Romania

Fiscal Council

Fiscal Council's Opinions

2016

FISCAL COUNCIL
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I. Fiscal Council's opinion on the Romanian Government's initiative regarding "The hedging policy of the Romanian state regarding the risks related to Romanian investment abroad and exports to new markets outside the European Union"

The Fiscal Council received on 18.04.2016 from the Ministry of Public Finance (MPF) the letter no. 539238/11.04.2016 requesting, under art. 53, paragraph (2) of the Fiscal Responsibility Law no. 69/2010 republished (FRL), the opinion and the endorsement on the Romanian Government's initiative regarding "The hedging policy of the Romanian state regarding the risks related to Romanian investment abroad and exports to new markets outside the European Union". The project is accompanied by the estimation made by Eximbank S.A. of the direct impact on the budget deficit implied by the implementation of the proposed project.

According to the aforementioned law article, the attributions of the Fiscal Council include "analyzing and issuing opinions and recommendations on the annual budget laws before approval by the Government and before 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", this project falling within the category of legislative initiatives with possible impact on government spending.

Essentially, the project envisages a better use of the institutional framework provided by the Law no. 96/2000 republished on the activity of Eximbank in the name and on behalf of the state, by increasing the role of Eximbank as an Export Credit Agency. Thus, a support is considered for the exporters that identify export opportunities in non-EU areas where the risks are very high and they cannot find solutions of protection on the private market insurance, by offering insurance policies for credit risk, whereby the state takes over the commercial and political risks of these exports, so that those opportunities are achieved.

The project proposal is also accompanied by an assessment of the impact on the budget deficit, carried out by Eximbank, according to which in the pessimistic scenario, it could result in a negative impact on the budget deficit of 1.85 million lei in 2016, 5.99 million lei in

2017 and respectively 6.91 million lei in 2018, while in the optimistic scenario the impact could be favorable, respectively 1.18 million lei in 2016, 1.8 million lei in 2017 and 3.09 million lei in 2018.

Regarding the opportunity of the draft legislation, the Fiscal Council has no competences to adjudicate, given that the establishment of the ways to support export activities is the prerogative of the Government or other institutions. Concerning the conformity with the principles and fiscal rules stated in the Fiscal Responsibility Law, the Fiscal Council considers that, subject to the validity of the assumptions on which we cannot pronounce, the proposed project envisages in the pessimistic scenario reduced budgetary outlays, relative to the size of the general consolidated budget, whose increase can be easily accommodated by reducing other categories of expenditure so that the budgetary targets and rules stated by FRL can continue to be respected.

Regarding the endorsement of the project proposal, the Fiscal Council considers that it does not fall in the situations mentioned in the FRL which require its issuance, limiting to appreciate the compliance with principles and fiscal rules stated by the law.

The above opinions and recommendations of the Fiscal Council were approved by the Chairman of the Fiscal Council, under art. 56, paragraph (2), letter d) of the Fiscal Responsibility Law no. 69/2010 republished, based on the vote of the Fiscal Council members in the meeting on 27th April 2016.

27th April 2016

Chairman of the Fiscal Council,

IONUȚ DUMITRU

II. Fiscal Council's opinion on the legislative proposal amending and supplementing Law no. 227/2015 regarding the Fiscal Code

On the 29th of March 2016, the Romanian Senate remitted to Fiscal Council, the letter no. XXXV/1605 from the 22nd of March 2016, requesting, under art. 53, paragraph (2), letter e) of the Fiscal Responsibility Law no. 69/2010 republished, the Fiscal Council's opinion on a parliamentary initiative for amending the Fiscal Code.

According to the aforementioned article of the FRL, among the main tasks of the Fiscal Council are:

> e) analysis and issuing opinions and recommendations on the annual budget laws before approval by the Government and before 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;
>
> f) preparing estimates and issuing opinions on the budgetary impact of the normative ordinances, other than the ones mentioned on (e) and the amendments made on the annual budget law during the parliamentary debates.

For the case in question it is also relevant art. 21 of FRL, according to which "*proposals for any legislation leading to a reduction of budgetary revenues must provide a financial statement according to article 15 of Law no. 500/2002, as amended and supplemented and meet at least one of the following conditions:*

> *a) to have the endorsement of the Ministry of Public Finance and of the Fiscal Council, confirming that the financial impact was taken into account in the budgetary revenue forecast and does not affect the annual budget targets and medium term targets;*
>
> *b) to be accompanied by proposals for measures to compensate the financial impact, by increasing other budgetary revenues."*

In this regard, the present opinion is intended to facilitate the computation of the above-mentioned financial statement.

Brief description of the legislative proposal and its budgetary impact

The legislative proposal which is subject to the Fiscal Council's examination stipulates changes to many of the current provisions of the Fiscal Code regarding (see Annex 1):

- Raising the ceiling for deductibility of expenses incurred with sponsorship, patronage and expenses incurred with private scholarships from 5% to 10% from the tax base;

- Introducing the taxpayers' possibility for deciding on the destination of an amount representing 4% of the annual income tax to support the private providers of social services mentioned in article 37, paragraph (3), letters a) and b) of the Law no. 292/2011 on social services;
- Changing the tax base and tax rate related to the transfer of real estate from the personal property;
- Extending the application scope of the reduced VAT rate of 9% for sewerage services, production, transmission, distribution and supply of heat in a centralized system, electricity supply, gas supply and public sanitation service of the localities;
- Extending the tax exemption on lands and buildings publicly or privately owned by the administrative - territorial units used for sports activities;
- Annual revision by the local authorities of the value of non-residential buildings owned by individuals;
- Canceling the uptake of arable land which is around the construction area up to 400 square meters as being construction land and proceeding to the taxation of them as arable land;
- Changing the date on the application of the exemption / reduction of tax payment from January 1st of the year following the one in which the person submitted the supporting documents, to the first day of the month following the one in which the person submitted the supporting documents.

The Fiscal Council considers that among the measures from the list, the highest negative impact on budget revenues is represented by the extension of the application scope of the reduced VAT rate. Although all the proposed measures have a certainly negative impact on budget revenues, under certain conditions some of them do not end up affecting the general government balance, while for others is possible only an approximate evaluation of the first-round impact or a quantitative assessment of this impact wasn't possible. Concerning the latter category, Fiscal Council couldn't identify information that would determine the first-round impact for:

- Raising the deductible ceiling from 5% to 10% from the tax base for expenses incurred with sponsorship, patronage and expenses incurred with private scholarships given that there isn't a database in which the deductible expenses from the past are identified separately;
- Canceling the assimilation of arable land which is around the construction area up to 400 square meters as being construction land and proceeding to the taxation of them as arable land, given that there isn't a database in which the lands that can be affected of this law can be identified differently;

Also, a quantitative assessment of the impact on local budget revenues was not possible for the case of extending the tax exemption area on lands and buildings publicly or privately owned by the administrative - territorial units for sports activities, given the lack of data on the value of the properties concerned. However, the impact of this proposal on general consolidated budget is potentially neutral given the fact that at the level of the consolidated budget, there are taxes that the state owes itself and whose removal would entail a corresponding reduction in expenses.

Concerning the measures whose impact is likely to be quantified, the Fiscal Council considers that the first-round effect of the proposed extension of the reduced VAT rate of 9% (the sewerage, production, transmission, distribution and supply of heat in centralized system, supply of electricity, supply of natural gas and public sanitation service of the localities) is estimated at the level of the year 2017[1] - assuming that the reduction in the VAT rate would be from 19% to 9% - at a level between 1,200 million lei (amount determined at the level of the relevant expenditure in 2014, based on the National Institute of Statistics' survey "Coordinates of the living standard in Romania. Income and private consumption in 2014") and 1,480 million lei (extrapolating the relevant expenditure with the National Commission for Economic Forecasting's prediction for the dynamics of the nominal aggregate consumption of services).

On the proposed amendment granting the possibility to decide on the destination of 4% of the annual income tax owed by taxpayers to support private providers of social services, it is difficult to achieve an accurate assessment of the impact, given that it necessarily depends on the share in total taxpayers who choose to redirect the legal percentage of the income tax of those who decide to redirect 4% (in favor of supporting private providers of social services as referred in the legislative proposal). Taking as a starting point the amount redirected in 2015 (about 140 million lei, and by default the assumption that the prevalence of the decision in favor of redirecting remains the same), updated in 2017 with the forecasted dynamics of the average salary and the number of employees, and assuming that the percentage of those who choose to redirect in favor of the entities eligible for the transfer of 4% of the income tax is 50%, the shortfall in the revenue at the budget level would be around 90 million lei.

Regarding the proposed measure amending the tax base and the tax rate related to the transfer of real estates from the personal property, the Fiscal Council considers as likely to happen, that most of the impact to be derived from changing the tax base from the value of the property to the difference between the sale price and the acquisition price of the ownership, and in the case where the difference is negative the tax due should be zero. An accurate assessment of the first-round impact is also impossible due to difficulties in establishing the new tax base through the information required on the purchase price of the buildings. However, given the fact that the prices in the property market currently represents about 60% of the 2008 prices (top of the housing boom in the pre-crisis period), it is expected that a part more than significant from the current revenues from the tax on

[1] See Annex 2.

transfer of real estate properties – which, in 2015, amounted to 692.8 million lei (this value should be regarded as a ceiling for the potential loss), to disappear[2].

Conclusion

Despite the difficulties in quantifying the first-round impact for the whole set of proposed legislative changes, the negative impact on the budget revenues seems to be significant, representing, most likely, the equivalent of 0.2-0.3% of GDP, if the measures are implemented in 2017. In the absence of compensatory measures, either on the revenue side or on the expenditure side, the operationalization of the proposed measures would lead to, *caeteris paribus*, an equal increase in the structural deficit[3] and, to a lesser extent, in the actual budget deficit, given the increasing in the cyclical component of the budget deficit caused by a possible stimulating effect on the GDP growth. The previous assessments of the Fiscal Council, developed in the context of the last year's opinion on the revision of the Fiscal Code, would indicate the recovery of 25-30% of the first-round effect as a result of the additional economic growth after a period of 3-4 years[4].

The proposed measures would come in the conditions of which the 2016 budget already confirms a major slippage (about 1.7% of GDP, as assessed by the Ministry of Public Finance, or 2% of GDP according to the European Commission’s winter forecast) of the structural balance from the medium term objective of a structural deficit of 1% of GDP, in accordance with the combined provisions of the preventive arm of the Stability and Growth Pact and the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (the Fiscal Compact), operationalized in the national legislation through the republished Fiscal Responsibility Law. Moreover, the budget construction of this year involves a deficit placed immediately below the reference threshold of 3% of GDP for the actual budget balance established by the corrective arm of the Stability and Growth Pact, above which would be entailed a re-entry of Romania under the Excessive Deficit Procedure.

A possible implementation of the proposed measures in 2017 without compensatory measures would come at a time when the second round of measures of fiscal relaxation approved in September 2015 is assessed by the European Commission to aggravate the structural slippage to 3% of GDP, considering that its projections indicate a structural deficit of 4% of GDP and an actual budget deficit situated significantly above the reference level of

[2] Furthermore, promoting these legislative amendments would introduce a difference in treatment concerning the taxation of income from real estate transactions and those from securities transactions (given that capital gains related to the latter are taxed at 16%). In its current form, the legislative proposal has at least one parallelism with the business taxation, a.i. there are a tax profit rate of 16%, and a turnover tax rate for micro-enterprises between 1-3% (depending on number of employees).

[3] See Section 3 of the Fiscal Council’s opinion on the draft revision of the Fiscal Code from March 2015 for a discussion on the implications of formulating budgetary targets in structural terms.

[4] Under an impact multiplier of 0.4 and a multiplier in t + 3 period of about 1.1.

3% of GDP (3.8% of GDP according to the winter forecast); even taking the current government assessments for the next year[5], given that the indicated level of the budget deficit lies right next to the level of 3% of GDP, the entry into force of the proposed legislative changes in the absence of compensatory measures have the potential to lead the budget deficit above the 3% level and causing the re-entry of Romania under the Excessive Deficit Procedure.

Given all this, the Fiscal Council believes that there is no fiscal space to adopt the proposed measures relative to the current targets of budget deficit over the medium term, and their position close to the reference level of 3% along with the slippage already enshrined in the Budget Law of 2016 from the medium-term target of structural deficit, constitute aggravating circumstances for any breach thereof. Moreover, the opportunity for additional measures of fiscal relaxation in the current context, in which the cyclical position is close to balance or estimated to turn positive again (recording the existence of a positive output gap in 2017 according to the assessments of the European Commission) is at least questionable from the perspective of macroeconomic policies designed to mitigate the fluctuations in the economic cycle, as it is also questionable the opportunity for additional discretionary measures to stimulate consumption (as it is the case for the proposed VAT reductions), while currently there are registered double-digit annual growth rates at the retail level. In these circumstances, the Fiscal Council reiterates its previous warnings about the situation of maintaining an upward trend of the ratio of public debt to GDP in a period of high growth and the associated risks from the perspective of long term sustainability.

The Fiscal Council considers that a reflection on the existing budgetary constraints is welcome and should be part of the subsequent proceeding course of the legislative proposal in question, so the desire to increase disposable income in the short term do not end up having adverse consequences on medium and long term.

The above opinions and recommendations of the Fiscal Council were approved by the Chairman of the Fiscal Council, under art. 56, paragraph (2) of the Fiscal Responsibility Law (FRL) no. 69/2010 republished, based on the vote of the Fiscal Council members in the meeting on 27th April 2016

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[5] The Fiscal Council has expressed its reservations about the fiscal projections for 2017 in the context of "The Fiscal Council's opinion on the State Budget Law, the Social Insurance Budget Law for 2016 and the Fiscal Strategy for 2016-2018" in December 2015.

ANNEX 1

Chapter	ART.	Law 227/2015 regarding the Fiscal Code (last updated: Law no. 358 of December 31, 2015)	Proposal for amending
		TITLE IV - Income tax	
CHAPTER II - Income from independent activities	ART. 68 - General rules for determining the net annual income from independent activities, determined in real system, based on accounting data	(5) The following expenses are deductible within a limit: a) sponsorship expenses, corporate patronage and private scholarships, made under the law, within a limit of 5% of the base calculated in accordance with paragraph (6).	(5) The following expenses are deductible within a limit: a) sponsorship expenses, corporate patronage and private scholarships, made under the law, within a limit of **10%** of the base calculated in accordance with paragraph (6).
CHAPTER III - Income from wages and assimilated to wages	ART. 79 - Granting the right to the taxpayer to decide on the destination of an amount of the tax	(1) Taxpayers may decide on the destination of an amount up to 2% of the tax due on art. 78 para. (5) to support non-profit entities that are established and operate under the law, religious units, as well as private scholarships, in accordance with the law. Individuals who earn income assimilated to wages benefit from the same provisions.	(1) Taxpayers may decide on the destination of an amount up to 2% of the tax due on art. 78 para. (5) to support non-profit entities that are established and operate under the law, religious units, as well as private scholarships, in accordance with the law, **either up to 4%, for supporting the private providers of social services referred to in art. 37 para. (3) a) and b) of Law no. 292/2011 on social assistance.** Individuals who earn income assimilated to wages benefit from the same provisions.
CHAPTER III - Income from wages and assimilated to wages	ART. 82 - Payment of tax for certain income from wages and assimilated to wages	(6) Taxpayers may decide on the destination of an amount up to 2% of annual tax to support non-profit entities that are established and operate under the law, religious units, as well as private scholarships, in accordance with the law.	(6) Taxpayers may decide on the destination of an amount up to 2% of annual tax to support non-profit entities that are established and operate under the law, religious units, as well as private scholarships, in accordance with the law, **either up to 4%, for supporting the private providers of**

			social services referred to in art. 37 para. (3) a) and b) of Law no. 292/2011 on social assistance.
CHAPTER VI - Income from pensions	Art. 102 - Granting the right to the taxpayer to decide on the destination of an amount of the tax	(1) Taxpayers may decide on the destination of an amount up to 2% of the tax due on art. 101 par. (11) for supporting non-profit entities that are established and operate under the law, religious units, as well as private scholarships, in accordance with the law.	(1) Taxpayers may decide on the destination of an amount up to 2% of the tax due on art. 101 par. (11) for supporting non-profit entities that are established and operate under the law, religious units, as well as private scholarships, in accordance with the law, **either up to 4%, for supporting the private providers of social services referred to in art. 37 para. (3) a) and b) of Law no. 292/2011 on social assistance.**
CHAPTER IX - Income from transfer of real estate from the personal property	ART. 111 - Definition of the income from transfer of real estate from the personal property	(1) At the transfer of the property rights and its dismemberments, by legal acts between living, on the constructions of any kind and their associated land, as well as on the lands of any kind without any construction, taxpayers owe a tax which is calculated as follows: a) for the constructions of any kind and their associated land, as well as on the lands of any kind without any construction, acquired within a period of up to 3 years inclusively: (i) 3% up to value of 200.000 lei inclusively; (ii) over 200.000 lei, 6.000 lei + 2% calculated on the amount exceeding 200.000 lei inclusively; b) for the real estates listed in subparagraph a), acquired at an earlier date than 3 years: (i) 2% up to value of 200.000 lei inclusively; (ii) over 200.000 lei, 4.000 lei + 1% calculated on the amount exceeding 200.000 lei	(1) At the transfer of the property rights and its dismemberments, by legal acts between living, on the constructions of any kind and their associated land, as well as on the lands of any kind without any construction, taxpayers owe a tax **of 3% calculated on the difference between the purchase price or the value of the estate, where appropriate, and the selling price. If the difference is negative, no tax is due.**

		inclusively.	
CHAPTER XI - Annual taxable net income	Art. 123 - The establishment and payment of the annual tax due	(2) Taxpayers may decide on the destination of an amount of the annual tax to support non-profit entities that are established and operate under the law, religious units, as well as private scholarships, in accordance with the law, amount representing up to 2% of the tax on the annual taxable net income, annual taxable net gain determined according to art. 119. (3) Taxpayers who realized income from independent activities/agricultural activities imposed based on income norm, and/or lease of goods, which do not have to submit the declaration on income, can provide the destination of an amount to support non-profit entities that are established and operate under the law, religious units, as well as private scholarships, in accordance with the law, amount representing up to 2% of the tax on the annual income. (4) The competent fiscal body is obliged to calculate, withhold and pay the amount representing up to 2% of the tax for: a) annual taxable net income; b) annual taxable net gain determined according to art. 119; c) income mentioned in para. (3).	(2) From the tax on the annual taxable net income, annual taxable net gain determined according to art. 119., taxpayers may decide on the destination of an amount representing up to 2% to support non-profit entities that are established and operate under the law, religious units, as well as private scholarships, in accordance with the law, **either up to 4%, for supporting the private providers of social services referred to in art. 37 para. (3) a) and b) of Law no. 292/2011 on social assistance.** (3) From the tax on the annual income, taxpayers who realized income from independent activities/agricultural activities imposed based on income norm, and/or lease of goods, which do not have to submit the declaration on income, can provide the destination of an amount representing up to 2% to support non-profit entities that are established and operate under the law, religious units, as well as private scholarships, in accordance with the law, **either up to 4%, for supporting the private providers of social services referred to in art. 37 para. (3) a) and b) of Law no. 292/2011 on social assistance.** 4) The competent fiscal body is obliged to calculate, withhold and pay the amount representing up to 2% **or 4%**, as the case, of the tax for: a) annual taxable net income;

			b) annual taxable net gain determined according to art. 119; c) income mentioned in para. (3).
TITLE VII – Value Added Tax			
CHAPTER VIII - Tax rates	ART. 291 – Tax rates	There are no letters h), i), j), k), l) at para. (2).	(2) The reduced rate of 9% applies to the base of taxation for the following supplies of services and/or goods delivered: **h) sewerage services;** **i) production, transmission, distribution and supply of heat in centralized system;** **j) the supply of electricity;** **k) delivery of natural gas;** **l) the public service of sanitation for localities.**
TITLE IX - Local taxes			
CHAPTER I - General provisions	ART. 453 - Definitions	There is no para. (2).	**(2) For the purposes of this title, individuals doing business under the Government Emergency Ordinance no. 44/2008 on economic activities by authorized individuals, individual enterprises and family businesses, as amended and supplemented, shall be assimilated individual taxpayers.**
CHAPTER II – Tax on buildings	ART. 456 - Exemptions	(1) The tax on buildings is not payable for the following: d) buildings that by their destination are cult premises belonging to religious cults recognized by law and parts of their local components, with the exception of enclosures that are used for economic activities.	(1) The tax on buildings is not payable for the following: d) buildings that by their destination are cult premises belonging to religious cults recognized by law and parts of their local components, with the exception of enclosures that are used for economic activities, **halidom; under the denomination of buildings**

			which by destination, constitute houses of worship meaning churches, places of praying, prayer houses and their annexes; Church's annexes refers to any place that has the constitutive elements of a building, ownership of a legally recognized religion or religious association, such as: belfry, the parochial chancellery, holy water basin, mortuary chapel, the place where to lit and sale candles, trinity, warehouse to store cult objects, places for social-charitable events, xenodochium, hermitage, dining hall, places for ecclesiastical-administrative activities, Hierarch resident and others like it; by institution of social-charitable is understood a social service organized in accordance with the classification of social services, approved by Government Decision no. 867/2015.
CHAPTER II - Tax on buildings	ART. 456 - Exemptions	After letter d), paragraph (2), there is no letter d^1).	After the letter d), para. (2) is introduced a new paragraph d^1). Local councils may decide to grant exemption or reduction of the building tax owed for the following buildings: d) buildings used exclusively by non-profit companies for activities without economic purpose; **d^1) buildings that are public or private property of the administrative territorial units assigned to develop sports activities, leased, rented, or given into administration or in use, as appropriate.**
CHAPTER II - Tax	ART. 456 -	(3) The exemption or reduction of tax established	(3) The exemption or reduction of tax established

on buildings	Exemptions	under paragraph (2) shall apply from January 1st of the following year in which the person submitted the supporting documents.	under paragraph (2) shall apply from **the first day of the month following the one in which the person submitted the supporting documents. The competent fiscal authority shall recalculate the tax due to/due proportion to the period from the beginning of the fiscal year, regulates the amount paid with the taxpayer's agreement compensated by other taxes due, and the remaining amount, if any, shall be refunded.**
CHAPTER II - Tax on buildings	ART. 458 – Computation of tax on non-residential buildings owned by individuals	1) For non-residential buildings owned by of individuals, the building tax is computed by applying a rate between 0.2 to 1.3% on the value that can be: a) the amount arising from an evaluation report compiled by an authorized evaluator during the last 5 years preceding the reference year submitted to the local tax authorities until the first payment in the reference year; b) the final value of construction works, for new buildings, built in the last 5 years prior to reference year; c) value of the buildings resulting from the act that transfer ownership right, for buildings acquired in the last 5 years preceding the reference year. (3) For non-residential buildings owned by individuals, used for work in agriculture, property tax is calculated by applying a rate of 0.4% on the taxable value of the building.	1) For non-residential buildings owned by of individuals, the building tax is computed by applying a rate between 0.2 to 1.3% on the value that can be: a) the amount arising from an evaluation report compiled by an authorized evaluator; b) the final value of construction works, for new buildings; c) value of the buildings resulting from the act that transfer ownership right, for acquired buildings. (3) For non-residential buildings owned by individuals **exclusively** used for agriculture activities, tax on building is calculated **according to art. 457.**
CHAPTER II -Tax on building	ART. 458 – Computation of	After paragraph 1 of Article 458, there aren't (1^1) and (1^2)	**(1^1) The value of non-residential buildings is annually updated by the local authority.**

	tax on non-residential buildings owned by individuals		**(1[2]) The calculated value may be challenged in an administrative contentious based on an independent authorized assessment.**
CHAPTER II -Tax on building	ART. 459 – Computation of tax on property for mixed-purpose owned by individuals	2) If the building is recorded at fiscal residence to which any economic activity is not conducted, the tax is calculated according to art. 457.	2) If the building is recorded at fiscal residence to which any economic activity is not conducted, **except liberal professions**, the tax is calculated according to art. 457.
CHAPTER III Tax on land	ART. 464 - Exemptions	At paragraph (2), after letter f), there isn't letter f[1])	(2) Local councils may decide to grant tax exemption or reduction land tax due for: **f[1]) lands for buildings publicly or privately owned by the administrative - territorial units with the purpose of developing sports activities, leased, rented, let it be in administration or in use, where it's appropriate.**
CHAPTER III Tax on land	ART. 464 - Exemptions	(3) The exemption or reduction of tax established under paragraph (2) shall apply from the first day of the year following the one in which the person submitted the supporting documents.	(3) The exemption or reduction of tax established under paragraph (2) shall apply from the first day **of the month following the one in which the person submitted the supporting documents The competent fiscal authority shall recalculate the tax due to/due proportion to the period from the beginning of the fiscal year, regulates the amount paid with the taxpayer's agreement compensated by other fees/taxes due, and the remaining amount, if any, shall be refunded.**

<table>
<tr>
<td>CAPITOLUL III – Tax on land</td>
<td>ART. 465 - Computation of tax on land</td>
<td>(2) For a plot of land located in an urban area, recorded in the agricultural registry in the “building land” category and for a plot of land recorded in the agricultural registry in any category other than “building land” with construction with a total area of less than or equal to 400 sqm, the tax on land is established by multiplying the surface of the terrain expressed in ha with the corresponding sum provided in the following table:
<table>
<tr><th rowspan="2">Area in the localities</th><th colspan="6">Levels of tax, according to localities ranks (Ron / ha)</th></tr>
<tr><th>0</th><th>I</th><th>II</th><th>III</th><th>IV</th><th>V</th></tr>
<tr><td>A</td><td>8282-20706</td><td>6878-17194</td><td>6042-15106</td><td>5236-13090</td><td>711-1788</td><td>569-1422</td></tr>
<tr><td>B</td><td>6878-17194</td><td>5199-12998</td><td>4215-10538</td><td>3558-8894</td><td>569-1422</td><td>427-1068</td></tr>
<tr><td>C</td><td>5199-12998</td><td>3558-8894</td><td>2668-6670</td><td>1690-4226</td><td>427-1068</td><td>284-710</td></tr>
<tr><td>D</td><td>3558-8894</td><td>1690-4226</td><td>1410-3526</td><td>984-2439</td><td>278-696</td><td>142-356</td></tr>
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<td>(2) For a plot of land located in an urban area, recorded in the agricultural registry in the “building land” category the land tax is established by multiplying the surface of the terrain expressed in ha with the corresponding sum provided in the following table:
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<td>ART. 465 - Computation of tax on land</td>
<td>(2^1) If a taxpayer who owns more land areas located in the urban area of the same unit / territorial-administrative subdivision, the surface of 400 m² referred in the para. (2) is calculated only once, by summing up land areas, in descending order.</td>
<td>Para (2^1) is repealed.</td>
</tr>
<tr>
<td>CAPITOLUL III – Tax on land</td>
<td>ART. 465 - Computation of tax on land</td>
<td>(3 In the case of land located in urban area, recorded in the Agricultural Register to another category of use than that of land with buildings, for the area exceeding 400 m², the land tax / land fee is determined by multiplying the and area, expressed in hectares by the corresponding amount as referred by the para. (4), and this result is multiplied by the corresponding correction coefficient as referred to in para. (5).</td>
<td>(3) In the case of land located in urban area, recorded in the Agricultural Register to another category of use than that of land with buildings, the land tax / land fee is determined by multiplying the and area, expressed in hectares by the corresponding amount as referred by the para. (4), and this result is multiplied by the corresponding correction coefficient as referred to in para. (5).</td>
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ANNEX 2

General assumptions:
1. The starting point for estimating the revenue loss involved by the legislative proposal is represented by the household expenditure with the considered services for applying a reduced VAT rate of 9%, extracted from the NIS publication "Coordinates of living standard in Romania. Population income and consumption in 2014 ".
2. The input data refer to the money spent on electrical and thermal energy, natural gas, water, sewerage, sanitation and communal services (Table 75 of the above mentioned publication), from which the household expenditure for water supply (already in the scope of the reduced VAT rate of 9%) were deducted. They were calculated using the data provided by NIS "The amount of drinking water supplied to consumers on macro-regions development areas and counties in the year 2014", on which we applied an average tariff for the distribution of cold water at the national level (data provided by the agency Apa Nova) and the number of people in the year 2014, according NIS data.
3. The resulting data are expressed in monthly expenditure per person and include VAT. These data were converted to the total expenses net of VAT, considering the VAT rate of 24% and the number of people in the year 2014.
4. We assumed that the measure will enter into force starting January, 1, 2017. To determine the budgetary impact for the period 2017-2019, the estimated revenue loss for the year 2014 was extrapolated with the growth of the household final consumption expenditures related to payment for services recorded or projected by NCEF for the period 2015-2019, and considering that in 2017 the standard VAT rate will be 19%.

