



REPORT ON THE ECONOMIC SITUATION

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The impact of the decision by the Federal Constitutional Court

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The decision by the Federal Constitutional Court with regard to the second supplementary budget for 2021 from 15 November 2023 has made big waves. How did we get to this point? Where is the money supposed to come from? Will the federal government be able to agree on the 2024 budget? Is this a real government crisis? What is really going on?

Roughly speaking, the Federal Constitutional Court has made a determination as to what is allowed in the context of the "Schuldenbremse" (debt brake). In a second supplementary budget for 2021, which was only approved in January 2022, the federal government had transferred unused credit approvals from the economic stabilisation fund (WSF) for the COVID-19 crisis to the climate and transformation fund (KTF), so the funds could be used in subsequent years. These credit approvals were granted in 2021 using the exemption available under the Schuldenbremse, which allowed the federal government to raise the debt above 0.35 percent of the GDP, plus additional debt based on economic activity. Any additional debt must be formally repaid in subsequent years. This means that the federal government gave itself additional leeway to take on new debt by adding the credit approval from the year 2021 to the debt, even though this debt would only be taken on in subsequent years.

The court determined that this action was unconstitutional, and that credit approvals could not be simply transferred to later years. They have to be used in the year for which they were approved, with unused credit approvals expiring at the end of the year. Moreover, the court specified the financial policy options available in an emergency, i.e. with regard to the exemption under the Schuldenbremse. An emergency does not exist simply because it is perceived as such in the media or by politicians. The emergency must be traced back to a specific event that is beyond the control of the government, and which has a significant negative impact on the country's financial situation. The financial measures that are taken as a result must be appropriate to manage the situation, and they must be limited in terms of the amount - in other words, only do what is necessary. With this verdict, the KTF credit approvals in the amount of EUR 60 billion must be removed. However, this is not the first time the federal government has acted in this manner - the relaunch of the WSF for the gas and electricity price brake and

other funds also follow the same pattern. Therefore, a federal budget that conforms to the constitution requires a supplementary budget according to which the funds spent in 2023 for the gas and electricity price brakes must be posted in the year 2023 and not in the year 2022 (affecting the Schuldenbremse). As a result, the deficit exceeds the limit permitted under the Schuldenbremse, so that an emergency is declared after the fact; this was apparently avoided by the accounting practice chosen by the federal government, which is why the emergency was not stated at the end of 2022.

For the 2024 budget, this means a shortfall of approximately EUR 17 billion. Based on a federal budget of around EUR 470 billion, it is a manageable sum. Reductions in financial assistance, social transfers and tax breaks would lead to a structural improvement of the federal budget and could easily be managed economically.

There is no way of declaring another emergency for 2024 without violating the constitution. While economic growth is only moderate, there is no sign of an economic crisis involving the collapse of the GDP (as was the case in 2009 and 2020). There are also no signs of natural disasters affecting the whole country. The energy crisis that followed Russia's attack on Ukraine has abated. The Ukraine war has already raged for two years, Germany is not directly affected as a party in the war, and the additional support for Ukraine in the coming year does not pose a major problem for the government's financial situation. All of this also applies to the federal states that have set up unconstitutional transformation funds as defined by the court decision.

Overall, this leads to a moderate burden on economic activity in the coming year, but not more than that. Neither climate protection nor the social balance are at risk. All that is required is that federal and state governments return to financial normality. This is not a government crisis.

Sincerely yours

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