Fiscal Council of Romania

Position Note on the Public Budget and Fiscal Rules

Introduction

On September 23, 2024, the Government adopted, through Emergency Ordinance no. 113 and Emergency Ordinance no. 114, the first revision of the general consolidated budget for the current year. This included a significant increase in the cash budget deficit target, from 5% of GDP in the initial draft budget to 6.94% of GDP.

In its Opinion on the September 2024 budget revision proposal, the Fiscal Council (FC) assessed that the budget deficit target of 6.94% of GDP was optimistic, being based on assumptions that overestimated budget revenues and underestimated budget expenditures. Consequently, the FC considered a cash budget deficit of around 8% of GDP in 2024 to be more plausible, also highlighting the risk of significantly exceeding this level in the event of a rapid increase in expenditures.

On December 5, 2024, the Government adopted Emergency Ordinance no. 138 regarding the amendment and supplementation of certain legislative acts in the fiscal domain, as well as for regulating other measures. Under this ordinance, by derogation from the Fiscal Responsibility Law no. 69/2010 and the provisions of Law no. 417/2023 approving the ceilings of certain indicators specified in the 2024 fiscal framework, several provisions were adopted aimed at modifying these ceilings compared to the values established during the budget revision of September 2024.

The revision of the ceilings targeted both the general consolidated budget balance and the state budget balance, as well as the ceilings set for total expenditures and personnel expenditures. As a result of these adjustments, **the ceiling for the general consolidated budget deficit for 2024 was increased to 7.9% of GDP in ESA terms and to 8.58% of GDP in cash terms. This revision effectively amounts to a new adjustment of the public budget**.

In 2024, similar to the previous year, the Government continued to make extensive and discretionary use of the contingency reserve fund at the Government's disposal, through derogations from the provisions of the Fiscal Responsibility Law and the Public Finances Law.

It is worth noting that the Fiscal Council has consistently advocated in its analyses for realism and prudence in budgetary planning, as well as for measures that adhere to fiscal rules, consider transparency criteria, and follow best practices.

The revision of the ceilings for certain indicators specified in the 2024 fiscal framework

On December 5, 2024, the Government adopted Emergency Ordinance no. 138 concerning the amendment and supplementation of certain legislative acts in the fiscal domain, as well as the regulation of other measures. This ordinance introduced, by way of derogation from the Fiscal Responsibility Law no. 69/2010 and Law no. 417/2023 regarding the approval of ceilings for certain indicators specified in the 2024 fiscal framework, a series of provisions aimed at revising these ceilings compared to the values established in the September 2024 budget revision.

The revision of the ceilings targeted both the general consolidated budget balance and the state budget balance, as well as the ceilings set for total expenditures and personnel expenditures. As a result of these adjustments, **the ceiling for the general consolidated budget deficit for 2024 was increased to 7.9% of GDP in ESA terms and to 8.58% of GDP in cash terms**.

The main revisions to the ceilings, compared to those established in the September 2024 budget revision, are detailed below:

- The nominal ceiling for the general consolidated budget deficit was increased by 29 billion lei, from 122.8 billion lei to 151.8 billion lei. This revision corresponds to an increase in the general consolidated budget deficit, in cash terms, from 6.94% of GDP to 8.58% of GDP.
- The ceiling for the general consolidated budget deficit, in ESA terms, was set at 7.9% of GDP. In the initial budget for 2024, the target for the ESA deficit was 4.9% of GDP.
- The nominal ceiling for the primary deficit of the general consolidated budget was increased by 29 billion lei, from 85.6 billion lei to 114.6 billion lei. This adjustment corresponds to an increase in the primary deficit of the general consolidated budget from 4.84% of GDP to 6.48% of GDP.
- The nominal ceiling for the state budget deficit was increased by 30.3 billion lei, from 131.1 billion lei to 161.4 billion lei. This change corresponds to an increase in the state budget deficit from 7.41% of GDP to 9.12% of GDP.
- The ceiling for public debt was revised upward from 51.5% of GDP to 54.5% of GDP.
- The nominal ceilings for total expenditures, excluding financial assistance from the European Union and other donors, were revised upward:
  - +19.3 billion lei for the general consolidated budget, from 665.9 billion lei to 685.2 billion lei, equivalent to an increase of 1.1 percentage points of GDP compared to the September 2024 revision (from 37.65% of GDP to 38.75% of GDP);
  - +16.6 billion lei for the state budget, from 387.7 billion lei to 404.3 billion lei, implying an increase from 21.9% of GDP to 22.9% of GDP;
  - +6.6 billion lei for the general centralized budget of administrative-territorial units, from 138.2 billion lei to 144.8 billion lei, equivalent to an increase from 7.8% of GDP to 8.2% of GDP;
  - +5 million lei for the budget of the National Health Insurance Fund;

