Romania

Fiscal Council

Fiscal Council's opinions

2013

Note:

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I. Fiscal Council opinion on the State Budget law, Social Insurance Budget law for 2013 and the updated version of the 2013-2015 Fiscal Strategy

On January 21st, 2013, the Fiscal Council received from the Ministry of Finance the letter no. 350.147, requesting, under Art. 40, paragraph (2) of Law no. 69/2010, in the shortest time possible, opinions on the draft budget law for 2013, the report on the macroeconomic situation for 2013 and projections for the years 2014-2016, the draft budget law for the 2013 social security budget and the revised fiscal strategy for 2013-2015. However, the complete set of documents required for the elaboration of the Fiscal Council’s opinion (specifically the report on the macroeconomic situation in 2013 and projection for the period 2013-2016, respectively the updated version of the Fiscal Strategy for 2013-2015) was not received until the date of January 23rd, 2013, while the first document was submitted to the Fiscal Council at 6pm on Tuesday, 22nd of January, and the updated strategy at 10.30 on Wednesday, 23rd of January.

Given the Government's intention to approve the above documents at the meeting on 23.01.2013, the time is obviously insufficient for their thorough review and the Fiscal Council is unable to develop a complete opinion regarding those documents. Despite the fact that the urgency for the 2013 budget approval is understandable, the legislative procedure should respect the principle of transparency stated in law no. 69/2010, which provides that "the Government and the local authorities have the obligation to make public and to maintain in public debate, for a reasonable period of time, all the information necessary to allow the assessment of the implementation of fiscal and budgetary policies, the respective outcomes and the stance of central and local public finances". In this context, the Council recommends for the future a period of at least one week between the sending of the documentation by the Ministry of Public Finance and the time of adopting the relevant legislation, this interval being the minimum necessary in order to develop a rigorous analysis. In addition, the draft budget contains a package of amendments to the Tax Code which will come into effect starting with the 1st of February 2013, without being subject to public debate for a reasonable time, contrary to the spirit of Article 4.1 of the Tax Code which states that "the code is amended only by law, promoted, usually 6 months before the date of entry into force."

Under article 40, paragraph (2), letter d) of the fiscal responsibility law, the Council has the legal attribution to "analyze and issue opinions and recommendations, both before Government approval, and before submission to Parliament, on the annual budget laws." Thus, given its mandate in accordance with the law 69/2010, the Fiscal Council issues the following opinions and recommendations on the budget projection for 2013:

The consolidated budget for 2013 (and therefore the medium-term budgetary projection) is based on a scenario significantly more unfavorable regarding the macroeconomic developments compared to the one taken into account in developing the Fiscal Strategy for 2013-2015 as adopted by the Government in June 2012. According to the updated macroeconomic projections, the economic growth in 2013 is estimated to reach the value of 1.6% in real terms, compared with a forecasted growth of 3.1% used in the Fiscal Strategy from June 2012. Moreover, the nominal GDP for 2013, relevant to determining the budgetary aggregates' share of GDP is substantially revised downwards as a result of the statistical review for nominal GDP in 2011 (-21.9 billion, or -3.8%) and the lower than expected economic advance during 2012 (the updated projection of National Commission of Prognosis is indicating a growth of only 0.2%, compared with a forecast of 1.7% envisaged in the Fiscal Strategy 2013-2015 as adopted by the Government in June 2012). Moreover, the projection of economic growth in 2013 is lower than the latest assessment of the European Commission from November 2012 (2.2%). The updated projections for economic growth are lower than the potential GDP growth rates for both 2012 and 2013 (assessed by the latest European Commission forecast at 2.1% and 2.4%), which implies a widening of the output gap in the economy and hence worse cyclical component of the budget balance. This means that reducing the headline deficit to 2.3% of GDP at the end of 2012 involved a structural adjustment effort higher than initially envisaged. At the same time, maintaining the 2013 proposed structural adjustment in accordance with the commitment for achieving the medium-term objective of a structural deficit of 1% of GDP in 2014 will result in a higher effective deficit.

The Fiscal Council considers the macroeconomic scenario implemented in the budget construction to be realistic, assessing the balance of risks to be relatively balanced. On the one hand, amid persistent sovereign debt crisis, major uncertainties remain regarding the economic growth in the euro area, which imply the existence of adverse risks to the realization of the economic growth forecast. On the other hand, the good performance of Romania so far in terms of adjusting budgetary imbalances and the relatively low level of public debt compared to the euro area and to the Central and Eastern Europe are expected to have a favorable effect on the investor sentiment, which could be strengthened as well by further progress in structural reforms and by the projected exit from the excessive deficit procedure this year.

The significant revision of the macroeconomic framework implies that the Fiscal Strategy for 2013-2015 as adopted by the Government in June 2012 is no longer valid. In fact, that version of the fiscal strategy and the associated law approving ceilings for certain indicators specified in the budgetary framework had not undergone a complete legislative process (the latter has only passed in the Senate) and from a strictly legal point of view, one of the consequences of the installation of a new government is the fact that it is not bound by the provisions of the fiscal strategy. Although the Government has developed an updated Fiscal Strategy, it is desirable that it goes through the full legislative approval before the elaboration of the next year's budget, making it able to anchor the fiscal policy parameters for the medium term and to assess compliance with the fiscal rules stipulated by Law no. 69/2010. At the same time, the Fiscal Council is unable to comment on the updated form of the Fiscal Strategy for 2013-2015 given the very short notice (the document reached the institution on January 23rd, 2013, 10:30 AM).

The draft budget for 2013 foresees a deficit target of 13.394 billion lei, or 2.15% of GDP, higher by 1.7 billion (or 0.35 pp. of GDP, of which 0.1pp. as a result of the revision of nominal GDP assumption due to the reasons previously mentioned) than the proposed threshold following the adoption of the Fiscal Strategy for 2013-2015 by the government in June 2012. The upward revision of the deficit target reflects, on the one hand, the worsening growth prospects in 2013 and, on the other hand, the partially accommodated additional costs resulting from the Government's acceptance in December 2012 of lump corrections (valued at 3.11 billion lei) proposed by the European Commission in order to prevent disengagement of the 2007-2013 allocation of grants for those operational programs for which major weaknesses in procurement procedures were discovered, following audits. Given the foregoing, the Fiscal Council considers that the proposed target is consistent with the structural adjustment path (according to the ESA95 deficit) required to achieve the 2014 the medium term objective of a 1% structural deficit (which would ensure compliance with the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union ratified by Romania in June 2012).

Total general government revenues are estimated to reach a level of 209.285 billion lei (33.6% of GDP), registering an increase of 15.586 billion lei (8.05%) compared to the preliminary execution at the end of 2012, a significant portion of the revenue increase being attributable to larger inflows from post-accession grants (+3.08 billion lei, respectively 37%). The projected revenues include an extraordinary component (*one-off*) valued at 3.16 billion lei, coming from the rest of 2.1 billion due by the mobile operators for renting frequency bands (910 million were already paid in 2012) and the implementation of a new compensation (swap) scheme designed to clear outstanding obligations to the state budget (1 billion impact both on revenues and on expenditures). In addition, beyond the already announced fiscal policy measures (oil and tobacco excise indexation according to the calendar, increase in the share of social contributions transferred to the second pension pillar), the draft budget includes a package of measures on the revenue side of which the estimated impact is 2.98 billion lei (the detailed list of discretionary measures and their impact is presented in Annex 1). A consistency assessment has been undergone by the Fiscal Council (included in Annex 2), indicating that the revenue projection for the year 2013 is realistic, being in line with the expected evolution of the relevant macroeconomic bases and the impact of discretionary measures (which also appears as correctly evaluated).

General government expenditures are valued at 222.68 billion lei (35.7% of GDP), up by 15.3 billion (or 0.3 pp. of GDP) compared to the level recorded at the end of last year according to the preliminary execution. Adjusting for inflows related to the financial assistance from the EU and other donors (pre-accession and post-accession funds and other donations), the increase is lower than the one of nominal GDP and as a result the expenditures decrease as a share of GDP (compared with adjusted level from 2012) with 0.2 percentage points (from 34.9% of GDP to 34.7% of GDP). Thus, the dynamics of spending respects the spirit of the fiscal rule stated in article 6, letters d) of Law no. 69/2010, which provides that "until the consolidated general budget balance is in surplus in the previous year, the annual rate of growth in the forecasted consolidated general budget expenditures will be maintained below the annual rate of growth of the forecasted nominal GDP for the three-year period of the fiscal strategy". Beyond the financial correction applicable to certain EU funds operational programs, the level of expenditures accommodates 0.9 billion lei corresponding with the payment of an installment of 10% of final court rulings regarding outstanding wages to certain categories of public sector employees (included in personnel costs) and about 3.5 billion lei at the expense of goods and services for the implementation of the EU directive on combating late payment in commercial transactions. Since both the above expenses have been recorded in the previous years in the ESA95 accrual system, this should contribute to a significant narrowing of cash and ESA95 deficits in 2013, which is likely to cause a significant adjustment of the latter in comparison with its cash counterpart, sufficient from the perspective of the necessary structural adjustment step.

The above opinions and recommendations of the Fiscal Council were approved by the Chairman of the Fiscal Council, according to Article 43, paragraph (2), letter d) of Law no 69/2010, based on the vote of the Fiscal Council members in the meeting on January 23rd, 2013.

January 23rd, 2013

Chairman of the Fiscal Council

IONUŢ DUMITRU

Annex I		- million RON
	Budgetary impact	Revenue category
I. Fiscal policy measures, of which	2280.3	
Monthly ceiling of RON 18,000 for deductibility of depreciation expenses incurred for vehicles	168.8	**Profit tax**
Solidarity tax for increasing the price of gas (gas profit)	335.0	**Taxes on using goods, authorizing the use of goods or on carrying activities**
Gradual liberalization of gas and electricity prices	297.0	**Total impact on revenue, of which:**
	103.4	**Profit tax**
	193.6	**VAT**
Special fee for exploitation of mineral resources (other than natural gas)	106.9	**Taxes on using goods, authorizing the use of goods or on carrying activities**
Fee for transportation of gas and electricity	205.0	**Taxes on using goods, authorizing the use of goods or on carrying activities**
Establishing the standard notional income for income from agricultural activities	413.3	**Personal income tax**
The inclusion in the tax base of allowances	30.0	**Total impact on revenue, of which:**
	6.8	**Personal income tax**
	23.3	**Social security contributions**
The increase of excise duty on cigarettes, of which:	311.8	**Total impact on revenue, of which:**
- indexation from 1 July according with the previous schedule	157.2	**Excises**
- increasing the excise duty on April 1 instead of July 1	94.3	**Excises**
- indexation from 1 July according with the previous schedule	37.7	**VAT**
- increasing the excise duty on April 1 instead of July 1	22.6	**VAT**
The increase of excise duty on diesel fuel from January 1, 2013	402.5	**Total impact on revenue, of which:**
	324.6	**Excises**
	77.9	**VAT**

I. Fiscal policy measures (cont.)		
The increase of excise duty on beer	79.7 64.3 15.4	**Total impact on revenue, of which:** **Excises** **VAT**
The increase of minimum gross salary	328.0 93.00 310.00 -75.00	**Total impact on revenue, of which:** Personal income tax Social security contributions Profit tax
Environmental tax for registration of vehicles	100.0	**Taxes on using goods, authorizing the use of goods or on carrying activities**
The increase of deduction ceiling for research and development expenditure	-5.4	**Profit tax**
Property tax increase for local authorities with arrears	285.0	**Property tax**
The introduction of the 3% tax on turnover for micro-enterprises with annual revenues of maximum EUR 65,000	457.0	**Capital gains and other taxes**
Supplementary transfer to the second pension pillar (+0.5 pp. of pension contribution paid by employee)	-500.0	**Social security contributions**
Reimbursement to retirees of health contributions collected during the period 1 January 2011 - 30 April 2012 under a provision declared unconstitutional	-796.0	**Social security contributions**
The increase of natural gas royalties	61.7	**Nontax revenue**
II Extraordinary revenue, of which:		
The impact of SWAP schemes for clearing outstanding payments for 20131	1000.0	**VAT**
Income from renting frequency bands by mobile operators	2159	**Taxes on using goods, authorizing the use of goods or on carrying activities**