	No.	2014
Expenses for the electrical energy (lei/person /month)	1	32.2
Expenses for the thermal energy (lei/person /month)	2	5.5
Expenses for the natural gas (lei/person /month)	3	17.6
Expenses for water, sewerage, sanitation and communal services (lei/person /month)	4	20.1
Expenses for water (lei/person /month)	5	13.3
Expenses for the considered services for applying a reduced VAT rate of 9% (lei/person /month)	6=1+2+3+4-5	62.2
Expenses for the considered services for applying a reduced VAT rate of 9% net of VAT (lei/person /month)	7=6/1.24	50.2
Population (million inhabitants)	8	19.9
Total annual expenses for the considered services for applying a reduced VAT rate of 9% net of VAT (million lei)	9=7*8*12	12013.2
Annual revenue loss due to the application of a reduced VAT rate of 9% (million lei)	10=9*0.10	1201.3

The impact of applying a reduced VAT rate of 9% for electrical and thermal energy, natural gas, sewerage, sanitation and communal services						
	2014	2015	2016	2017	2018	2019
Annual revenue loss due to the application of VAT rate of 9% (million lei)	1,201.3	1,291.2	1,376.0	1,480.9	1,590.7	1,700.5

The growth of household final consumption for services	
2015/2014	7.48%
2016/2015	6.57%
2017/2016	7.62%
2018/2017	7.42%
2019/2018	6.90%

III. Fiscal Council's Opinion on the Draft Budget Revision for 2016 and the Half-Year Report regarding the Economic and Budgetary Situation

On July 29th 2016, the Fiscal Council received from the Ministry of Finance by letter no. 9665/28.07.2016, the draft of the budget revision for 2016, the explanatory note and the draft Government Ordinance project regarding the draft of the budget revision for 2016, as well as the explanatory note and the Government Ordinance project regarding the draft of the revised social security budget for 2016, requesting the Fiscal Council's opinion under article 53, paragraph (2) of the Law no. 69/2010 republished. In addition, the Fiscal Council also received the Half-Year Report regarding the Economic and Budgetary Situation of which conclusions, alongside the Fiscal Council's opinion on it, should be taken into account in the construction of the budget revision proposal in accordance with article 23, paragraph (1) of the Fiscal Responsibility Law (FRL) republished.

1. Compliance with the fiscal rules

Compared to the initial approved budget, the draft budget revision maintains the nominal budget balance of -20,905.4 million lei, thus respecting the budget deficit ceiling defined by the Law no. 338/2015 (the law for approving ceilings for certain indicators specified in the budgetary framework) and ensuring the observance of the fiscal rule established by article 12 letter b) of FRL. Since the projection of interest expenses is revised upward by 319.1 million lei, the general consolidate budget (GCB) primary deficit is programmed to fall by the same amount (from 9836.5 million to 9517.3 million lei), which is below the ceiling set by Law no. 338/2015.

If the budget deficit remains unchanged compared to the initial level, both revenues and expenditures are scheduled to significantly increase, implying deviations from the rules established by FRL as follows:

- The programmed level in the budget revision for the personnel expenditures (58,703 million lei, respectively 7.8% of GDP) exceeds the corresponding ceiling defined by the Law no. 338/2015 both in terms of nominal level (by 1,368.1 million lei), as well as percentage of GDP (by 0.1 pp, despite an upward revision of the nominal GDP by 10.431 million lei compared to the estimation used in the initial budgetary construction). The absence of compliance with the fiscal rules occurs at the level of art. 12 letter a) (for the level expressed as percentage of GDP) and letter c) (for nominal level) of FRL and in terms of the rule established by art. 17 paragraph 2, which prohibits increasing the personnel expenses during the budgetary revisions.

- The programmed level of the GCB expenditures, excluding the financial assistance from the EU and other donors (242,220.1 million lei), exceeds the corresponding ceiling defined by the Law no. 338/2015 by 3,344.6 million lei, the absence of the conformity occurring at the level of the rule established by art. 12 letter c) of the FRL, as well as at the rule established by art. 24 which prohibits the increase of the GCB expenditures, net of financial assistance from the EU and other donors during the budget revisions, unless it is due to the supplementing of the interest expenses or those related to Romania's contribution to the EU budget. Given that the total expenditure increase is also due to the supplementary allocation in interest expenses (by 319.1 million lei), the exceeding of the ceiling ruled by Law no. 338/2015 appears as partially justified from the perspective of the fiscal rules (within that amount).

The draft Government Ordinance regarding the budget revision for 2016 provides the corresponding derogations from the aforementioned fiscal rules and redefines the limits of the ceilings stipulated in the Law 338/2015 according to the levels proposed by the budget revision for the budgetary aggregates. In the opinion issued earlier on the first budget revision for 2015, the Fiscal Council ascertained, given the experience of systematic recourse to derogations from FRL, the *de facto* existence of two classes of fiscal rules, one of "strong" rules (those relating to budget balance) – which usually operates successfully, respectively one of "weak" rules (those concerning mandatory ceilings for all other elements relevant from the perspective of the law – primary balance, personnel expenditures, total expenditures excluding the financial assistance from the EU and other donors, strengthened by the interdiction of increasing total expenditure and personnel expenditures during budget revisions) for which the lack of *ex ante* compliance represents the rule rather than the exception, the derogation interfering in almost all budget revisions occurred after the entry into force of FRL in April 2010 (however, the below under program execution of the expenditures made sometimes the fiscal rules to be respected *ex post*). The Fiscal Council considers that the developments after the issuance of the aforementioned opinion (opinion issued during the first budget revision for 2015) only serve to validate that statement and maintain its recommendations made at that time, inviting the Government to reflect on them.

2. The updated coordinates of the budgetary revenues and expenditures

The draft budget revision massively supplements, in an equal amount, revenues and expenditures (+3,757 million lei, or 0.5% of GDP). At the level of budget revenues, the sources of the operated revisions are as follows:

- Tax revenues: +2,892.5 million lei, of which:

- Corporate income tax: +1,052.7 million lei. The proposed revision for the corporate income tax receipts appears to be justified by the over performance recorded at the end of the first quarter in relation with the initial half-year program - the achievement degree, according to the Half-Year Report on Economic and Budgetary Situation, was 107.5% (+534.5 million lei). The illustrated figure appears to be consistent with the performance at the end of the first quarter and the upward revision of the projected dynamic of the nominal GDP for 2016 (to 6.2%), given the high sensitivity of this revenue category to the relevant macroeconomic base.
- Personal income tax: +896 million lei. Updating the programmed level for the whole year appears to be justified in relation with the over performance compared to the initial program at the end of the first semester - the achievement degree, according to the Half-Year Report on Economic and Budgetary Situation, was 103.3% (+428.7 million lei in nominal terms), given that the actual wage dynamics appears to be higher compared to the estimates that underpinned the initial budgetary construction. Moreover, this phenomenon is reflected in the projections of the National Commission for Economic Forecasting (NCEF), that estimates a gross wage growth of 8.9% in the spring projection, compared to the prior projection of 7.2%.

In addition, the impact of reducing the tax on dividends (from 16% to 5%) on the budgetary revenues was strongly offset by the tripling (according to quarterly Report realized by the Ministry of Public Finance) of the dividends' distributions from the profit recorded in the previous years - however, it is assumed that the increase is a temporary phenomenon, which from the budgetary perspective is translated into a simple postponement of the unfavorable impact of tax rate's reduction on budgetary revenues in the coming years. Furthermore, encouraging the system for taxing dividends (to the detriment of capitalization and reinvestment of profits) can lead to de-capitalization of the companies, with the possible consequence of reduction of the potential for investment and of the profitability in the long term, as far as shareholders' behavior tends to be dominated by short-term considerations. This effect could be even more damaging as the corporate sector is already undercapitalized, the share of total equity in the total financing of companies in Romania being small compared to other European countries[6].

Moreover, the compensation payments made in accordance with the Law no. 85/2016 have a positive temporary correspondent on the revenue side, which in case of the personal income tax amounts to about 110 million. In conclusion, the Fiscal Council considers that the estimated receipts for this chapter of revenue are prudent, an even higher level being

[6] See Florian Neagu, Dragu Florin Adrian Costeiu, *"After 20 years: structural changes in the Romanian economy in the first post-revolutionary decades"*, Working Papers NBR no. 42/2016.

possible as far as the current trend of growth of earnings that seems to suggest higher increases than those from the updated projection of NCEF, is maintained.

- Other taxes on income, profit and capital gains: +470 million lei. Increasing the planned level for the full year appears justified by the exceeding in six months' execution of the planned level of about 38% of the related program (+220 million lei).
- VAT: +406,3 million lei. The revision takes into account the exceeding of the program for receipts at the level of the first six months (+406 million lei, corresponding to an achievement degree of 101.6%). The lack of its extrapolation is justified by the fact that the exceeding of the program appears to be localized at the level of the first month of the year, whose revenues continue to reflect, on the one hand, the level of the standard rate of 24%, and on the other hand, possibly related VAT execution of public investment from 2015, concentrated largely in the last month of the previous year. The reservations raised by the Fiscal Council on the receipts planned for this revenue category in the context of the opinion on the initial budgetary construction are invalidated, in roughly equal proportions of the higher than expected revenues in January, of a private consumption dynamic higher to the estimates (otherwise reflected in the upward revisions of dynamics designed by the NCEF for purchases of goods and services of the population), and by the upper level of VAT receipts for the year 2015 compared to the forecasts available when drawing up the draft budget for 2016 (and which were the starting point for the projection).
- Excise duties: +180 million lei. The proposed upward revision appears as prudent, given that the execution at 6 months exceeded the program with 256 million lei, corresponding to an achievement degree of 102%.
- Tax on foreign trade and international transactions (customs duty): +178.9 million lei. The proposed upward revision appears as prudent, given that the execution at 6 months exceeded the program with 106.8 million lei, corresponding to an achievement degree of 129.5%.
- Social security contributions: -982 million lei. The execution at the end of the first semester was significantly below program, the revenues being less by about 1,090 million lei (corresponding to an achievement degree of 96.4%). This evolution is worrying considering the fact that it appears localized at the level of pensions contributions (which justifies a broader downward revision of the Social Insurance Budget's annual revenue with 1,597 million lei) and disengaged from the dynamics of other revenue categories with the same tax base such as health insurance contributions, unemployment contributions and the personal income tax, considering also that the developments in wages appear more favorable than the assumptions used when drafting the

initial budget, these elements indicating the existence of a significant collection problem. Given that the minimum wage increase, the public sector wage increases from August and the compensation payments arising from the provisions of Law no. 85/2016 will generate flows of social contributions in the second half of the year, the Fiscal Council considers, however, that the updated target for social contributions receipts is achievable. The Fiscal Council recommends the investigation of the causes which led to a negative effect on revenue from pension contributions, these being lower than would have been justified by the discretionary measures adopted[7] and the adoption of necessary corrective actions, especially given that the deficit in the pension system has already reached an unsustainable level.

- Non-tax revenues: +1,484.2 million lei. Compared to the half-year program, the execution at the end of June 2016 reveals an underperformance, considering the achievement degree of 91% (-831.6 million lei). In the second part of the year are foreseen exceptional receipts of about 847 million lei corresponding to the reclassification of certain amounts arising from the previous year's budgetary execution. In the view of the Fiscal Council, it is difficult to reconcile the underperformance occurred at the level of the half-year execution with the upward revision of the program for the entire year, even taking into account the above mentioned temporary revenues; consequently, the Fiscal Council considers that there is a risk that the effective non-tax revenues at the end of the year to be below the updated program.
- Amounts received from the EU in the account of payments made and pre-financing (related to the financial year 2007-2013): +407.1 million lei. The half-year execution reveals an achievement degree of 76.1%, the revenues being lower by about 150 million lei. However, the amounts recorded in the execution relating to this chapter of revenue (477 million lei) appear as significantly higher than the initial program for the entire year 2016 (337 million lei), which makes the figure put forward in the draft budget revision to appear as feasible.

The sources of the upward revisions for the budgetary spending amounting to 3,756.8 million lei are the following:

- Personnel expenses: +1,367.9 million lei. The upward revision appears as a combined effect of the compensatory amounts arising from the Law no. 85/2016 (about 1 billion lei), the wage increases expected to occur in August 2016 (about 873 million lei) and the savings revealed by the budgetary execution at the end of the first

[7] The increase in 2016 of the contribution rate related to the private pension funds by 0.1 percentage points and removing the employers' requirement to pay state social insurance contribution for personnel of the army, police and civil servants with special status.

semester, considering that the payments represented 48.5% of the initial amount allocated for the full year.

- Goods and services: +388.8 million lei. This increase appears to be quite surprising given the substantial underperformance for this spending category at the end of the first semester, as the achievement degree is only 40% of the initial level for this year and the pace of growth of spending on goods and services at the end of June in nominal terms was 1.5%, given that the initial budgetary allocation involves a nominal rate of spending growth of 5.6% compared with the execution of 2015.
- Social assistance: +1,375.9 million lei. The proposed revision is due in a proportion of one third to the legislative measures subsequent to the 2016 budget approval (Law no. 66/2016 on the increase and changing the system of setting the monthly child allowance and incentive insert, + 305 million lei, namely Law no. 342/2015 - approved on December 22, 2015 – referring to the excluding the state allowance from the family income for determine the social aid, + 140 million lei) but also to the trends revealed by the first semester's execution, given that spending at the end of June indicated achieving more than half of the initial allocation for the whole year, predicting additional expenditure of about 900 million lei). The MPF provides only a partial explanation of the higher spending revealed by the half-year execution, respectively the upward revision of the estimated impact on the increase of the state allowance for children decided last year (+294 million lei).
- Interest spending: +319.1 million lei.
- Investment spending: +355 million lei. An increased allocation is recorded for the investment projects financed by external funds (+279 million lei), other transfers of the nature of investment (+150 million lei) and for the projects financed by reimbursable funds (+46 million lei), the capital expenditures registering a downward revision of 120 million lei.

In conclusion, in the opinion of the Fiscal Council, the significant upward revisions made at the level of the budgetary revenues appear to be substantiated given the actual execution, as result of an effective economic growth not necessarily superior to the initial estimates, but with a composition more favorable to the budgetary revenues (a higher dynamic for consumption – which is a reference for indirect taxes). The Fiscal Council validates in principle the government's revenue estimates, but considers that there is a risk of proceeds inferior to the program for non-tax revenue and the social contributions, but at the aggregate level the effect is probably offset by the conservative estimates for the revenue from excise duties, custom duties and taxes on income and wages.

In the meantime, the Fiscal Council is extremely skeptical that the proposed level for the revenues from the post-accession funds for the financial year 2014-2020 is achievable, given that at the end of the first semester the corresponding revenues (680.1 million lei) accounted for only 5,1% of the amount envisaged for the entire year (12.8 billion lei).

In the context of the execution for the first six months which revealed a weak absorption of the European funds and investment expenditure under the program, although to a lesser extent than in the previous year, the decision to increase their amount appears as surprising, especially given that past experience indicates it is unlikely that even with an acceleration of the European funds inflows in the second half of the year to be sufficient to attain the programmed levels. Moreover, the underachievement of the revenues from EU funds will not lead to an increase in the budget deficit, under the hypothesis of automatic adjustments of the corresponding spending.

The Fiscal Council also considers that the revised budget has the potential to generate a greater gap between the ESA 2010 deficit (on accrual basis, and relevant in terms of the European treaties) and the deficit according to the national methodology (on cash basis).

The non-tax revenues for 2016 according to the national methodology includes extraordinary revenues amounting to 847 million lei for sums resulting from the reclassification of the amounts from the previous years, while the methodology ESA 2010 will require most likely reviewing the executions from the previous years rather than include the respective amounts in the current year's revenues. Moreover, it is expected that according to the ESA 2010 methodology, as happened in the past, the entire impact of the Law no. 85/2016 that generates compensatory payments for teachers staggered over five years to be fully recorded in the current year - an indicative estimate suggests an amount of about 3 billion lei compared to only 1 billion lei according to the cash execution.

Together, these two items sum up for 2.85 billion lei (0.37% of GDP), which would add to the already estimated gap of about 0.2% of GDP between ESA 2010 and cash deficits (whose source largely consist in that, for the year 2016, the measures included in the Fiscal Code affects only 11 months or three quarters in terms of the cash execution for some budgetary aggregates, while ESA 2010 execution will imply a full annual impact).

Under these circumstances, it is possible that a deficit of 2.76% of GDP in cash standards cannot provide a sufficient margin against breaching the 3% level of GDP in ESA 2010 standards which, in conjunction with the current assessments of the European Commission that indicates a budget deficit above 3% in 2017, could lead to the entry in the excessive deficit procedure in the next year.

On the other hand, having more expenditure aggregates, especially investment spending, significantly below the program according to the first half year execution suggests a probable under-execution of them, which could lead to a budget deficit according to national methodology lower than the current target, and though capable of ensuring the avoidance of exceeding the threshold of 3% of GDP for the budget deficit according to ESA 2010, even taking into account the above mentioned items. In conclusion, the Fiscal Council considers that attaining the fiscal deficit target for the current year in the context of maintaining the actual parameters of fiscal policy is possible, and the balance of risks appears to be in equilibrium.

However, the Fiscal Council reiterates the assessment expressed when approving the budget for 2016, namely that budget deficits close to 3% of GDP in 2016 and over 3% of GDP estimated for 2017 (in a scenario of no policy change), under the circumstances of an economic growth higher than the potential, are contraindicated, as fiscal policy will be pro-cyclical, pressing the accelerator in the expansion phase of the economic cycle, while risking to be forced to implement structural adjustment measures in a future phase of recession.

The above opinions and recommendations of the Fiscal Council were approved by the Chairman of the Fiscal Council, according to article 56, paragraph (2), letter d) of Law no. 69/2010, republished, after being approved by the Council members through vote, on 9th of August, 2016.

9th of August 2016 — Chairman of the Fiscal Council,

IONUȚ DUMITRU

ANNEX 1: Fiscal policy measures – Expenditure	Budgetary impact - 2016	- thousand lei Expenditure item
Fiscal policy measures:	**2,796,190.0**	
The increase in the allowance granted to the severely visual disabled adult by increasing with 25% the net wage for the debutant social assistant with average studies from the social assistance units in the public sector, other than those with beds, and the increase in the no. of persons classified within various types of disabilities (Order 707/538/2014), Law no. 293/2015	150,000	Social assistance
The increase in the personnel wages for the public authorities remunerated similar to the parliamentary services, Law no. 293/2015	19,149	Personnel expenditure
The increase in the child benefits (reviewed impact), Law no. 125/2015	293,626	Social assistance
The increase in the no. of social aid beneficiaries by excluding the state allowance from household income when determining the social aid, Law no. 342/22 December 2015	140,020	Social assistance
The increase and the change in the manner of establishing the monthly child care allowance and the incentive insertion, Law no. 66/2016 (effective from July 1, 2016)	304,695	Social assistance
The teaching personnel which did not obtain court decisions for the payment of wage differences for the period October 2008 - May 13, 2011 benefit of these rights since 2016, Law no. 85/2016	1,015,700	Personnel expenditure
The increase in wages for the medical personnel and the teaching personnel, GEO no. 20/2016 (according to the GEO's explanatory note)	873,000	Personnel expenditure

Source: Ministry of Public Finance

ANNEX II – budget execution semester I 2016 vs. the half-year program	The half-year program 2016 with *swap* (mil. lei)	Budget execution semester I 2016 with *swap* (mil. lei)	Program swap semester I 2016	The half-year program 2016 without *swap* (mil. lei)	Budget execution semester I 2016 without *swap* (mil. lei)	Sem. 1 2016/ Sem. 1 2015 without *swap*	Differences from the half-year program 2016 without *swap* (mil. lei)	The achievement degree of the half-year program without *swap* (%)	Differences from the half-year program 2016 with *swap* (mil. lei)	The achievement degree of the half-year program with *swap* (%)
	1	2	3	4=1-3	5	6	7=5-4	8=5/4	9=2-1	10=2/1
TOTAL REVENUE	**113,097.5**	**108,390.5**	**1,070**	**112,027.5**	**108,082.4**	**-2.1%**	**-3,945.1**	**96.5%**	**-4,707.1**	**95.8%**
Current revenue	107,221.0	106,647.6	1,070	106,151.0	106,339.6	0.7%	188.6	100.2%	-573.4	99.5%
Tax revenue	67,395.3	68,743.8	1,070	66,325.3	68,435.7	-0.6%	2,110.5	103.2%	1,348.5	102.0%
Taxes on profit, wages, income and capital gains	20,650.3	21,833.1		20,650.3	21,775.2	5.7%	1,124.9	105.4%	1,182.8	105.7%
Corporate income tax	7,160.9	7,695.4		7,160.9	7,661.3	12.0%	500.4	107.0%	534.5	107.5%
Personal income tax	12,910.7	13,339.4		12,910.7	13,315.6	2.5%	404.9	103.1%	428.7	103.3%
Other taxes on income, profit and capital gains	578.7	798.3		578.7	798.3	9.6%	219.6	138.0%	219.6	138.0%
Property tax	3,806.0	3,776.8		3,806.0	3,776.8	6.3%	-29.2	99.2%	-29.2	99.2%
Taxes on goods and services	42,357.0	42,203.7	1,070	41,287.0	42,108.6	-4.9%	821.6	102.0%	-153.3	99.6%
VAT	26,007.6	26,414.1	1,070	24,937.6	26,319.0	-9.6%	1,381.4	105.5%	406.5	101.6%
Excises	12,671.9	12,928.4		12,671.9	12,928.4	7.7%	256.5	102.0%	256.5	102.0%
Other taxes on goods and services	1,994.6	1,039.1		1,994.6	1,039.1	-34.7%	-955.4	52.1%	-955.4	52.1%
Taxes on using goods, authorizing the use of goods or on carrying activities	1,682.9	1,822.1		1,682.9	1,822.1	15.5%	139.1	108.3%	139.1	108.3%
Tax on foreign trade and international transactions	362.5	469.3		362.5	469.3	32.8%	106.8	129.5%	106.8	129.5%
Other tax revenue	219.5	460.9		219.5	452.7	89.8%	233.3	206.3%	241.4	210.0%
Social security contributions	30,554.9	29,464.7		30,554.9	29,317.8	6.3%	-1,237.1	96.0%	-1,090.3	96.4%
Nontax revenue	9,270.7	8,439.2		9,270.7	8,439.2	-6.6%	-831.6	91.0%	-831.6	91.0%
Capital revenues	449.5	347.0		449.5	347.0	-22.6%	-102.5	77.2%	-102.5	77.2%
Grants	10.4	0.0		10.4	0.0	-100.0%	-10.4	0.0%	-10.4	0.0%
Amounts received from the EU in the account of payments made and prefinancing	627.1	477.1		627.1	477.1	-88.1%	-150.0	76.1%	-150.0	76.1%

