

## **Fiscal Council's Opinion on the Second Supplementary Budget for 2013**

The Ministry of Finance sent by letter no. 82490/28.10.2013 the second supplementary budget draft for 2013 to the Fiscal Council, requesting its opinion under article 40, paragraph (2) of Law no. 69/2010. Under this article of law, the Fiscal Council has the task to „analyze and issue opinions and recommendations on the annual budget laws preceding Government's approval and the submission to Parliament, on the supplementary budgets and other legislative initiatives that may have an impact on the budgetary targets, as well as assessing their compliance with the principles and rules specified in this Law”.

### **1. General Considerations**

Compared with the parameters approved in the first budget amendment, the current draft amendment forecasts a fall in general government revenue of 3.4 billion lei and a decrease in expenditure of 2.2 billion lei, the budget deficit target being revised upward at 15.9 billion lei (1.2 billion lei higher or 0.2 percentage points of GDP), respectively 2.54% of GDP (evaluated at 625.6 billion lei).

Regarding individual revenue items, the largest downward revision is reflected in the nontax revenue (-1.65 billion lei, respectively 0.2% of GDP). The main sources of the aggregate revision of the tax revenue (-1.8 billion lei) are the estimation of lower revenue from excises (-901 million lei), VAT (-365 million lei) and personal income tax (-308 million lei).

Excluding the impact of the compensation scheme (amounting 2.12 billion lei, whose distribution by expenditure category has undergone some changes compared to the scheme considered in the first budget amendment), the reduction in total expenditure is mainly due to cuts made at the level of goods and services acquisitions (-744 million lei), at the level of social assistance expenditure (-556 million lei), the use of existing reserves in the budgeted amount of interest expenditure (-477 million lei), the reduction of other transfers component (-446 million lei) and the decrease of expenditure related to projects funded by external grants (-287 million lei). Investment expenditure, including capital expenditure, expenditure funded from reimbursable funds and other transfers related to investments, decreased by 1.2 billion lei compared to the level approved in the first budget amendment.

The Fiscal Council still has serious doubts about the ability to fulfill the end-year target regarding the revenues from post-accession EU funds, given that, with only three months remaining, the level of revenues (5.03 billion lei) is less than half of the estimated amount for the entire year (12.15 billion lei), and the government estimations regarding the performance of EU funds absorption were systematically greater than the actual execution.

## ***2. The assesment of compliance with the fiscal rules***

The Fiscal Council's opinion on the first budget amendment recorded the violation (by derogation) of the rules stipulated by article 6 letters b) and c) and article 16 of the Fiscal Responsibility Law no. 69/2010 (FRL) regarding the budget revisions. Although the current budget revision, through the spending cuts operated to partially offset the downward revision of the projections for budgetary revenue brings the total expenditure (excluding financial assistance from the European Union and other donors) within the expenditure ceiling set by Law no. 4/2013 and restores compliance with the provisions of article 6 letters c), a new violation of article 6 letter b) of Law 69/2010 is recorded. The latter provision of Law no. 69/2010 states that "the balance and respectively the primary balance of the general government for the next budget year shall not exceed the ceiling set by the fiscal strategy approved by the Parliament". Thus, the draft amendment foresees a deficit of 15.9 billion lei, up by 2.5 billion lei (0.4% of GDP) than the ceiling of 13.394 billion lei established by Law no. 4/2013, the deviation from the legal ceiling increasing by another 1.2 billion lei compared to the level considered in the first budget amendment. In addition, if the cash deficit increase operated on the occasion of the first budget revision did not lead, as assessed by the government, to an increase in the budget deficit target according to ESA95 (relevant in terms of relations with the EU), this does not happen now, the failure of the ESA95 deficit target initially set at 2.4% of GDP being probably unavoidable. In the opinion of the Fiscal Council, it is essential to ensure the compliance of the budgetary outturn in 2013 with the ceiling of 3% of GDP (even with an enough comfortable margin to accommodate potential future data revisions<sup>1</sup>) stated in the Stability and Growth Pact, so that entering into a new excessive deficit procedure will be avoided.