ANNEX II	2012			2013						
	2012 preliminary budget execution	The influence of the two compensation schemes	2012 preliminary budget execution excluding schemes effect	The influence of compensation scheme in 2013	Fiscal policy measures in 2013 according with Annex I	Explanations	Relevant macroeconomic basis*	Revenue projection 2013 FC	CGB revenues states by the budget draft 2013	Differences
	1	2	3 = 1-2	4	5	6	7	8=3*7+4+5	9	10=9-8
TOTAL REVENUE	193698.2	2211.9	191486.3	1000.0	4432.7			208961.4	209285.0	-323.6
Current revenue	184386.8	2211.9	182174.9	1000.0	4432.7			196422.4	196747.7	-325.3
Tax revenue	113980.4	2143.9	111836.5	1000.0	4915.5			122619.4	122937.8	-318.4
Corporate income tax	11784.4	95.0	11689.4		648.7			13099.1	13200.7	-101.6
Profit	10826.8	95.0	10731.8		191.7		Nominal GDP (+6,51%)	11622.2	11721.7	-99.5
Capital gains and other taxes	957.6		957.6		457.0		Nominal GDP (+6,51%)	1476.9	1479.0	-2.1
Personal income tax	20893.8	67.1	20826.7		513.1			22998.0	23159.1	-161.1
Wages, dividends, capital gain	20880.8	67.1	20813.7		513.1		The average number of employees (+0,9%) Average gross earning (+7%)	22984.2	23146.2	-162.0
Other (local) taxes	13.0		13.0				Nominal GDP (+6,51%)	13.8	12.9	0.9
Property tax	4059.0		4059.0		285.0		Indexation with cumulative inflation rate over the past three years (16.9%), assuming that 80% of local authorities which don't have arrears and for which indexation is not binding will chose indexation	4480.9	4466.3	14.6
Taxes on goods and services	76163.6	1574.2	74589.4		3468.7			80897.2	80980.9	-83.7
VAT	50517.4	1570.9	48946.5	1000.0	562.8	Although the excise increases and the liberalization of electricity and natural gas prices (which implies price increases) generate additional revenue from VAT, their impact should be included in the deflator's projection for the relevant macroeconomic base considered. The calculation reported here reflect only changes in nominal consumption without separately adding additional revenues for these measures.	Household's final consumption expenditure excluding own account consumption and the related market (+6,3%)	53026.0	52948.8	77.2
Excises	20269.6	3.3	20266.3		0.0		Household's final consumption expenditure excluding own account consumption and the related market, in real terms (+2.1%) Variation of the reference exchange rate for excises (+5.17%)	22241.4	22363.2	-121.8
Other taxes on goods and services	2110.8		2110.8			The budget revenues for 2012 include about 1.8 mld. lei from clawback tax. The revenue projection for 2013 does not include revenue from this tax.	Household's final consumption expenditure excluding own account consumption and the related market (+6,3%)	330.4	320.4	10.0
Taxes on using goods, authorizing the use of goods or on carrying activities	3265.8		3265.8		2905.9	The starting point of extrapolation (the revenues from 2012 preliminary budget execution) is adjusted excluding the extraordinary income from renting frequency bands by mobile operators during 2012 (910 million).	Real GDP (+1.6%)	5299.4	5348.4	-49.1
Tax on foreign trade and international transactions	707.4		707.4				Imports of goods and services (+5.7%)	747.7	741.8	5.9
Other tax revenue	372.2		372.2				Nominal GDP (+6,51%)	396.4	389.0	7.4
Social security contributions	51648.6	407.6	51241.0		-544.5	The starting point of extrapolation (the revenues from 2012 preliminary budget execution excluding the compensation schemes implemented in 2012) is adjusted excluding health contributions colected from pensioneers durring the period 1 January 2011 - 30 April 2012 under a provision declared unconstitutional (413 million) and adding compensatory transfers to affected persons begining with 1 June 201, which were recorded as negative revenues (619 million)	The average number of employees (+0,9%) Average gross earning (+7%)	54247.9	54355.2	-107.3
Nontax revenue	18757.8	68.0	18689.8		61.7		The average rate of inflation forecasted in 2013 (4,3%)	19555.2	19454.7	100.5
Capital revenues	660.4		660.4				The average rate of inflation forecasted in 2013 (4,3%)	688.8	687.1	1.7
Subsidies	0.0		0.0					0.0	0.0	0.0
Grants	365.0		365.0			according with the projection of Ministry of Public Finance		629.9	629.9	0.0
Amounts received from the EU	8139.3		8139.3			according with the projection of Ministry of Public Finance		11220.3	11220.3	0.0

II. Fiscal Council's opinion on the revised Fiscal Strategy for 2013-2015

Under article 23, letters b) and c) of the Fiscal Responsibility Law (FRL) no. 69/2010, the fiscal framework of the fiscal strategy (FS) may be reviewed when there is a significant worsening of the macroeconomic indicators that were used in the fiscal strategy elaboration or when a change of Government occurs, a case in which at the beginning of the mandate, the new Government will make public whether its program complies with the latest fiscal strategy approved by the Parliament or not. In the latter case, the Ministry of Public Finance will prepare a new fiscal strategy. The Fiscal Council considers that the present case is consistent with both situations stated in the above mentioned law articles and the Government's initiative to update the previous version of the strategy is justified. Moreover, the first form of the strategy and the associated law approving ceilings for certain indicators specified in the budgetary framework had not undergone a complete legislative process and were not approved by the Parliament.

Under article 40, paragraph (2), letter b) of the Fiscal Responsibility Law, the Fiscal Council has the legal attribution to “analyze and issue opinions and recommendations on the Fiscal Strategy and assess its compliance with the principles and rules specified in this law". Moreover, according to article 40, paragraph (2), letter a), the Fiscal Council has the legal attribution to "analyze and issue opinions and recommendations on official macroeconomic and budgetary forecasts".

Thus, given its mandate in accordance with law no. 69/2010, **the Fiscal Council issues the following opinions and recommendations on the revised Fiscal Strategy for 2013-2015 (FS 2013-2015)**:

Compliance with the rules from the Fiscal Responsibility Law (FRL)

Given the above arguments, the only rule that can be evaluated is the one defined in article 6, letter d), which states that "*until the consolidated general budget balance is in surplus in the previous year, the annual rate of growth in the forecasted consolidated general budget expenditures will be maintained below the annual rate of growth of the forecasted nominal GDP for the three-year period of the fiscal strategy*”. The Fiscal Council recalls that, in its opinion regarding the original form of FS 2013-2015, it warned about the existence of an inconsistency between the provisions of the above mentioned article and article 6, letter c), which refers to "total budgetary expenditure eliminating financial assistance from the European Union and other donors". This inconsistency has the potential to penalize the Government for better performance in terms of EU funds absorption by imposing a constraint to operate cuts in other chapters of expenditure and the Fiscal Council considers that an amendment of this article is adequate in order to use the same definition of total expenditure, respectively the definition stated at article 6, letter c). Considering an *ad litteram* interpretation of the budgetary rule mentioned above, the trajectory for total expenditure would only partially comply with the fiscal rules, given that the marginal reduction of total expenditure as a share of GDP would be recorded only in the years 2014 and 2015 (from 35.73% of GDP in 2013 to 35.72% of GDP in 2014 and 35.7% in 2015), while in 2013 an increase of total expenditure as a share of GDP would be recorded (from 35.53% in 2012 to 35.73% in 2013). However, adjusting total expenditure with the projections of revenues regarding the financial assistance from the EU and other donors, its growth rate is maintained below the one of nominal GDP and its trajectory expressed as a percentage of GDP registeres a continuous decreasing (from 34.09% of GDP in 2012 to 33.82% in 2013, respectively 33.49% and 33.23% of GDP in 2014 and 2015), which would respect the spirit of the fiscal rule mentioned above.

Assessment of the macroeconomic framework underlying the FS for 2013-2015

The economic growth assumption underlying the updated FS 2013-2015 is significantly more unfavorable than the one used in the previous version of the strategy, noting a downward revision compared to the latest projections of the European Commission (November 2012). Thus, the current projection is based on an increase of real GDP of 1.6% in 2013 (3.1% in the previous version of FS and 2.2% in the projection of the European Commission), 2.2% in 2014 (3.6% in the previous version of FS and 2.7% in the projection of the European Commission), respectively an increase of 2.8% in 2015 (3.9% in the previous version SFB). For the year 2013 the downward revision is explained by the inertial effect of GDP dynamics, which was far below expectations during the year 2012 (the economic growth is estimated to register a value of only 0.2% compared with a growth assumption of 1.7% in the previous form of FS 2013-2014), but the trajectory for the coming years reflects mainly, according to the updated FS, a weaker than expected performance of the European economy.

The Fiscal Council considers as relatively realistic the macroeconomic scenario taken into account in the elaboration of the revised FS 2013-2015, assessing the balance of risks as relatively neutral. However, in the Fiscal Council's opinion, the upward trend considered for the economic growth is conditioned over the medium and long term by the recovery of the structural reforms implementation delays and substantial improvement of EU funds absorption (which would have positive effects in the short term). Also, the magnitude of the structural fiscal consolidation effort necessary to achieve the medium-term objective (respectively a structural deficit of 1% of GDP) is substantially lower than in previous years, thus supporting an acceleration of economic growth.

Regarding the projections of labor market indicators, the average growth rate of employment in the period 2013-2015 (1.3%) remains unchanged compared to the previous strategy, despite the significant downward revision of the economic growth path during this interval. Although such a development appears to be validated by the unexpected increase in the number of employees in 2012, recorded in the conditions of an economic growth far below initial forecasts, this can be interpreted as an increase in advance of the number of jobs created by the private sector in anticipation of favorable developments in the aggregate demand, which materialized in a lesser extent (as indicated by the recent macroeconomic projections in Europe) would have the potential to trigger future corrective actions in order to recover the 2012 losses of competitiveness. Given the statistical inertial effect associated with the new jobs created in 2012, the projection for the current year seems to be plausible, but for the period 2014-2015 the Fiscal Council considers as more prudent a lower employment than the one from the current projection.

The Fiscal Council appreciates that the assumptions for the number of employees and average wage in the public sector for the year 2013 are explicitly presented in the strategy. Nevertheless, the Fiscal Council notes that despite its previous recommendations, an explicit presentation of these assumptions for the entire period covered by the strategy is still missing, although these hypotheses are underlying both the economic aggregates trajectories and the level of personnel spending of the general consolidated budget.

Assessment of the fiscal framework in the 2013-2015 period

The updated Fiscal Strategy reaffirms the commitment regarding fiscal consolidation over the next three years, the budget deficit (cash methodology) being projected to fall from 2.5% of GDP in 2012 to 1.8% of GDP in 2014, while in 2015 it is forecasted to remain at the same level as in 2014. According to the strategy, the deficit reduction of about 0.7 percentage points of GDP in the period 2012-2015 is projected to be achieved by increasing revenues (with 0.9 percentage points of GDP, from 33.0% of GDP in 2012 to 33.9% of GDP in 2014), while budget expenditures are forecasted to increase in 2013 by 0.2 percentage points of GDP, to 35.7% of GDP, after that being projected to remain at this level. The above figures incorporate the expected substantial growth of inflows from EU funds and adjusting for that, the reduction in the deficit for the years 2013 and 2014 is the result of maintaining the growth rate of total expenditures below the dynamics of nominal GDP (0.6 pp of GDP cumulative adjustment) and a slight increase in the share of revenues in GDP (0.1 pp of GDP, cumulatively between 2012 and 2014).

The Fiscal Council considers that the proposed target is consistent with achieving in 2014 of the medium term objective of 1% structural deficit (which would ensure compliance with the Treaty on Stability, Union – the Fiscal Compact, ratified by Romania in June 2012). It should be noted that the objective of medium-term structural deficit that Romania needs to align to as a result of its status as an EU member state, determined from the deficit that stabilizes the share of GDP of the public debt stock plus an adjustment due to the incorporation of a portion of the long-term costs of aging, was revised upwards by the European Commission to 1.25% of GDP as a result of the favorable impact of structural reforms on pensions in the latter, assessed in the context of the *Ageing Report 2012*. However, given the maximum limit set by the Fiscal Compact, which was signed by Romania, the operational level of the medium-term objective is 1% structural deficit. The necessary structural adjustment effort in the years 2013 and 2014 appears to be significantly lower the one from 2010 to 2012, its cumulative two-year level (about 0.8 to 1 pp of GDP) accounting for about half of that already implemented deficit reduction during 2012. In addition, the economic growth in 2012 and its revised projection for 2013 is translated into a widening negative output gap in these two years, and therefore a greater negative cyclical component of the budget balance, which make the structural deficit objective for 2014 consistent with a higher headline deficit (ESA95) - 2% of GDP in 2014 (corresponding to a structural deficit of 1% of GDP), compared with 1.3% in the previous version of the FS 2013-2015 (corresponding to a structural deficit of 0.7%).

The FS 2013-2015 anticipates a reduction of the gap between the deficit calculated using the national methodology (cash) and the ESA 95 (accrual), given that the first will incorporate expenditures that have already been recorded in the previous years under ESA95; in particular, they relate to the amount of state obligations to certain categories of employees in the public sector that occurred after final court rulings (about RON 6.4 billion recorded in accrual system in 2011, but began to be paid in 2012 and thus continuing to burden the cash budget system in increasing proportions until 2016), and the allocation of funds necessary to reduce the invoice payment period to 60 days, in accordance with EU Directive 2011/7.

Budgetary revenues and expenditures

The level of revenues as a percentage of GDP is projected to increase in the FS from the a level of 33% of GDP in 2012 to 33.9% of GDP in 2015, due solely to improved post-accession EU funds absorption, which is expected to add revenues of 1.2% of GDP at the end of 2015 compared to 2012. The main categories of taxes are expected to grow in line with nominal GDP, fluctuations occurring at the level of "other general taxes on goods and services" (fall in 2013), as a result of non-including revenues from the clawback tax and "tax on the use of goods, authorizing the use of goods or conducting activities" (fall in 2014), given the exceptional income in 2013 from renting frequency bands by mobile operators (+2.1 billion). Non-tax revenues are expected to register a slight increase as a share of GDP since 2014, following the intentions stated by the Government to reassess the level of royalties for natural resources since 2014 (non-tax revenues are projected to increase in 2014 by 0.2 pp of GDP, the main factor driving the reduction in the projected budget deficit from 2.1% of GDP in 2013 to 1.8% of GDP in 2014).

In the Fiscal Council's opinion, the projected trajectory of the main categories of budget revenues appears consistent with maintaining the current system of taxes. Although the FS 2013-2015 states that the authorities intend to operate over the period covered by the strategy's substantial changes in the tax code with a major impact on budgetary revenues (the return to a 19% VAT, VAT reduction to agricultural producers from 24% to 9%, reduction in employers' social contributions by 5 pp, introducing a differentiated income tax revenue, with rates lower than 16% for certain portions of income), it does not contain any details of the moment when the measures will be implemented or any assessment of their impact. Thus, the Fiscal Council finds serious deficiencies of transparency in underlying the medium-term trajectory of budgetary revenues, given that a detailed assessment of the impact of discretionary measures is provided only to those adopted in the context of the 2013 budget.

While in the conditions of accepting the hypothesis of not changing the current tax system, the revenue projections generally appear as realistic, in the Fiscal Council's opinion, a slight overestimation of the receipts from VAT and excise duties can be identified in 2014 and 2015. Even if a superior dynamic compared to the one of the relevant macroeconomic bases can be justified by a potential increase in the efficiency of the collection process, the Fiscal Council reiterates its call for caution, considering as risky an ex-ante inclusion of the result of the measures against tax evasion and recommending the ex-post inclusion, after the efforts to improve the collection are materialized.

While noting a significant improvement of transparency regarding the projections of the budgetary aggregates for the first year covered by the FS 2013-2015, the Fiscal Council considers as necessary a more detailed overview of the macroeconomic bases and elasticities considered for each category of revenue and the impact of discretionary measures affecting the projections for the rest of the period covered by the strategy in accordance with the transparency principle stated in article 4 of Law no. 69/2010.

Under article 20, paragraph (2) of Law no. 69/2010, the Fiscal Strategy should include a sensitivity analysis of the fiscal targets to changes in the macroeconomic indicators. However, the Fiscal Council notes the absence of this analysis that we consider mandatory, especially in the current economic environment which is still difficult to predict, for both the European economy and, implicitly, for the Romanian economy.