ANNEX II – budget execution semester I 2016 vs. the half-year program	The half-year program 2016 with *swap* (mil. lei)	Budget execution semester I 2016 with *swap* (mil. lei)	Program swap semester I 2016	The half-year program 2016 without *swap* (mil. lei)	Budget execution semester I 2016 without *swap* (mil. lei)	Sem. 1 2016/ Sem. 1 2015 without *swap*	Differences from the half-year program 2016 without *swap* (mil. lei)	The achievement degree of the half-year program without *swap* (%)	Differences from the half-year program 2016 with *swap* (mil. lei)	The achievement degree of the half-year program with *swap* (%)
	1	2	3	4=1-3	5	6	7=5-4	8=5/4	9=2-1	10=2/1
Amounts collected in the single account	0.0	162.0		0.0	162.0	-265.4%	162.0		162.0	
Other amounts received from the EU for operational Programmes funded under the convergence objective	0.0	76.7		0.0	76.7	1752.3%	76.7		76.7	
Amounts received from the EU/other donors in the account of payments made and pre-financing for financial framework 2014-2020	4,789.6	680.1		4,789.6	680.1	67.6%	-4,109.5	14.2%	-4,109.5	14.2%
TOTAL EXPENDITURE	**129,901.4**	**112,245.3**	**1,070.0**	**128,831.4**	**111,937.3**	**5.4%**	**-16,894.1**	**86.9%**	**-17,656.1**	**86.4%**
Current expenditure	121,586.7	107,211.8	1,070	120,516.7	106,903.7	3.8%	-13,613.0	88.7%	-14,375.0	88.2%
Personnel	29,596.9	27,815.9		29,596.9	27,815.9	10.7%	-1,780.9	94.0%	-1,780.9	94.0%
Goods and services	21,076.8	17,390.6		21,076.8	17,390.6	1.5%	-3,686.1	82.5%	-3,686.1	82.5%
Interest	7,005.5	6,318.1		7,005.5	6,318.1	9.5%	-687.4	90.2%	-687.4	90.2%
Subsidies	3,827.3	2,671.0		3,827.3	2,671.0	-16.6%	-1,156.3	69.8%	-1,156.3	69.8%
Total Transfers	59,809.8	52,879.4	1,070	58,739.8	52,571.4	1.8%	-6,168.4	89.5%	-6,930.4	88.4%
Transfers for public entities	727.6	473.8	1,070	-342.4	165.8	-14.2%	508.2	-48.4%	-253.8	65.1%
Other transfers	6,165.3	4,724.4		6,165.3	4,724.4	-22.0%	-1,440.8	76.6%	-1,440.8	76.6%
Projects funded by external post-accession grants	6,500.2	4,806.0		6,500.2	4,806.0	-17.0%	-1,694.2	73.9%	-1,694.2	73.9%
Social assistance	40,276.1	40,155.6		40,276.1	40,155.6	8.0%	-120.5	99.7%	-120.5	99.7%
Projects funded by external post-accession grants 2014-2020	4,305.4	949.3		4,305.4	949.3	97.6%	-3,356.2	22.0%	-3,356.2	22.0%
Other expenditure	1,835.2	1,770.2		1,835.2	1,770.2	-8.7%	-64.9	96.5%	-64.9	96.5%
Reserve funds	0.0	0.0		0.0	0.0		0.0	0.0%	0.0	
Expenditure funded from reimbursable funds	270.4	136.7		270.4	136.7	-16.6%	-133.8	50.5%	-133.8	50.5%
Capital expenditure	8,314.7	5,033.5		8,314.7	5,033.5	31.4%	-3,281.1	60.5%	-3,281.1	60.5%

ANNEX II – budget execution semester I 2016 vs. the half-year program	The half-year program 2016 with *swap* (mil. lei)	Budget execution semester I 2016 with *swap* (mil. lei)	Program swap semester I 2016	The half-year program 2016 without *swap* (mil. lei)	Budget execution semester I 2016 without *swap* (mil. lei)	Sem. 1 2016/ Sem. 1 2015 without *swap*	Differences from the half-year program 2016 without *swap* (mil. lei)	The achievement degree of the half-year program without *swap* (%)	Differences from the half-year program 2016 with *swap* (mil. lei)	The achievement degree of the half-year program with *swap* (%)
	1	2	3	4=1-3	5	6	7=5-4	8=5/4	9=2-1	10=2/1
Payments made in previous years and recovered in the current year	0.0	0.0		0.0	0.0	-100.0%	0.0		0.0	
EXCEDENT(+) / DEFICIT(-)	**-16,803.9**	**-3,854.9**		**-16,803.9**	**-3,854.9**	**-191.9%**	**12,949.0**	**22.9%**	**12,949.0**	**22.9%**

Source: Ministry of Public Finance, Fiscal Council's calculations

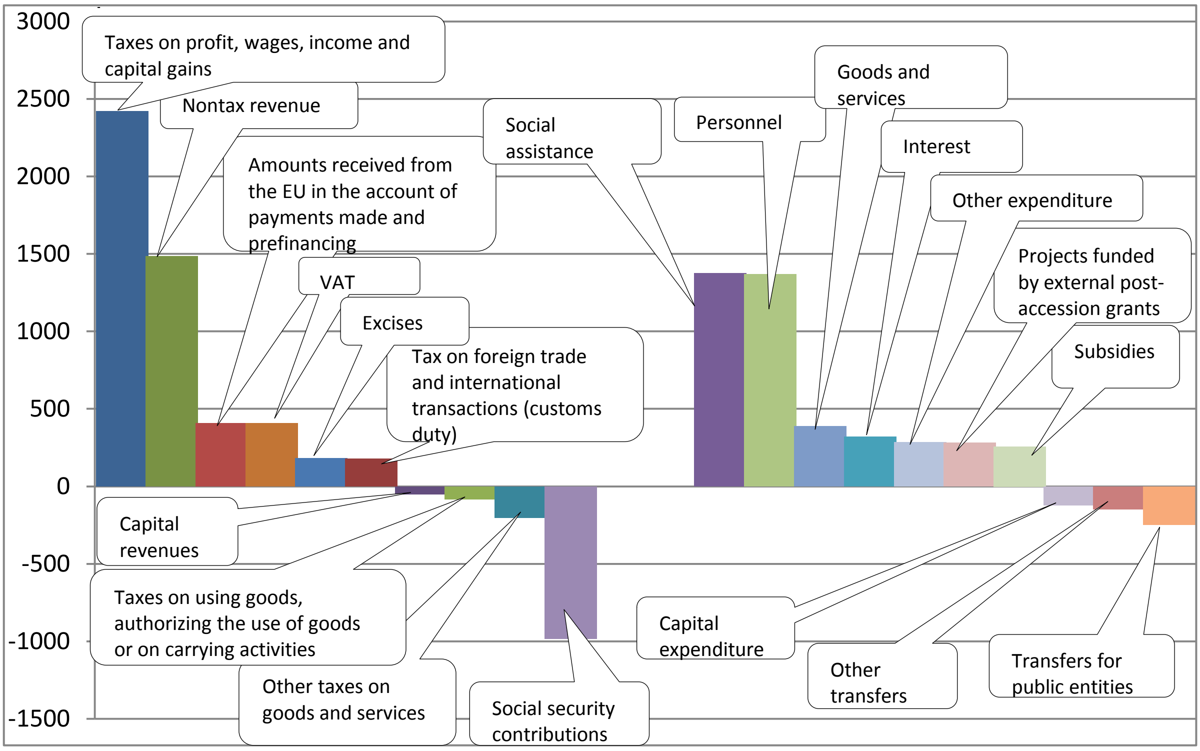
ANNEX III	Initial budget 2016	*Swap* program 2016	Initial budget 2016 without *swap*	First budget revision (R1) 2016	Additional *swap*	First budget revision 2016 without *swap*	R1 - Initial budget 2016 with *swap*	R1 - Initial budget 2015 without *swap*	Budget execution semester I 2016/ Budget execution semester I 2015 with *swap*	R1 2016/ Budget execution 2015 without *swap*
	1	2	3=1-2	4	5	6=4-5	7=4-1	8=6-3	9	10
TOTAL REVENUE	**231,125.5**	**1,070.0**	**230,055.5**	**234,882.4**	**1,070.0**	**233,812.4**	**3,757.0**	**3,757.0**	**-2.01%**	**100.58%**
Current revenue	217,018.2	1,070.0	215,948.2	220,412.9	1,070.0	219,342.9	3,394.7	3,394.7	0.75%	102.35%
Tax revenue	136,123.0	1,070.0	135,053.0	139,015.5	1,070.0	137,945.5	2,892.5	2,892.5	-0.53%	100.14%
Taxes on profit, wages, income and capital gains	41,759.6		41,759.6	44,179.3		44,179.3	2,419.6	2,419.6	5.94%	105.25%
Corporate income tax	14,384.9		14,384.9	15,437.5		15,437.5	1,052.7	1,052.7	12.48%	111.90%
Personal income tax	26,206.9		26,206.9	27,103.8		27,103.8	896.9	896.9	2.30%	102.07%
Other taxes on income, profit and capital gains	1,167.8		1,167.8	1,637.9		1,637.9	470.0	470.0	9.63%	100.70%
Property tax	5,980.1		5,980.1	5,982.7		5,982.7	2.6	2.6	6.26%	104.26%
Taxes on goods and services	87,137.6	1,070.0	86,067.6	87,438.2	1,070.0	86,368.2	300.5	300.5	-4.85%	96.99%
VAT	52,342.3	1,070.0	51,272.3	52,748.6	1,070.0	51,678.6	406.3	406.3	-9.48%	90.70%

ANNEX III	Initial budget 2016	*Swap* program 2016	Initial budget 2016 without *swap*	First budget revision (R1) 2016	Additional *swap*	First budget revision 2016 without *swap*	R1 - Initial budget 2016 with *swap*	R1 - Initial budget 2015 without *swap*	Budget execution semester I 2016/ Budget execution semester I 2015 with *swap*	R1 2016/ Budget execution 2015 without *swap*
	1	2	3=1-2	4	5	6=4-5	7=4-1	8=6-3	9	10
Excises	27,382.3		27,382.3	27,562.3		27,562.3	180.0	180.0	7.71%	105.94%
Other taxes on goods and services	3,958.6		3,958.6	3,757.1		3,757.1	-201.5	-201.5	-34.70%	139.06%
Taxes on using goods, authorizing the use of goods or on carrying activities	3,454.5		3,454.5	3,370.2		3,370.2	-84.3	-84.3	15.47%	100.42%
Tax on foreign trade and international transactions (customs duty)	836.7		836.7	1,015.6		1,015.6	178.9	178.9	32.76%	124.46%
Other tax revenue	409.0		409.0	399.9		399.9	-9.1	-9.1	93.17%	90.99%
Social security contributions	61,748.8		61,748.8	60,766.8		60,766.8	-982.0	-982.0	6.34%	105.98%
Nontax revenue	19,146.4		19,146.4	20,630.6		20,630.6	1,484.2	1,484.2	-6.56%	108.85%
Capital revenues	951.7		951.7	901.8		901.8	-50.0	-50.0	-22.62%	98.21%
Grants	20.6		20.6	22.5		22.5	1.9	1.9	-100.00%	359.24%
Amounts received from the EU in the account of payments made and prefinancing	13,135.0		13,135.0	13,545.3		13,545.3	410.3	410.3	26.27%	77.86%
TOTAL EXPENDITURE	**252,031.0**	**1,070.0**	**250,961.0**	**255,787.8**	**1,070.0**	**254,717.8**	**3,756.8**	**3,756.8**	**5.48%**	**104.90%**
Current expenditure	232,848.4	1,070.0	231,778.4	236,725.5	1,070.0	235,655.5	3,877.1	3,877.1	3.81%	104.21%
Personnel	57,335.0		57,335.0	58,703.0		58,703.0	1,367.9	1,367.9	10.72%	112.83%
Goods and services	43,111.4		43,111.4	43,500.2		43,500.2	388.8	388.8	1.54%	106.60%
Interest	11,069.0		11,069.0	11,388.1		11,388.1	319.1	319.1	9.53%	118.98%
Subsidies	6,464.3		6,464.3	6,721.3		6,721.3	257.0	257.0	-16.59%	107.12%
Total Transfers	114,235.8	1,070.0	113,165.8	115,631.8	1,070.0	114,561.8	1,396.0	1,396.0	1.90%	97.92%
Transfers for public entities	1,966.8	1,070.0	896.8	1,720.8	1,070.0	650.8	-246.0	-246.0	5.10%	53.05%
Other transfers	12,311.1		12,311.1	12,163.2		12,163.2	-147.9	-147.9	-22.01%	107.90%
Projects funded by external	4,600.7		4,600.7	6,864.9		6,864.9	2,264.2	2,264.2	-16.98%	28.52%

ANNEX III	Initial budget 2016	*Swap* program 2016	Initial budget 2016 without *swap*	First budget revision (R1) 2016	Additional *swap*	First budget revision 2016 without *swap*	R1 - Initial budget 2016 with *swap*	R1 - Initial budget 2015 without *swap*	Budget execution semester I 2016/ Budget execution semester I 2015 with *swap*	R1 2016/ Budget execution 2015 without *swap*
	1	2	3=1-2	4	5	6=4-5	7=4-1	8=6-3	9	10
post-accession grants										
Social assistance	79,373.4		79,373.4	80,749.4		80,749.4	1,375.9	1,375.9	8.01%	106.33%
Projects funded by external post-accession grants 2014-2020	12,449.2		12,449.2	10,464.0		10,464.0	-1,985.2	-1,985.2	97.57%	2110.76%
Other expenditure	3,534.5		3,534.5	3,669.5		3,669.5	135.0	135.0	-8.72%	92.01%
Reserve funds	100.0		100.0	202.5		202.5	102.5	102.5		
Expenditure funded from reimbursable funds	532.8		532.8	578.5		578.5	45.8	45.8	-16.61%	126.91%
Capital expenditure	19,182.6		19,182.6	19,062.4		19,062.4	-120.3	-120.3	31.40%	107.57%
Payments made in previous years and recovered in the current year	**-20,905.5**		**-20,905.5**	**-20,905.5**		**-20,905.5**	**0.0**	**0.0**	**-191.86%**	**201.88%**
EXCEDENT(+) / DEFICIT(-)	**231,125.5**	**1,070.0**	**230,055.5**	**234,882.4**	**1,070.0**	**233,812.4**	**3,757.0**	**3,757.0**	**-2.01%**	**100.58%**

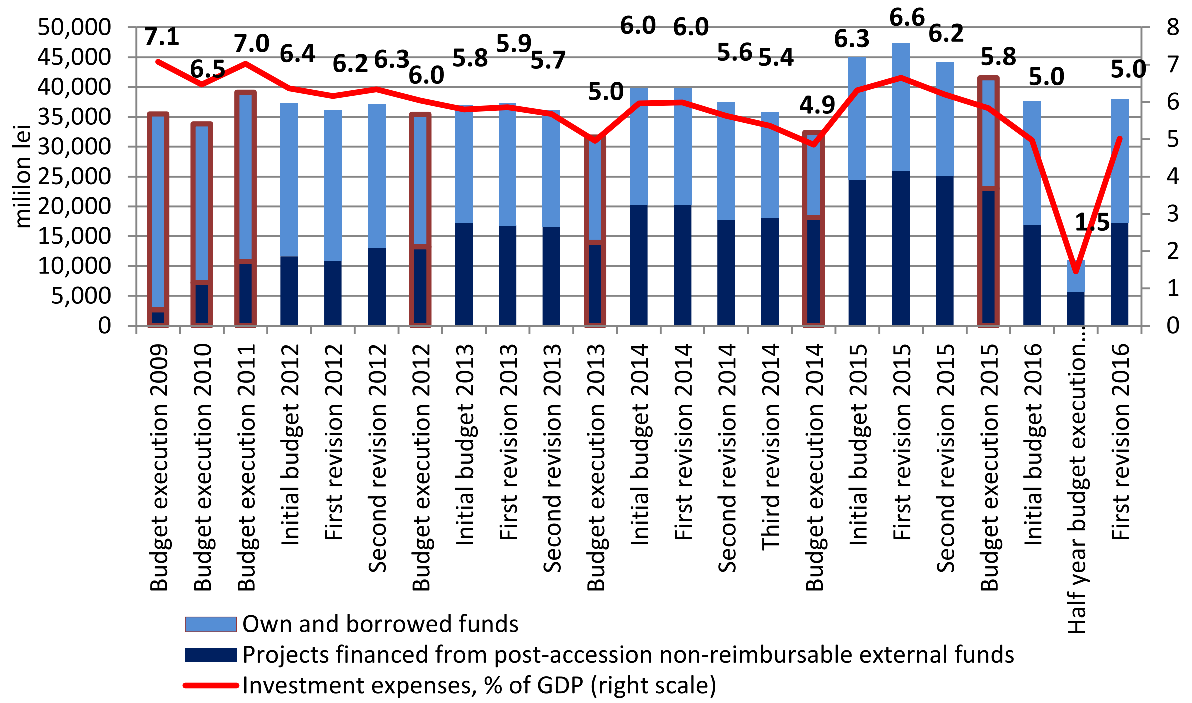
Source: Ministry of Public Finance, Fiscal Council's calculations

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



Source: Ministry of Public Finance, Fiscal Council's calculations

Figure 2: Evolution of the investment expenditure in the period 2009-2016 - planned vs. execution, million lei



Source: Ministry of Public Finance

IV. Fiscal Council's opinion on the amendments introduced by the Report adopted by the Parliament on the Law approving the Government Emergency Ordinance no. 20/2016 for amending and supplementing GEO no. 57/2015 regarding the remuneration of staff paid from public funds in 2016

On the 9th of November 2016, the Ministry of Public Finance (MPF) remitted to the Fiscal Council (FC) the letter no. 11899/8.11.2016, requesting the Fiscal Council's opinion on the amendments introduced in the Parliament following the adoption by the Chamber of Deputies of the Report on the Law approving Government Emergency Ordinance no. 20/2016 regarding the remuneration of personnel paid from public funds.

The introduced amendments aim at granting increased wages for the personnel in health and education sectors, as follows:

a) The increase of base salaries starting with 1st January, 2017 for teaching personnel, on average by 15%;
b) Increase of the base salary with effect from 1st December, 2016 for healthcare personnel (including administrative staff), on average by 15%;
c) The calculation of bonuses as a percentage of the increased salaries for the health and social assistance personnel;
d) Increase of the base salary with effect from 1st December, 2016 for social assistance personnel;
e) The increase of base salaries starting with 1st December, 2016, for the personnel within the National Health Insurance House;
f) Establishing the wages for the staff of the Counties' Health Insurance Houses and the Counties' Departments of Public Health at 85% of the increased wages for the National Health Insurance House's personnel;
g) Setting salaries for the staff of the Romanian Agency for Rescuing Human Life at Sea similar to the salary rights for the General Inspectorate for Emergency Situations' personnel.

The fiscal statement associated to the adopted amendments (see Annex 2) estimates, *ceteris paribus*, an increase of 4.85 billion lei for the personnel spending in 2017, respectively a first-round net impact on the budget deficit amounting to 2.9 billion lei, after considering the additional budgetary revenues generated by the wage increases on social contributions and personal income tax.

Introduction – a brief overview of the fiscal rules stipulated by Law no. 69/2010

The central element of the Fiscal Responsibility Law no. 69/2010, republished (hereinafter FRL) is the homonym principle which states that "*the Government has an obligation to conduct the fiscal policy prudently and manage the resources and budgetary obligations and fiscal risks in a manner that ensure the sustainability of the fiscal position in the medium and long term*", while stating that the "*sustainability of public finances means that, in the medium and long term, the Government should be able to manage financial risks or unforeseen events without having to introduce significant adjustments to expenditure, revenue or deficit with economic or social destabilizing effects*."

The actual implementation of this principle into the national legislation is achieved through a series of fiscal rules targeted to:

- stipulate the objective of "maintaining the budgetary position in balance or in surplus", this being considered achieved as long as the annual structural deficit of the general government converges to the medium-term objective, defined as the structural budget balance as a percentage of GDP that is no lower than the level of -1%, temporary deviations from this level being allowed only in exceptional circumstances (art. 6 - art. 8 of FRL);
- establish nominal ceilings for the budget balance of the general consolidated budget (GCB), for the primary balance of the GCB, for the GCB's total expenses (net of financial assistance from the EU and other donors) and for personnel spending, mandatory for the first year covered by the Fiscal Strategy (FS) approved by the Parliament (art. 12 letter b) and letter c) of FRL);
- setting ceilings defined as a percentage of GDP for the budget balance and for personnel spending, mandatory for the first two years covered by the FS approved by Parliament (art. 12, letter a) of FRL).

Additional relevant fiscal rules target the personnel costs: art. 17 paragraph 1 of FRL explicitly prohibits the promotion of legislative proposals which may lead to an increase of personnel expenditure 180 days before the Government mandate cease and paragraph 2 of the same article prohibits the increase of the personnel expenditure during the budget year, when the budget revisions appear. Moreover, art. 15 states that the introduction of measures/policies/legislative initiatives whose adoption attracts increased government spending requires the elaboration of the financial statement in accordance with art. 15 of Law no. 500/2002 (of the Public Finance) and the submission of a declaration stating that the increase in expenditure involved is consistent with the strategic priorities set out in the FS, the annual budget law and the expenditure ceilings set in the FS. In this regard, Public

Finance Law stipulates that financial statement must contain the measures that cover the increase of the expenditure, in order to not influence the budget deficit.

FRL provisions indicate that the legislator paid special attention to personnel expenditure, instituting rules that individualize it among other categories of expenditure. An argument in favor of this approach relates to the fact that this category of expenditure is substantially more vulnerable than others to the prevalence of short-term considerations, to the detriment of medium and long term strategic objectives. Moreover, these expenses have, by their nature, a permanent feature – an increase of the salary generates *ceteris paribus* an increase in perpetuity of the wage bill, in contrast, for example, with an increase in investment spending, which expires once the investment objective concerned is completed.

The permanent feature naturally involves risks on the medium and long-term sustainability - such increase in expenditure cannot be justified by the existence of a temporary fiscal space, due either to a failure in the programmed expenditure, or to the appearance of exceptional/temporary revenues.

The individualization of personnel expenses by law is not at all intended to prevent salary increases - any level of increase is possible within the constraints exercised by the deficit target and therefore of those concerning total expenditure of the general government, but to discipline wage negotiations and the budgetary process, favoring the adoption of a medium-term perspective regarding the dynamics of personnel expenses within total expenditures of the general government rather than determining their level on an *ad hoc* basis. However, as the Fiscal Council showed in successive opinions, the fiscal rules which do not directly target the budget deficit (those concerning the mandatory ceilings for all other elements relevant from the law perspective - primary balance, personnel expenses, total expenses net of financial assistance from the EU and other donors, strengthened by the prohibition of increasing total expenditure and personnel expenditure during budgetary revisions) were proved in practice to be "weak" rules, whose breach (at least in the context of the proposed parameters of the budget revisions) was the rule rather than the exception, derogations from these intervening in almost all budget revisions that took place after the entry into force of the FRL in April 2010 (the execution under the program of the expenditures made that sometimes some of these "auxiliary" fiscal rules to be respected *ex post*). Three recent examples of *de facto* non-binding nature, despite the formal prohibition, of the rules relating to personnel expenditure, are:

- Personnel expenditures at the end of 2015 were 52 billion lei, compared to the ceiling established by Law no. 182/2014 of 48.4 billion lei. Even adjusting for the additional costs deriving from the executory titles whose payments was decided during subsequent budget revisions (1.5 billion lei), these expenses stood at about 2 billion lei above the ceiling.

- The initial budget construction for the current year provided personnel expenditures amounting to about 7.6% of GDP, despite the fact that the ceiling expressed as a percentage of GDP stated by Law no. 182/2014 indicated a maximum level of 6.8% (it is true that the Government change entails a reset of the ceilings that the new authorities are free to place at any level since it is in line with the deficit targets which are consistent with medium-term objective or the adjustment path towards it).
- The first budget revision of this year involved, as showed in the opinion of the Fiscal Council issued on that occasion, a deviation from the ceiling of personnel expenditure stated by Law no. 338/2015 of 1.37 billion lei (out of which the related impact of the Law no. 85/2016 in the current year represents about 1.02 billion lei, while the rest was caused by changes in wages implied by GEO no. 20/2016, partially accommodated however by some savings in this aggregate, highlighted by the budget execution).