In the opinion of the Fiscal Council, with only two months to the end of the year, the need to offset the impact on the deficit following a very large downward revision of the revenue projections raises important challenges. However, the Fiscal Council highlights that when the first budget revision was operated, it was sufficient evidence indicating that the revenue projection for the whole year is not prudent, and the Fiscal Council warned the Government in this regard in the Opinion issued on the occasion of the Half-year report on the budget execution and the first budget revision. The way the budgetary process was conducted this year - both budgetary amendments increased the deficit target, despite the existence of an explicit legal prohibition and of sufficient evidence, based on the budget execution at the end of the first 6 months on the high probability to achieve much lower budget revenue than the estimates, call into question the relevance of the budgetary rules and the commitment to fiscal discipline. The effectiveness of a fiscal rule is determined by the constraint that it exercises over fiscal policy formulation. The ease with which the fiscal rules have been repeatedly

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<sup>1</sup> See the case of the year 2012 in which the initial budget deficit in ESA95 standards was assessed to 2.9%, that led to the European Commission decision of removing Romania from the excessive deficit procedure, but recently, due to data revisions, the budget deficit for 2012 was increased to 3% of GDP.

circumvented this year (by derogation considering the rules established by article 6, letter b) regarding the budget deficit, respectively article 6, letter c) and article 21 regarding the level of public expenditure), alongside with the violations recorded in the years that have passed since the adoption of the Fiscal Responsibility Law in 2010 (of the rules stated by article 6, letter c) and article 21) highlights the weakness of the constraints exerted by the FRL fiscal rules and raises serious concerns about the commitment to the future fiscal policy rules that will be established given the provisions of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (the Fiscal Compact).

Beyond the impact on this year budget execution, the substantial revision of the budgetary revenues projections significantly alters the outlook for the budget of 2014, because any forecast will necessarily have as a starting point the current achievements. Consequently, in the opinion of Fiscal Council, significant additional discretionary measures are necessary to ensure the compliance with the budget deficit ceiling for the next year (especially since the budget revenues in 2012 and 2013 were favorably affected by temporary revenues from rental of frequency bands to mobile operators).

The above opinions and recommendations of the Fiscal Council were approved by the Chairman of the Fiscal Council, according to article 43, paragraph (2), letter d) of Law no. 69/2010, after being approved by the Council members through vote, on October 30<sup>th</sup>, 2013.