Regarding the expenditures, their projected trajectory shows an increase from 35.4% of GDP in 2012 to 35.7% of GDP in 2013 and maintaining this level until 2015. The above figures incorporate the expected substantial growth of inflows from EU funds while adjusting for that, the budget expenditures are projected to have a growth rate below the dynamics of nominal GDP (cumulative adjustment of 0.6 pp of GDP in 2013-2014 of total expenditure minus EU funds absorption). This trend is driven mainly by the social assistance category dynamics as a result of the application of the new pension indexation scheme in the coming years (average inflation plus half of the previous year's real wage growth), plus the scheduled replacement of capital expenditure from own resources with EU funds and spending cuts to subsidies.

Regarding the spending on goods and services, the revised FS projects a slight increase as a share of GDP in 2013 to 5.98% from 5.89% in the previous year, followed by a reduction to a level of 5.54% of GDP in 2015. Increased spending on goods and services in 2013 is explained by the application of the European Commission Directive 7/2011 on combating late payment in commercial transactions. The Government will have to reduce the invoice payment period to 60 days and the financial effort is of approximately RON 3.5 billion (0.54% of GDP). In the Fiscal Council's opinion, reducing spending on goods and services to around 5.5% of GDP will be a major challenge given their evolution in the previous years characterized by frequent overruns compared to the allocations from the initial budget and the intention to reduce the arrears of the general consolidated budget. In this context, the expenditures with goods and services seem undersized and there are significant risks of exceeding the amounts provided in the FS. In the Fiscal Council's opinion, such a reduction is not possible without very deep structural reforms, particularly in the health system, and without a more efficient public procurement system in general.

The projected dynamic of personnel costs shows an advance as a percentage of GDP in 2013 to 7.4% from 6.97% in 2012 while afterwards entering on a downward trend, the 2015 forecasted level being 6.94% of GDP. The level of personnel expenses in the FS accommodate increases in salaries due to return to June 2010 wages and the amounts resulting from obligations of the state towards certain categories of employees in the public sector following final court rulings. Excluding the impact of the latter, personnel costs are expected to increase in nominal terms by only 2.56% in 2014 and 2.75% in 2015. In the context of the declared intention of maintaining the number of employees in 2013 at the level recorded in November 2012 and in the absence of projections regarding the number of employees in the public sector for the period 2014-2015, the Fiscal Council considers as undervalued the staff costs, as their growth rate is lower than the expected average inflation. Also, according to article 6, letter a) of the Fiscal Responsibility Law "personal expenses of the general government as a percentage of GDP cannot exceed the annual ceilings set under the fiscal strategy for the first two years covered by it". Therefore, a nominal wage increase in 2014 over the level provided in the FS 2013-2015 can be legally sustained only by a higher than expected advance of nominal GDP.

The expenditures on projects financed through post-accession EU funds are expected to significantly accelerate from 2.26% of GDP in 2012 to 4.68% of GDP in 2015 while reducing capital expenditures from own resources from 3.3 % in 2012 to 2.97% of GDP in 2015; thus the investment financing will be done mainly from EU funds. In the context of the so far very poor performance regarding EU funds absorption, the Fiscal Council draws attention to the significant risks to the fiscal targets generated by the failure to attract EU funds while using own resources to ensure the continuity of the projects, the experience of 2012 being eloquent in this respect.

The above opinions and recommendations of the Fiscal Council were approved by the Chairman of Fiscal Council, according to article 43, paragraph (2), letter d) of Law no. 69/2010, after being approved by the Council members through vote, on February 5th, 2013.

February 5th, 2013

Chairman of the Fiscal Council

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III. Fiscal Council's opinion on the Fiscal Strategy for 2014-2016

The Ministry of Finance sent to the Fiscal Council by letter no. 81681/21.05.2013 the Fiscal Strategy for 2014-2016 (FS 2014-2016) and the draft law approving ceilings for certain indicators specified in the budgetary framework. Under article 40, paragraph (2), letter b) of the Fiscal Responsibility Law (FRL), the Fiscal Council has the legal attribution to *"analyze and issue opinions and recommendations on the Fiscal Strategy and assess its compliance with the principles and rules specified in this law"*. Moreover, according to article 40, paragraph (2), letter a), the Fiscal Council has the legal attribution to "analyze and issue opinions and recommendations on official macroeconomic and budgetary forecasts".

Thus, given its mandate in accordance with law no.69/2010*, **the Fiscal Council issues the following opinions and recommendations on the Fiscal Strategy for 2014-2016**:*

General remarks

Earlier this year, after the installation of the new government, a revised form of the Fiscal Strategy 2013-2015 (FSr 2013-2015) was developed and approved, on which the Fiscal Council has expressed its opinion on February 5th. Given the relatively short time elapsed between that moment and the formulation of FS 2014-2016 and considering that the macroeconomic developments were broadly in line with the expectations, as it was also revealed by the insignificant differences between the European Commission forecasts (the interim European economic forecast from February 2013 and the spring forecast from May 2013), the FS 2014-2016 records minor changes compared to the parameters considered in the previous version. In fact, the revenue projection remains unchanged, while minor changes occur at the level of some expenditure chapters in 2014 and 2015; in addition the deficit target for 2015 is revised downwards (-0.2 pp of GDP).

Compliance with the rules from the Fiscal Responsibility Law

Under article 6, letter d), of the Fiscal Responsibility Law "*until the consolidated general budget balance is in surplus in the previous year, the annual rate of growth in the forecasted consolidated general budget expenditures will be maintained below the annual rate of growth of the forecasted nominal GDP for the three-year period of the fiscal strategy*". The FS 2014-2016 respects this rule, considering that the total expenditures of the general government in amount of 35.72% of GDP in 2014, 35.50% of GDP in 2015 and 35.47% of GDP in 2016 are on a downward path and given that the budget for the current year sets total expenditures at 35.73% of GDP. Moreover, if total expenditure are adjusted by eliminating the financial assistance from the EU (post-accession grants) and other donors, the growth rate of the budget expenditures is maintained below the one of nominal GDP and its downward trajectory is even more obvious: 33.5% of GDP in 2014, 33.0% of GDP in 2015 and 32.9% of GDP in 2016, compared to a planned level of 33.8% of GDP in 2013. The Fiscal Council reiterates its recommendation to amend the rule described in article 6 letter d) of the Fiscal Responsibility Law, so that it should not refer to *"total expenditure of the general government"*, but to *"the total budget expenditures minus financial assistance from the European Union and other donors"*; a revised formulation has the advantage of being consistent with the definition used in the rule stated at art. 6 letter c), while the Government will not be penalized for a possible better performance in terms of EU funds absorption by imposing a constraint to operate cuts in other chapters of expenditure.

Under article 18, paragraph (3) of the Fiscal Responsibility Law, *"the ceiling for the total balance and personnel spending of the general consolidated budget specified in article 20 paragraph (1) sub-paragraphs (a)-(b) shall be approved by the Parliament and it shall be binding for the next two budget years"*. Following the elaboration of the revised Fiscal Strategy 2013-2015, the Parliament passed the Law no. 4/2013 for approving ceilings for certain indicators specified in the budgetary framework. Under article 20, paragraph (1), letter a) and b) of the FRL, it sets mandatory ceilings for the budget deficit at 2.1% of GDP in 2013 and 1.8% of GDP in 2014, respectively 7.4% of GDP for personal expenditures in both years. For the first year covered by the FS 2014-2016, the budgetary parameters namely the budget deficit of 1.8% of GDP and personal expenses of 7.4% of GDP comply with the provision of FRL, respecting the limits stipulated by Law no. 4/2013.

Assessment of the macroeconomic framework underlying the FS for 2013-2015

The economic growth assumption underlying the 2014-2016 FS is almost unchanged compared to the one used in the updated FS 2013-2015 (increases of 1.6%, 2.2% and 2.8% in 2013, 2014 and respectively in 2015), only one change occurring in 2015 where the current projection of real GDP growth (2.4%) records a downward revision compared to the previous one of 2.8%, without specifying the reasons for this update (especially given that the projections for 2014 and 2016 remain unchanged). However, at the level of GDP deflator a symmetrically opposite revision was operated so there is no change in the considered path of nominal GDP. Both in 2014 and 2015, minor changes in the expenditure components of GDP are operated in the FS 2014-2016 compared to the previous version (see Table 1), without influencing the nominal GDP for 2014 or the trajectory for budget revenues in any of these years, which is likely to suggest symmetrical and opposite revisions of the correspondent deflators. In this context, the downward revision of the economic growth forecast for 2015 seems to be motivated by the cumulative impact of lower private consumption dynamics (-0.4 pp lower growth rate) and faster advance in imports (+0.2% of GDP).

Table 1: Assumptions regarding the dynamic of total GDP and demand components

	Δ (%) real GDP		Δ (%) nominal GDP		Δ (%) real private consumption		Δ (%) real government consumption		Δ (%) real GFCF		Δ (%) real exports		Δ (%) real imports	
	2014	2015	2014	2015	2014	2015	2014	2015	2014	2015	2014	2015	2014	2015
- FS 2013-2015 (1)	2.2	2.8	6.0	5.4	1.7	2.1	1.4	1.3	5.6	6.7	3.2	5.1	4.3	5.7
- FS 2014-2016 (2)	2.2	2.4	6.0	5.4	2.0	1.7	1.4	1.3	6.0	6.7	3.4	5.1	5.1	5.9
- Differences (2)-(1)	0.0	-0.4	0.0	0.0	0.3	-0.4	0.0	0.0	0.4	0.0	0.2	0.0	0.8	0.2

The Fiscal Council has no major objections regarding the macroeconomic framework used in FS 2014-2016 (identical with the one from the Convergence Programme 2013-2016 submitted to the European Commission at the beginning of May), which we appreciate as realistic considering the information available at this moment. Nevertheless, the Fiscal Council notes that the upward trend of economic growth is conditioned over the medium and long term by a better performance of EU funds absorption (as reflected in the budget projection) and by further implementation of structural reforms in the economy. Also, the Fiscal Council assesses the balance of risks to be relatively neutral, even with a slight tilt in the sense of a higher economic growth than the one forecasted for the current year, taking into account the unexpected GDP advance recorded in the first quarter of 2013 (the interim estimation of NIS indicates that the annual real GDP recorded an increase of 2.1% for the unadjusted series and of 1.4% for the seasonally adjusted series), the upward revision of the real GDP growth rate in 2012 (+0.7% compared with an initial estimate of 0.3%) and the possible positive influence in the coming quarters of an agricultural production superior to initial expectations. Also, the GDP dynamics in the first quarter is difficult to be interpreted as the beginning of a long term recovery of the economic growth, given that the short-term indicators are still offering contradictory signals: the contraction of imports in the conditions of a real exchange rate appreciation indicates a weak aggregate demand dynamics, bank lending growth is still negative, while the quarterly acceleration growth of retail sales in the first quarter occurred in the conditions of a monthly trajectory that suggests a deceleration in the next quarter (negative carry-over). In addition, the GDP dynamics excluding the agriculture sector (a less volatile measure of the economic activity) indicate an economic slowdown in the first quarter of 2013, as the growth rate of this aggregate was the lowest in the last five quarters. Also, the structural problems of Romania's main trading partner - the Euro Zone - are still far from being solved and this generates an important source of uncertainty throughout the forecast horizon.

Assessment of the fiscal framework in the 2014-2016 period

For the first year covered, the FS 2014-2016 does not change the budget deficit target (1.8% of GDP), but compared to the previous version of the document which stipulates the same deficit for the next year, the new strategy plans a further reduction of the budgetary imbalance by 0.2 pp of GDP for 2015 (to 1.6% of GDP), the target for 2016 being also set at this level. The budget deficit according to ESA95 methodology is planned to decline from 2.4% of GDP in the current year to 2% in the next year and to 1.8% in 2015 and 2016. The trajectory of the budgetary deficit is chosen in order to ensure compliance with the conditions imposed by the Fiscal Compact (ratified by Romania in June 2012) regarding the maximum level of the structural deficit.

The medium-term objective in terms of the structural deficit that Romania needs to align to as a result of its status as an EU member is determined starting from the deficit that stabilizes the share of GDP of the public debt stock plus an adjustment due to the incorporation of a portion of the long-term costs of aging. The MTO was revised upwards by the European Commission at 1.25% of GDP (from 0.7% of GDP) as a result of the favorable impact of structural reforms on pensions, assessed in the context of the *Ageing Report 2012* developed by the European Commission. However, given that the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (the Fiscal Compact), ratified by Romania, sets a maximum limit of the structural deficit at 1% of GDP for countries with a low public debt (significantly below 60% of GDP), the operational medium-term objective for Romania is set at this latter level.

If the expected substantial improvement in EU funds absorption is eliminated, the decrease by 0.5 pp of the budget deficit during 2014-2016 is attributable entirely to cuts in total expenditure, whose share in GDP is expected to decrease by 0.9 pp, compensating the reduction of revenues by 0.4 pp of GDP in the same period as a result of the expiration in 2015 of some additional taxes for the energy and natural resource exploitation sectors.

Given the assumptions regarding the potential GDP included in the Convergence Programme - which are in fact very close to those of the European Commission (a growth rate of 2.1% percent in 2013, followed by an acceleration to 2.6% in the next year), the projected trajectory for the real GDP growth implies a continuous widening of the output gap up to 2015 (to a level of 3.1% of potential GDP), followed by a relative stabilization in 2016. Under these conditions, the size of negative cyclical component of the budget balance is expected to increase compared to the starting point, which implies that the adjustment of the structural deficit will be higher than the one of the actual budget deficit. Thus, if in ESA95 terms, the deficit is expected to decline from 2.4% of GDP in 2013 to 1.8% of GDP in 2015 and 2016 (-0.6 pp of GDP), the structural deficit would decline from 1.6% of GDP to 1% of GDP in 2014 (a level that ensures the fulfillment of the MTO - structural deficit of 1% of GDP), and in addition to a level of 0.8% of GDP in 2015 and 2016 (a cumulative structural adjustment of 0.8 pp of GDP).