Remarks on the amendments introduced through the Report adopted by the Parliament regarding the Law of approving the Government Emergency Ordinance no. 20/2016 for amending and supplementing the Government Emergency Ordinance no. 57/2015 regarding the remuneration of personnel paid from public funds in 2016

Considering the above mentioned, the Fiscal Council notes that:

- The notification of the Fiscal Council in order to issue an opinion on the financial impact of the amendments introduced and the compliance with fiscal rules has intervened after the adoption of these amendments by the Parliament.
- The introduction of some amendments which specify wage increases above those already provided by GEO no. 20/2016 it is not in accordance with art. 17 para. 1 of the FRL which prohibits the promotion of some normative acts with less than 180 days before the expiry of the Government's mandate, leading to increased personnel expenditure or pensions in the public sector. It has to be noted that the salary increases introduced by GEO no. 20/2016 were initiated before the deadline of 180 days, although involving a lack of conformity with the ceiling of personnel expenditure stated by Law no. 338/2015 and art. 17 para. 2 of FRL which prohibits increases of personnel expenditure during the budget revisions. In both cases, the Government has resorted to derogations from FRL, without affecting the deficit target, the changes being made in the context of an update of the budget construction that identified additional revenue.
- The Fiscal Council validates the computed fiscal impact received from MPF (and shown in Annex 3) according to which the approved amendments would entail an increase in personnel expenses in 2017 to 4.85 billion lei and*, ceteris paribus*, a first round effect budget deficit of 2.9 billion lei, after considering the additional income which the salary increases would automatically lead to in the social security

contributions payable by employers and employees, as well as in the revenues from the personal income tax.

- The second-round effects on budget revenues would only arise in the absence of compensatory measures and thus only to the extent that the deficit in 2017 would be allowed to increase the amount of the first-round effect identified (2.9 billion lei or 0.35% of GDP). Even accepting the existence of a high fiscal multiplier of about 0.8 for personal expenses, the income generated by an additional growth of 0.2-0.3 pp would be less than one billion lei, which implies an increase in budget deficit of at least 2 billion lei (0.25% of GDP).
- The Fiscal Council considers that the ceiling on personnel expenses for the year 2017, established by the Law no. 338/2015 at a level of 7.4% of GDP, would be impossible to meet given the current parameters regarding the number of public sector employees and the proposed wage increases, after considering the additional GDP growth caused by the latter in the event of a lack of compensation - we estimate that the personnel expenses following the implementation of the amendments would be equivalent to at least 7.8% of GDP in 2017. Art. 15 para. 1 letter b) of the FRL indicates that this ceiling, as that on total expenses and deficit, are relevant for the legislative initiatives adopted by the current legislature. It should be noted, however, that an equivalent measure adopted by the future legislature would not fall within the scope of this ceiling of expenditure, given that changing the Government implies its freedom to undertake new parameters for the medium term fiscal strategy, within the constraints exerted by the rules laid down by art. 6-8 of the FRL described above with respect to the budget deficit.
- The Fiscal Council believes that the adopted amendments would increase the budget deficit in the absence of compensatory measures in terms of revenues or expenditures with at least 0.25% of GDP in 2017. The budgetary execution for the current year indicates that, *ceteris paribus*, a lower deficit under national methodology is likely, especially due to an under-execution at the level of investment expenditure for projects financed from European funds for the financial year 2014-2020 which appears as inevitable. However, the fiscal space related to the deficit target which has this source is only temporary and its existence cannot be extrapolated to 2017, the implementation of investment projects with European funding under the new financial year being likely to accelerate significantly in the years to come. A temporary fiscal space in 2016 cannot be a source of coverage in 2017 for the permanent impact caused by the wage increases.
- The Convergence Programme 2016-2019 and the last Fiscal Strategy estimated a deficit of 2.9% of GDP for 2017, therefore being placed in close proximity of the ceiling that might trigger the excessive deficit procedure, given that for the next year the Fiscal Code adopted in 2015 foresees additional cuts in indirect taxes. The latest forecast of the European Commission indicates an increase in the ESA 2010 deficit from 2.8% in 2016 to 3.2% in 2017, without including the impact of the

amendments generating wage increases or other tax cuts recently passed by Parliament (and being in the process of endorsement by the President). Therefore, there is already a substantial risk that the reference value of 3% of GDP for the budget deficit to be exceeded. The proposed amendments, in the absence of compensatory measures, greatly increase this risk, entailing an additional vulnerability for a fiscal position already inconsistent with the principle of fiscal responsibility mentioned above, in an international context more complicated and more volatile than last year[8].

The above opinions and recommendations of the Fiscal Council were approved by the Chairman of the Fiscal Council, according to article 56, paragraph (2), letter d) of Law no. 69/2010 republished, after being approved by the Council members through vote, on the 10th of November, 2016.

10th of November 2016 Chairman of the Fiscal Council,

IONUȚ DUMITRU

[8] For a review of the vulnerabilities caused by the placement of the budget deficit in the close proximity of the ceiling level of 3% see the preamble to the Fiscal Council's Opinion on the 2016 budget of December, 2015 (http://www.fiscalcouncil.ro/FCopinion2016budget.pdf).

ANNEX 1 - Amendments admitted according to GEO no. 20/2016

	Budgetary impact (mil. lei)
Increase in basic salaries with effect from 1 December 2016 for healthcare professionals (including administrative staff) on average with 15%	1,116.20
Increase in basic salaries with effect from 1 December 2016 for staff in the social welfare system on average with 15%	292.40
Calculation of bonuses as a percentage of the increased salaries for staff in the health system and the social assistance	1,414.02
Increase in basic salaries as of 1 January 2017 for education personnel on average with 15%	1,788.24
Increase in basic salaries from 1 December 2016 with 25% for staff in the apparatus of the National Health Insurance House	5.88
Establishing salaries for the staff of the County Health Insurance Houses and the County Departments of Public Health to 85% of the increased wages for the National Health Insurance House	231.27
Establishing salaries for the staff of the Romanian Agency for Saving Human Life at Sea similar to the remuneration of staff of the General Inspectorate for Emergency Situations	2.20
Total	**4,850.22**

Source: Ministry of Public Finance

ANNEX 2 - Financial statement (financial impact on the consolidated general budget)

Indicators	Current year mil. lei
1. Changes in budget revenues, plus / minus, of which:	**1,940.1**
a) the state budget	465.6
b) the centralized general budget of the administrative-territorial units	
c) the state social insurance budget	1,016.6
d) the unemployment insurance budget	38.6
e) the budget of the Sole National Fund for social health insurances	419.3
f) the budget of institutions / activities funded wholly and / or partially from own revenues	
2. Changes in budgetary expenditures plus / minus, of which:	**4,850.2**
a) the state budget	291.4
b) the centralized general budget of the administrative-territorial units	3,620.3
c) the state social insurance budget	
d) the unemployment insurance budget	
e) the budget of the Sole National Fund for social health insurances	106.6
f) the budget of institutions / activities funded wholly and / or partially from own revenues	831.9
3. Financial impact plus / minus, of which:	**-2,910.1**
a) the state budget	174.2
b) the centralized general budget of the administrative-territorial units	-3,620.3
c) the state social insurance budget	1,016.6
d) the unemployment insurance budget	38.6
e) the budget of the Sole National Fund for social health insurances	312.7
f) the budget of institutions / activities funded wholly and / or partially from own revenues	-831.9

Source: Ministry of Public Finance

ANNEX 3 - Additional impact on personnel expenditure (mil. lei, 2017)

The 15% personnel salaries increase in the healthcare system		
Expenses with the base salaries in the healthcare system (monthly average)	1	505.8
15% wage increase (monthly)	2=1*15%	75.9
Monthly impact	3=2*122.6%	93.0
Impact at 12 months	**4=3*12**	**1,116.2**
The 15% personnel salaries increase in the social assistance system		
Expenses with the base salaries in the social assistance system (monthly average)	5	132.5
15% wage increase (monthly)	6=1*15%	19.9
Monthly impact	7=2*122.6%	24.4
Impact at 12 months	**8=7*12**	**292.4**
The calculation of bonuses as a percentage applied to the increased salaries for health and social care staff		
Expenses with the bonuses in the healthcare and social assistance system (monthly average)	9	124.1
Percentage bonuses (30% in base salaries)	10=1*30%	220.2
Monthly impact on bonuses	11=10-9	96.1
Monthly impact on expenditures	12=11*122.6%	117.8
Impact at 12 months	**13=12*12**	**1,414.0**
The 15% personnel salaries increase in the education system		
Expenses with the base salaries in the education system (monthly average)	14	884.0
15% wage increase (monthly)	15=14*15%	132.6
Monthly impact	16=15*122.6%	162.6
Impact at 12 months	**17=16*11**	**1,788.2**
Increase of the salaries for NHIS staff		
NHIS personnel salaries expense (monthly average)	18	1.6
15% wage increase (monthly)	19=18*25%	0.4
Monthly impact	20=19*122.6%	0.5
Impact at 12 months	**21=20*12**	**5.9**

Increase of the salaries for Departments of Public Health Directorate and County Health Houses staff at 85% of NHIS wages		
No. of Public Health Department jobs	22	3,873
The average salary base at the Public Health Directorate (lei)	23	3,362
No. of Counties' Departments of Public Health jobs	24	2,990
The average salary base at Counties' Department of Public Health (lei)	25	3,362
Expenses with the base salaries system (monthly average)	26=(22*23+24*25)/1,000,000	23.07
The average salary base at NHIS (lei)	27	5,320
The average base salary increased by 25% for the NHIS (lei)	28=27*125%	6,650
The base salary increased to 85% of the increased salaries for NHIS (lei)	29=28*85%	5,653
Expenses with the increased base salaries	30=29*(22+24)/1,000,000	38.8
Monthly impact on the base salaries	31=30-26	15.7
Monthly impact on expenditures	32=21*122.6%	19.3
Impact at 12 months	**33=32*12 months**	**231.3**
Payroll for the Romanian Agency for Rescuing Human Life at Sea staff similar to the remuneration of General Inspectorate for Emergency Situations		
Impact	**34**	**2.2**
Total impact on personnel expenditures		**4,850.2**

Source: Ministry of Public Finance

V. Fiscal Council's Opinion on the Second Budget Revision for 2016

On November 16th 2016, the Fiscal Council received from the Ministry of Public Finance by letter no. 55263/14.11.2016, the draft of the second budget revision for 2016, the explanatory note and the draft Government Ordinance project regarding the second budget revision for 2016, as well as the explanatory note and the Government Ordinance project regarding the second revised social security budget for 2016, requesting the Fiscal Council's opinion under article 53, paragraph (2) of the Fiscal Responsibility Law no. 69/2010 republished (FRL).

The coordinates of the Second Supplementary Budget Draft – the compliance with the fiscal rules

Compared with the budget approved on the occasion of the first budget amendment, the general consolidated budget (GCB) revenues increase by 813.1 million lei and the GCB expenditures increase by 766.1 million lei, so that the GCB budget deficit is projected to a level of 20,858.4 million lei, standing by about 47 million lei below the ceiling for the budget deficit defined by Law no. 338/2015 (the law for approving ceilings for certain indicators specified in the budgetary framework).

The project regarding the second budget revision for 2016 records a number of exemptions from the provisions stipulated by article 12 letters b) and c), article 17 paragraph (2), article 24 and article 26 paragraph (4) and (5) of the Fiscal Responsibility Law republished and also from the provisions stipulated by article 3 letter (5) and (7) of the Law no. 338/2015, stating thus the failure to comply with practically all the fiscal rules excepting the GCB balance rule. Article 12 letters a), b) and c), article 24 and article 26 paragraph (4) and (5) of the FRL state as mandatory the ceilings established by the Fiscal Strategy and by the accompanying law regarding the ceilings for the nominal level of the GCB deficit, the GCB primary deficit, the total spending excluding the financial assistance from the EU and other donors and also for the personnel spending, allowing the possibility of increasing total expenditure of the GCB on the occasion of the budgetary revisions exclusively for servicing public debt and, respectively, for paying the contribution to the EU budget.

- The first budget revision already recorded significant deviations from the mandatory ceilings stipulated in the Law no. 338/2015 for the personnel expenditure (by 1368.1 million lei in nominal terms, or by about 0.1 pp as a percentage of GDP) and for the total spending excluding the financial assistance from the EU and other donors (by 3,344.6 million lei, only partially justified under the fiscal rule established by art. 24 of FRL for the amount of 319.1 million lei corresponding to the supplementation of the interest spending occurred on this occasion). The absence of compliance with the fiscal rules intervened also at those stated by art. 12 letter a) (regarding the level expressed as a percentage of GDP for personnel spending) and letter c) (for the nominal level of the total expenditure and personnel spending) and with the rules established by art. 17 paragraph (2) (which prohibits increasing personnel spending during the budget revisions) and of art. 24 (which allows the increase in the context of budgetary amendments of the total GCB expenditure net of financial assistance from the EU and other donors, exclusively for paying the debt service[9], or for the Romania's contribution to the EU budget).

- The changes introduced by the second supplementary budget draft increases the size of the non-compliance with the ceiling for personnel expenditures by 132.4 million lei (i.e. the ceiling on personnel expenditure of GCB is exceeded in nominal terms with 1,500.5 million lei and as a percentage of GDP by 0.1 pp, given the increase in the forecast for GDP with 11,600 million lei compared to the one available when the Law no. 338/2015 was drafted), the increase by another 755.6 million lei compared to the first supplementary budget draft regarding the ceiling for total expenditure excluding financial assistance from the EU and other donors, the ceiling ruled by the Law no. 338/2015 being exceeded with 4,100.2 million lei. Furthermore, the compliance with the limits stipulated by the Law no. 338/2015 for the ceiling on primary balance of GCB (the primary deficit exceeds the ceiling with 375.6 million lei) was not met, given that the downward revision of interest expenditure (-742 million lei compared to the first supplementary budget draft and -422.7 million lei compared to the initial budget) is accompanied by an increase of other expenses, not entailing an equivalent reduction in the GCB deficit. Therefore, the second supplementary budget draft violates the provisions of art. 12, letter a), b) (except the ceiling on GCB balance in nominal terms and as a percentage of GDP) and c), art. 17, para. (2), art. 24 and art. 26, para. (4) and (5).

The government ordinance draft concerning the second supplementary budget draft for 2016 provides the corresponding derogations from the fiscal rules mentioned above and redefines the ceilings of the Law. 338/2015 according to the levels of the budget aggregates in the second supplementary budget draft. In the Opinion on the first supplementary budget draft for 2016, the Fiscal Council noted, as well as in the Opinion on the second supplementary budget draft for 2015, that, in the light of experience of systematic recourse

[9] Under the circumstances that less than one-tenth of the increase in expenses was related to the debt service payment

to derogations from the provisions of the FRL and redefining the parameters stipulated in the ceilings Law during each budget amendment, there is *de facto* existence of two classes of fiscal rules, one of "strong" rules (those relating to the GCB balance) - which usually operates successfully, and one of "weak" rules (the rules concerning mandatory ceilings for all the other elements relevant from the perspective of the law - primary balance, personnel expenditure, total expenditure excluding financial assistance from the EU and other donors, strengthened by the FRL through the interdiction of increasing the total expenditure and personnel expenditure during the budget amendments), for which the lack of *ex ante* compliance is the rule rather than the exception, the derogation being involved in almost all budget amendments that occurred following the entry into force of the FRL in April 2010. The execution below the program for expenditures, especially for investment, sometimes has led to *ex post* compliance with the fiscal rules. Such a scenario appears to be very likely for the current year given the coordinates of the budget execution, there being the premises of a major under the program execution for investment expenditure, in the conditions of a much lower absorption of European funds than that foreseen in the draft budget. A lower than expected absorption usually entails lower co-financing expenses, which should lead to a budget deficit lower than the target. In these circumstances, it is likely to exist an *ex post* compliance with the ceilings on total expenditure and primary deficit, in contrast to the situation regarding the rules on personnel expenditure, where non-compliance with the fiscal rules appears as being certain.

The Fiscal Council ascertains once again the violation of most fiscal rules, except the GCB deficit rule, noticing the *de facto* inoperability of a large subgroup of fiscal rules and reiterates its recommendations regarding the compliance with those rules[10]. The perpetuation of the *de facto* inoperability of the fiscal rules associated to the budget deficit requires a serious discussion.

The coordinates of the second budget revision - budgetary revenues

GCB revenues are revised upwards by 813.1 million lei compared to the level programmed in the first budget revision. This value includes the effect of the swap reduction, which has a symmetric effect on the revenues and expenditures, by 147 million lei, thus the budgetary revenues, adjusted with swap, are forecasted to increase by 960.5 million lei. The important sources for revisions compared to the estimated values in the first budget revision, taking into account swap adjusted values are:

- *Personal income tax*: +567.3 million lei. Updating the programmed level for the whole year appears to be justified from the perspective of the up to date budget execution and updated forecasts regarding the dynamic of salaries. Moreover, in its opinion on the first amendment, the Fiscal Council

[10] See "The Fiscal Council's Opinion on the Second Supplementary Budget Draft for 2015", http://www.fiscalcouncil.ro/Opinion-R2_FC_2015.pdf

appreciated that a wage dynamics higher than the projection from the spring forecast of the National Commission for Economic Forecasting (NCEF) was possible given the evolution of earnings and the autumn projection of NCEF records an upward review of the gross wages dynamics from 8.3% to 10.2%.

- *VAT*: +526.4 million lei. The revision program takes over the exceeding of the receipts at the level of the third quarter of revenue program, excluding the swap scheme (+336 million lei), corresponding to a degree of achievement of 102.7%. The updated execution data indicates that the proposed value is feasible.
- *Non-tax revenues*: +182.5 million lei. The Fiscal Council reiterates its concerns expressed during the first budget revision regarding the proposed level for this revenue aggregate, given the evolution of revenues at the end of September 2016. If an acceleration during the last quarter of the year is possible, given the registration of some extraordinary revenues of about 847 million from the recovery of some amounts from previous years of budgetary funding already provided during the first budget revision, it isn't enough for generating the convergence with the annual target, given the historical evolution of monthly flows of non-tax revenues.
- *Taxes on using goods, authorizing the use of goods or on carrying activities:* -121,9 million lei due to the under-program receipts at 9 months from taxes on gambling.

The budget revision leaves virtually unchanged the estimated amounts to be attracted from the European Union for the year 2016: 13,55 billion lei. Given that the revenues at the end of September (2.9 billion lei) represented only 22% of the amount proposed for the entire year, achieving the programmed levels appears highly unlikely. Even taking into account an accelerated of the entries of the last quarter of the 2015 proportions (most likely exceptional given that 2015 was the final year of financial framework), it appears unlikely even achieving revenues which would be half of the amount advanced for the whole year. *Ceteris paribus*, such a development, accompanied by a symmetrical reduction in financing costs, should lead to budget deficits considerable lower than programmed.

The budget expenditures are revised upward by 766.1 million lei or by 913.6 million lei if we eliminate the influence of the updated swap scheme. In essence, the fiscal space relative to the annual deficit target created by the increases of the budget revenues described above along with the significant reduction of the estimated annual interest and goods and services expenditures, is used to significantly increase allocations for social assistance and capital expenditure. Specifically, the relevant changes in the level of expenditures programmed occurs in the following categories (the numbers are net of the impact of swap, and the comparison base is the first budget revision as notified by the Fiscal Council at the end of July 2016):

- *Interest expenses*: -741.8 million lei.

- *Goods and services*: -456.2 million lei.
- *Social assistance*: +1,132.9 million lei. The upward revision of the consolidated budget expenditures has as sources: the increase of the allocation for this chapter in the state budget with 426.3 million lei, as well as the increased social spending planned for local budgets by 674.6 million lei. Additional expenses have not occurred as a result of new legislative measures, but as a result of the under-budgeting the state budget for the military pension expenditures, and the local budgets for the expenses occasioned by the payment of allowances for persons with disabilities who gives up the accompanying person.
- *Personnel expenses*: +132.4 million lei.
- *investment expenses*: +710 million lei. The projected level of capital expenditure is revised upward by 1.1 billion lei, while reducing the allocations for other investment transfers (-138.8 million lei), EU projects (-125.3 million lei) and for expenses related to the reimbursable financing programs (-119.6 million lei). Data on execution at the end of three quarters of 2016 indicate the 45% spending of the annual allocation of the investment expenditure, with relatively similar levels of achievement of the subcomponents. Basically, the convergence with the annual target regarding investment spending would require spending 21.4 billion lei in the fourth quarter, more than double the amount spent in the first three quarters of the year. The Fiscal Council is skeptical that an acceleration of this magnitude is possible, especially given that the absorption of European funds in the new financial year appears to be delayed (the expenditure related to EU funded projects from the 2014-2020 framework at the end of September was only 18.5 % of the annual programming).

In conclusion, the Fiscal Council considers that the budget deficit will rather stand at the end of the year under the proposed level of 2.75% in GDP, as investment spending is likely to have an execution under the program. We appreciate that the size of this under the program execution is likely to considerably exceed the probable non-realization of the forecasted level of non-tax revenues. The existence of a fiscal space relative to the fiscal deficit target for 2016 must, however, be seen as a temporary situation, given that the delays in implementing investment projects with European financing of the new financial year are likely to be recovered in the coming years.

The opinions and the recommendations above mentioned by the Fiscal Council were approved by the Chairman of the Fiscal Council, according to art. 56, para (2) letter d) of the Law no. 69/2010 republished, after being approved by the Council members through vote, on 22nd November 2016.

22nd of November 2016 Chairman of the Fiscal Council,

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ANNEX 1 - The main sources for increasing the budgetary expenditure on the occasion of the second budget revision in 2016		
	Budgetary impact – million lei	**Expenditure item**
Special pension recalculation and refunding the differences between the pensions due for December 2010 and those established according to the Law no. 119/2010 (the budgets of the Ministry of Internal Affairs, the Ministry of National Defense and the Romanian Intelligence Service)	336.70	Social assistance
Provide the funding needed to finance the rights for people with disabilities within the budget of the Ministry of Labor, Family, Social Protection and Elderly Persons	110.00	Social assistance
Ensuring the funding of benefits for the people with disabilities who renounce to their attendant	562.30	Social assistance
Increase allocations for the National Program for Local Development and ensure funding of the Loan Agreement "Integrated systems for rehabilitation of the water supply and sewage, of drinking water treatment plants and of wastewater treatment plants in towns with a population of up to 50,000 residents "(budget of the Ministry of Regional Development and Public Administration)	1,255.00	Capital spending
Ensuring the funding for the remuneration of clerical and cult places personnel (budget of the Government's General Secretariat)	92.70	Personnel spending

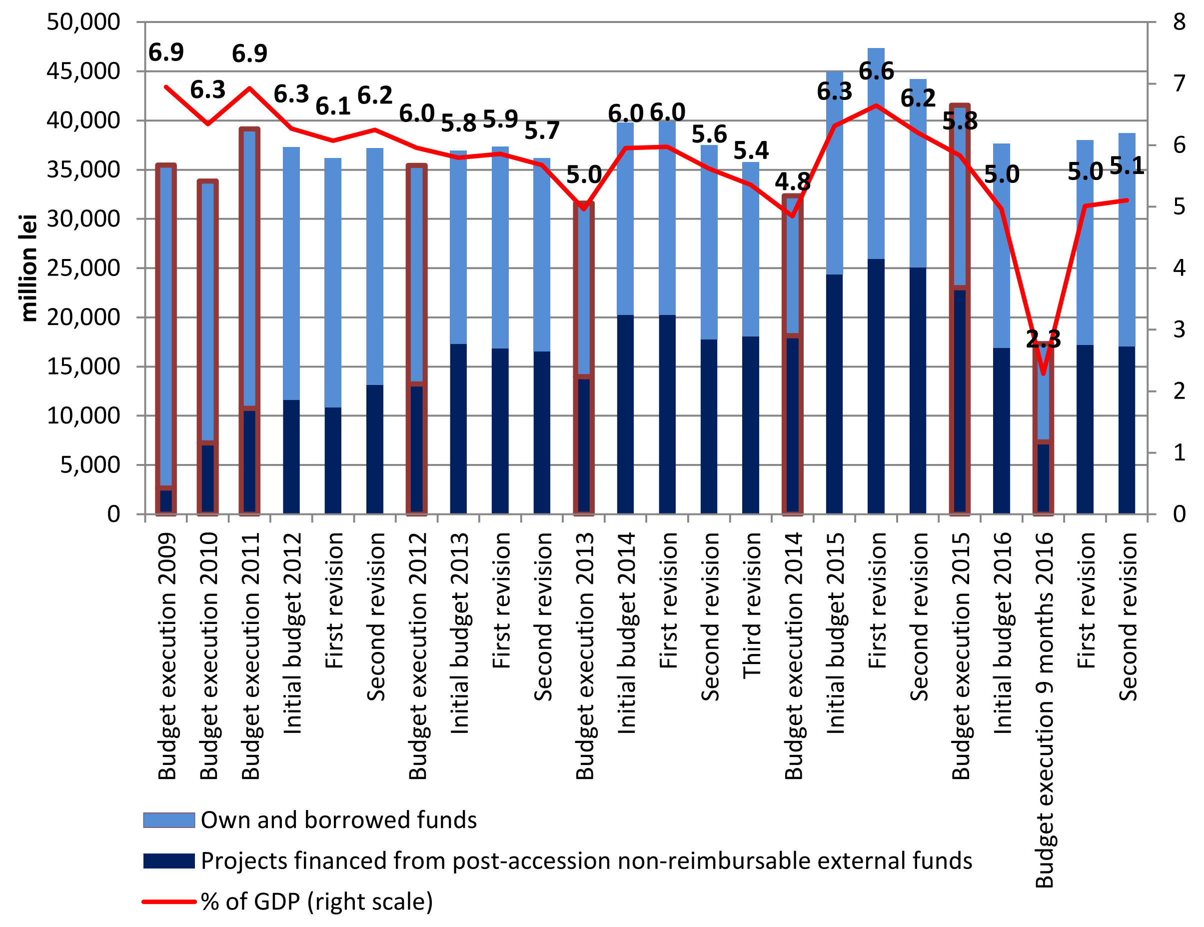
Source: Ministry of Public Finance

ANNEX 2	Initial budget 2016	*Swap* program 2016	Initial budget 2016 without *swap*	First budget revision (R1)	Additional *swap*	R1 without *swap*	Second budget revision (R2)	Additional *swap*	R2 without *swap*	R1 - Initial budget	R2 - Initial budget	R2-R1
										without *swap*		
	1	2	3=1-2	4	5	6=4-5	7	8	9=7-8	10=6-3	11=9-3	12=9-6
TOTAL REVENUE	231125.5	1070.0	230055.5	234882.4	1070.0	233812.4	235695.5	922.6	234773.0	3757.0	4717.5	960.5
Current revenue	217018.2	1070.0	215948.2	220412.9	1070.0	219342.9	221242.9	922.6	220320.3	3394.7	4372.1	977.4
Tax revenue	136123.0	1070.0	135053.0	139015.5	1070.0	137945.5	139618.4	922.6	138695.9	2892.5	3642.9	750.3
Taxes on profit, wages, income and capital gains	41759.6		41759.6	44179.3		44179.3	44711.0		44711.0	2419.6	2951.3	531.7
Corporate income tax	14384.9		14384.9	15437.5		15437.5	15361.4		15361.4	1052.7	976.5	-76.1
Personal income tax	26206.9		26206.9	27103.8		27103.8	27671.1		27671.1	896.9	1464.2	567.3
Other taxes on income, profit and capital gains	1167.8		1167.8	1637.9		1637.9	1678.4		1678.4	470.0	510.6	40.5
Property tax	5980.1		5980.1	5982.7		5982.7	5883.5		5883.5	2.6	-96.6	-99.2
Taxes on goods and services	87137.6	1070.0	86067.6	87438.2	1070.0	86368.2	87660.9	922.6	86738.3	300.5	670.7	370.1
VAT	52342.3	1070.0	51272.3	52748.6	1070.0	51678.6	53127.6	922.6	52205.0	406.3	932.7	526.4
Excises	27382.3		27382.3	27562.3		27562.3	27562.3		27562.3	180.0	180.0	0.0
Other taxes on goods and services	3958.6		3958.6	3757.1		3757.1	3722.7		3722.7	-201.5	-235.8	-34.3
Taxes on using goods, authorizing the use of goods or on carrying activities	3454.5		3454.5	3370.2		3370.2	3248.3		3248.3	-84.3	-206.2	-121.9
Tax on foreign trade and international transactions (customs duty)	836.7		836.7	1015.6		1015.6	950.2		950.2	178.9	113.5	-65.4
Other tax revenue	409.0		409.0	399.9		399.9	412.9		412.9	-9.1	3.9	13.0
Social security contributions	61748.8		61748.8	60766.8		60766.8	60811.3		60811.3	-982.0	-937.5	44.6
Nontax revenue	19146.4		19146.4	20630.6		20630.6	20813.1		20813.1	1484.2	1666.7	182.5
Capital revenues	951.7		951.7	901.8		901.8	874.5		874.5	-50.0	-77.2	-27.2
Grants	20.6		20.6	22.5		22.5	22.6		22.6	1.9	2.1	0.1
Amounts received from the EU in the account of payments made and prefinancing	336.9		336.9	744.0		744.0	756.1		756.1	407.1	419.2	12.1
Financial operations	0.0		0.0	0.0		0.0			0.0	0.0	0.0	0.0
Amounts collected in the single account	0.0		0.0	0.0		0.0			0.0	0.0	0.0	0.0