    - +2.9 billion lei for the budget of institutions/activities fully and/or partially funded from own revenues, from 50.4 billion lei to 53.3 billion lei, implying an increase from 2.85% of GDP to 3% of GDP;
    - +4.6 billion lei for other budgets within the general consolidated budget, from 20.1 billion lei to 24.7 billion lei, equivalent to an increase from 1.1% of GDP to 1.4% of GDP.

- The nominal ceilings for personnel expenditures were increased by:
    - +1.6 billion lei for the general consolidated budget, from 164.2 billion lei to 165.8 billion lei, equivalent to a revision from 9.3% of GDP (as established in the September 2024 revision) to 9.4% of GDP;
    - +1.6 billion lei for the state budget, from 88.7 billion lei to 90.3 billion lei, equivalent to a change in its share of GDP from 5.01% to 5.1%;
    - +5 million lei for the budget of the National Health Insurance Fund.

In addition to revising the ceilings, Emergency Ordinance no. 138/2024 authorized the Ministry of Finance to reduce the amounts allocated under the “Additional revenues collected from digitalization” chapter. It should be noted that revenues of 10.5 billion lei were allocated under this category in the 2024 budget, and this level was maintained during the September revision. The reduction of the amounts allocated to this chapter implicitly leads to an increase in the budget deficit.

The revision of previously established ceilings, as well as the reduction of additional revenues collected from digitalization confirmed the opinions expressed by the Fiscal Council regarding the 2024 budget and the September revision. The FC highlighted in its assessments the underestimation of certain categories of public expenditures, raised concerns about discretionary measures to increase personnel expenditures, pointed out uncertainties surrounding social assistance expenditures, and warned that the *ex-ante* inclusion of anticipated revenues from digitalization in the budget framework is not a prudent approach.

Use of the contingency reserve fund at the Government’s disposal in 2024

On May 14, 2024, the Government adopted Emergency Ordinance no. 46/2024 concerning certain budgetary measures and the amendment and supplementation of legislative acts, which revised, through a series of derogations from the Public Finances Law, the Fiscal Responsibility Law, and other laws, the operation of the contingency reserve fund for 2024. Specifically, the ordinance provided that in 2024: i) funds from the contingency reserve fund could be allocated, based on Government decisions, for financing current and capital expenditures of main authorizing officers; ii) main authorizing officers of the state budget were required to release to the contingency reserve fund, within one working day of the Ministry of Finance’s request, the commitment and budgetary credits retained in a 10% proportion; iii) the amounts allocated in the budgets of main authorizing officers under title 56: “Projects financed from post-accession non-reimbursable external funds"; title 58: "Projects financed from non-reimbursable external funds for the 2014-2020 financial framework"; title 60: "Projects financed from non-reimbursable financial assistance under the NRRP"; title 61: "Projects financed from amounts under the loan component of the NRRP" could be transferred to the contingency reserve fund, as provided in the 2024 state budget, in compliance with Article 54(1) of Law no. 500/2002, as subsequently amended and supplemented.