The Fiscal Council considers as prudent the additional structural adjustment introduced by the FS 2014-2016 for 2015, even though strictly speaking, maintaining the structural deficit of 1% of GDP, expected to be reached in 2014 would have been sufficient for compliance with the conditions imposed by the Fiscal Compact. The reasons underlying the new deficit target are related to the inherent uncertainty associated to the estimation of unobserved variables such as the potential GDP and also the significant differences between the results of the alternative methodologies used in the estimation of the output gap; thus, it appears adequate to choose a level of the headline budget deficit that would ensure reaching the MTO, regardless of any further revision of the economy's cyclical position. The compliance with the medium-term objective in 2014 is assured only if the subsequent assessments of the potential GDP growth will continue to show the same path as today. There are significant differences in the results generated by alternative methodologies used by the European Commission[1]: in the case of the production function method, the potential GDP growth path shows a rapid acceleration (from a growth rate of 1.8% in 2012, to 2.1% in 2013 and 2.6% in 2014), which implies a widening output gap from 2.1% in 2012 to 3% of potential GDP in 2014, while the univariate filters are suggesting a more "smooth" dynamic (potential GDP growth rate of 1.9% to 2% in the period 2012-2014) and in the Fiscal Council's opinion also a more plausible one, with the negative output gap reaching a maximum of 2.8% in 2013 and later entering on a downward trend[2] (to a level of 2.5% of potential GDP in 2014). If the first method is used, the cyclical component of the budget deficit in 2014 would be about 1% of GDP, which would ensure that the medium-term objective of 1% structural deficit is consistent with a 2% of GDP level in 2014 for the headline budget deficit (ESA 95). If univariate filters are used, the cyclical component would be only 0.8% of GDP, implying the existence of a structural fiscal consolidation gap to the MTO (0.2 pp of GDP), a gap that can only widen given the trajectory of the output gap in the coming years according to the said method of estimating the potential GDP.

Budgetary revenues and expenditures

The FS 2014-2016 maintains the revenue trajectory as in the previous version of the strategy (the revised Fiscal Strategy for 2013-2015), on which the Fiscal Council expressed an opinion in early February 2013. Given the set of available information and the relatively unchanged macroeconomic coordinates considered, the Fiscal Council reaffirms its view that the projected medium-term revenues trajectory is realistic. In addition, based on the information received regarding the implementation of new compensations schemes in the years 2014-2016 (swap schemes) designed to clear outstanding obligations to the budget with a favorable impact on revenue from VAT (but neutral on the budget deficit), the Fiscal Council is no longer querying the projected evolution of this category of revenue as the institution raised doubts in its opinion on the revised Fiscal Strategy for 2013-2015.

The FS 2014-2016 mentions as future directions for modifying the tax system a gradual reduction in the level of employer social contributions and in the VAT rate. However, the 2013-2016 Convergence Programme submitted to the European Commission (in which the

[1] https://circabc.europa.eu/sd/d/0417d489-a9c7-4521-876c-abda2aae61cd/OG_2013_Spring_Final%20MSs_tables.xlsx

[2] A similar trajectory is suggested by the most recent assessment of the NBR (Inflation Report May 2013) on the cyclical position of the economy

revenue projection is the correspondent in the ESA95 methodology of the forecast in cash terms from the FS 2014-2016) explicitly acknowledges (see Annex 2b thereof[3]) that the current projection is drawn on a scenario of no policy change, respectively assuming that the current system of taxes is maintained. Moreover, the FS 2014-2016 states that changes in the tax system are dependent on an increased revenue collection in the future, suggesting that reducing taxes is rather an objective than a definite decision. However, the Fiscal Council reiterates that caution is needed, also considering the principle of fiscal responsibility stated in the FRL, and insists that the assessment of tax collection efficiency improvements should be made strictly ex post, i.e. after year-end revenues will exceed the original estimates (which, ceteris paribus, would result in a budget deficit below the proposed target) and their trajectory is not attributable to a more favorable than expected development of the relevant macroeconomic bases. This latter aspect is particularly relevant given that the nominal deficit target is set based on the structural deficit, which means that a more favorable macroeconomic evolution (a higher economic growth) will often lead to an improvement in the cyclical position of the economy – a reduced negative cyclical component of the budget deficit when there is a negative output gap, i.e. a higher positive cyclical component in the case of a positive output gap. The higher revenues in such a situation would lead to a lower actual deficit, but that would not translate into an equivalent adjustment of the structural budgetary position.

In addition, the Fiscal Council reiterates that the materialization of the government's intention to reduce tax rates is possible, under Article 13 of the FRL, only if the proposed regulations respect at least one of the following conditions:

(a) To have the endorsement of the Ministry of Public Finance and the Fiscal Council, confirming that the financial impact was taken into account in the budgetary revenue forecast and that it does not affect the annual budget targets and the medium term targets.

(b) To be accompanied by proposals for measures to compensate the financial impact, by increasing other budgetary revenues.

From the perspective of the necessary assessments above mentioned, the Fiscal Council considers as absolutely necessary the materialization of its repeated recommendations related to the inclusion in the Fiscal Strategy of an explicit and detailed presentation of the macroeconomic bases and elasticities for each revenue category, and also of the budgetary impact divided by years of considered discretionary measures that affect the trajectory of revenues; the disclosure of these information is also an imperative given the principle of transparency stated in article 4 of Law no. 69/2010.

[3] http://ec.europa.eu/economy_finance/economic_governance/sgp/pdf/20_scps/2013/01_programme/ro_2013-04-30_cp_en.pdf

Under Article 20 paragraph (2) of Law 69/2010, the Fiscal Strategy should include a sensitivity analysis of the changes in fiscal targets in response to changes in the macroeconomic indicators. However, the Fiscal Council notes again the lack of this analysis, which is absolutely necessary especially in the current context characterized by an economic environment still difficult to predict, both in the European economy and, consequently, in the Romanian economy.

Regarding budgetary expenditures, the FS 2014-2016 provides some reallocation between chapters compared with the revised FS 2013-2015, along with a decrease in the amount of total expenditure of the general government in 2015, while the majority of expenditure chapters remain unchanged. In the first year covered by the new strategy compared to the levels from the previous version of the document, we can observe a reduction in the chapters "other transfers" (-501.8 million lei) and capital expenditure (-8.3 million lei), a decrease which is fully offset by the rise of the allocations for procurement of goods and services (510.1 million lei), leaving total spending unchanged. The reduction by 0.2 pp. of GDP of the deficit target for 2015 (from 1.8% of GDP in the revised FS 2013-2015 to 1.6% of GDP in the current version) is achieved due to lower total expenditure (-1392.5 million lei), explained by reduced allocations under "other transfers" (-1,001.7 million lei) and of projects from EU funds (-964.3 million lei), accompanied by an increase in spending on goods and services by 573.5 million lei. In the year 2016, which is beyond the scope covered by the previous version of the Fiscal Strategy, but it is covered in the Report on the macroeconomic situation in 2013 and the projections for 2014-2016 released alongside with the 2013 budget draft, the reduction of the budget deficit target is propagated (-0.2 pp of GDP, from an initial level of 1.8% to 1.6% of GDP), and it is also due to lower allocations for other transfers (in the same amount as in the previous year, respectively -1,001.7 million lei) and for projects funded by external grants (-1,207.6 million lei), while supplementing spending on goods and services by 739.8 million lei.

The Fiscal Strategy does not describe the specific measures underpinning the substantial reductions in the planned budgetary allocations for the chapters mentioned above. Also, the inflows from post-accession funds and spending for projects financed through reimbursable post-accession funds condition each other: while the estimate of EU funds absorption is not changed, it is difficult to explain to what extent it is possible to reduce expenditure for the projects implemented with EU funds related to the national contribution or considered as ineligible, without seriously affecting the implementation of these projects and thus the materialization of revenues. In this regard, the Fiscal Council considers as absolutely necessary to include in the text of the strategy the concrete measures underlying the planned spending cuts.

The Fiscal Council notes that despite its previous recommendations, an explicit presentation of the assumptions regarding the variation of average earnings and the number of employees in the public sector is still missing, while these information are underlying the trajectory for personnel expenditure for the period covered by the FS 2014-2016 and also the assumptions on the average remuneration per employee and number of employees in the economy. The personnel costs in the public sector, which include for the period 2014-2016 the amounts related to the obligations of the State to certain categories of employees in the public sector as a result of final court rulings[4], remain unchanged compared to the previous version of the strategy. Eliminating the influence of these amounts, the wage bill is expected to increase by 2.76% in 2014, 2.63% in 2015 and only 0.5% in 2016 (an election year). These growth rates involve that in the absence of significant reductions in the number of public sector employees in the coming years, the annual rise of the average wage in the public sector will be below the average forecasted inflation taken into account in the budget construction (3.3% in 2014, 2.8% in 2015 and 2.5% in 2016) and substantially lower than those projected for the private sector[5], which do not appear to be plausible. Given the above, the Fiscal Council maintains its view that the personnel costs during the 2014-2016 periods appear as undervalued.

The above opinions and recommendations of the Fiscal Council were approved by the Chairman of Fiscal Council, according to article 43, paragraph (2), letter d) of Law no. 69/2010, after being approved by the Council members through vote, on May 28th, 2013.

May 28th, 2013

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[4] The budgeted amounts are 900 million in 2013, about 2.2 billion lei in 2014 and 2015, respectively about 3 billion lei in 2016.

[5] The 2013-2016 Convergence Programme takes into account annual increases in the average remuneration per employee in the economy of 4.8% in 2014, and 4.4% in 2015 and 2016.

IV. Fiscal Council's Opinion on the Draft Budget Revision for 2013

On July 29th 2013, at 10:22 PM, the Fiscal Council received from the Ministry of Finance by letter no. 82016/29.07.2013 *The half-year report regarding the economic and budgetary situation, The draft of the budget revision for 2013, the explanatory note and the Government Ordinance project regarding the draft of the budget revision for 2013,* as well as *The explanatory note and the Government Ordinance project regarding the draft of the revised social security budget for 2013*, requesting the Fiscal Council's opinion under article 40, paragraph (2) of Law no. 69/2010. Given the Government's intention to approve the documents mentioned above during the government session taking place on July 30th 2013, the time frame in which the Fiscal Council should elaborate a rigorous analysis is clearly insufficient, therefore the institution will not be able to develop a complete opinion regarding the documents submitted in such a short period of time, reserving its right to issue a more detailed opinion afterwards. The Fiscal Council is forced to reiterate its previously stated recommendation to ensure a period of at least one week between the submission of the documentation by the Ministry of Finance and the adoption of the relevant legislation, this interval being an absolute minimum required to elaborate an accurate analysis. In addition, the draft of the revised budget contains a set of amendments to the Tax Code that will come into force starting September 1st 2013, without being subjected to a public debate for a reasonable period of time, contrary to the spirit of the provisions of article 4, paragraph (1) of the Tax Code, which states that "the present code can be modified and supplemented only by law, after being typically promoted for 6 months before the date of its entry into force".

Given its mandate in accordance with the provisions of the Law no. 69/2010, article 40, paragraph (2), letter d), **the Fiscal Council states and issues the following opinions and recommendations on the draft revised budget:**

1. The assessment of compliance with the rules established by Law no. 69/2010

a. The draft of the revised budget does not comply with the rule established by article 6, letter b) of Law no. 69/2010, according to which "the balance (overall and primary) of the general consolidated budget for the forthcoming budget year should not exceed the threshold specified in the fiscal framework section of the fiscal strategy approved by the Parliament". The draft of the revised budget states a 14.7 billion lei budget deficit , higher by 1.3 billion lei than the limit of 13.394 billion lei stipulated by Law no. 4/2013.

b. The draft budget amendment does not comply with the rule established by article 6, letter c) of the Law no. 69/2010, according to which "the total expenditure (which shall exclude EU funds and personnel expenditure) for the state budget, social budgets, local budgets, self-financed institutions budgets, special funds budgets and other budgets shall not exceed the ceilings specified in the fiscal strategy for the forthcoming year". The total expenditures of the draft budget revision, net of the impact of financial assistance from the EU and from other donors, are 211.3222 billion lei, exceeding with 493 million lei the threshold stated in Law no. 4/2013. However, the proposed personal expenditure of 46.1527 billion lei is within the stated ceiling of 46.156 billion lei.

c. Also, the draft budget revision does not meet the requirements stipulated in article 16 of Law no. 69/2010, according to which "the total expenditure of the consolidated general budget, excluding the financial assistance from the EU, shall not be increased during budgetary revisions, except for adjustments concerning debt service payments or Romania's contribution to the EU budget", considering that the increase of total expenditure with 493 million lei as defined in the above article is mainly due to the increase in spending on goods and services (+2,503 million lei compared with the initial budget), partially offset by cuts in expenditure related to projects funded by external post-accession grants (-465 million lei), social assistance (-603.7 million lei) and other transfers (-480.3 million lei).

In the Fiscal Council's opinion, the violation of the fiscal rules seriously undermines their credibility, especially in terms of budget deficit target rule, for which the derogation is a first (the increase of last year's target budget deficit was covered by the escape clauses specified in Law no. 69/2010).

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

July 30th, 2013

Chairman of the Fiscal Council

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V. Fiscal Council's Opinion on the Half-Year Report Regarding the Economic and Budgetary Situation and Fiscal Council's Opinion on the Draft Budget Revision for 2013

The Fiscal Council issued a preliminary opinion on the draft budget revision on July 30th 2013, but, considering the insufficient time available to assess the relevant documents, the Fiscal Council reserved the right to complete it later. This opinion incorporates the assessment of the Half-Year Report regarding the economic situation in the first 6 months of 2013, uncovered by the previously opinion, as well as the additions to the latter regarding the draft of the revised consolidated budget for 2013.

1. Fiscal Council's Opinion on the Half-Year Report Regarding the Economic and Budgetary Situation

Under article 40, paragraph (2) of the Fiscal Responsibility Law no. 69/2010, the Fiscal Council has the legal requirement to "assess the budgetary performance of the Government against the fiscal targets and policies specified in the fiscal strategy and the compliance of such policies with the principles and rules specified in this law, through analyzing and issuing opinions and recommendations on the half-yearly report regarding the economic and budgetary situation".

According to article 29 of Law no. 69/2010, each year by the end of July, the Ministry of Finance should publish on its website a half-year report on the economic and budgetary situation.