**October 30, 2013**

**Chairman of the Fiscal Council**

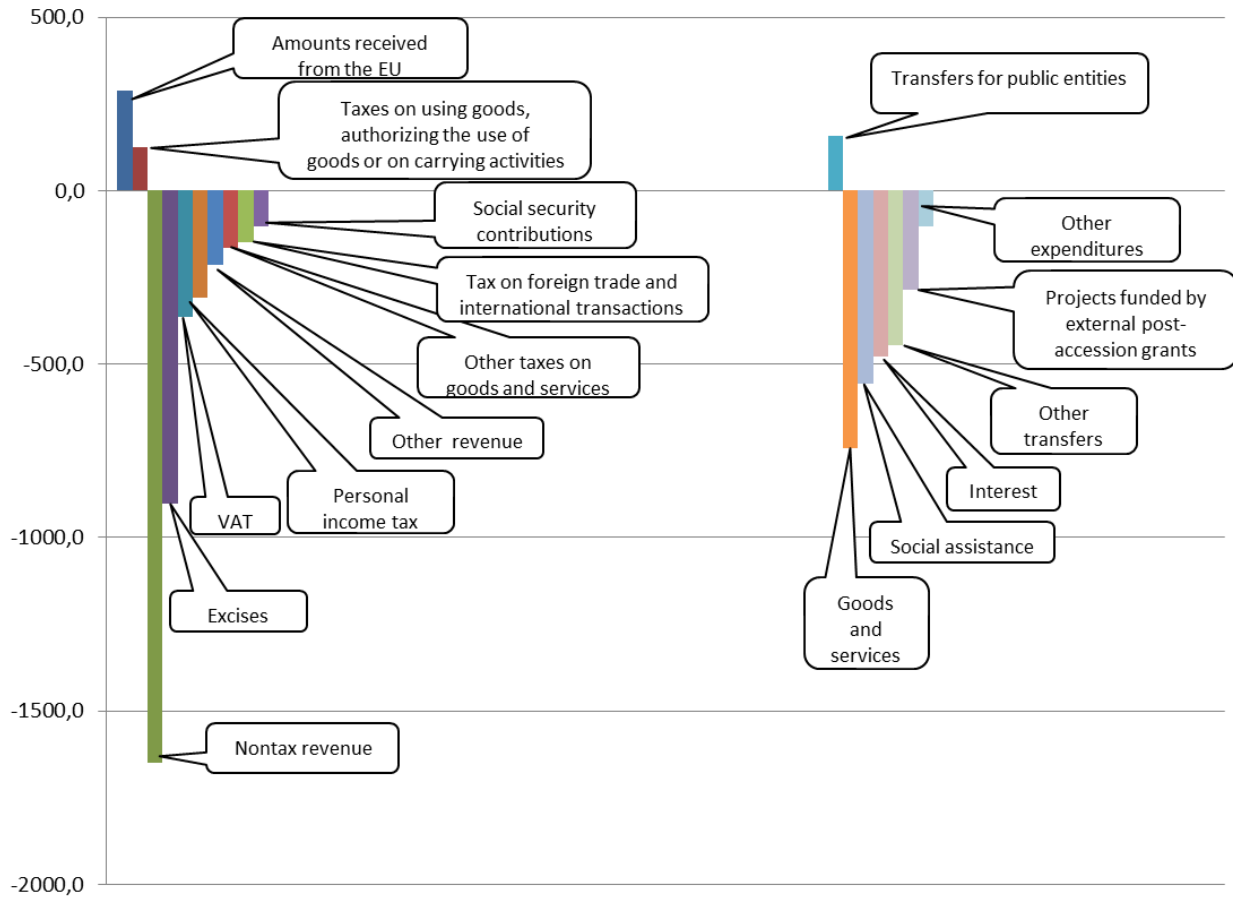
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## Annex I