Other amounts received from the EU for operational Programmes funded under the convergence objective	0.0		0.0	0.0		0.0			0.0	0.0	0.0	0.0
Amounts received from the EU/other donors in the account of payments made and pre-financing for financial framework 2014-2020	12798.1		12798.1	12801.3		12801.3	12799.5		12799.5	3.2	1.4	-1.8
TOTAL EXPENDITURE	252031.0	1070.0	250961.0	255787.8	1070.0	254717.8	256554.0	922.6	255631.4	3756.8	4670.4	913.6
Current expenditure	232848.4	1070.0	231778.4	236725.5	1070.0	235655.5	236397.4	922.6	235474.8	3877.1	3696.4	-180.6
Personnel	57335.0		57335.0	58703.0		58703.0	58835.4		58835.4	1367.9	1500.4	132.4
Goods and services	43111.4		43111.4	43500.2		43500.2	43116.6	72.6	43044.1	388.8	-67.4	-456.2
Interest	11069.0		11069.0	11388.1		11388.1	10646.3		10646.3	319.1	-422.7	-741.8
Subsidies	6464.3		6464.3	6721.3		6721.3	6933.5		6933.5	257.0	469.1	212.2
Total Transfers	114235.8	1070.0	113165.8	115631.8	1070.0	114561.8	116304.9	850.0	115454.9	1396.0	2289.1	893.2
Transfers for public entities	1966.8	1070.0	896.8	1720.8	1070.0	650.8	1680.1	850.0	830.1	-246.0	-66.7	179.2
Other transfers	12311.1		12311.1	12163.2		12163.2	11800.5		11800.5	-147.9	-510.6	-362.7
Projects funded by external post-accession grants	4600.7		4600.7	6864.9		6864.9	6682.1		6682.1	2264.2	2081.4	-182.8
Social assistance	79373.4		79373.4	80749.4		80749.4	81882.2		81882.2	1375.9	2508.8	1132.9
Projects funded by external post-accession grants 2014-2020	12449.2		12449.2	10464.0		10464.0	10521.5		10521.5	-1985.2	-1927.7	57.5
Other expenditure	3534.5		3534.5	3669.5		3669.5	3738.5		3738.5	135.0	204.0	69.0
Reserve funds	100.0		100.0	202.5		202.5	101.8		101.8	102.5	1.8	-100.7
Expenditure funded from reimbursable funds	532.8		532.8	578.5		578.5	458.9		458.9	45.8	-73.9	-119.7
Capital expenditure	19182.6		19182.6	19062.4		19062.4	20156.6		20156.6	-120.3	973.9	1094.2
Financial operations	0.0		0.0	0.0		0.0	0.0		0.0	0.0	0.0	0.0
Payments made in previous years and recovered in the current year	0.0		0.0	0.0		0.0	0.0		0.0	0.0	0.0	0.0
EXCEDENT(+) / DEFICIT(-)	-20905,5		-20905,5	-20905,5		-20905,5	-20858,4		-20858,4	0,0	47,1	47,1

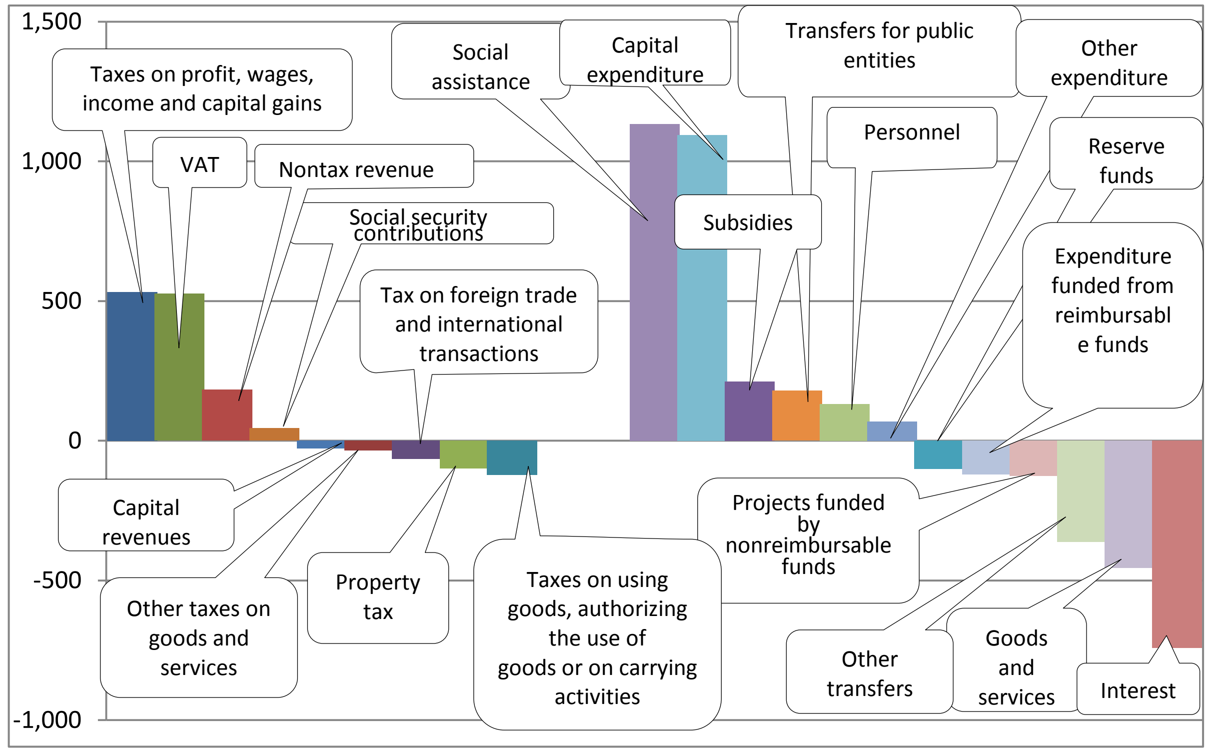
Source: Ministry of Public Finance, Fiscal Council's calculations

Figure 1: The evolution of investment expenses between 2009-2016 – planned level vs. execution (million lei)



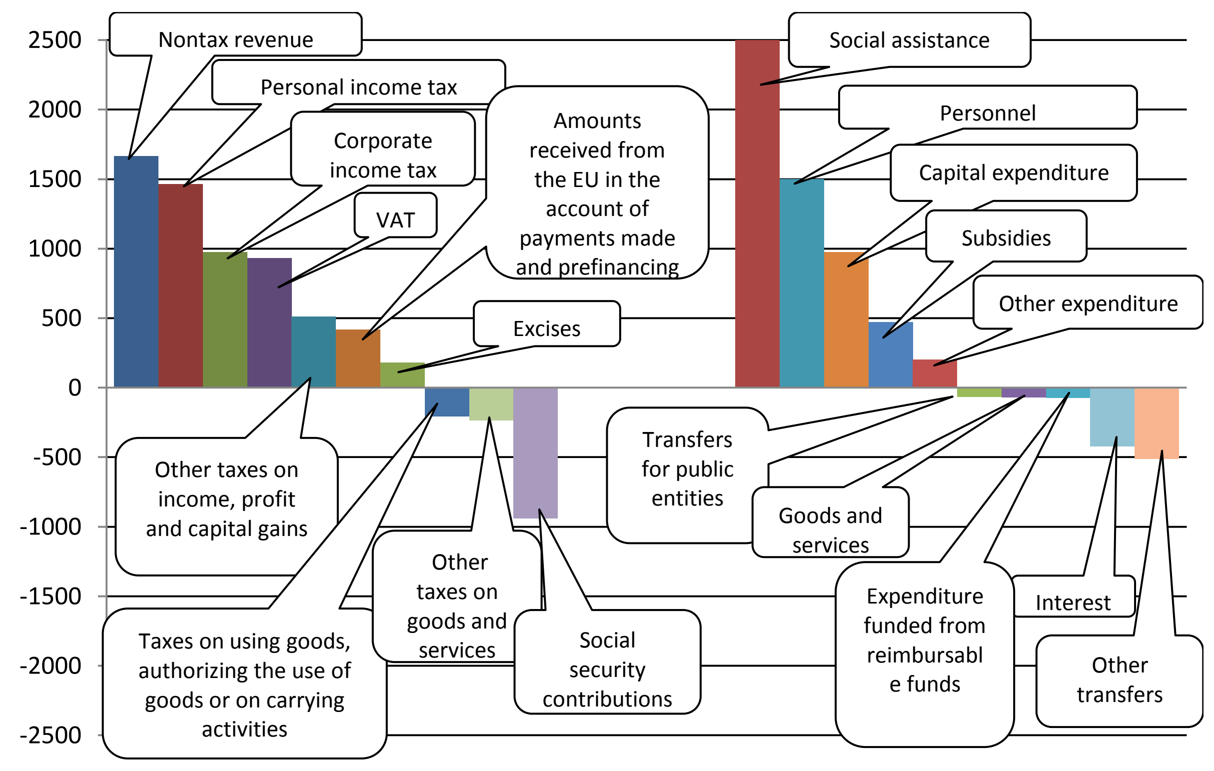
Source: Ministry of Public Finance, Fiscal Council's calculations

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



Source: Ministry of Public Finance, Fiscal Council's calculations

Figure 3: The main changes in revenues and expenditures compared to initial budget (without the impact of swap schemes), million lei



Source: Ministry of Public Finance, Fiscal Council's calculations

VI. Fiscal Council's Opinion on the legislative proposal regarding the functioning of the Romanian Development Bank – EximBank S.A.

On November 24th 2016, the Fiscal Council received from the Department for Relations with the Parliament the letter no. 9743F/DRP requesting the Fiscal Council's opinion on supporting or rejecting a legislative initiative on the functioning of the Romanian Development Bank - Eximbank S.A. for formulating the government's point of view in this regard.

According to article 53, paragraph (2) of the Fiscal Responsibility Law (FRL), the Fiscal Council has among its tasks „analyzing and issuing opinions and recommendations on the annual budget laws before approval by the Government and before submission to Parliament, on the supplementary budgets and other legislative initiatives that may have an impact on the budgetary spending, as well as assessing their compliance with the principles and rules specified in this Law". The present legislative proposal could be included in the category of legislative initiatives with a potential impact on the budgetary expenditures.

In essence the draft law amends the regulatory framework of Eximbank S.A. activity in the name of and in the account of the state, by extending the current mandate to that of a bank of national development, provides complementarity of the activities of a commercial bank (in own name and own account) with those pursued in the mandate of a development bank in the name and on behalf of the Romanian state, redefining the funding sources at its disposal including explicitly the possibility of getting reimbursable financing in the name and on behalf of the state, which are considered to have the nature of government debt liabilities.

The explanatory statement attached to the legislative project includes a preliminary estimate of the necessary additional funds that should be made available to the Romanian Development Bank - Eximbank S.A., of 317 million lei in 2017, 240 million lei 2018 and 239 million in 2019, while stating that those amounts would not have an impact on the budget deficit, representing financial investments of the State at the Development Bank of Romania. The Fiscal Council has no competences to decide on the opportunity of the legislative proposal and also cannot assess the amount of additional resources needed for extending the mandate of Eximbank due to the inherent discretionary nature of these allocations of financial resources. As regards the compliance with the principles and fiscal rules provided by FRL, the Fiscal Council considers that, to the extent that the necessary additional resources will be treated in statistical terms as a financial transaction, as indicated in the explanatory statement attached to the legislative proposal, the additional allocations should not transit through the consolidated budget and would not lead to a higher deficit.

However, we appreciate that, given the provisions of the legislative proposal, the risk is that the transfer of additional resources to be reflected as a non-financial transaction (capital transfer) which, unlike a financial transaction would result in increased budgetary spending and, *ceteris paribus*, of the budget deficit.

In this respect, it is relevant quoting the Eurostat[11] Handbook on government deficit and debt, 2016 edition that designate (page 158, paragraph 9) as conditions for recording non-financial transactions (transfer of capital) one of the following cases:

- Funding is provided without receiving anything of equal value in return;
- Funds are provided without expecting a sufficient level of return on investment;
- Funds are provided for a corporation having a recent history of losses.

We consider that the second condition mentioned above is the source of the risk of classifying the transactions as non-financial operations, given that art. 5 paragraph. (2) of the legislative proposal stipulates that "the activity undertaken by the Development Bank of Romania aims to support sustainable and well-adjusted economic development and reducing social disparities, being directed towards the public interest and not to obtain profit."

However, even assuming that the additional sources of financing needed should be treated as non-financial transactions (transiting the budget), the budgetary expenditure resulted would not automatically put at risk the targets of the annual budget deficit, given the inherent discretionary nature of allocation of funds for this purpose and the fact that the allocations will be precisely defined only later, in the context of the actual budgetary construction. Moreover, the preliminary assessments of the necessary additional resources do not suggest, in the case it would be not treated as financial transactions, but as non-financial transactions, a major impact on the consolidated budget.

Another risk that the Fiscal Council identifies is that of a possible reclassification within the government sector (becoming part of the general consolidated budget), given the provisions of the legislative proposal, for at least those activities of the Development Bank of Romania

[11] http://ec.europa.eu/eurostat/documents/3859598/7203647/KS-GQ-16-001-EN-N.pdf/5cfae6dd-29d8-4487-80ac-37f76cd1f012

- EximBank S.A. carried out in the name and behalf of the state. In this respect, it is worth also to cite the Handbook on government deficit and debt, Edition 2016 published by Eurostat - this provides at paragraph 47 on page 69 that "an entity that undertakes financial activities and is controlled by the state would have the characteristics of a captive financial institutions and therefore it should be classified in the governmental sector and not in the financial institutions' sector (S.12) if the following conditions are cumulatively met:

1. The entity carries out a limited spectrum of activities limited by certain constraints established by the government (in the general framework of the public policy objectives);
2. The influence of the state and constraints would be highlighted at the same time at the level of both assets and liabilities of the entity;
3. The entity would not behave like a "normal" commercial one (it is not anticipated to generate return on investments).

Also, there are relevant the Eurostat opinions from 2014 on the Export Bank of Czech Republic[12], respectively in 2016 on the Export-Import Bank of Hungary[13] (also called Eximbank), which in both cases concluded that those entities have the characteristics of captive financial institutions that should therefore be part of the government sector.

The clarification of statistical treatment in the two cases above mentioned is not a simple matter, and the Fiscal Council recommends the prior consultation of Eurostat about a possible change of statistical treatment that might arise from the changes introduced by the legislative proposal.

Considering the foregoing, the Fiscal Council believes that the proposal is not inconsistent with the provisions of FRL.

The opinions and the recommendations above mentioned by the Fiscal Council were approved by the Chairman of the Fiscal Council, according to Art. 56, para (2) letter d) of the Law no. 69/2010 republished, after being approved by the Council members through vote, on 6th December 2016.

6th December 2016 Chairman of the Fiscal Council,

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[12]http://ec.europa.eu/eurostat/documents/1015035/2990403/CZ-Treatment-of-Czech-Export-Bank.pdf/bf86654a-9475-4b1a-8b78-d909d7adbbae

[13]http://ec.europa.eu/eurostat/documents/1015035/7142247/Advise-2016-HU-Statistical-classification-of-Eximbank-Letter-1.pdf/e381865d-ca8b-44f5-89a2-822537dcdf52

VII. Analysis of the economic and financial performance of Romania's state owned companies in 2015

A potential risk for the fiscal sustainability on the medium term is represented by the accumulation of losses and arrears in the sector of companies where the state is the major shareholder (SOEs), because if these companies fail to streamline their activity, the Government will eventually be forced to intervene with public resources, which may lead to a deterioration of public finances, respectively increasing the budget deficit.

According to the Ministry of Public Finance, the arrears of state owned companies represent delayed payments to banks, state budget, social security budget, suppliers and other creditors by more than 30 days compared to contractual or legal terms that generate payment obligations. It is worth noting that since 2000, reducing the arrears of the state-owned companies has been a constant concern of the Government, the SOEs being closely monitored, inclusively under the agreements with the international financial institutions (IFIs). However the pace of their decline was a slow one, the assumed targets being missed on several occasions.

State owned companies' arrears have a higher share in total economy compared to the contribution of these enterprises to the economic activity, but it has diminished significantly in the recent years, 2015 marking the post-crisis minimum. Thus, the state owned companies' financial discipline has improved.

At the end of 2015, there were 1,143 SOEs that reported financial statements to the Ministry of Public Finance, most of them being organized as companies and autonomous administrations (additional information on the evolution of the number and type of state-owned companies are included in *Table 1*), with an aggregate turnover of nearly 48.57 bln. lei.

Although the state-owned companies' aggregate turnover grew by more than 4 bln. lei compared to the value recorded in 2014, it is far below the maximum value obtained in 2011 (58.51 bln. lei). Although the contribution of these companies to the overall economy turnover was only 4.09% in 2015 (4% in 2014) and the value added produced stands at 10.24% of the total (9.85% in 2014), the accumulated outstanding payments represented 18.28% of the arrears registered in the economy. However, this level represents the minimum of the period 2007-2015, being by about 2.36 pp (or 11.5%) lower than in 2014 and respectively 17.26 pp (or approximately 48.5%) lower than the peak of the period reached in 2009. In nominal terms, the state-owned companies' arrears decreased by 12.9% compared to 2014 and with approximately 38.3% compared to 2009, while the outstanding payments of private firms increased compared to 2014 with 1.46%, but was with 4.2% lower than the peak recorded in 2013. Basically, the state-owned companies have reduced their arrears in a fast pace in the post-crisis period, while private firms experienced a significant increase in their arrears in 2009-2013, followed by a slight decrease between 2014-2015. Given these aspects, it can be concluded that state owned companies' financial discipline has improved, and the higher share of their stock of arrears in the total economy is also caused by the higher starting point.

The development of the main economic indicators of Romania's state owned companies is presented in *Table 2*.

The labor productivity in state owned companies increased in 2015 compared to 2014, reaching the post-crisis peak, but it was achieved mainly by reducing the number of employees.

The number of employees in state owned companies in the period 2007-2015 has experienced a continuous decrease to a level of about 291 thousand persons, with 6 thousand (or 2%) lower than the previous year and about 115 thousand persons lower than in 2007 (or 28.32%), provided that the gross added value in these companies increased in nominal terms by 5.81% compared to 2014 and 40.1% respectively compared to 2007. Considering values expressed in real terms[14], the gross value added increased in 2015 by 2.82% compared to the previous year, but decreased by 7.5% compared to 2007. In these circumstances, the labor productivity in state owned companies increased by 4.9% in 2015 compared to the previous year and by about 29% compared to 2007, mainly due to the decrease in the number of employees.

Apparently, the profitability of state owned companies, considering the gross profit level is in 2015 the post-crisis peak, but a significant part comes from the debt cancellation

In terms of profitability of state owned companies, measured through the level of gross profit obtained, it is apparently at the maximum level of the analyzed period, reaching in 2015 a level of 4,890 mln. lei. But this evolution must be mandatory analyzed in the context of the special situation recorded by S.C. Oltchim S.A. Thus, this company recorded a net profit of 2,329.78 mln. lei, representing 47.64% of the total gross profit recorded by the state-owned companies. The profit reported

[14] The price index used for expressing values in constant prices is the GDP deflator.

of S.C. Oltchim S.A. Without this factor, total profit has fallen, but remains significantly better compared to the 2007-2012 period.

last year by S.C. Oltchim S.A. resulted from debt cancellation, according to the reorganization plan, the insolvent[15] company's current activity actually generating a loss of approximately 41 million lei. Thus, the total profit achieved was an accounting one that hasn't resulted from the company's core activity and had no impact on cash flows. If from the total profit of state owned companies we subtract the artificial profit recorded by S.C. Oltchim S.A. caused by erasing a large portion of the debt, we see that the total gross profit actually records a decrease in 2015 (reaching approximately 2,560 million lei) compared to the previous year (when it reached 3,568 million lei), being very close to the 2013 value. In these circumstances, it is appropriate to exclude the scriptic profit recorded by this company from the following detailed analysis to obtain undistorted results. Even excluding the influence of this factor it can be appreciated that the profitability of state owned companies at the aggregate level has improved during 2013-2015, being well above the levels recorded in 2007-2012 period.

A small number of state owned companies generates a profit higher than the total, and the analysis will consider separately both the aggregated values and those obtained by excluding the five most profitable state owned companies - Top 5.

The analysis of the profitability of state owned companies may be extended by excluding from the total the Top 5 companies in terms of the level of gross profit obtained[16] (Top 5 from now - they are found in *Table 3*) provided that to a small number of companies are attributable significant profits that influence considerably the aggregate results. Thus, if we eliminate the influence of the Top 5 state owned companies in terms of profit, one can notice a deepening of the negative aggregate result in 2015 compared to 2014, from -957 million lei to -1,527 million lei.

Moreover, throughout the analyzed period of time, the aggregate gross profit of state owned companies, excluding

[15] 2,371 million lei scriptic gross result caused by debt cancellation, mainly unsecured claims, as a result of the confirmation of the reorganization plan by the syndic judge by Sentence no. 892 / 04.22.2015, rendered in the Case of insolvency no. 887/90/2013 before the Court Valcea. Under the provisions of the Insolvency Act and the Tax Code, the cancellation of debt is a scriptic income of the period, influencing the result.

[16] S.C. Oltchim S.A. is not included in this Top from considerations mentioned above and all analyzes that include the indicator net/gross profit do not take into account the value from this company's debt cancellation.

Top 5, remained in negative territory, the 2008-2012 period being characterized by high losses, which declined considerably in 2013 and 2014, followed by a worsening in 2015. In contrast, Top 5 recorded significant profits consistently in the last three years, their gross profit increasing by 1.65 times compared to 2012 (i.e. from 2,465 million lei to 4,088.16 million lei at the end of 2015).

It should be noted that the profit of Top 5 in 2015 amounted 3,311.29 million lei, thus below the profit of Top 5 in 2014 (3,724 million lei). We note, however, the good profitability recorded by the companies S.N.G.N. Romgaz S.A., S.P.E.E.H. Hidroelectrica S.A., S.N.T.G.N. Transgaz S.A. Medias and C.N.A.D.N.R. S.A., which are in Top 5 in the last three years (2013-2015).

In the case of C.N.A.D.N.R. S.A. we can talk also about an apparent profit, the company having revenues arising mainly from amounts received from the state budget and from the European Union, to which are added revenues from sales of the vignette and fees for roads and bridges, and the most of the company's expenses are actually investment in construction and rehabilitation of roads. A very high net profit is determined by the failure of the investment objectives to materialize and does not reflect a favorable situation from an economic point of view.