In addition, under article 30 of Law no. 69/2010, the Half-Year report on the economic and budgetary situation must include, without being limited to, the following:

a) A review of the macroeconomic framework and the latest data on macroeconomic indicators identifying significant trends and changes since the annual budget law was finalized.
b) An assessment of the impact on the fiscal targets of any changes in the macroeconomic framework and the presentation of necessary measures to be taken to correct such impacts.
c) Data on the consolidated general budget revenues, detailed on each category of revenue, indicating the initial forecast, the revenues collected in the first six months and an updated forecast for the entire year.
d) Data on the consolidated general budget expenditures, detailed by economic and functional classification for each constituent budget of the consolidated general budget, indicating the approved expenditure, the expenditures incurred in the first six months and an updated forecast for the entire year.

e) Data on the state budget expenditure, detailed in economic classification for each central government institution, indicating the approved expenditure, the expenditures incurred in the first six months and an updated forecast for the entire year.
f) Data on the budgetary balance for both the consolidated general budget (total and primary) and for each budget of the consolidated general budget, indicating the approved program, the result achieved in the first six months and an updated forecast for the entire year.
g) Data on the absorption of European funds, indicating the approved program, the results achieved in the first six months and an updated forecast for the entire year.
h) Data on outstanding expenditure payments for the end of Q1 and forecast for half-year, including arrears and floating debt, for each constituent budget in the consolidated general budget.
i) Data on the government debt and the financing of the budget deficit.
j) Explanations for any failure to collect the forecasted revenues, indicating the measures taken and those planned to improve the collection.

Thus, given its mandate in accordance with Law no. 69/2010, **the Fiscal Council states and issues the following opinions and recommendations:**

The Half-Year Report on the economic and budgetary situation conducts an analysis of the latest data regarding macroeconomic indicators, but it does not identify the trends and significant changes compared to the projections included in the state budget and social security budget laws as required by Law no. 69/2010. In addition, the impact of macroeconomic forecasts revision for the current year and the medium term over the budgetary targets is not quantified and no details regarding the measures to be adopted are mentioned, as required by Law no. 69/2010, under article 30 letter b). In the Fiscal Council's opinion, an assessment of the macroeconomic framework revision's impact over the budget would have been necessary even more, although the economic growth forecast for 2013 has been revised upwards from 1.6% to 2%, mainly based on an evolution beyond expectations of the agricultural sector, on the supply side, respectively of the net exports, on the demand side, and that revenues are not very sensitive to these components of GDP. At the same time, the domestic demand (consumption and investment) registered a weak evolution in the first half of 2013, the updated forecasts pointing that the domestic demand's dynamic could be far below the initial expectations for 2013, with a negative impact on revenues.

The budget execution on the revenue side in the first six months shows a significant underperformance, with a gap of over 6.5 billion lei between the program for the first semester and the actual revenues (leading to a level of only 93.7% achievement of the program), excluding the impact of swap schemes which led to the clearing of state companies' overdue payments. The biggest revenues gaps compared to the program have been recorded in the case of amounts received from the EU (-3,347 million lei), corporate income tax (-827 million lei), excises (-713 million lei), VAT (-485 million lei) and non-tax revenues (-467 million lei).

On the expenditure side compared to the targets set for the first semester, total expenditures have been fulfilled at a rate of 93.5%, an achievement of over 100% being recorded in the personnel expenses and other expenses. A significantly lower than expected ratio can be observed in capital expenditures (-1,471 million lei gap) and other investment expenses (including EU funds, -1,881 million lei gap), reflecting a tool to reach the budget deficit target for the first semester, but also an inability to absorb EU funds for planned investments.

On the tax revenue side, the worst performance was recorded by the corporate income tax, revenues in this area decreasing by 5.5% compared to the first semester of 2012, leading to an 827 million lei lower result than the half-year program. The negative evolution was determined by repayments to commercial banks[6] as a result of lower than expected profits, but also by the very weak evolution of revenues from non-financial businesses (registering an increase of only 0.2% over the same period of 2012, compared to a forecasted increase in the initial budget for 2013 of 8.3%), the latter being negatively influenced by the poor financial performance of companies[7]. The second worst performance on the tax revenue side was recorded in the case of *excises,* the revenues being 713 million lower than the target set in the half-year program (only a 93.3% ratio of achievement), and increasing by only 4.2% compared to the first semester of the previous year, well below the 10.4% projected growth in the initial budget for 2013, given that in 2013 the excise taxes on beer, cigarettes and diesel fuel were increased and the exchange rate used for calculating the excise increased by 5.2% in comparison with the one registered in 2012, suggesting a decrease in consumption of excisable goods and/or an increase in tax evasion.

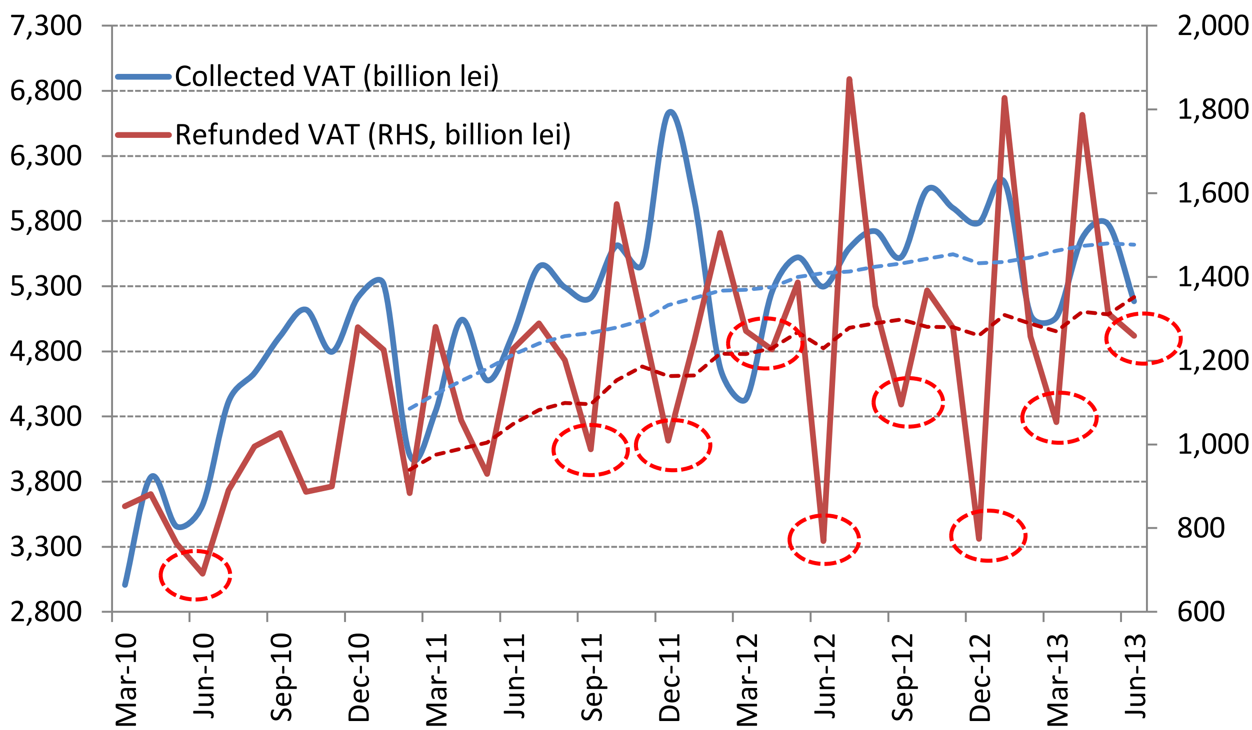
In the case of *VAT* revenue, the execution at 6 months shows a result lower by 485 million lei compared to the program, the net VAT revenues increasing by only 3.3% over the first semester of 2012 (excluding the impact of swap schemes). The evolution of VAT revenues was negatively affected by the lower household final consumption in the first part of the year (-0.3% in real

[6] Banking companies contributors – Romanian legal entities and branches of banks in Romania – foreign legal entities that are required under the Tax Code to declare and pay corporate income tax annually (with submission of the declaration by March 25th the following year), with prepayments that are performed quarterly and indexed to inflation. Given that 2012 recorded an aggregate loss of 2.347 billion lei of the banking system compared to 0.786 billion lei in 2011, the regularization made in early 2013 to prepayments from 2012 meant corporate income tax refunds for the amounts overpaid in 2012.

[7] According to the National Trade Register Office data, the number of companies that became insolvent in the first 5 months of 2013 was 9.5% higher compared to the first 5 months of 2012, reaching a new record high. Moreover, according to a Coface study, the insolvencies rate – the number of insolvencies opened to the number of active companies – in Romania is very high, reaching in 2012 a level of 5.67% compared to 0.35% in Bulgaria, 0.04% in Poland, 0.47% in Czech Republic, 0.1% in Slovakia and 3.84% in Hungary. In addition, during the first 5 months of 2013, the average turnover of a company that entered in the insolvency procedure was over 60% higher than the same period of 2012.

terms in the first quarter of 2013 compared to the same period of last year) and by the decrease of extra-EU imports (-6.0% in January – June 2013 over the same period of 2012). In addition, it is worth noting that although the trend of VAT collected and VAT refunded is similar, the net VAT revenues had a volatile evolution, induced by the very high monthly volatility of VAT refunds. Thus, as noted in the chart below, since September 2011, at the end of each quarter there is a pronounced decrease of VAT refunds compared to the previous months, the discretionary mitigation of refunds being probably used to achieve the deficit targets in cash terms. The Fiscal Council recommends reducing the volatility of VAT refunds, which is likely to adversely affect the liquidity and the overall financial situation of the companies receiving VAT refunds.

The monthly evolution of collected and refunded VAT



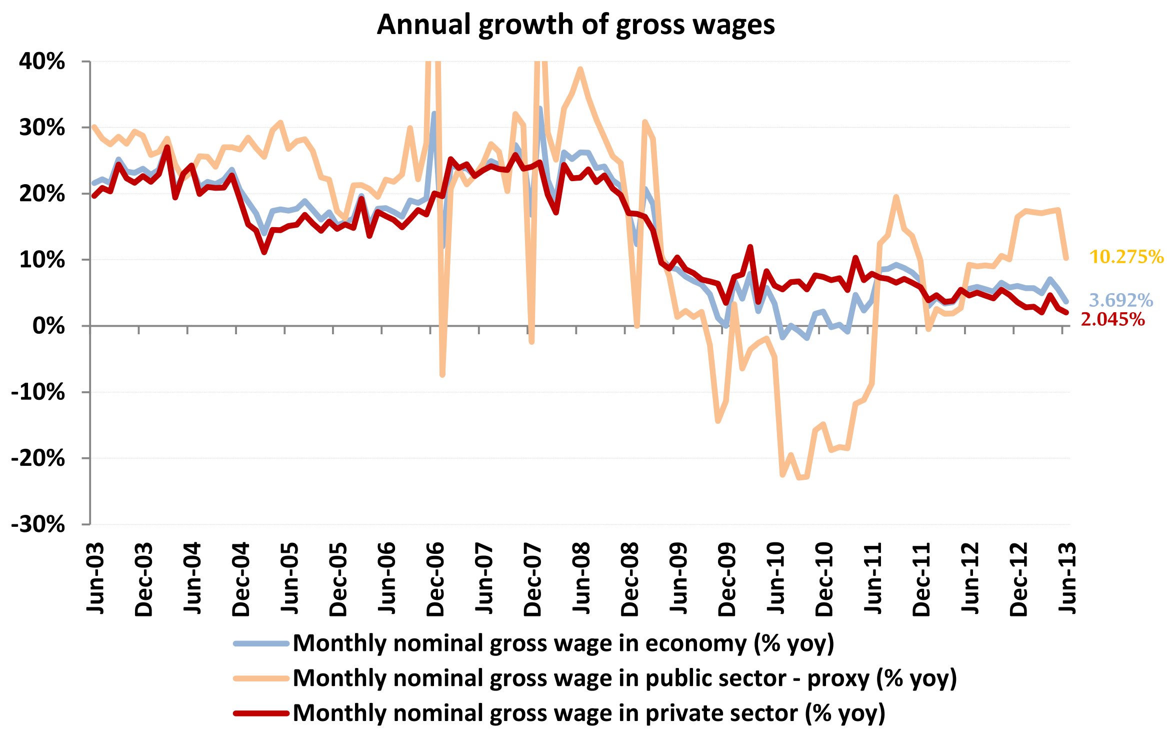
Source: Ministry of Public Finance

Note: The dotted lines are the 12-month moving averages

Receipts from *personal income tax* had an evolution in line with expectations, achieving 99.9% of the half-year program target and registering an increase of 9.3% over the first half of 2012, being mainly influenced by the reunification of the salaries in the public sector, the augmentation of the average gross wage (with 5.4% in the first half of 2013 compared to the first half of 2012), the increase in the number of employees (with 2.4% in the first 5 months of 2013 compared to the same period of 2012) and by the increase of the minimum wage[8]. However, the developments in recent months show that the increase of the gross average wage in the economy is registering a slowdown, especially in the private sector, where gross

[8] From 700 lei to 750 lei, from the 1st of February 2013 according to G.D. No. 23/2013.

wages expressed in real terms have decreased in the last 3 quarters, rendering the expectations embedded in the original budget for 2013, of a gross average wage growth in the economy by more than 7% in 2013, barely plausible.



Source: NIS, Ministry of Public Finance

Receipts from *property tax* rose by 9.5% in the first half of 2013 compared to the first half of 2012, due to the update of the taxable value for property tax, the degree of achievement of the revenue program being 105.7%. The collections from the *taxes on using goods, authorizing the use of goods* or *on carrying activities* grew considerably with 163.9% in the first half of 2013 compared to the first half of 2012, due to the collection, in June 2013, of the license fees for rights of use of radio frequencies, according to G.D. No. 605/2012, and the revenue program in this area registered an achievement rate of 109.5%.

Social security contributions collected by the consolidated general budget increased by 4.3% compared to the same period of the last year and the degree of achievement of the revenue program in this department was 99.8%. The growth was primarily driven by the same factors that influenced the development of revenues from personal income tax.

The *amounts received from the European Union* had an evolution considerably below expectations, the achievement degree of the half-year program being only 47.6%, reflecting a *significant failure in the absorption of EU funds*. According to European Commission data, in the case of structural funds, Romania had by far the lowest rate of absorption of EU funds in Europe in the period 2007-2013, the differences compared to other countries being very high.

The Half–Year Report regarding the economic and budgetary situation presents data on the absorption of EU funds received, stating the approved program and the result achieved in the first 6 months, but it does not present an updated forecast for the full year, as required by Law no. 69/2010. In addition, according to the Fiscal Council, an assessment of the potential impact that any financial corrections on EU funds might have on the budget in the coming years is absolutely necessary.