	2013 Initial budget	Swap schemes	2013 Initial budget excluding schemes effect	2013 Budget after the first rectification	Updated swap schemes	2013 Budget after the first rectification excluding schemes effect	2013 Budget after the second rectification	Updated swap schemes	2013 Budget after the second rectification excluding schemes effect	Revised budget I - Initial budget	Revised budget II - Initial budget	Revised budget II - Revised budget I
	1	2	3=1-2	4	5	6=4-5	7	8	9=7-8	Levels adjusted for the impact of swaps		
										10=6-3	11=9-3	12=9-6
<b>TOTAL REVENUE</b>	209285,0	1000,0	208285,0	209406,6	2118,0	207288,6	205964,3	2118,0	203846,3	-996,4	-4438,7	-3442,3
<b>Current revenue</b>	196747,6	1000,0	195747,6	195935,0	2118,0	193817,0	192284,0	2118,0	190166,0	-1930,6	-5581,6	-3651,0
<b>Tax revenue</b>	122965,3	1000,0	121965,3	122468,1	2118,0	120350,1	120569,9	2118,0	118451,9	-1615,2	-3513,5	-1898,3
<b>Taxes on profit, wages, income and capital gains</b>	36359,9		36359,9	35293,9	0,0	35293,9	34921,0		34921,0	-1066,0	-1439,0	-373,0
Profit	11721,8		11721,8	10869,8	0,0	10869,8	10805,0		10805,0	-852,0	-916,8	-64,8
Personal income tax	23146,2		23146,2	23146,2	0,0	23146,2	22838,1		22838,1	0,0	-308,1	-308,1
Other taxes on income, profit and capital gains	1491,9		1491,9	1277,9	0,0	1277,9	1277,9		1277,9	-214,0	-214,0	0,0
Property tax	4493,8		4493,8	4493,8	0,0	4493,8	4452,8		4452,8	0,0	-41,0	-41,0
<b>Tax on goods and</b>	80980,7	1000,0	79980,7	81519,5	2118,0	79401,5	80214,1	2118,0	78096,1	-579,2	-1884,6	-1305,4
VAT	52948,8	1000,0	51948,8	53175,0	2118,0	51057,0	52810,0	2118,0	50692,0	-891,8	-1256,8	-365,0
Excises	22363,2		22363,2	21843,2	0,0	21843,2	20942,1		20942,1	-520,0	-1421,1	-901,1
Other taxes on goods and	956,2		956,2	1788,8	0,0	1788,8	1622,9		1622,9	832,6	666,7	-165,9
Taxes on using goods, authorizing the use of goods	4712,5		4712,5	4712,5	0,0	4712,5	4839,1		4839,1	0,0	126,6	126,6
<b>Tax on foreign trade and international transactions</b>	741,8		741,8	741,8	0,0	741,8	591,8		591,8	0,0	-150,0	-150,0
Other tax revenue	389,1		389,1	419,1	0,0	419,1	390,1		390,1	30,0	1,0	-29,0
<b>Social security contributions</b>	54355,3		54355,3	54428,2	0,0	54428,2	54325,2		54325,2	72,9	-30,1	-103,0
<b>Nontax revenue</b>	19427,0		19427,0	19038,7	0,0	19038,7	17389,0		17389,0	-388,3	-2038,0	-1649,7
<b>Capital revenues</b>	687,1		687,1	687,1	0,0	687,1	607,1		607,1	0,0	-80,0	-80,0
<b>Grants</b>	629,9		629,9	630,7	0,0	630,7	631,9		631,9	0,8	2,0	1,2
<b>Amounts received from the EU</b>	11220,2		11220,2	12153,8	0,0	12153,8	12441,4		12441,4	933,6	1221,2	287,6
<b>TOTAL EXPENDITURE</b>	222679,2	1000,0	221679,2	224106,7	2118,0	221988,7	221864,4	2118,0	219746,4	309,5	-1932,8	-2242,3
<b>Current expenditure</b>	205009,7	1000,0	204009,7	206258,2	1500,0	204758,2	204108,8	1600,0	202508,8	748,5	-1500,9	-2249,4
Personnel	46154,0		46154,0	46152,7	0,0	46152,7	46152,0		46152,0	-1,3	-2,1	-0,8
Goods and services	37262,9		37262,9	39766,8	500,0	39266,8	39522,6	1000,0	38522,6	2003,9	1259,8	-744,2
Interest	11383,0		11383,0	11362,9	0,0	11362,9	10885,3		10885,3	-20,1	-497,7	-477,6
Subsidies	5229,8		5229,8	5242,9	0,0	5242,9	5213,8		5213,8	13,1	-16,0	-29,1
<b>Total Transfers</b>	103990,2	1000,0	102990,2	102568,5	1000,0	101568,5	101073,2	600,0	100473,2	-1421,7	-2517,0	-1095,3
Transfers for public entities	1632,8	850,0	782,8	1692,4	850,0	842,4	1448,7	450,0	998,7	59,6	215,9	156,3
Other transfers	12265,7	150,0	12115,7	11785,4	150,0	11635,4	11338,7	150,0	11188,7	-480,3	-927,0	-446,7
Projects funded by external post-accession grants	17311,2		17311,2	16845,7	0,0	16845,7	16558,3		16558,3	-465,5	-752,9	-287,4
Social assistance	69979,4		69979,4	69375,7	0,0	69375,7	68819,4		68819,4	-603,7	-1160,0	-556,3
Other expenditure	2801,1		2801,1	2869,3	0,0	2869,3	2908,1		2908,1	68,3	107,0	38,8
<b>Expenditure funded from</b>	782,9		782,9	976,8	0,0	976,8	896,3		896,3	193,9	113,4	-80,5
<b>Capital expenditure</b>	17669,5		17669,5	17848,5	618,0	17230,5	17755,6	518,0	17237,6	-439,0	-431,9	7,1
<b>Overall Balance</b>	-13394,2		-13394,2	-14700,0	0,0	-14700,0	-15900,0		-15900,0	-1305,9	-2505,9	-1200,0

Source: The Ministry of Finance

**Figure 1: The main changes in expenditures and revenues compared to first budget revision (without the impact of swap schemes), million lei**



**Figure 2: The main changes in expenditures and revenues compared to the initial budget (without the impact of swap schemes), million lei**