Thus, it can be noticed a decisive influence of Top 5 on the aggregated performance of state owned companies, and in this context, in order to analyze more closely the evolution of the financial performance of the whole sector of state owned companies, in this analysis will be presented specific indicators both at the aggregate level and eliminating the influence of Top 5.

Table 1: The evolution of the number of SOEs that report financial statements by components									
	2007	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**
Autonomous administrations	128	117	150	152	173	180	196	193	135
Companies owned 100% by the state	385	358	333	389	437	431	479	479	500
National companies and societies	50	41	45	50	61	48	45	46	43
Other companies entirely owned by state or where the state is the major shareholder	62	51	51	57	130	132	158	154	161
State-owned companies, local and foreign state capital (state capital >= 50%)	13	5	25	9	44	40	56	54	66
State-owned companies, local and foreign private capital (state capital >= 50%)	21	7	20	9	16	18	20	28	23
State-owned companies and with local private capital (state capital >=50%)	105	85	87	82	98	85	103	102	102
State-owned companies and with foreign private capital (state capital >=50%)	5	4	11	12	15	12	21	22	17
State-owned companies, privatized in the reporting year	50	50	52	31	74	60	73	77	96
Total number of SOEs	819	718	774	791	1,048	1,006	1,151	1,155	1,143

Table 2: The evolution of certain financial indicators of Romanian companies that report financial statements considering the form of ownership

		2007	2008	2009	2010	2011	2012	2013	2014	2015
Number of companies	SOEs	819	718	774	791	1,048	1,006	1,151	1,155	1,143
	Total companies excluding financial sector	617,272	663,860	602,190	613,080	644,379	630,066	657,500	643,644	647,872
	Share of SOEs in total	0.13%	0.11%	0.13%	0.13%	0.16%	0.16%	0.18%	0.18%	0.18%
Total income, mil. lei	SOEs	51,953	56,660	50,756	55,022	58,511	49,853	51,208	44,487	48,578
	Total companies excluding financial sector	779,968	977,619	845,396	920,600	1,056,190	1,072,777	1,101,386	1,113,445	1,186,900
	Share of SOEs in total	6.66%	5.80%	6.00%	5.98%	5.54%	4.65%	4.65%	4.00%	4.09%
Gross value added, mil. lei	SOEs	19,048	21,744	20,454	22,881	24,202	22,339	25,131	25,220	26,687
	Total companies excluding financial sector	166,722	203,875	189,633	195,849	196,151	197,392	233,734	255,957	260,530
	Share of SOEs in total	11.42%	10.67%	10.79%	11.68%	12.34%	11.32%	10.75%	9.85%	10.24%
Gross value added in real terms, mil. lei (constant prices 2010)	SOEs	24,316	24,013	21,562	22,881	23,107	20,373	22,162	21,872	22,488
Employees number, thous. of persons	SOEs	406	390	364	364	343	327	321	297	291
	Total companies excluding financial sector	4,620	4,618	4,019	3,962	4,040	3,898	4,016	3,882	3,959
	Share of SOEs in total	8.79%	8.44%	9.05%	9.19%	8.49%	8.40%	8.00%	7.64%	7.36%
Labour productivity mil. lei /1,000 employees (constant prices 2010)	SOEs	59.89	61.57	59.24	62.86	67.37	62.30	69.04	73.64	77.28
Percentage change in labor productivity (relative to the previous year)	SOEs		2.8%	-3.8%	6.1%	7.2%	-7.5%	10.8%	6.7%	4.9%
Gross profit, mil. lei	SOEs	1,400	(1,026)	(2,777)	(2,101)	1,372	(561)	2,203	3,568	4,890
	SOEs, excluding best performing 5 comp.	(563)	(3,927)	(4,329)	(4,202)	(2,449)	(3,026)	(1,278)	(957)	(1,527)
	Private companies	43,008	23,513	19,914	27,934	10,421	15,623	22,570	27,479	42,753
Arrears, mil. lei	SOEs	13,690	17,294	34,405	28,012	26,251	25,363	26,217	24,369	21,226
	Private companies	44,050	53,127	62,406	69,193	88,882	91,536	99,052	93,508	94,874
	Total companies excluding financial sector	57,740	70,422	96,811	97,205	115,133	116,899	125,269	117,878	116,101
	Share of SOEs in total	23.71%	24.56%	35.54%	28.82%	22.80%	21.70%	20.93%	20.67%	18.28%
Arrears, % of GDP	SOEs	3.3%	3.3%	6.7%	5.2%	4.6%	4.3%	4.11%	3.6%	3.0%
	Private companies	10.5%	10.1%	12.2%	13.0%	15.7%	15.4%	15.54%	14.0%	13.3%

Table 3: Top 5 SOE's net profit

Top 5 net profit in 2015

	Company name	Net profit (mil. lei)
1	S.N.G.N. ROMGAZ S.A..	1,194.29
2	S.P.E.E.H. HIDROELECTRICA S.A.	899.41
3	S.N.T.G.N. TRANSGAZ S.A. MEDIAŞ	488.73
4	C.N.A.D.N.R. S.A.	368.80
5	C.N.T.E.E. TRANSELECTRICA S.A.	360.05
	Total	**3,311.29**

Top 5 net profit in 2014

	Company name	Net profit (mil. lei)
1	S.N.G.N. ROMGAZ S.A.	1,409.88
2	S.P.E.E.H. HIDROELECTRICA S.A.	941.54
3	S.N.T.G.N. TRANSGAZ S.A. MEDIAŞ	502.52
4	SOCIETATEA UZINA MECANICĂ CUGIR S.A.	442.01
5	C.N.A.D.N.R. S.A.	428.61
	Total	**3,724.56**

Top 5 net profit in 2013

	Company name	Net profit (mil. lei)
1	S.N.G.N. ROMGAZ S.A.	1,300.64
2	S.P.E.E.H. HIDROELECTRICA S.A.	901.58
3	S.N. NUCLEARELECTRICA S.A.	517.69
4	S.N.T.G.N. TRANSGAZ S.A. MEDIAŞ	429.93
5	C.N.A.D.N.R. S.A.	330.39
	Total	**3,480.24**

Top 5 net profit in 2012

	Company name	Net profit (mil. lei)
1	S.N.G.N. ROMGAZ S.A	1,244.05
2	S.N.T.G.N. TRANSGAZ S.A. MEDIAŞ	329.31
3	C.N.A.D.N.R. S.A.	174.14
4	COMPANIA NATIONALĂ DE CĂI FERATE CFR S.A.	144.65
5	COMPLEXUL ENERGETIC OLTENIA S.A.	118.33
	Total	**2,010.47**

Top 5 net profit in 2011

	Company name	Net profit (mil. lei)
1	TERMOELECTRICA S.A.	1,597.22
2	S.N.G.N.ROMGAZ S.A.	1,031.75
3	S.N.T.G.N. TRANSGAZ S.A.	379.57
4	C.N.A.D.N.R. S.A.	246.29
5	S.C. ELECTROCENTRALE BUCUREŞTI S.A.	106.85
	Total	**3,361.69**

Top 5 net profit in 2010

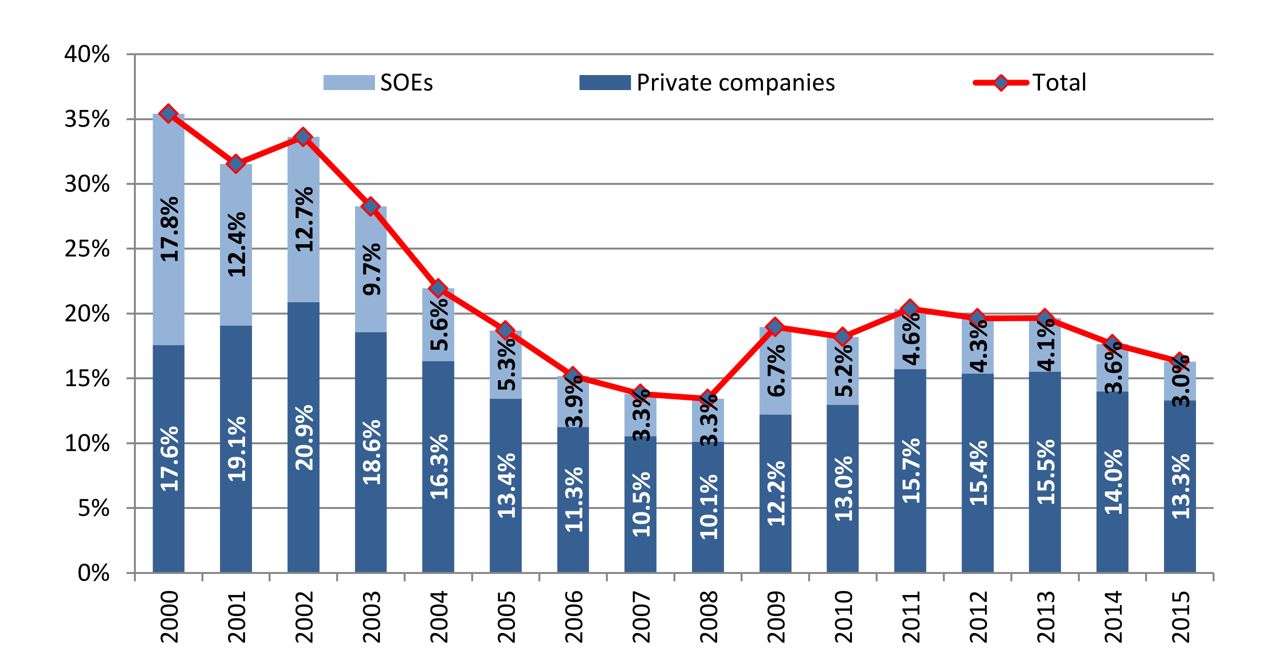
	Company name	Net profit (mil. lei)
1	S.N.G.N. ROMGAZ S.A.	651.21
2	S.N.T.G.N. TRANSGAZ S.A.	376.35
3	S.C. HIDROELECTRICA S.A.	292.37
4	S.C. ELECTROCENTRALE BUCUREŞTI S.A.	166.97
5	COMPANIA NATIONALĂ LOTERIA ROMÂNĂ S.A.	121.15
	Total	**1,608.05**

Source: MPF, based on balance sheets data submitted by the economic agents from non-financial sector

The state-owned companies' arrears as a percentage of GDP have declined starting with 2009, respectively from 6.7% of GDP to 3.0% of GDP in 2015 under the measures agreed with the international financial institutions in 2011-2015.

Since 2000, the share of the accumulated outstanding payments in the economy has considerably declined, from 35.4% of GDP in 2000 to 13.7% of GDP in 2008 (i.e. a reduction in nominal value amounting to 41.7 billion lei), but the financial crisis that started in 2008 led to their increase to a maximum of 20.7% of GDP in 2011, but without reaching the very high values from the early 2000s. The SOEs' and private companies' arrears as a percentage of GDP have declined starting with 2012 (19.6% of GDP), reaching a level of 16.3% of GDP in 2015. The state-owned companies' arrears as a percentage of GDP have declined starting with 2009, respectively from 6.7% of GDP to 3.0% of GDP in 2015 under the measures agreed in the context of the balance of payments agreements with the international financial institutions (European Commission, IMF, World Bank), established in 2011-2015. These measures aimed at framing the arrears in the quarterly indicative targets and included budget transfers, placing SOEs into voluntary liquidation or insolvency or arrears' conversion into shares.

Figure 1: The evolution of SOEs’ and private companies’ arrears (% of GDP)

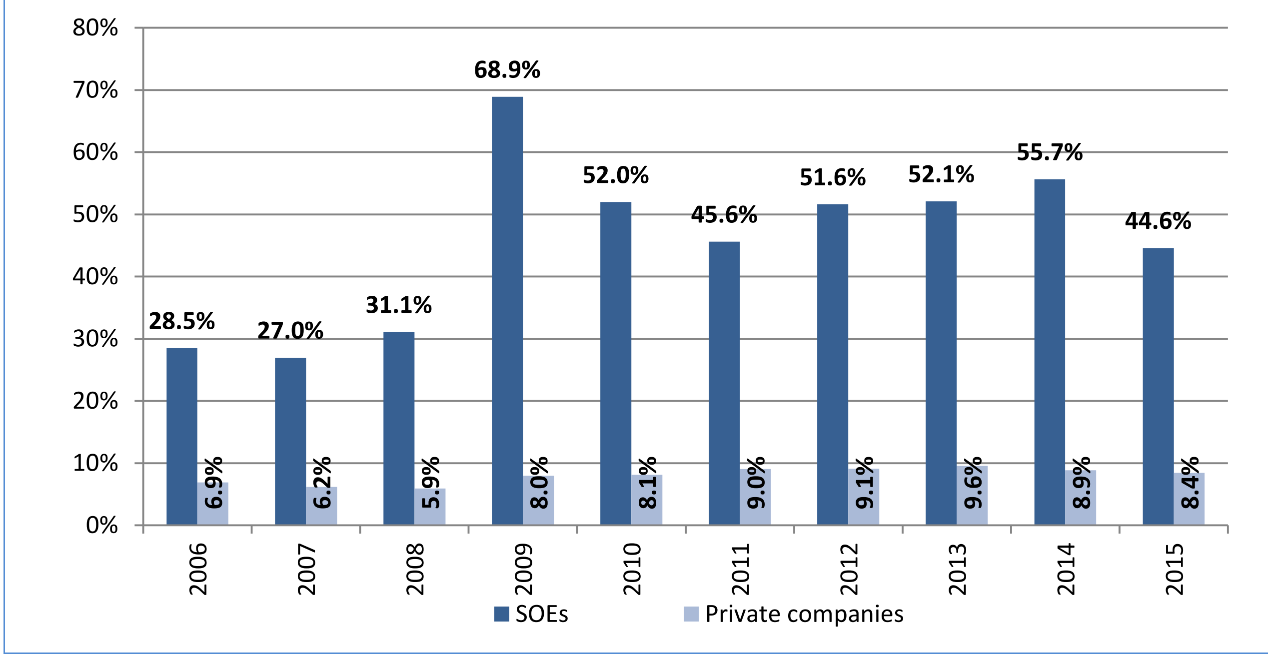


Source: MPF, based on balance sheets data submitted by the economic agents from non-financial sector

In the private sector the share of arrears had declined since 2012, reaching a level of 13.3% of GDP at the end of 2015.

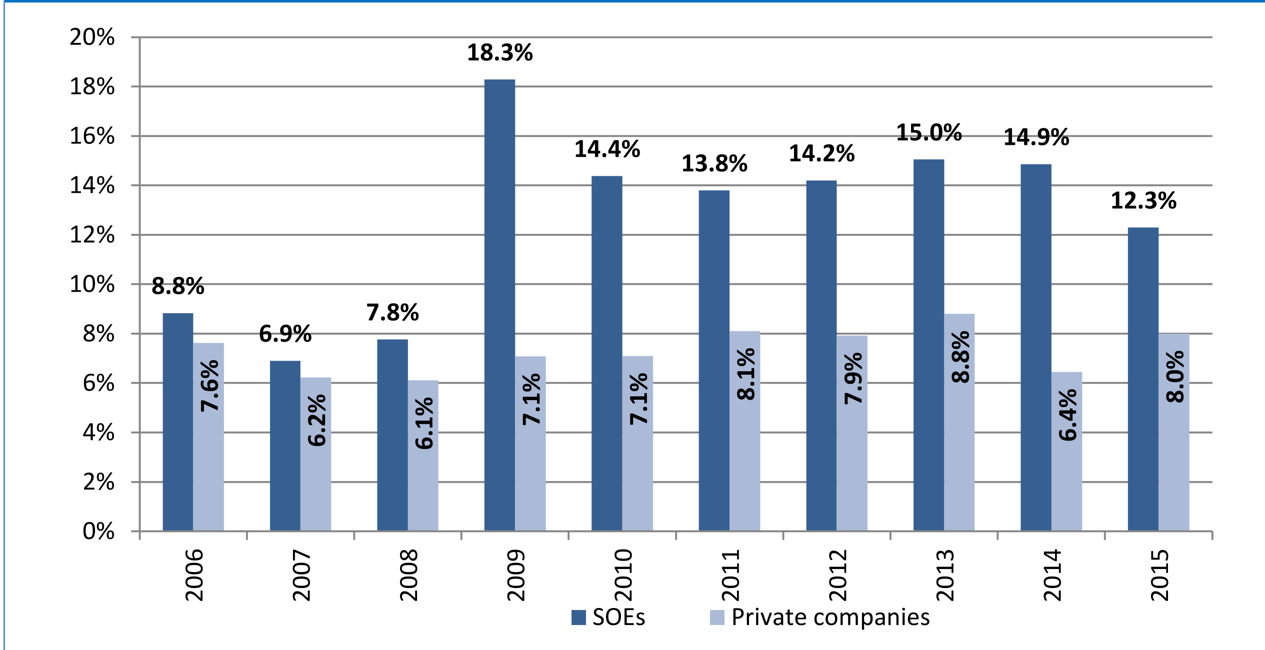
In the private sector the share of arrears recorded a peak in 2002 (20.9%), while during 2003-2008 it has been reduced significantly to 10.1% of GDP in 2008. The effects of the financial crisis led to an accumulation of arrears in 2009-2011 (from 12.2% of GDP to 15.7% of GDP), since 2012 being registered a decrease to a level of 13.3% of GDP at the end of 2015.

Figure 2: Arrears (% of turnover)



Source: MPF, based on balance sheets data submitted by the economic agents from non-financial sector

Figure 3: Arrears (% of total assets)



Source: MPF, based on balance sheets data submitted by the economic agents from non-financial sector

The evolution of the share of arrears in the turnover for the state-owned companies registered a significant reduction from the peak of 68.9% in 2009 to 44.6% at the end of 2015, while during the same period the private sector has experienced a slightly deterioration of this indicator (from 7.1% in 2009 to 8% in 2015).

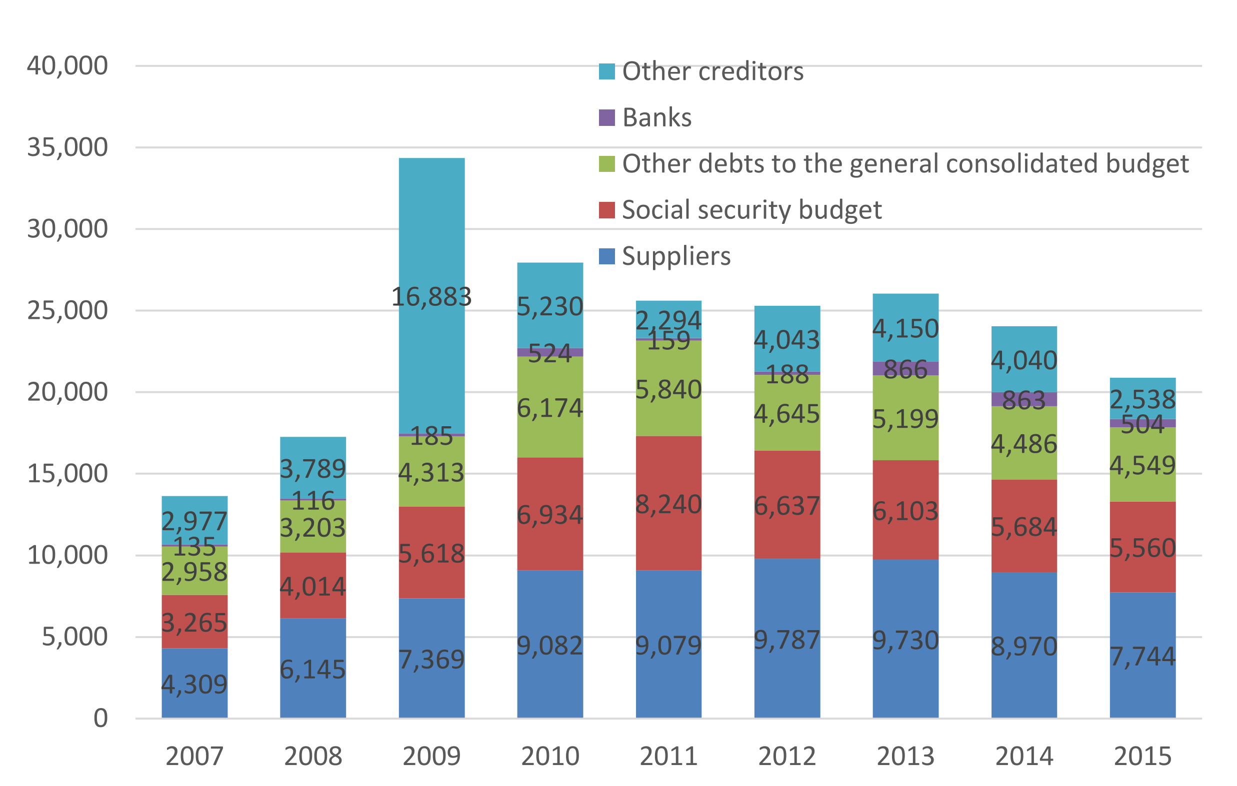
From the perspective of the structure by creditor, in 2015 the state-owned companies recorded a share of 48% of total arrears to the general consolidated budget and 36% of the total arrears to suppliers, while private companies have cumulated 50% of the total arrears to suppliers and 22% to the general consolidated budget.

With the onset of the financial crisis, the share of arrears in the turnover reached a peak in 2009, when the share of SOEs' arrears in the turnover recorded a significant jump compared to the previous year of over 100% (from 31.1% in 2008 to 68.9%), while the share of private companies' arrears in the turnover recorded a lower jump (from 5.9% to 8% of the turnover). After a significant reduction in the share of arrears in the turnover in 2009-2011 (with of 23.3 pp), the state-owned companies were on a upward trend in the share of arrears in the turnover from 2012 to 2014, this ratio reaching a level of 55.7% at the end of 2014 (compared to 45.6% in 2011), then in 2015 registering a significant reduction (11 pp, to 44.6%) below the level of 2011. Note that the decreasing share of arrears in the turnover for the state-owned companies in 2015 compared to the previous year can be explained by a rapid decline in the value of arrears (-13%) and an increase in turnover (+9%). In nominal terms, in 2015, unlike the state-owned companies that have managed to reduce arrears by 13%, the private companies' arrears increased by 1% compared to the previous year, but as the private companies' turnover increased by 7%, the share of arrears in the turnover reduced to 8.4% from 8.9% in the previous year.

In addition, most of the state owned companies' arrears in 2015 are directed towards the general consolidated budget (48% of total arrears and among these 55% are to the social security budget), followed by arrears to suppliers (accounting for 36% of total arrears, of which 74% represents outstanding payments over 1 year), unlike private companies that have arrears mostly to suppliers (50% of total arrears, of which 61% represents outstanding payments over 1 year) and a share of 22% of total arrears to the general consolidated budget.

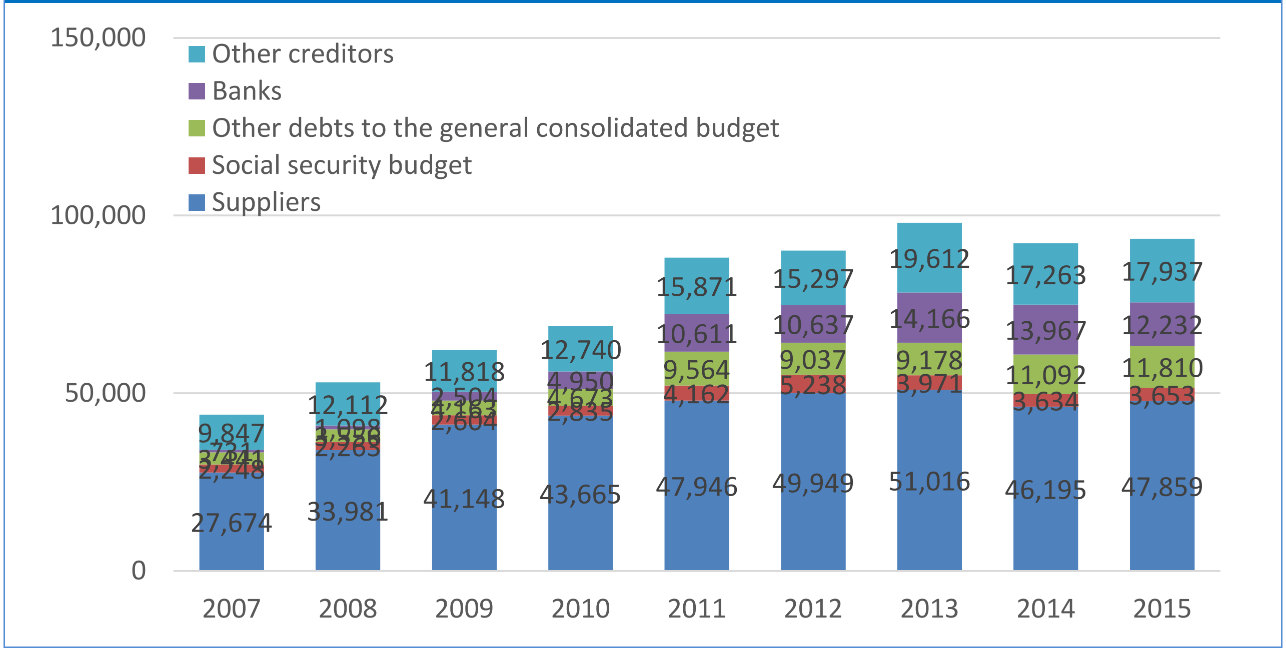
The total state owned companies' outstanding debts towards the general consolidated budget amounted 10.1 billion lei (1.4% of GDP) in December 2015, of which 5.6 billion lei were towards the social security budgets (0.8% of GDP). In general, the state-owned companies do not pay on time their debts to the general consolidated budget (especially to the social security budgets) and to other state owned companies. The suppliers were ranked the second place among creditors of SOEs in 2015, the amount due by them being 7.7 billion lei (1.1% of GDP). Compared to the previous year, in 2015 the share of SOEs' arrears to the suppliers and to the general consolidated budget declined with 13.7% and 1%.