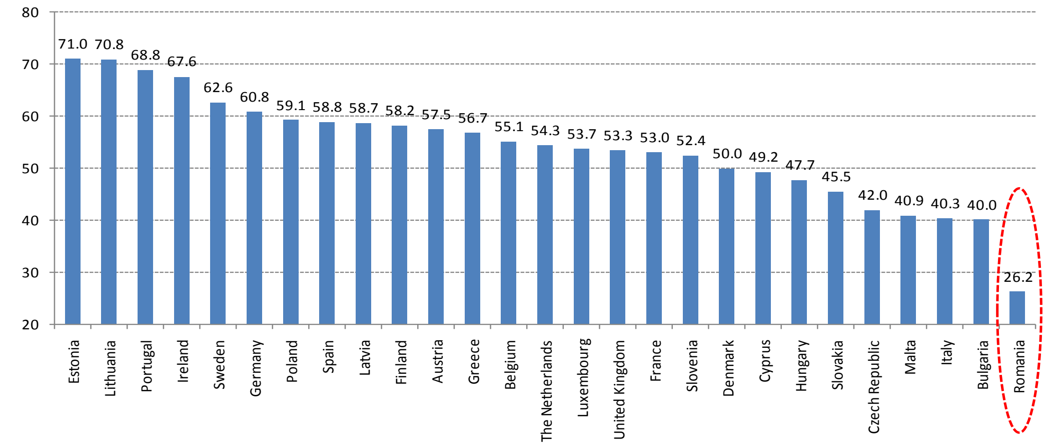
The evolution of financial flows between Romania and the European Union at 30.06.2013

billion euros

No.	Name	Initial program 2013	Actual 30.06.2013		Cumulative 2007-2013
			billion euros	%	
0	A	1	2	3	4
1	**I. AMOUNTS RECEIVED FROM THE EU BUDGET (A+B)**	**8.707,6**	**2.524,0**	**29,0**	**18.045,0**
2	A. Pre-accession funds	81,1	27,7	34,1	2.656,0
3	B. Post-accession funds, of which:	8.626,5	2.496,3	28,9	15.389,0
4	i) Advances	106,7	46,6	43,7	3.802,3
5	ii) Reimbursements (including FEGA)	8.519, 8	2.449,7	28,7	11.586,7
6	B1. Structural and cohesion funds, of which:	5.754,7	755,5	13,1	5.128,0
7	a) Advances	0,0	0,0	0,0	2.125,8
8	b) Reimbursements	5.754,7	755,5	13,1	3.002,2
9	B2. Funds for rural development and fishing, of which:	1.416,8	608,4	42,9	4.501,8
10	a) Advances/Pre-financing	0,0	0,0	0,0	601,0
11	b) Reimbursements	1.416,8	608,4	42,9	3.900,8
12	B3. The European Agricultural Guarantee Fund (EAGF)	1.323,6	1.082,2	81,8	4.550,9
13	B4.Other (post-accession), of which:	131,4	50,2	38,2	1.208,3
14	a) Advances	106,7	46,6	43,7	1.075,5
15	b) Reimbursements	24,7	3,6	14,6	132,8
16	**II. AMOUNTS PAID TO EU (C+D)**	**1.542,8**	**1.012,4**	**65,6**	**8.679,6**
17	C. Romania's contribution to the EU budget	1.477,8	952,5	64,5	8.393,0
18	D. Other contributions	65,0	59,9	92,0	286,6
19	**III. The balance flows = I - II**	**7.164,8**	**1.511,6**	**21,1**	**9.365,4**

Source: Ministry of Public Finance

The absorbtion rate of structural and cohesion funds in EU countries (%, 13th of June, 2013)



Source: Current data published by the European Commission - DG Regio[9]. Data include the advances received.

In the Fiscal Council's opinion, the Half–Year Report regarding the economic and budgetary situation is not sufficiently detailed in terms of justifying the significant failure in achieving the forecasted revenues for the first 6 months and it does not particularize the measures taken and those planned specifically for improving the collection in the second semester.

On the *expenditure side*, the amounts reached a level of 93.5% of the planned expenditure in the first semester, increasing by 4.8% in nominal terms over the same period of the previous year (excluding the impact of swap schemes). Expenditure increases were recorded over the first semester of 2012 in personnel expenses (+18%), goods and services expenses (+6.8%), subsidies (+9.3%), other transfers (+19%) and interest payments (+0.7%). Expenditure decreases were recorded only in projects funded by external post-accession grants (-19.2%), capital expenditure (-9.8%) and expenditure funded from reimbursable funds (-33.3%).

Personnel expenses increased by 18% over the previous year, primarily due to the reunification of budgetary wages, recording a surplus of 0.6% (136 million lei) over the half-year program target. The difference was generated by the fact that the original budget for 2013 considered funding a maximum of 1,187,000 jobs in the public sector, but the monthly average number of occupied jobs in the public sector in the first 6 months was higher by 2,197 jobs (1,189,197 total occupied jobs).

Compared to December 2008, the number of occupied jobs in the public sector declined to a minimum of 1,187,070 in September 2012, recording a decrease of over 15% (-211,152 occupied jobs), mainly due to the introduction of a rule stating that only 1 new employee shall be hired for every 7 departures from the system. The largest decreases were registered in this period in the case of local executive authorities (-87,119), pre-university education (-38,305), health care (-23,604[10]), the Ministry of Internal Affairs (-12,401), the Ministry of Public Finance (-5,504), the Ministry of Agriculture and Rural Development (-3,518) and the Ministry of

[9] http://ec.europa.eu/regional_policy/thefunds/funding/index_en.cfm
[10] Some hospitals have been moved under the authority of local governments.

National Defense (-3,036). The highest increases were registered in this period in the case of the General Secretariat of the Government (+4,653), the Ministry of Labor (+1,840), the Ministry of Justice (+1,649) and the Ministry of Economy (+1,502). Since October 2012, after the implementation of the rule 1 to 7 became more lax, the number of occupied jobs in the public sector began to increase (+2,325 during September 2012 – June 2013), the highest increases up to June 2013 being registered by the Ministry of Internal Affairs (+2,062), in the department of pre-university education (+1,493), the Ministry of Regional Development and Public Administration (+908) and by the Ministry of Justice (+419), while the largest decreases were recorded in the case of GSG (-1,539), local executive authorities (-865) and the Ministry of Finance (-413).

In light of these developments, the Fiscal Council recommends a cautious approach in the transition from rule 7 – 1 to 1 – 1 and a very careful monitoring of monthly personnel expenditure in order to avoid overruns related to personnel expenses for 2013, which would lead to a renewed violation of the Fiscal Responsibility Law No. 69/2010.

Evolution of public sector employment

	Differences (September 2012 - December 2008)		Differences (June 2013 - September 2012)
	jobs number	%	jobs number
Total employment, of which:	-211,152	-15.1%	2,325
I. CENTRAL ADMINISTRATION, of which:	-179,507	-25.8%	1,469
1.Institutions financed from the state budget	-20,560	-6.1%	13,759
Presidential Administration	-35	-15.6%	13
Senate of Romania	-32	-3.9%	40
Chamber of Deputies	-124	-6.9%	107
High Court of Cassation and Justice	-36	-7.7%	25
Constitutional Court of Romania	-2	-2.1%	-1
Legislative Council	-21	-21.0%	-3
Romanian Court of Accounts	134	10.0%	28
Competition Council	-13	-4.2%	15
Romanian Ombudsman	-18	-18.2%	5
The National Council for the Study of the Securitate Archives	-22	-8.6%	1
National Audiovisual Council of Romania	-32	-19.3%	-2
General Secretariat of the Government	4,653	169.6%	-1,539
Ministry of Foreign Affairs	-487	-19.1%	145
Ministry of Regional Development and Public Administration	113	17.9%	908
Ministry of Public Finance	-5,504	-16.3%	-413
Ministry of Justice	1,649	12.2%	419
Ministry of National Defense	-3,036	-3.8%	171
Ministry of Internal Affairs	-12,401	-8.4%	2,062
Ministry of Labor, Family, Social Protection and Elderly	1,840	62.2%	26
Ministry for Youth and Sports	-535	-100.0%	171
Ministry of Agriculture and Rural Development	-3,518	-32.7%	-120
Ministry of Environment and Climate Changes	33	0.8%	82
Ministry of Transportation	-245	-30.5%	27
Ministry of National Education	-2,972	-27.4%	-67

	Differences (September 2012 - December 2008)		Differences (June 2013 - September 2012)
	jobs number	%	jobs number
Ministry of Health	-1,132	-15.3%	11,206
Ministry of Culture	-377	-43.4%	-95
Ministry of Communication and Information Society	62	44.6%	-3
Public Ministry	185	3.6%	99
The National Integrity Agency	-34	-29.1%	2
The Protection and Guard Service	-129	-8.0%	20
The Special Telecommunications Service	-201	-6.9%	14
Ministry of Economy	1,502		174
The Romanian Academy	-325	-8.7%	4
State Secretariat for the Revolutionary Problems	-6	-16.2%	0
The National Office for Prevention and Control of Money Laundering	-11	-10.8%	1
National Registry Office tor Classified Information	-21	-17.9%	3
National Council for Combating Discrimination	2	3.1%	-2
Superior Council of Magistracy	-9	-2.5%	30
Permanent Electoral Authority	-24	-15.9%	12
The National Supervisory Authority For Personal Data Processing	-3	-6.3%	-3
The Economic and Social Committee	-4	-12.5%	-1
National Council for Solving Complaints	89		2
State Assets Management Authority	260		-15
Ministry of European funds	227		58
National Authority for Properties' Restitution	0		153
2. Institutions financed from the social security's budget	-2,506	-22.6%	-79
3. Institutions subsidized from the state budget and unemployment insurance fund	-4,939	-12.0%	-162
4. Self-financed institutions, of which:	-151,502	-49.8%	-12,049
- hospitals	-140,305	-67.0%	-11,929
- universities	214	0.3%	9
- other institutions	-11,411	-42.6%	-129
II. LOCAL AUTHORITIES, of which:	-31,645	-4.5%	856
1. Institutions financed from the local budgets, of which:	-125,424	-19.5%	628
- pre-university education	-38,305	-11.5%	1,493
- local executive authorities	-87,119	-28.0%	-865
2. Institutions fully or partly funded from own revenues, of which:	93,779	156.6%	228
- hospitals from the health network of local authorities	116,701		1,259

Source: Ministry of Public Finance

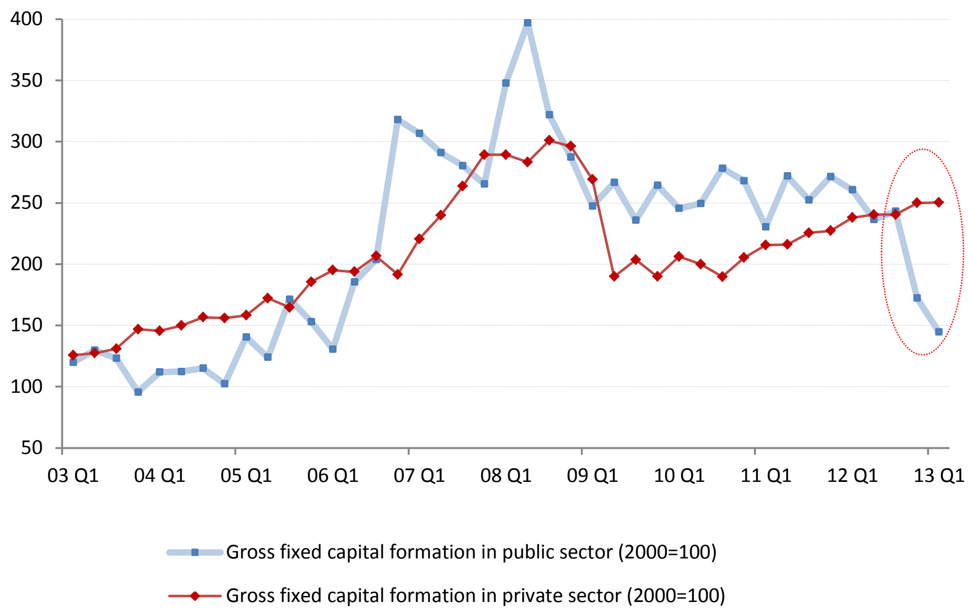
Expenditure on goods and services increased by 6.8% in the first semester of 2013 compared to the first semester of 2012, recording a half-year program underperformance of 1,057 million lei also as a result of the delay of implementation of the EU Directive 7/2011 on combating late payments in commercial contracts[11] until August 2013.

[11] This directive states that “agreements between enterprises should provide limited payment terms, as a rule, at 60 calendar days”. In addition, “it should provide specific norms regarding commercial transactions for the supply of goods and services by enterprises to public authorities, rules to determine, in particular, payment terms that do not normally exceed 30 calendar days, unless the contract expressly provides otherwise, which must be objectively justified by the nature or features of the contract, but not exceed, in any case, 60 calendar days.”

Investment expenditure including projects funded from post-accession external grants, expenditure from reimbursable funds, capital expenditure and other transfers for investments are revised downward by 11.1% compared to the first semester of 2012, representing only 74.5% of the half-year program (with -4,149 million lei less than half-year program). This significant underperformance of the half-year program was generated by the far below expectations EU funds absorption (68.2% achievement of the half-year program) and by the reduction in capital expenditure from own sources (-1,471 million lei compared to the first half of 2012, 83.3% achievement of the half-year program).

The public investment spending decrease of 11.1% in the first half of 2013 compared to the first half of 2012 in cash standards was significantly higher is ESA95 terms (accrual based accounting). Thus, according to the available data, in real terms, public investment expenditure in ESA95 standards decreased by 29.9% in the fourth quarter of 2012, respectively by 32.8% in the first quarter of 2013 compared to the same period of the previous years, thus having a strongly negative contribution to economic growth.