Up to now, the data on allocations from the contingency reserve fund reflect an unprecedented use of this mechanism for balancing the budgets of the main authorizing officers, particularly those at the central administration level. As of December 12, 2024, a total of 62.5 billion lei has been allocated from the contingency reserve fund (57.2 billion lei directed to the central administration and 5.3 billion lei allocated to local administrations). The share of the contingency reserve fund allocations in total budget expenditures is currently approximately 9.4%, an increase of 4.2 percentage points (pp) compared to 2023 and 8.2 pp higher than the average share for the 2007-2023 period. Until 2022, the share of the contingency reserve fund allocations in total budget expenditures ranged between a minimum of 0.2% in 2015 and a peak of 1.9% in 2020.

In 2024, 96% of the allocations from the contingency reserve fund were made after May 14, when the derogations regarding the operation of the contingency reserve fund were adopted. Specifically, by May 14, 2024, 2.5 billion lei had been allocated from the contingency reserve fund. Between May 14 and September 23 (the date of the budget revision), 27.5 billion lei were allocated. From September 24 to December 12, 32.5 billion lei were allocated from the contingency reserve fund. It is noteworthy that, despite the budget revision adopted on September 23, the Government continued to use the contingency reserve fund to balance the budgets of the main authorizing officers. This suggests that the budgetary aggregates may have been based on unrealistic projections.

Through these measures, as in 2023, the authorities have established a framework that allows the use of the contingency reserve fund to balance local and central budgets without requiring amendments to the annual budgets. Under these circumstances, the FC's[1] warnings remain relevant, highlighting that the use of the contingency reserve fund for reallocating resources within the general consolidated budget entails significant risks. These risks include a lack of transparency in budget execution, discretionary use, and an increased reliance on derogations from fiscal rules.

Conclusions

In recent years, fiscal rules have been circumvented through multiple derogations from existing legislation. These discretionary derogations reflect a lack of realistic and balanced budgetary planning, fail to adhere to the principle of transparency, and are not accompanied by coherent

[1] See the FC's Position Note on the Reduction of Public Expenditures, published on October 31, 2023.

public communication to justify them. **This assessment does not underestimate the significant pressures on the budget caused by successive major adverse shocks (the pandemic, the energy crisis, the war in Ukraine). Rather, it emphasizes that these extraordinary circumstances do not eliminate the need for realistic budgetary planning.**

Starting in 2025, the general consolidated budget needs to be developed based on premises that comply with fiscal rules and, more importantly, initiate credible fiscal consolidation. With the adoption of the new governance framework in the EU, the general consolidated budget must align with the principles and rules established by this framework. These rules are to be implemented at the national level through the medium-term fiscal-structural plans (MTPs).

On November 26, 2024, the European Commission approved the national medium-term fiscal-structural plan submitted by Romania[2]. Through this plan, Romania commits to a series of targets regarding the share of budget revenues and expenditures in GDP over the next 7 years, aiming to reduce the budget deficit to below 3% of GDP and ensure a downward trajectory of the public debt-to-GDP ratio by the end of the adjustment period. The plan also establishes a set of reforms and investments for the next 7 years to ensure the sustainable development of the economy.

The national fiscal rules and those of the European Union's new governance framework, as transposed into the national medium-term fiscal-structural plan, can serve as credible anchors around which realistic annual budgets can be built. In this context, to ensure predictability for the domestic business environment, maintain investor confidence in Romania, and stimulate sustainable economic development, it is essential for the 2025 draft budget to include credible and transparent measures for adjusting the budget deficit.

According to Article 13 of the Fiscal Responsibility Law no. 69/2010, the Government is obligated to adopt specific measures considering the current and projected levels of public debt. For 2025, the national medium-term fiscal-structural plan of Romania, which was agreed upon with the European Commission, stipulates a budget deficit of 7% of GDP.

This position note was approved by the Chairman of the Fiscal Council, in accordance with the provisions of Article 56, paragraph (2), letter d) of the republished Law no. 69/2010, following its adoption by the Council members through vote during the meeting held on December 17, 2024.

December 17, 2024 | Chairman of the Fiscal Council

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[2] https://economy-finance.ec.europa.eu/economic-and-fiscal-governance/stability-and-growth-pact/preventive-arm/national-medium-term-fiscal-structural-plans_en#romania