Figure 4: Structure of arrears – SOEs (million lei)



Source: MPF, based on balance sheets data submitted by the economic agents from non-financial sector

Figure 5: Structure of arrears – private companies (million lei)



Source: MPF, based on balance sheets data submitted by the economic agents from non-financial sector

The accumulation of outstanding payments by the companies in the public sector is concentrated in the following sectors: mining, distribution of heat and chemical industry and in a proportion of about 63% is attributable to the first 10 SOEs ranked in terms of outstanding payments in total economy. Within the Top 10, the first 3 companies with the largest outstanding debts have accumulated over the past three years about 70% of the total arrears for the Top 10.

Besides direct fiscal consequences generated by SOE's arrears – revenue shortfalls to the general consolidated budget - the accumulation of outstanding payments towards the private sector is likely to create liquidity problems and to hamper economic growth. The top 10 companies in terms of outstanding payments account for over 62,9% of the total arrears of SOEs, the arrears being particularly high in the mining, distribution of heat and chemical sectors. Like in the previous years, the first three companies in the top are Compania Națională a Huilei, RADET București and S.C. Oltchim S.A. which have aggregate arrears representing over 71% of the top 10's total arrears, or 45% of the total arrears of the public sector in 2015. The first 10 companies in the top of bad payers have accumulated at the end of 2015 about 72% of the total arrears of state owned companies towards the general consolidated budget, standing out Compania Națională a Huilei with over 60% of total debts of top 10 and a share of 23% of the total arrears of state owned companies.

Table 4: Top 10 SOE's arrears

Top 10 arrears in Dec 2015

	Company name	Arrears (mil. lei)
1	COMPANIA NAȚIONALĂ A HUILEI S.A. ÎN LICHIDARE	4,865.05
2	RADET BUCUREȘTI	3,407,85
3	S.C. OLTCHIM S.A.	1,224.,82
4	S.C. COMPLEXUL ENERGETIC HUNEDOARA SA	662.83
5	COMPANIA NAȚIONALĂ A METALELOR PRETIOASE ȘI NEFERO	572.35
6	SOCIETATEA ROMÂNĂ DE TELEVIZIUNE	559.39
7	CENTRALA ELECTRICĂ DE TERMOFICARE IAȘI (C.E.T.) S.A	557.35
8	SOCIETATEA NAȚIONALĂ A CĂRBUNELUI S.A.	518.80
9	ELECTROCENTRALE BUCURESTI S.A.	498.46
10	S.N.T.F.C. CFR CĂLĂTORI S.A.	490.28
	% total	**62.93%**

Top 10 arrears in Dec 2014

	Company name	Arrears (mil. lei)
1	COMPANIA NAȚIONALĂ A HUILEI S.A. ÎN LICHIDARE	4,865.05
2	S.C. OLTCHIM S.A.	3,397.19
3	RADET BUCUREȘTI	3,157.86
4	REGIA AUTONOMĂ PENTRU ACTIVITĂȚI NUCLEARE R.A.	1,097.06
5	COMPANIA NAȚIONALĂ A METALELOR PRETIOASE ȘI NEFERO	570.30
6	SOCIETATEA ROMÂNĂ DE TELEVIZIUNE	553.10
7	CENTRALA ELECTRICĂ DE TERMOFICARE IAȘI (C.E.T.) S.A	545.38
8	SOCIETATEA NAȚIONALĂ A CĂRBUNELUI S.A.	518.77
9	FORTUS S.A.	405.21
10	CENTRALA ELECTRICĂ DE TERMOFICARE BRAȘOV S.A.	394.55
	% total	**63.62%**

Top 10 arrears in Dec 2013

	Company name	Arrears (mil. lei)
1	COMPANIA NAȚIONALĂ A HUILEI SA ÎN LICHIDARE	4,978.38
2	S.C. OLTCHIM S.A.	3,372.78
3	RADET BUCUREȘTI	2,763.47
4	CNCF CFR S.A.	1,051.87
5	S.N.T.F.C. CFR CĂLĂTORI S.A.	914.45
6	REGIA AUTONOMĂ PENTRU ACTIVITĂȚI NUCLEARE	651.71
7	C.N.A.D.N.R. S.A.	592.86
8	C.N.M.P.N REMIN S.A.	580.95
9	SOCIETATEA ROMÂNĂ DE TELEVIZIUNE	547.76
10	CENTRALA ELECTRICĂ DE TERMOFICARE IAȘI (C.E.T.) S.A	525.63
	% total	**60.95%**

Top 10 arrears to consolidated general budget in Dec 2015

	Company name	Arrears (mil. lei)
1	COMPANIA NAȚIONALĂ A HUILEI S.A. ÎN LICHIDARE	4,851.92
2	S.C. COMPLEXUL ENERGETIC HUNEDOARA SA	531.69
3	SOCIETATEA NAȚIONALĂ A CĂRBUNELUI S.A.	505.68
4	SOCIETATEA ROMÂNĂ DE TELEVIZIUNE	459.49
5	CENTRALA ELECTRICĂ DE TERMOFICARE IAȘI (C.E.T.) S.A	419.91
6	MOLDOMIN S.A.	261.41
7	SOCIETATEA NAȚIONALĂ A CĂILOR FERATE ROMÂNE R.A.	241.71
8	SC ELECTROCENTRALE CONSTANȚA	197.58
9	REGIA AUTONOMĂ PENTRU ACTIVITĂȚI NUCLEARE RA	174.39
10	AVERSA S.A.	160.93
	% total	**77.20%**

Top 10 arrears to consolidated general budget in Dec 2014

	Company name	Arrears (mil. lei)
1	COMPANIA NAȚIONALĂ A HUILEI S.A. ÎN LICHIDARE	4,851.92
2	SOCIETATEA NAȚIONALĂ A CĂRBUNELUI S.A.	505.66
3	SOCIETATEA ROMÂNĂ DE TELEVIZIUNE	454.51
4	CENTRALA ELECTRICĂ DE TERMOFICARE IAȘI (C.E.T.) S.A.	407.93
5	SC COMPLEXUL ENERGETIC HUNEDOARA S.A.	293.48
6	MOLDOMIN S.A.	260.77
7	SOCIETATEA NAȚIONALĂ A CĂILOR FERATE ROMÂNE R.A.	241.74
8	SC ELECTROCENTRALE CONSTANȚA	185.97
9	REGIA AUTONOMĂ PENTRU ACTIVITĂȚI NUCLEARE RA	175.80
10	INTERVENȚII FEROVIARE S.A.	175.01
	% total	**74.27%**

Top 10 arrears to consolidated general budget in Dec 2013

	Company name	Arrears (mil. lei)
1	COMPANIA NAȚIONALĂ A HUILEI SA ÎN LICHIDARE	4,968.50
2	SOCIETATEA NAȚIONALĂ A CĂRBUNELUI SA	505.37
3	SOCIETATEA ROMÂNĂ DE TELEVIZIUNE	501.87
4	COMPANIA NAȚIONALĂ ROMARM S.A. BUCUREȘTI FILIALA S	453.54
5	S.C. ELECTROCENTRALE BUCUREȘTI S.A.	421.53
6	CENTRALA ELECTRICĂ DE TERMOFICARE IAȘI (C.E.T.) S.A	388.18
7	SNCFR R.A.	267.51
8	S.C.MOLDOMIN S.A.	263.03
9	S. U.M.SADU S.A.	183.17
10	S.C. INTERVENȚII FEROVIARE S.A.	168.99
	% total	**71.86%**

Source: MPF, based on the balance sheets submitted by the economic agents from non-financial sector

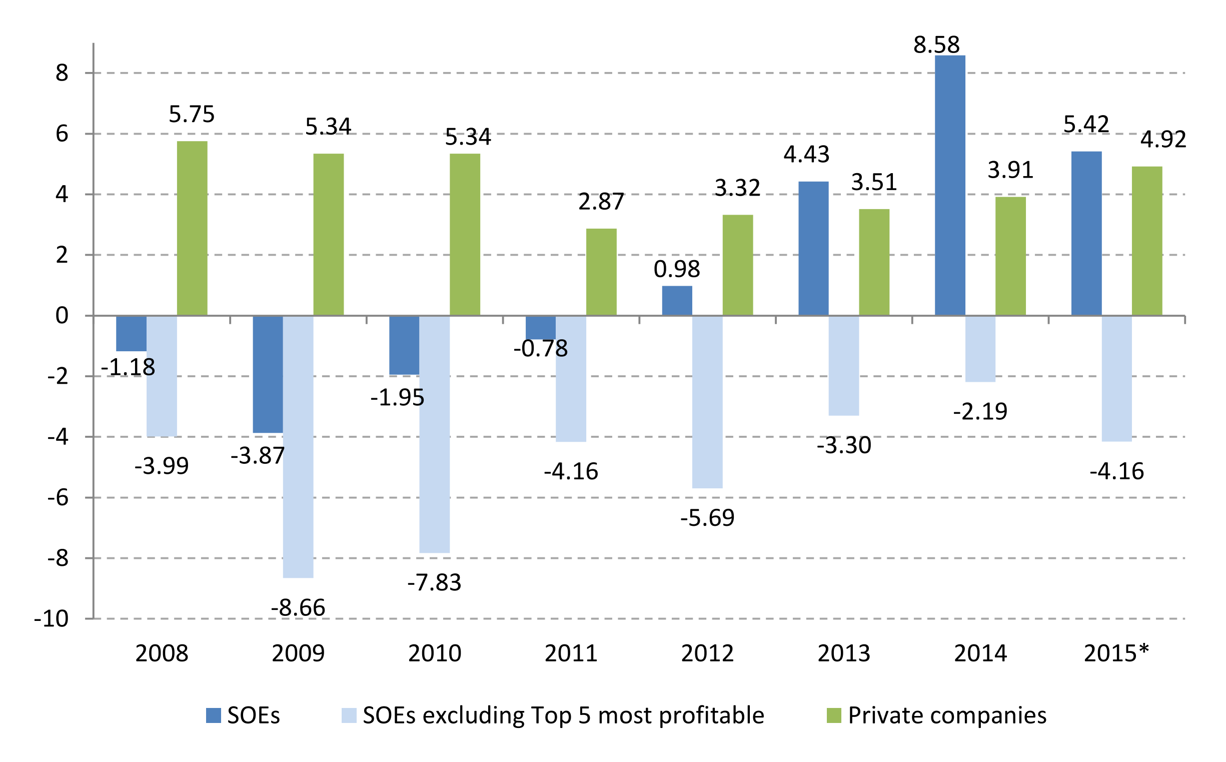
Table 5: SOEs arrears evolution by type of company								
Total arrears (million lei)	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**
Autonomous administrations	1,130.70	1,411.14	2,019.32	3,153.75	3,662.52	4,541.85	5,515.00	5,110.99
Companies owned 100% by the state	6,802.97	8,102.41	9,648.19	7,670.87	5,605.94	6,341.70	5,378.51	5,174.00
National companies and societies	7,945.22	23,710.69	15,032.90	12,773.24	10,350.17	8,658.11	7,300.42	7,071.76
Other state – owned companies or majority-state – owned companies	77.60	184.32	298.81	769.32	879.87	1,484.98	1,187.36	914.92
State – owned companies, local and foreign state capital (state capital >= 50%)	5.52	1.05	0.26	46.28	3.27	0.81	1.76	2.60
State –owned companies, local and foreign private capital (state capital >=50%)	717.28	35.38	78.59	330.44	2,551.90	3,412.91	3,423.14	1,229.97
State –owned companies and with local private capital (state capital >=50%)	609.37	957.00	932.08	1,504.96	2,308.42	1,775.47	1,560.32	1,699.95
State –owned companies and with foreign private capital (state capital >=50%)	0.86	1.66	0.37	0.47	0.43	0.77	1.17	2.80
State –owned companies, privatized in the reporting year	4.81	1.38	1.79	2.06	0.62	0.51	1.80	19.30
TOTAL arrears	**17,294.33**	**34,405.02**	**28,012.31**	**26,251.39**	**25,363.13**	**26,217.11**	**24,369.48**	**21,226.29**

Source: MPF, based on the balance sheets submitted by the economic agents from non-financial sector

The rate of the operating surplus for state-owned companies has deteriorated in 2015 compared to the previous year, from 8.58% to 5.42%, remaining, however, higher than in the private sector. Excluding the Top 5 companies, the indicator has recorded negative values throughout the period 2008-2015 showing a persistently lack of performance of the state companies.

The year 2015 marked an unfavorable development of the aggregate financial performance of the state owned companies (the profits resulting from the cancellation of a part of SC Oltchim S.A.' debt were excluded). Considering the indicator rate of operating surplus, which measures the profitability of the core business by reporting incomes before the payment of interest and profit tax to the total revenue, we can notice that its level dropped by 3.16 percentage points compared to 2014, to 5.42%, however being higher than that registered by private companies (4.92%). This development was determined mainly by reduction in the operating profits by about 31%, while the total revenues increased by 9.2%. By excluding the Top 5 most profitable state companies, the indicator is placed in the negative territory throughout the analyzed period, the level registered in 2015 being -4.16%, the operating surplus also worsening compared to the previous year. The gap recorded when we exclude the best performing five state owned companies is significant, suggesting an extremely high impact of these five companies on the aggregate level. In addition, the top five companies manage to record a performance which counterbalance the underperformance of the other state owned companies, positively adjusting the average of the whole sector of state-owned companies.

Figure 6: Operating surplus ratio (%)



Source: MPF, based on the balance sheets submitted by the economic agents from non-financial sector

*Note: Operating surplus (%)=Operating surplus/ Total income * 100*

**In 2015 at the level of SOEs was excluded the profit of S.C. Oltchim S.A. originated from the cancellation of a part of debt.*

*** The operating surplus does not include the interest expenses and those related to income taxes.*

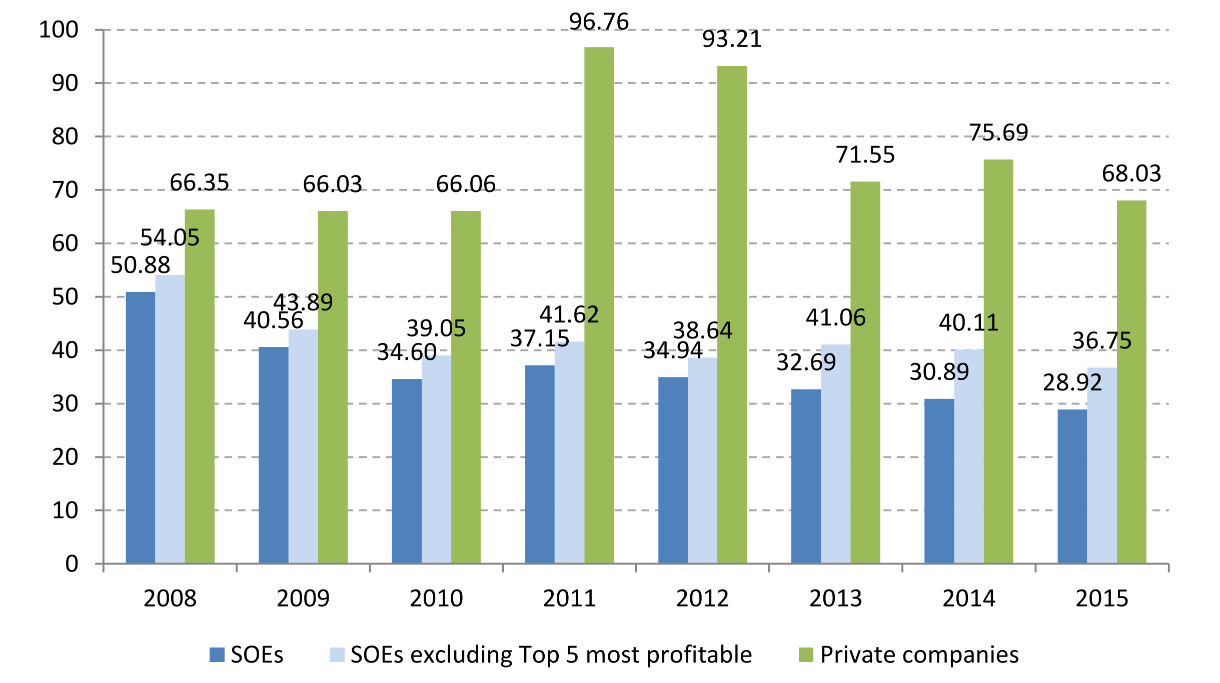
The ability of the state companies to cover their debts improved at the aggregate level, but there is an uneven distribution of indebtedness, some of state companies having very low debt, while others being heavily indebted. Overall, the share of debt in total assets of the state companies remains far

Regarding state companies' ability to cover their debts with the available assets, reflected by the degree of solvency, there has been a favorable development, the share of debt in total assets dropped to 28.92% in 2015 from 30.89% in the previous year, due to reducing total debt, the level being significantly lower than the 68.03% recorded by the private companies. Also, the latter reduced their debt ratio in the past year compared to 2014 when they registered a degree of solvency of 75.69%. This result is influenced, however, by the uneven distribution of indebtedness at the level of the state companies, among which are found very large companies with a very low degree of debt. Thus, excluding the top five best performing companies, the solvency ratio was reduced from

below compared to the level of private ones.

40.11% to 36.75% due to a higher growth of the assets relative to debts. It is worth noting that at the level of all state companies, the solvency ratio falls by 1.97 pp compared to the previous year, while excluding the top five companies, the solvency ratio drops by 3.36, which highlights that in 2015 the debt reduction was driven by lowering the debt of the other state companies.

Figure 7: Solvency ratio (%)



Source: MPF, based on the balance sheets submitted by the economic agents from non-financial sector

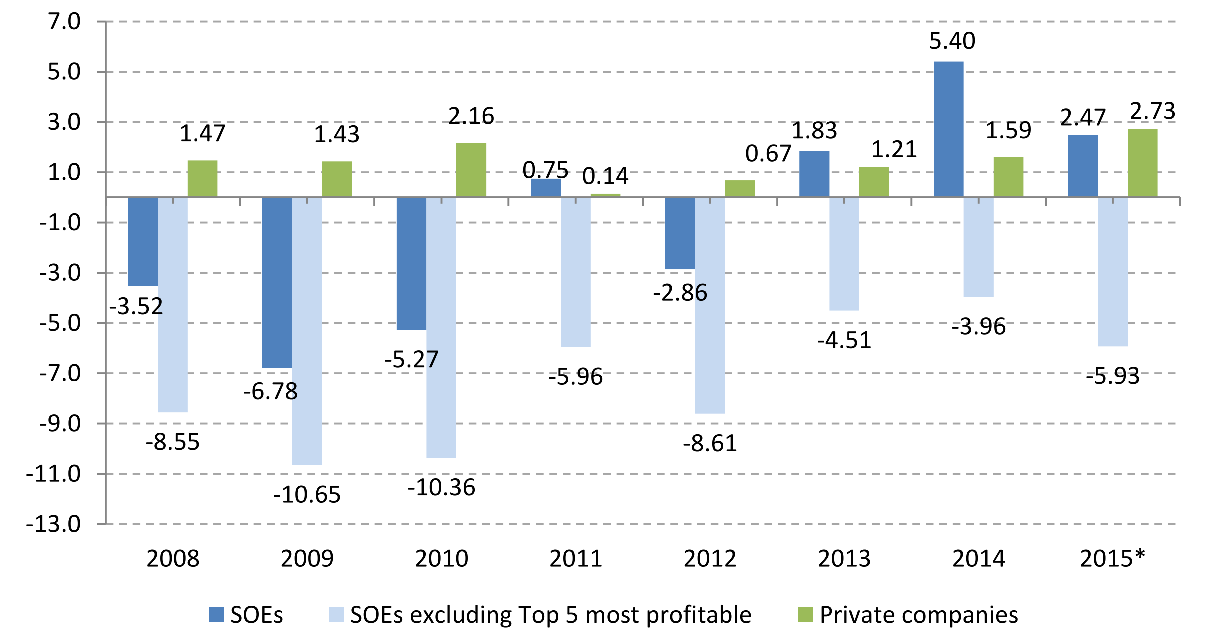
*Solvency ratio (%)=Total debt / Total assets * 100*

The profit margin of state companies has deteriorated significantly in 2015 compared to 2014, from 5.4% to 2.5%, the development being opposite to that registered in the private sector and also to the positive dynamics of the

The worsening of the operating position of state companies is visible at the level of the profit margin that decreased significantly from 5.4% in 2014 to 2.47% in 2015. Moreover, the profit margin for state companies is lower than that registered by the private companies (2.73% in 2015, superior by 1.14 percentage points compared to the previous year). Thus, when excluding the Top five companies, the profit margin recorded negative values throughout the analyzed period, reaching -5.93% in 2015, respectively it worsened by 1.97 percentage points compared to the previous year, but showing an improvement of 2.68 percentage points compared *economic activity.*

with 2012. The differences between the rate of operating surplus and the profit margin is explained by the fact that the latter indicator takes into account the financial and the extraordinary results. Thus, due to the negative impact of interest expenses on the net profit, throughout the period under review, the profit margin has lower values compared to the operating surplus.

Figure 8: Profit margin (%)



Source: MPF, based on the balance sheets submitted by the economic agents from non-financial sector

*Note: Profit margin (%)=Net result/Total income*100*

**In 2015 at the level of SOEs was excluded the profit of S.C. Oltchim S.A. originated from the cancellation of a part of debt.*

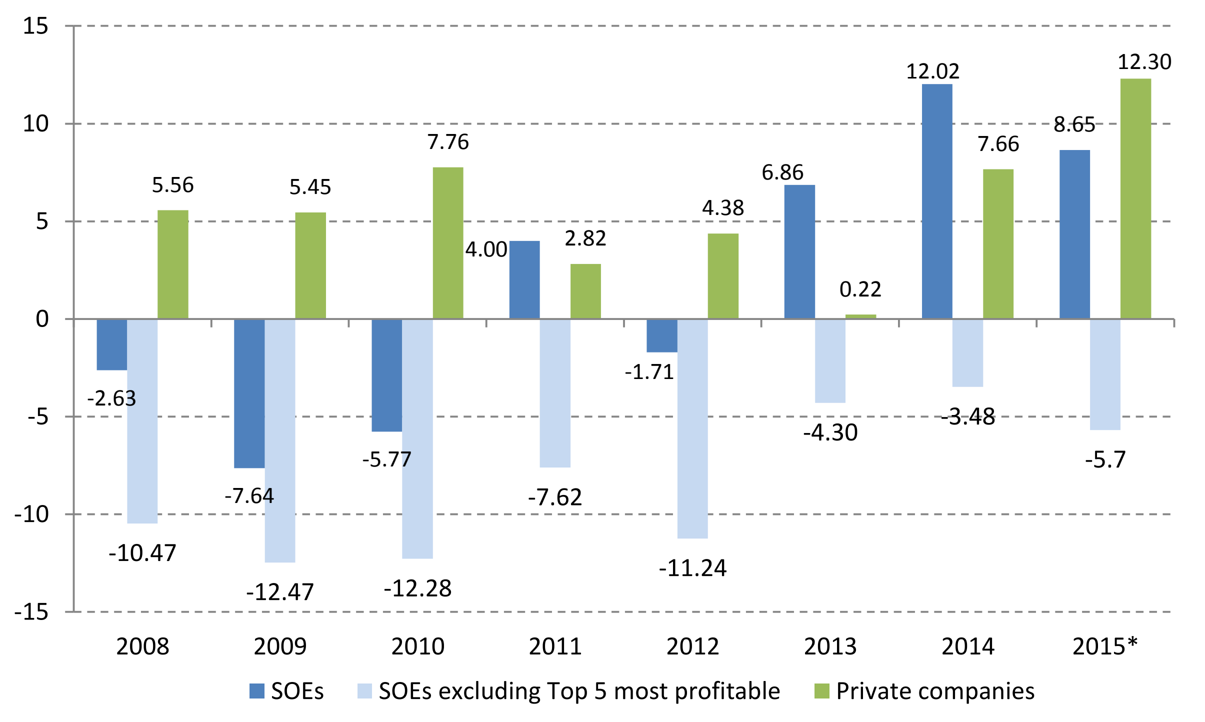
The indicator gross profit per 1,000 employees has deteriorated at the level of the state companies despite the reduction in the number of employees in 2015 compared to the previous year, both at the aggregate level and by excluding the Top 5, being

The gross profit per 1,000 employees is an indicator that measures the average revenue generated by each 1,000 employees of the company, representing a measure of the efficiency in the use of its own employees to maximize profits. The indicator registered a decrease in 2015 compared to the previous year for the state companies, the gross profit per 1,000 employees being in 2015 8.65 thousand lei, thus lower than in the previous year by 28%. Also, the level of gross profit per 1,000 employees for the sector of state companies is about 30% lower than in the private sector in 2015. The

significantly lower than in the private sector, the latter registering a trend of accelerated growth.

development of the indicator for the state companies, however, is favored by the top five best performing companies in terms of profit, accounting for a gross profit of 4,088 million lei in 2015, while other state companies recorded losses of 1,527.7 million lei. Consequently, the gap between the gross profit corresponding to the Top 5 companies and the other is considerable, significantly influencing the overall assessment of profitability of the state companies in Romania in a positive sense. Excluding the Top 5, the deterioration is widening compared to last year, as the gross profit per 1,000 employees decreasing at -5.7 thousand lei compared to 2014, when it registered a value of -3.5 thousand lei. The year 2015 represents the maximum of the period in terms of the value of gross profit per 1,000 employees registered by the private sector (12.3 thousand lei), showing a significant improvement compared to 2014, when the indicator recorded a value of 7.66 thousand lei (+ 60.5%).