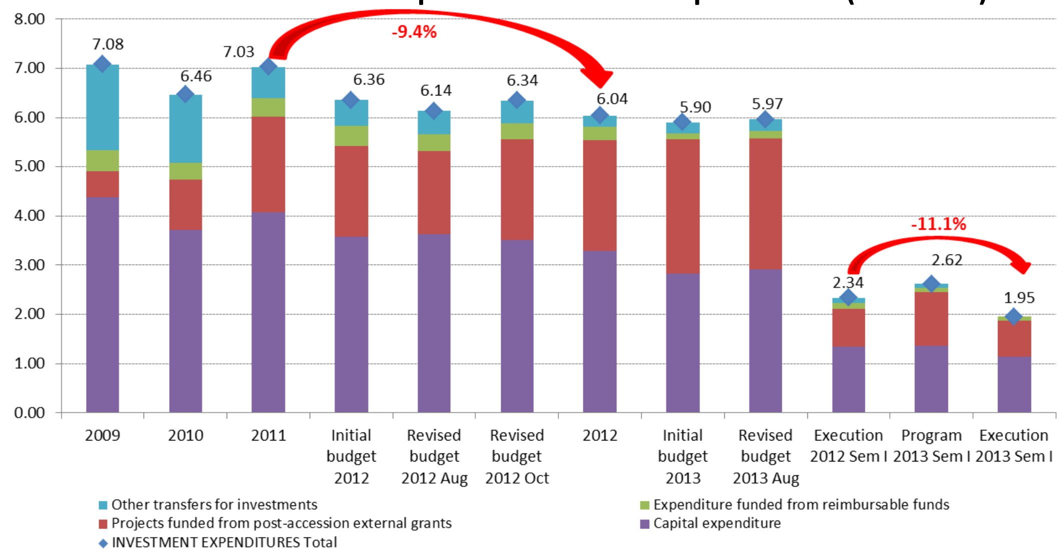
Evolution of investment expenditures in real terms (ESA95)



Source: INS, EUROSTAT

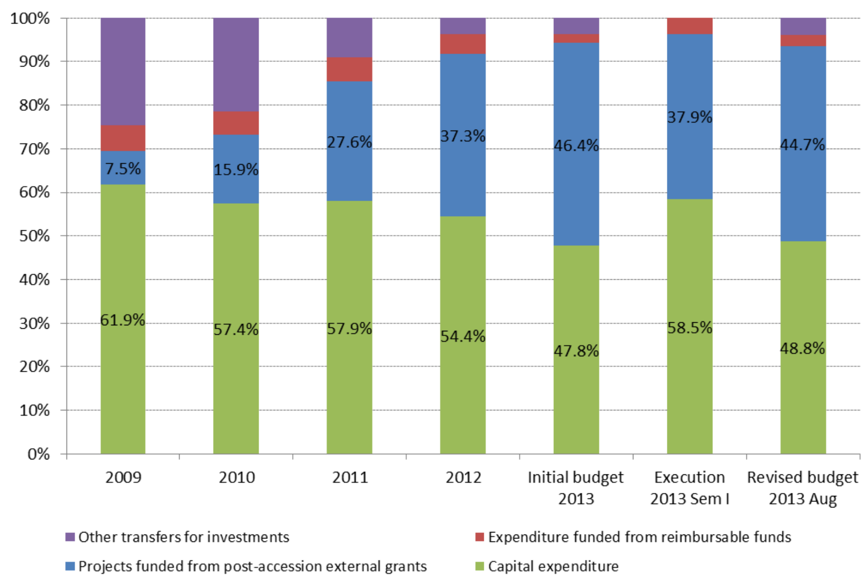
In the initial budget for 2013, it was intended to increase the share of EU funds absorption in total investment expenditure, a right and welcomed approach in the Fiscal Council's opinion, but unfortunately the budget execution in the first 6 months shows a failure in this regard. Within this context, the Fiscal Council recommends the urgent implementation in the legislation of some clear criteria for prioritizing public investments in order to also promote a shift in funding from own resources to European funds, doubled by a budgeting on a multiannual basis.

The evolution of public investment expenditures (% of GDP)



Source: Ministry of Public Finance

The structure of public investment expenditures



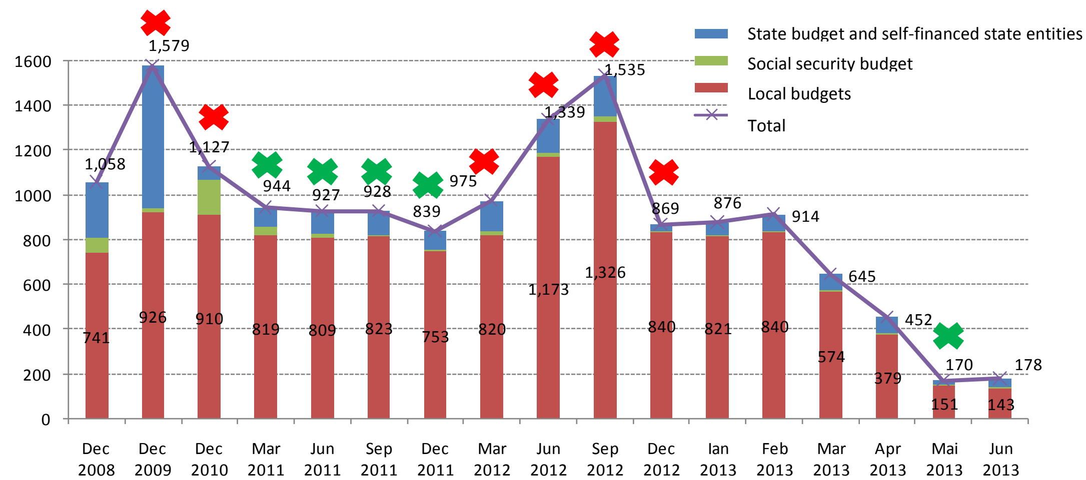
Source: Ministry of Public Finance

In conclusion, a significant underperformance on the revenue side of the budget was balanced during the first 6 months of 2013 primarily by reducing investment expenditure, by maintaining goods and services expenditure at a level well below the planned one, by interest expenditure under the half-year program and by social assistance expenditure well below expectations.

Regarding ***arrears,*** after 2011 when the targets were met, with arrears recording a downward trend, the targets for 2012 were again missed. The arrears monitored by the IMF (overdue more than 90 days) decreased decisively during March –June 2013. However, if we consider all the ammounts overdue, not only those over 90 days, their current level is still high, at about 0.39% of GDP in June 2013. Most of the arrears are located on the social security budget and on the local budgets. Local budgets arrears' problem appears as a recurring structural problem and it mainly reflects a lack of financial discipline and lack of enforcement of Local Public Finance Law (Law 273/2006, with its subsequent amendments).

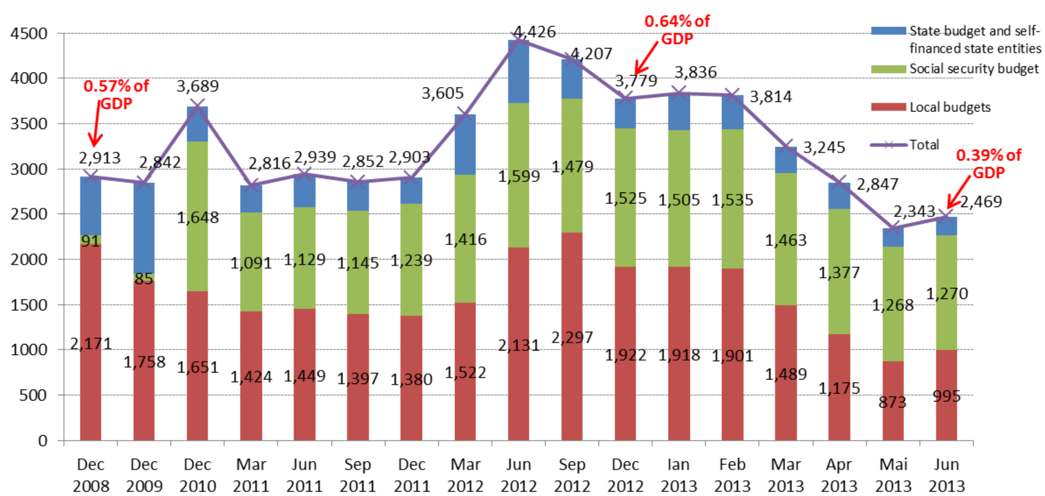
Moreover, although arrears over 90 days to the social security budget appear to be eliminated, those between 0-90 days for invoices issued in this sector seem to remain high. In addition, there are unpaid bills[12] for drugs that do not yet appear to be arrears in the system, as the contractual payment terms were extended to 210 days. Effectively, these invoices are paid when appearing as arrears over 90 days, that is at over 300 days of the issue, which makes it more difficult to apply the EU Directive no. 7/2011.

The evolution of budget arrears 90-360 days (mn lei)



Source: Ministry of Public Finance

The evolution of budget arrears 0-360 days (mn lei)



Source: Ministry of Public Finance

[12] The amount is over 1 billion euro equivalent according to the Association of Pharmaceutical Distributors and Retailers in Romania (ADRFR), http://adrfr.ro/ro/a/60dezile.html.

Regarding ***the financing of the budget deficit and of the public debt***, the Half-Year Report on the economic and budgetary situation shows how the budget deficit was financed and how the public debt was refinanced in the first semester. The Fiscal Council considers the strategy adopted by the Ministry of Finance in the first semester of 2013 to be adequate, as it managed ***to build a comfortable liquidity buffer and to improve the public debt maturity profile.***

2. Additions to the preliminary opinion on the Draft Budget Revision for 2013

The draft budget revision is based on an economic growth of 2%, the economic advance being revised upward from the initial projection of 1.6%, mainly as a result of the evolution beyond expectations of the economic activity in the first quarter of the current year and as a consequence of a higher than expected evolution of the agricultural sector. The increase in real GDP in the first three months of 2013 was entirely due to the external demand, given that consumption and investment had a negative contribution to the growth rate. The short-term economic indicators (the evolution of the industrial production, turnover in retail trade, data on international trade of goods of Romania, etc.) points out to the continuation of this trend also in the second quarter of 2013, which could lead to further changes in the structure of the forecasted economic advance. The Fiscal Council considers as realistic the prognosis of economic growth for 2013, the balance of risks being tilted on the positive side, respectively registering a higher economic advance, given that a normal agricultural year only will contribute substantially to the economic growth rate, taking into account the significant base effect caused by the very poor agricultural production in 2012. However, a further deterioration in international financial markets sentiment, primarily due to concerns about the withdrawal of the financial stimulus in the U.S., but also as a result of the modest economic activity in the euro area could contribute negatively to the growth rate. Moreover, an additional increase of GDP determined by the agricultural production is unlikely to be reflected in a proportional increase of revenues given the experience of the previous years. Also, the explanatory memorandum accompanying the budget revision does not contain a sufficiently detailed macroeconomic framework, respectively the anticipated dynamics of the GDP components, which are absolutely necessary in order to rigorously perform a revenue forecast, are not specified.

Budgetary revenues and expenditures

The draft of the revised consolidated budget estimates an increase in the general government revenues by 0.12 billion lei and also an increase of the overall expenditure by 1.43 billion lei as compared to the initial program, revising upward the deficit target according to the cash methodology from 2.1 to 2.3 percent of GDP and thus violating the provisions of Law no. 4/2013 regarding the approval of ceilings for certain indicators specified in the Fiscal Strategy.

The increase in budget revenues is generated exclusively by a new swap scheme with the purpose of clearing budgetary arrears. According to this scheme, 1.12 billion lei will be transferred from the state budget to local budgets and to certain state owned companies, so that ultimately the outstanding obligations to the budget will be eliminated, while the influence on the budget deficit is neutral.

Excluding the impact of compensation schemes, the revenues are projected to decrease by 1 billion lei as a consequence of the unfavorable impact of the downward revision of VAT revenues (-0.89 billion lei), corporate income tax (-0.85 billion lei), excise revenues (-0.52 billion lei) and non-tax revenues (-0.39 billion lei). Extra revenues are projected to be collected from EU funds (+0.93 billion lei), due to the diminishing national contribution as a consequence of continuing the program with the EU and the IMF, and also from other taxes on goods and services (+0.83 billion lei), as the *clawback tax* revenues were not included in the initial projection. The downward revision for VAT and excise revenues is due to the adverse evolution of private consumption as the economic growth was supported by the external demand and it is also due to the reduction in VAT rate for bread, flour and wheat. In the case of corporate income tax, the reduction is attributable to the adjustment of commercial banks obligations, as the anticipated payments based on the 2011 profits were higher than the actual amounts due for 2012 (the profits from 2011, indexed with the 2012 inflation rate were used as tax base).

The Fiscal Council expresses serious reserves regarding the projection of certain budgetary revenues considering the outcomes registered in the first semester and the recent development of relevant macroeconomic indicators. For instance, the personal income tax (PIT) dynamics compared to the previous year's similar period of time is projected to speed up to 10.8% until the end of 2013 compared to 9.29% in the first semester, even if the annualized increase of wages in June decelerated at 3.7%, pointing to an unrealistic estimation of PIT revenues for this year. The evolution of wages dynamics can be explained by the unfavorable base effect generated by the dissipated impact of public sector wages' recovery and the very modest increase in private sector wages. Thus, the PIT projections were not revised downward, even if the macroeconomic forecast considered in the initial budget indicating a 7% increase in gross wages seems quite optimistic at this moment, while the increase in employment and the proposed discretionary measures seem not to fully compensate the adverse wage dynamics. The same reasoning is valid for the revenues from social contributions that are projected to increase by 6.2% compared to last year, even if in the first semester the annualized rate was only 4.26%, displaying an unrealistic projection for these revenues. Under these circumstances, the Fiscal Council assesses that the revenues from PIT and social contributions are overestimated by around 1 billion lei.

Also, in our opinion there are considerable downside risks regarding the projection of VAT revenues due to the adverse development of private consumption. Meanwhile, the loss in revenues attributable to the reduction of the standard VAT rate for bread, flour and wheat seems to be correctly evaluated, our estimations being close to those produced by the MoF. On the other hand, the Fiscal Council expresses reserves regarding the magnitude of the positive impact generated by the compensatory measures (increase in excise rate for alcohol and luxury products). In addition, achieving the targets regarding the absorption of EU funds seems to be a major challenge, the targets being practically unrealistic as the revised budget foresees an increase by 52.3% compared to 2012, while the budget execution for the first semester shows a reduction of 5% compared to the same period of the previous year. Regarding corporate income tax, despite the first semester's disappointing results, the operative figures for July are more favorable, therefore the revised projection can be appreciated as realistic.

In conclusion, even if the economic growth was revised upward to 2%, its structure is not the *tax rich* type (respectively favorable to an increase in budgetary revenues), which means that the collections could be even less significant than the ones stated in the initial budget.

