increase Austria’s capability to accord with the Maastricht criteria with a special focus on the total amount of public debt.” (Press Release of the Austrian Parliament on July, 3 1997)<sup>9</sup>

In detail, this reform focused on three main elements: first, ASFINAG’s general scope was extended and ASFINAG was transformed from a mere financing agency to a full-flexed motorway construction agency responsible for financing, planning, constructing and operating motorways. Second, and due to its new operative capabilities, ASFINAG acquired the right to collect (but not to set) tolls. Thirdly, the underlying accounting procedures were modified structurally to reflect the underlying intention with respect to the monocular character of the Maastricht criteria. Before 1997 ASFINAG’s credit liabilities were balanced by corresponding claims against the Austrian Republic, (which effectively provided an explicit governmental guarantee), whereas after 1997 ASFINAG was credited with an “usus fructus” (basically a concession) related to the construction outputs, for a duration of 50 years, in order to provide ASFINAG’s balance sheet with corresponding suitable assets. In the same act remaining governmental debts related to motorway construction were relocated to ASFINAG to gain additional budgetary leeway.

“And our second method, which contributed to a transfer of 170 billion Schilling [roughly 12 billion €] of debt out of the budget straight to the ASFINAG. The ASFINAG was a multi-purpose weapon. One the one hand, this helped with the deficit [because of a reduction in interest payments and new sources of revenue in the form of tolls] and on the other hand, we gave a debt-backpack to ASFINAG which reduced our total debts. Back then, our debt was greater than 60%, but the backpack for ASFINAG allowed us to fulfill this criterion.” (Interview with a Ministry of Transportation official)

To guarantee low (re)financing costs for motorway-construction, the ASFINAG in turn issued a special program of state-backed bonds, implying effectively that “the risk is back with the state”<sup>10</sup>. The public ownership of ASFINAG also remained unchanged. Although the suggested reform had its critics within the Austrian government, such opposition was swayed by the obvious advantages of the proposed maneuver.

“The Ministry of Economic Affairs was strongly against it. We just told them to come up with a better model, which fulfilled these criteria. Then there was silence, for quite a long time ((laughs)).” (Interview with a Ministry of Transportation official)

Against this backdrop, it is part of common knowledge in Austrian political discourse that ASFINAG’s emergence resulted from a strategic consideration to evade the rules imposed by the Maastricht criteria in the context of financing motorway construction. Consequently, political parties and commentators,

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<sup>9</sup> See: [http://www.parlament.gv.at/PAKT/PR/JAHR\\_1997/PK0464/index.shtml](http://www.parlament.gv.at/PAKT/PR/JAHR_1997/PK0464/index.shtml) (dl. 25-09-15)

<sup>10</sup> As stated by ASFINAG-official Anton Sieber in a conference organized with the support of the OECD in 2006 (Sieber 2006).

the scientific literature (Merli 2003), the central auditing authority (Rechnungshof 2008) as well as (members of) ASFINAG itself (e.g. Sieber 2006) also openly advanced this argument.

“The only thing that went around as a joke against ministers was that the reorganization of financing was a sort of creative accounting, which allowed us to conform to the Maastricht criteria – at least for now.” (email-correspondence with the former Minister of Transportation, December 16, 2014)

From a theoretical viewpoint the unanticipated conditions – political demands for expansionary fiscal policy and the existence of an external financing vehicle – play a differentiated role in this case: while the ASFINAG gave additional scope to the rule-following actor, that is, the Austrian government, by forcing the latter to interpret the relevant rules with respect to ASFINAG, the external political demands created an additional, reinforcing incentive to engage in rule-evading behavior.

While this arrangement surely created new opportunities for the Austrian government, the underlying maneuver also created new challenges in the form of unintended consequences. One such issue relates to the technical question of how to administer a state-owned but privately organized company in accordance with ESA 95? Another possible issue was that the rule-enforcing agency, i.e. Eurostat, might come up with a different interpretation of the Austrian situation and classify ASFINAG as part of the general government sector. The first question was resolved by ensuring formal public control with the supervisory board; a strategy complemented by close-knit personal contacts between government officials and representatives of ASFINAG, which made informal correspondence and decision-making more important. The second issue proved to be more complicated. ASFINAG’s original classification as part of the private sector was based on the argument that – given the right to collect tolls – the ASFINAG would be able to and, hence, was able to finance its activities without governmental support in the long-term. This classification was subjected to an individual assessment by Eurostat, which acted as the rule-enforcing agency. Again, informal contacts played a decisive role in finding an agreement in favor of the Austrian interpretation.

“Back then, in the ESA council, we found an agreement with them. We did this obviously because I knew some people from the central bank, who take part in this council of statistical experts, and they also said that everything was okay. And if the [Austrian] central bank says ‘it’s ok’ then it is easier for a proposal to be passed. [...] Back then we found it was easy for our proposal to get passed, because everybody employed tricks at that time. Even our German friends did so.” (Interview with a Ministry of Transportation official)

Eurostat changed its interpretation of the classification of ASFINAG according to the ESA 95 various times. These interventions made by the rule-enforcing agency led in turn to further adaptations on the side of the Austrian government to sustain the status quo and invoked a continuous mutual negotiation



on the budgetary status of the ASFINAG with respect to the Maastricht criteria. For instance, until 2003 ASFINAG's (state-backed) bonds were issued by the Austrian *Bundesfinanzierungsagentur*. This practice was contested by Eurostat in 2003 – in response the Austrian government allowed ASFINAG to issue these bonds directly (Beckers et al. 2006, 8). In 2008 the introduction of an IFRS-compatible accounting framework required the national authorities to grant ASFINAG concessions for an unlimited time-span instead of imposing a limit of 50 years.