Figure 9: Gross profit per 1,000 employees (thousands lei)



Source: MPF, based on the balance sheets submitted by the economic agents from non-financial sector

**In 2015 at the level of SOEs was excluded the profit of S.C. Oltchim S.A. originated from the cancellation of a part of debt.*

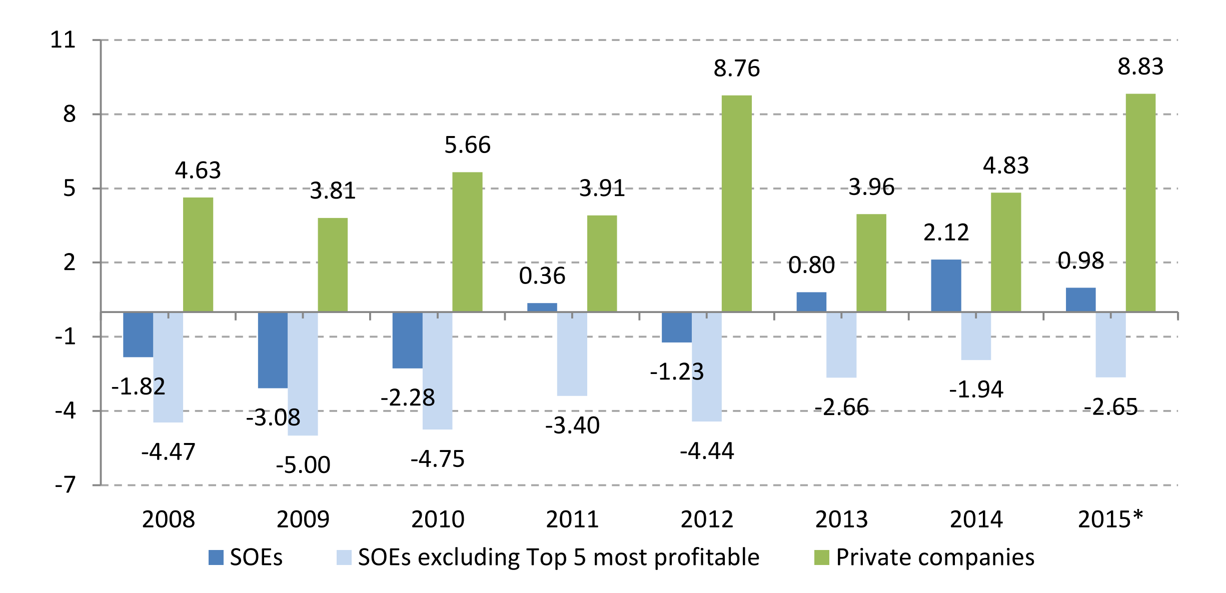
ROE is at a much lower level in the state companies compared with the private ones, 1% versus 8.8% in 2015. Thus, the ability of the state to generate value for shareholders is reduced. Moreover, this indicator decreased notably from the previous year, while private companies recorded a strong upward trend.

ROA of SOEs experienced a similar trend, decreasing by about 0.7% in 2015 from around 1.5% in 2014, showing a reduced capacity of the assets in state companies to generate profits. In the same period, ROA of private companies has increased from 1.2% to 2.8%.

The return on equity (ROE) and return on assets (ROA) are some of the most conclusive indicators of a company's profitability, ROE measuring the efficiency of equity in terms of the profit earned and ROA the efficiency of assets relative to the same reference. Therefore, ROE shows how many lei generates in the form of profits a leu invested in equity by the shareholders, while ROA indicates how many lei a leu invested in assets transform into profits.

In 2015, at the level of state companies was recorded a deterioration both in terms of ROE and ROA, as they stood at half of the level recorded in 2014, due to an unfavorable dynamic of the net profit compared to the previous year, the state companies recording a total net profit of 1,200 million lei in 2015 while in 2014 this indicator recorded a value of 2,401.3 mil. lei (-1,201.3 million. lei, respectively -50%). The return on equity for the state companies has reached a level of 0.98%, lower than in 2014 when it was 2.12% (-54%), while the return on assets was by 0.69% lower than the level recorded in the previous year of 1.46% (-53%), this dynamic being influenced positively by the profit of the Top 5 state companies. Excluding their influence, the change in the two indicators also shows a deterioration in 2015 compared to 2014, registering a level of ROE -2.65% compared to -1.94% in 2014, respectively -1.68% ROA versus -1.16% in the previous year. At the level of the private companies, the return on equity increased significantly, this indicator reaching a value of 8.8% compared to 4.8% in the last year, while the return on assets stood at a level significantly higher than in 2014 (2.8% compared to 1.2%), their net profit standing at 33,459.1 million lei in 2015, compared to 17,020.2 million lei in 2014 (+16,439 million lei, respectively +96.6%).

Figure 10: ROE (%)

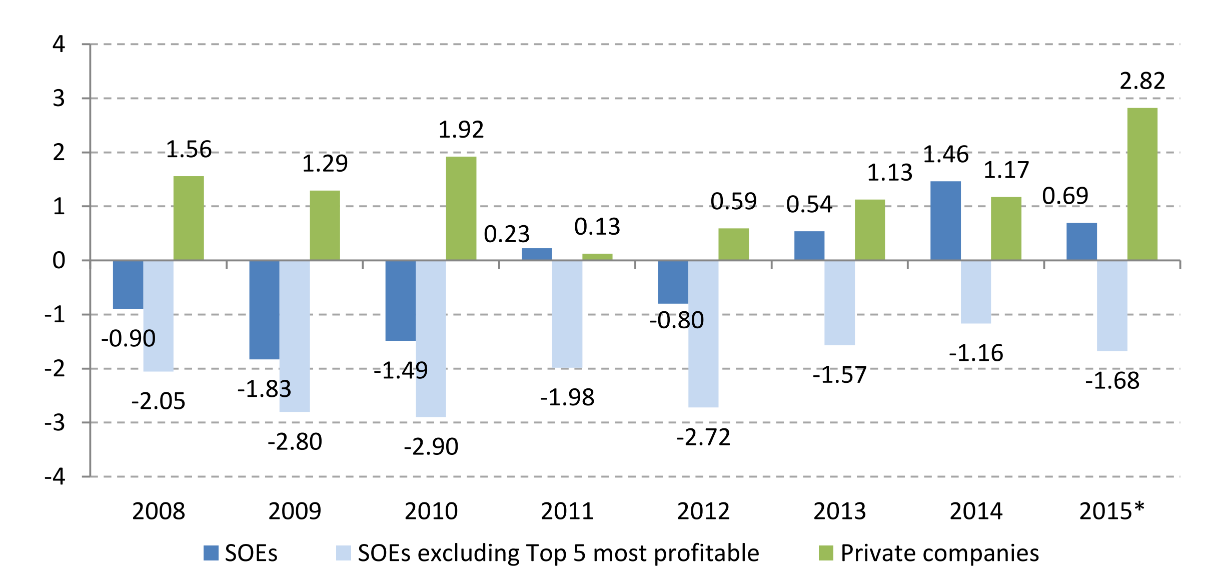


Source: MPF, based on the balance sheets submitted by the economic agents from non-financial sector

*Note: ROE(%) = Net Profit / Equity*100*

**In 2015 at the level of SOEs was excluded the profit of S.C. Oltchim S.A. originated from the cancellation of a part of debt.*

Figure 11: ROA (%)



Source: MPF, based on the balance sheets submitted by the economic agents from non-financial sector

*Note: ROA(%)=Net income / Total assets*100*

**In 2015 at the level of SOEs was excluded the profit of S.C. Oltchim S.A. originated from the cancellation of a part of debt.*

The interest coverage ratio of the state companies registered a significant boost from 3.23 to 13.1, but this evolution has to be interpreted with caution, being attributable to special circumstances.

The position of the private companies from the perspective of the ability to cover the interest expenditures is better compared to that of the state companies. They recorded a sustainable growth of this indicator in the context of increasing profitability and lower interest expenses.

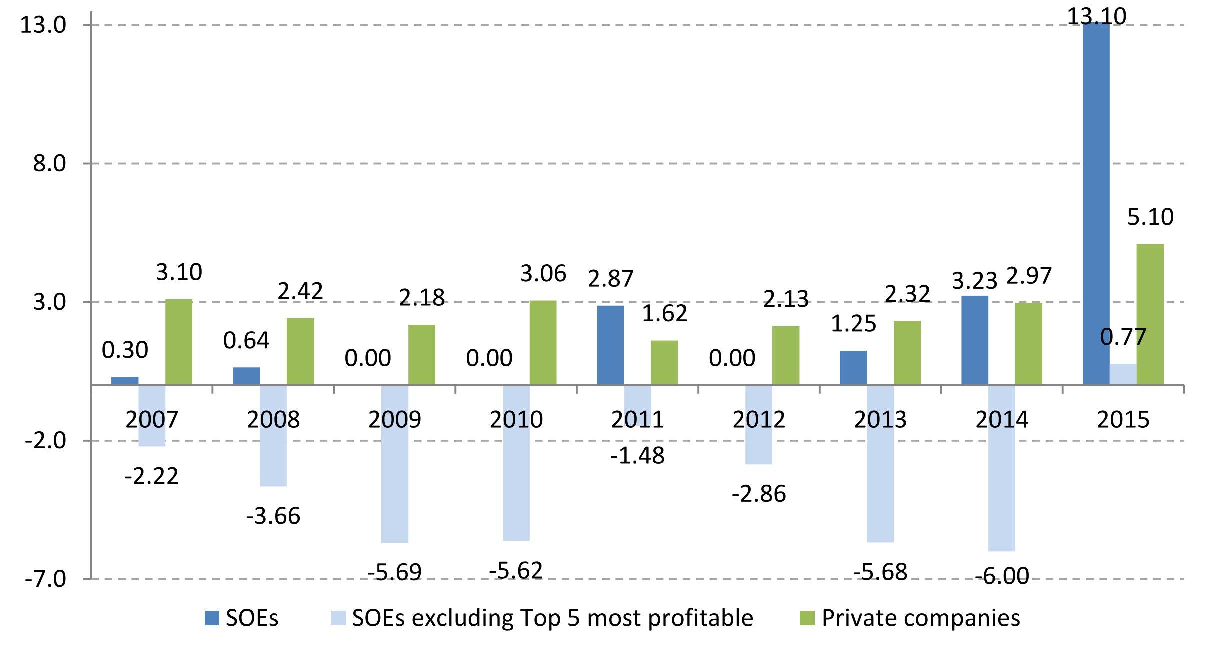
The interest coverage ratio is a solvency indicator that measures a company's ability to realize the payment of interest on the accumulated debt. In essence, this indicator shows how many times a company could pay the interest owed with its available earnings. The indicator is calculated by dividing company's revenues company before interest and taxes (EBIT) by the amount of interest on debts payable over a period of one year. An interest coverage ratio below 1 indicates that the company does not generate enough income to cover interest expenses and will have to use their reserves to cover the liabilities.

Both state and private companies recorded during the 2015 a significant increase of the interest coverage ratio, which reached a peak last year, surpassing even the 2007-2008 economic boom. The interest coverage ratio for the state companies recorded a significant boost from 3.23 to 13.1, being 4 times higher than the one recorded in 2014, mainly due to the significant increase in adjustments for provisions (+294%) and the increase by 31% of the operating result and the decrease of 23% of the interest costs due to the reduction of nominal interest rates. It is important to note that at the level of state companies the massive improvement of this indicator should be interpreted with caution, being determined by the fact that even if the increase expenses with provisions adversely affected the operating result, it did not involve an actual payment of the sums, their amount temporarily increasing the level of this indicator. When the risks will materialize and the amounts will be paid, both companies' liquidity and interest coverage rate will further deteriorate. Specifically, adjustments for provisions recorded in 2015 an increase of 1.85 billion lei compared to the previous year, mainly because of Hunedoara Energy Complex S.A. (+1.3 billion lei compared to 2014), a company which is in a very difficult financial situation.

Regarding the interest coverage ratio recorded in the state companies excluding Top 5, the value is back in positive territory, reaching in 2015 a level of 0.77. The value of this indicator is still below the minimum acceptable and suggests that the companies do not generate enough revenue to pay the interest owed. Moreover, the improvement in this indicator was driven primarily by higher expenses with provisions which have not yet affected the companies' liquidity, while the operating result as the financial result remained in negative territory in 2007-2015.

The position of the private companies regarding their ability to pay interest expenditure is better compared to that of state companies. They grew at a lower rate (from 2.97 to 5.10), but represents a more sustainable rate of this indicator in terms of both profitability growth and the reduction of interest expenditures.

Figure 12: Interest coverage ratio



Source: MPF, based on the balance sheets submitted by the economic agents from non-financial sector

Note: Interest coverage ratio = (Profit or current loss + Financial profit or loss + Adjustments for provisions - Other income + Other expenses + Interest expenses – Interest incomes)/Interest expenses

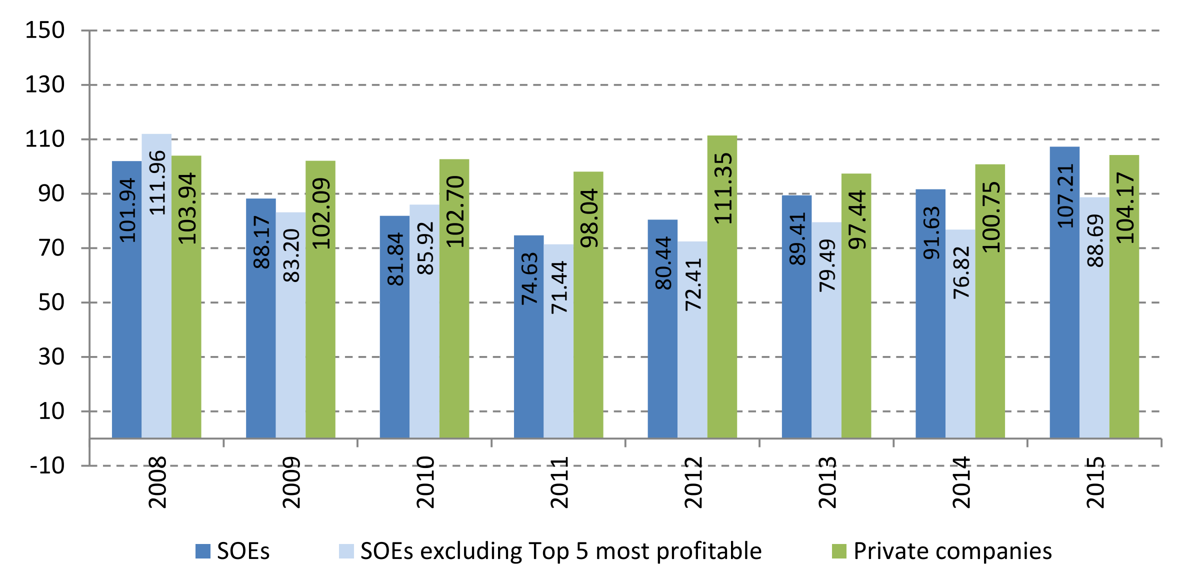
In 2015 the liquidity ratio of the state companies has increased significantly and is situated at a level higher than that registered in the private companies and even than that recorded in the economic boom years.

Excluding the Top 5 best performing companies, the liquidity ratio recorded in 2015 compared to 2014 an increase of 12 pp, but remains at a level lower than the recommended threshold.

The current liquidity ratio is an indicator that measures the company's ability to pay its obligations using short-term assets from the balance sheet. The greater this ratio is, the company has a greater ability to pay its obligations, and a ratio below 1 may indicate that a company might be unable to pay its debts if they are exigible at that moment. On the other hand a high liquidity ratio (over 3), does not necessarily imply that the company is in an exceptional situation in terms of liquidity. Depending on how the company's assets are allocated, a high current liquidity may suggest that this company does not use its assets or capital in an efficient manner, or it doesn't attract funding.

In terms of liquidity, state companies were significantly affected by the financial crisis, in 2009-2014 their liquidity rate being significantly lower than in the private sector, as well as lower than the threshold of 100%, indicating a significant deficit of current assets versus current liabilities. Instead, in 2015 the liquidity ratio of state companies has increased significantly and is situated at a level higher than that registered at the private companies and even than that recorded in the economic boom years, both groups of companies reaching a level that can be assessed as adequate. If we do not take into consideration the best performing companies, the liquidity ratio recorded in 2015 compared to 2014 an increase of 12 pp, but it remains at a lower level compared to that recorded at the aggregate level, as well as to the recommended threshold of 100%.

Figure 13: Liquidity ratio (%)



Source: MPF, based on the balance sheets submitted by the economic agents from non-financial sector

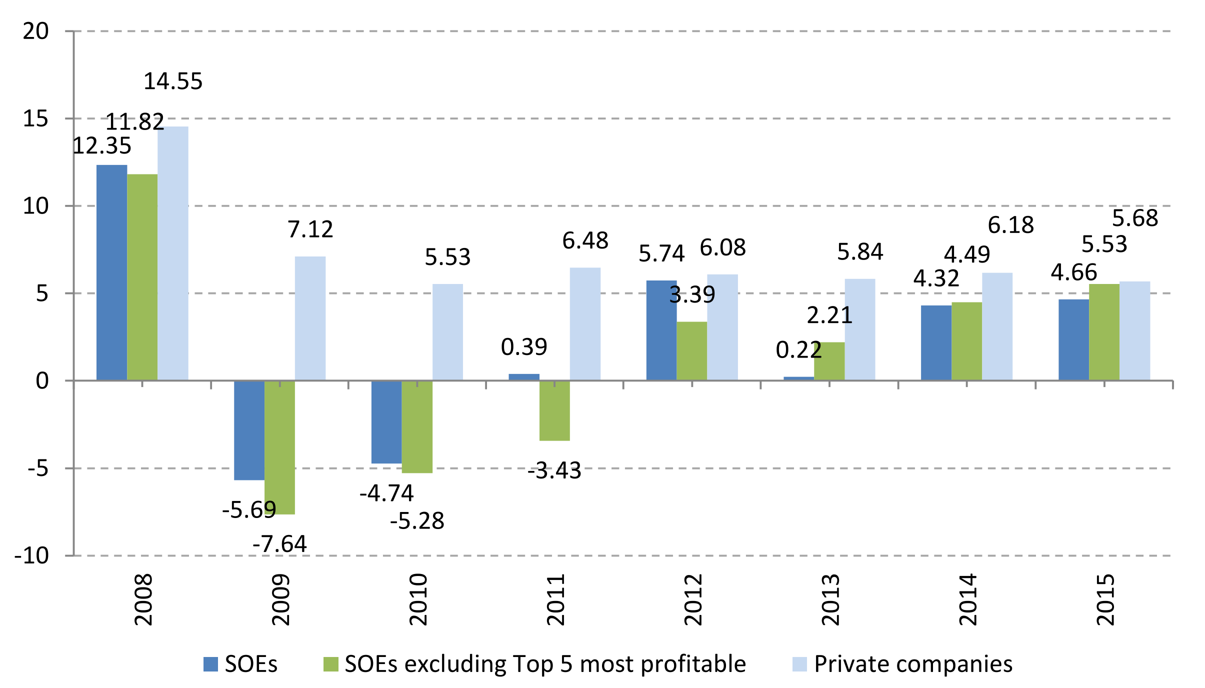
*Note: Liquidity ratio (%) = Current assets / Short term debts *100*

State-owned companies, both at an aggregated level and excluding the Top 5 were characterized by a higher capacity of making new investments, the period 2014-2015 registering a stabilization of the rate of new investments around 4%, lower than the rate achieved by the private sector which is placed at around 6%.

As a result of improved financial performance, the state-owned companies were characterized by a greater capacity of making new investments, the period 2014-2015 registering a stabilization of the rate of new investments around 4%, but lower than the one made by the private sector which is placed at 6%. Moreover, private companies continued to invest in the years that follow the crisis, the volatility of this indicator is much lower compared to that of SOEs. It should also be noted that the level of investments in both categories of companies is significantly lower than the one recorded in the boom period when it exceeded 10%.

For this indicator, the exclusion of Top 5 state companies does not result in a different interpretation of the results, other state enterprises are characterized by a similar investment rate recorded at the aggregate level. Even though the gap compared with private companies narrowed, the need for investment is more pronounced at SOEs than for private companies. Considering the deleveraging of SOEs, it can be appreciated that the new investments were mainly self-financed.

Figure 14: New investments (% of total assets)



Source: MPF, based on the balance sheets submitted by the economic agents from non-financial sector

Note: New investments are calculated as the change in non-financial assets + amortization and depreciation expenses.

During 2013-2015, the state-owned companies at the aggregate level have visibly improved their financial performance, and this is noticeable regarding almost all financial indicators. If we refer only to 2015, compared to 2014 a deterioration of the profitability indicators and an improvement in liquidity and financial discipline can be seen. However, it is important to mention that the level of financial performance is not evenly distributed among the state-owned companies and there are some highly profitable companies, which developed positively in recent years, but also many companies with problems both in terms of arrears, and profitability. In this context, reform in the domain of state companies must continue, and a special focus should be on the identification of the state companies facing problems and on proposal of some consistent recovery measures.

The improvement of SOEs' performance was also supported by the legislative reforms embodied by the enforcement of the Emergency Ordinance no. 109/2011 regarding corporate governance of public enterprises. This represented a major step in the implementation of the best corporate governance practices and aimed at depoliticizing and professionalizing the management of SOEs, both regarding the selection, appointment and functioning of the Board of Directors and managers, and in terms of increasing transparency and providing information in order to increase the public companies' accountability. The overall performance of SOEs has improved also due to the entry in liquidation procedure of the National Coal Company and Termoelectrica. However, further important steps should be taken in order to strengthen the progress made and to bring financial performance of SOEs to a level comparable with the private sector.

The impact of state companies on the budget balance in European standards based on commitments (ESA10) may be an additional pressure on the budget deficit targets undertaken by the government in accordance with the Maastricht criteria (below 3% of GDP in ESA10 terms) and the Fiscal Compact (structural deficit below 1% of GDP). The impact on the budget deficit in ESA10 standards manifests: (i) by the issuance of state guarantees (also subject to EU rules on state aid) and especially (ii) by the reclassification of the state enterprises within the public administration.

According to the Eurostat methodology for accrual accounting (ESA10), several SOEs have been reclassified in the government sector. The 168 SOEs consolidated in central government sector had a positive influence on the general consolidated budget balance in ESA10 standards in 2012-2015, except the year 2012. The table below shows the contribution to consolidated budget balance in ESA10 standards of the first 20 state owned companies included in the central government in 2015. Regarding the state owned companies consolidated in the local government, in 2015 they had a positive contribution to the consolidated balance in ESA10 standards, given the negative contributions in 2012-2014.

Table 6: Contribution of state companies included in the public sector to the consolidated budget balance (million lei), ESA10 standards

	2012	2013	2014	2015
1. Total companies at central level	**-376.4**	**2,784.9**	**3,401.5**	**1,400.9**
CN de Căi Ferate CFR SA	1,532.8	225.5	501.8	424.5
Compania Naţională de Autostrăzi şi Drumuri Naţionale	-1,435.0	2,171.6	2,244.2	341.0
CFR Călători SA	-186.3	95.5	473.0	308.0
Compania Naţională de Investiţii SA	-34.6	44.5	85.3	229.9
SN Radiocomunicaţii SA	0.0	138.3	102.4	72.0
SC Societatea de Administrare a Participaţiilor în Energie SA	0.0	0.0	-1.7	68.1
Societatea Română de Televiziune	-58.4	56.3	-5.0	51.3
Societatea Română de Radiodifuziune	0.7	24.1	15.2	25.9
Societatea Naţională Aeroportul Internaţional Mihail Kogălniceanu	-0.1	0.3	3.2	1.0
CN ROMARM SA	-11.3	-9.8	0.0	0.0
Administraţia Fluvială Dunărea de Jos Galaţi	-20.6	25.6	0.0	0.0
Fondul Proprietatea	-6.6	0.0	0.0	0.0
SC Intervenţii Feroviare SA	-8.3	-4.4	-3.6	0.0
SN a Cărbunelui	-0.4	1.3	-0.3	-0.2
CN a Huilei Petroşani	-57.9	-35.8	-19.4	-1.0
Regia Autonomă Tehnologii pentru Energie Nucleară	0.0	21.7	0.6	-1.1

CN de Radiocomunicaţii Constanţa	-0.2	0.2	0.1	-1.2
SC Termoelectrica SA	-89.0	-60.0	-8.6	-9.5
CN Administraţia Canalelor Navigabile Constanţa SA	4.9	13.2	-19.0	-33.8
Metrorex	-6.1	76.8	33.3	-74.0
2. Total companies at local level	**-204.3**	**-235.2**	**-20.8**	**43.5**
Local airports	-17.3	-11.3	-19.1	13.1
Heating stations with local subordination	-47.0	-66.5	-23.9	-5.2
Other local units	-140.0	-157.5	22.2	35.6
3. Total SOEs	**-580.7**	**2549.7**	**3,380.7**	**1,444.4**
% of GDP	**-0.10%**	**0.40%**	**0.51%**	**0.20%**

Source: NIS