Another unanticipated effect more visible to the Austrian populace is related to the introduction of motorway tolls for personal vehicles by the now-operating agency ASFINAG. Motorway tolls for private transport were in no way part of the governmental strategy in that period and even met opposition from the Minister of Transport on the first occasion. However, at the same time the introduction of such tolls was indeed necessary to substantiate the government's strategy vis-à-vis Eurostat by increasing ASFINAG's earnings to boost its financial viability.

“Our first idea was to introduce road pricing [a scale-dependent toll applying to trucks] for personal vehicles as well. In response to this suggestion, the Chancellor asked: ‘do you want to kill me?’ ((laughs)) and in response we came up with the vignette [a periodic toll]. That implied that there is a constant stream of additional income, now roughly half a billion Euros, although the greatest income stream is, of course, road pricing.”  
(Interview with a Ministry of Transportation official)

While the evolution of the Austrian solution to financing motorway transport often follows a rather arbitrary path, the mode of motorway construction and operation, which emerged through this process, seems highly preferable when compared to the experiences of other countries: motorway construction in Austria was (and still is) flexible and liquid, while potential increases in liabilities related to road construction have never interfered with the more short-term allegations regarding public deficit and debt. However, it was also a distant offspring from the introduction of the SGP: originally, the ASFINAG represented a rather powerless financing vehicle, with a purely functional purpose. Thereby, its institutional appreciation and the related outsourcing of public liabilities is to be seen as a purely strategic maneuver induced by the introduction of the Stability and Growth Pact. Ironically, there is no element of long-term planning to be found in this context, although the underlying context very clearly relates to long-term investments.

## **7. Conclusions**

The major point of this paper is to illustrate how rule-following in public accounting cannot be assessed solely by looking at numerical outcomes, since – as we have shown – similar outcomes, in terms of the underlying accounting framework, may arise from quite different political strategies and behaviors. In developing this argument we refer to a case of great political importance – the

implementation of a common fiscal accounting framework for purposes of mutual surveillance within the Eurozone in the spirit of the criteria spelled out by the Maastricht Treaty.

In theoretical terms, our main finding can be explained by referring to the concept of regulatory uncertainty, which emphasizes that rule following – in accounting and elsewhere – is an ambiguous undertaking. The inherent incompleteness of rules both requires and enables actors to fill a void by providing an interpretation of the relevant rule-set in the face of a given situation. In the cases under study, the underlying situations provided conditions not specifically anticipated within the SGP, which successively framed and embedded the implementation of the Maastricht criteria, and led to unanticipated outcomes on various policy levels. In the Berlin Wasserbetriebe case the interpretation and reception of the Maastricht criteria were shaped strongly by Berlin's already high debt-burden, mainly resulting from German reunification. In this context the Maastricht criteria were interpreted as an additional imperative for fast, large-scale privatizations of public infrastructure. While such privatizations are surely in accordance with the SGP, one unintended outcome in this context was that, due to the increased pressure for fast privatization, Berlin put itself in a rather bad bargaining position by framing privatization as the only viable alternative – and consequently struck a rather bad deal. In the case of the Austrian motorways one such unanticipated condition was the existence of ASFINAG as a financing agency, which offered an alternative perspective on the role of state-funding in public infrastructure. When dealing with the question of how to proceed with the ASFINAG, officials found that this institution added a substantial sum to Austria's debt-burden according to Maastricht. However, political demands for expansionary fiscal policy provided an incentive for politicians to introduce a more flexible institutional arrangement for the ASFINAG, to allow for an alternative interpretation of the Maastricht criteria in the given context. Hence, the reform of ASFINAG's organizational setup as documented in section 5 is shaped strongly by the introduction of the stability and growth pact. All the associated reforms in this context – such as the introduction of a periodic toll for personal vehicles – can be understood as indirect consequences of the local implementation of the Maastricht criteria. In both cases, the monocular nature of the SGP, which is primarily intended to act as an otherwise neutral tool to enforce budgetary discipline across member states, contributes strongly to the emergence of the unintended outcomes. The main reason for these outcomes is given by the shrewd incentives arising from the sole focus on debt in cases where massive public infrastructure assets are (partly) externally financed.

The labels we used for our cases – 'rule-following' and 'rule-evasion', respectively – indicate that we do believe that the actions of the Berlin government documented in our first case are much closer to the actual 'spirit' of the underlying accounting rule than the strategy of the Austrian government. Additionally, these different stances also translate into quite different policies. Nonetheless, on the level of outcomes in terms of the monocular framework of the SGP, both strategies led to similar outcomes – a reduction in debt and deficits. What the monocular framework overlooks, however, might be more substantial: while in Austria a large-sized, market-based company was *created* in the course of events, which now pays dividends to the Austria government, Berlin not only (temporarily) *lost* a

substantial part of its assets, but also had to forgo a sizeable income stream resulting from the activities of the BWB.

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