The upward revision of budgetary expenditure by 1.43 billion lei reflects a supplementation of the swap scheme for clearing budgetary arrears (1.12 billion lei, out of which „capital expenditures" 618 million lei, respectively „goods and services" 500 million lei) and of the overall spending by 310 million lei. This increase is mainly due to spending on goods and services (+2 billion lei, partially compensated through revenues from the *clawback* tax) and it is motivated by an acceleration of the payment of arrears in the healthcare system, reflecting the lack of reforms in this sector. Downward revisions of the expenditure are considered for the departments of „social assistance" (–604 million lei), „ capital spending" (-439 million lei), „projects financed through post accession grants" (-466 million lei), while the „other transfers" chapter is diminished by 565 million lei, but the reasons behind this revision are not explained.

Regarding the expenditure on goods and services, in February 2013, in the opinion on the revised Fiscal Strategy for the period 2013-2015, the Fiscal Council already drew attention on the underestimation of these allocations and warned about the significant risks of exceeding the amounts proposed in the budget. The initial level was quite difficult to achieve considering the impact of the EU Directive no. 7/2011 on combating late payments in commercial contracts, which was initially estimated at around 3.5 billion lei (0.54% of GDP). In this context, the Fiscal Council notices serious deficiencies in the budgeting process, as the initial projected levels were frequently exceeded during the last years, thus affecting the credibility of the trajectory projected for this category of expenditure. Even if the revenues from the claw*back* tax, which were not included in the initial budget, were to be used for financing goods and services expenditures, the magnitude of the revision (+2 billion lei, respectively around 0.3% of GDP) cannot be explained only by this influence. In this context, the Fiscal Council recommends an appropriate budgeting strategy for goods and services expenditure, in accordance with the assumed commitments, so that this category will no longer represent a factor of uncertainty that threatens the fiscal position on the occasion of a budget amendment. In the medium term, we consider that a more efficient spending strategy on goods and services is not possible without implementing deep structural reforms, mainly in the healthcare system, and without a more efficient public procurement system in general.

Also, the Fiscal Council notes the presence of reserves regarding interest expenditures (that seem to be overestimated) in the context of a significant reduction in financing costs recorded in the first 7 months of 2013. Even if the magnitude of the reduction in the interest rate paid by the government was quite large, the positive impact on the effective interest expenditure will be observed gradually, as the debt issued will reach its maturity and it will be refinanced under more favorable market conditions.

In conclusion, the Fiscal Council considers that achieving the new deficit target for this year seems to depend to a great extent on the realization of budgetary revenues projection, which appears to be optimistic, so there is a downside risks, respectively smaller revenues will be collected than the amounts projected in the draft revised budget, situation that should be compensated through a strict control of expenditures and through enhanced tax revenue collection efforts.

The above opinions and recommendations of the Fiscal Council were approved by the Chairman of the Fiscal Council, according to article 43, paragraph (2), letter d) of Law no. 69/2010, after being approved by the Council members through vote, on August 12th, 2013.

August 12th, 2013

Chairman of the Fiscal Council

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ANNEX I – Budget execution semester I 2013 vs. the half-year program	The half-year program 2013 without swaps (mn RON)	Budget execution semester I without swaps (mn RON)	Budget execution semester I 2013 / Budget execution semester I 2012 (without swap)	The half-year program 2013 – Budget execution semester I 2013 without swap (mn RON)	The achievement degree of the half-year program (%)
	1	2	3	4=2-1	5=2/1
TOTAL REVENUE	103,812	97,300	5.1%	-6,513	93.7%
Current revenue	96,793	94,254	5.6%	-2,540	97.4%
Tax revenue	60,495	58,464	7.3%	-2,031	96.6%
Taxes on profit, wages, income and capital gains	18,261	17,264	4.2%	-997	94.5%
Profit	6,236	5,409	-5.5%	-827	86.7%
Personal income tax	11,360	11,351	9.3%	-10	99.9%
Other taxes on income, profit and capital gains	665	504	9.5%	-161	75.8%
Property tax	2,590	2,737	9.5%	147	105.7%
Taxes on goods and services	39,652	38,178	8.0%	-1,475	96.3%
VAT	24,456	23,971	3.3%	-485	98.0%
Excises	10,682	9,969	4.2%	-713	93.3%
Other taxes on goods and services	956	698	-20.8%	-258	73.0%
Taxes on using goods, authorizing the use of goods or on carrying activities	3,009	3,295	163.9%	286	109.5%
Tax on foreign trade and international transactions	343	313	-5.2%	-30	91.1%
Other tax revenue	198	217	12.6%	19	109.5%
Social security contributions	26,645	26,603	4.3%	-42	99.8%
Nontax revenue	9,654	9,187	-1.0%	-467	95.2%
Capital revenues	325	286	-2.3%	-39	88.0%
Grants	308	48	-66.5%	-260	15.6%
Pre-accession funds	6,386	3,039	-1.3%	-3,347	47.6%
Amounts collected in the single account (State budget)	-	-327	74.2%	-327	
TOTAL EXPENDITURE	111,449	104,173	4.8%	-7,276	93.5%
Current expenditure	102,825	97,338	6.0%	-5,487	94.7%
Personnel	22,960	23,097	18.0%	136	100.6%
Goods and services	17,663	16,606	6.8%	-1,057	94.0%
Interest	6,959	6,325	0.7%	-634	90.9%
Subsidies	3,380	3,335	9.3%	-46	98.7%
Total Transfers	50,738	47,286	1.3%	-3,452	93.2%
Transfers for public entities	661	212	64.9%	-449	32.1%
Other transfers	6,949	6,346	19.0%	-603	91.3%
Projects funded by external post-accession grants	7,086	5,205	-19.2%	-1,881	73.5%
Social assistance	34,609	34,042	1.6%	-567	98.4%
Other expenditure	1,432	1,481	16.4%	49	103.4%
Expenditure funded from reimbursable funds	575	445	-33.3%	-130	77.4%
Capital expenditure	8,623	7,152	-9.8%	-1,471	82.9%
Payments made in perevious years	-	-317	-8.3%	-317	
Overall Balance	-7,086	-6,629	-2.4%	458	93.5%

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

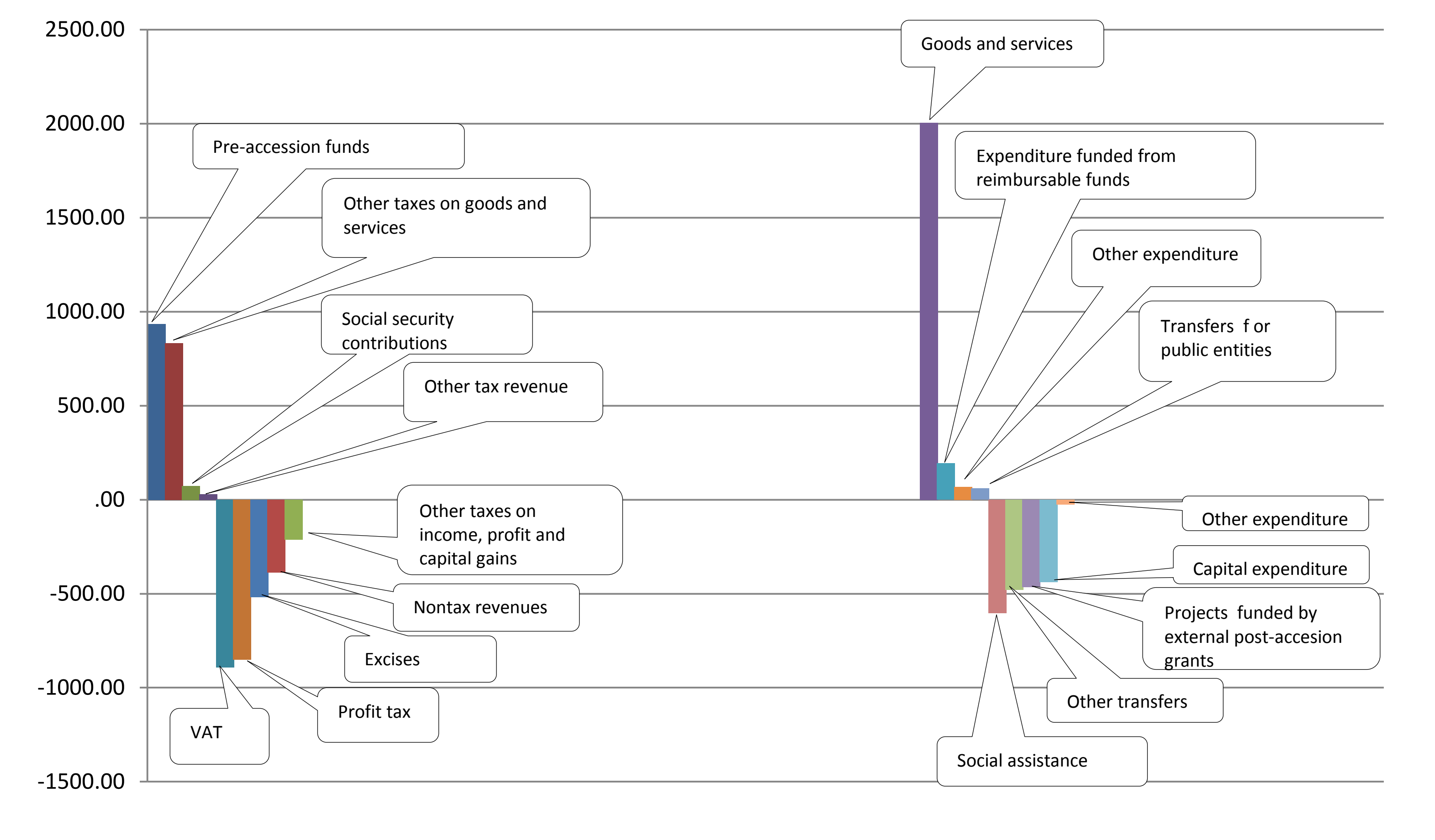
	Budget execution 2012	Initial budget 2013	Revised budget 2013
GDP, mn lei	587499	623300	626200

ANNEX II	Initial budget 2013	Swap program 2013	Initial budget 2013 without swap	Revised budget 2013	Additional swap	Revised budget 2013 without swap	Revised budget - Initial budget 2013 with swap	Revised budget - Initial budget 2013 without swap	Budget execution semester I 2013 / Budget execution semester I 2012 (without swap)	Initial budget semester II / Budget execution semester II (without swap)	Revised budget 2013 / Budget execution 2012 (without swap)
	1	2	3=1-2	4	5	6=4-5	7=4-1	8=6-3	9	10	11
TOTAL REVENUE	209285.0	1000.0	208285.0	209406.6	1118.0	207288.6	121.6	-996.4	5.1%	11.8%	8.56%
Current revenue	196747.6	1000.0	195747.6	195935.0	1118.0	193817.0	-812.6	-1930.6	5.6%	7.6%	6.60%
Tax revenue	122965.3	1000.0	121965.3	122468.1	1118.0	120350.1	-497.2	-1615.2	7.3%	7.8%	7.55%
Taxes on profit, wages, income and capital gains	36359.9		36359.9	35293.9		35293.9	-1066.0	-1066.0	4.2%	12.3%	8.19%
Profit	11721.8		11721.8	10869.8		10869.8	-852.0	-852.0	-5.50%	8.4%	1.03%
Personal income tax	23146.2		23146.2	23146.2		23146.2	0.0	0.0	9.3%	12.3%	10.80%
Other taxes on income, profit and capital gains	1491.9		1491.9	1277.9		1277.9	-214.0	-214.0	9.5%	51.3%	31.52%
Property tax	4493.8		4493.8	4493.8		4493.8	0.0	0.0	9.5%	12.5%	10.67%
Taxes on goods and services	80980.7	1000.0	79980.7	81519.5	1118.0	79401.5	538.8	-579.2	8.0%	5.2%	6.50%
VAT	52948.8	1000.0	51948.8	53175.0	1118.0	51057.0	226.2	-891.8	3.3%	5.2%	4.31%
Excises	22363.2		22363.2	21843.2		21843.2	-520.0	-520.0	4.2%	11.0%	7.83%
Other taxes on goods and services	956.2		956.2	1788.8		1788.8	832.6	832.6	-20.8%	-9.1%	-14.07%
Taxes on using goods, authorizing the use of goods or on carrying activities	4712.5		4712.5	4712.5		4712.5	0.0	0.0	163.9%	-29.9%	44.14%
Tax on foreign trade and international transactions	741.8		741.8	741.8		741.8	0.0	0.0	-5.2%	13.6%	4.88%
Other tax revenue	389.1		389.1	419.1		419.1	30.0	30.0	12.6%	16.1%	14.29%
Social security contributions	54355.3		54355.3	54428.2		54428.2	72.9	72.9	4.3%	8.0%	6.20%

ANNEX II	Initial budget 2013	Swap program 2013	Initial budget 2013 without swap	Revised budget 2013	Additional swap	Revised budget 2013 without swap	Revised budget - Initial budget 2013 with swap	Revised budget - Initial budget 2013 without swap	Budget execution semester I 2013 / Budget execution semester I 2012 (without swap)	Initial budget semester II / Budget execution semester II (without swap)	Revised budget 2013 / Budget execution 2012 (without swap)
	1	2	3=1-2	4	5	6=4-5	7=4-1	8=6-3	9	10	11
Nontax revenue	19427.0		19427.0	19038.7		19038.7	-388.3	-388.3	-1.0%	9.7%	4.27%
Capital revenues	687.1		687.1	687.1		687.1	0.0	0.0	-2.3%	11.4%	5.27%
Grants	629.9		629.9	630.7		630.7	0.8	0.8	-66.5%	94.8%	42.43%
Pre-accession funds	11220.2		11220.2	12153.8		12153.8	933.6	933.6	-1.3%	86.1%	52.32%
TOTAL EXPENDITURE	222679.2	1000.0	221679.2	224106.7	1118.0	221988.7	1427.5	309.5	4.8%	10.8%	7.91%
Current expenditure	205009.7	1000.0	204009.7	206258.2	500.0	204758.2	1248.5	748.5	6.0%	10.2%	9.11%
Personnel	46154.0		46154.0	46152.7		46152.7	-1.3	-1.3	18.0%	8.6%	13.12%
Goods and services	37262.9		37262.9	39766.8	500.0	39266.8	2503.9	2003.9	6.8%	22.5%	15.36%
Interest	11383.0		11383.0	11362.9		11362.9	-20.1	-20.1	0.7%	13.7%	6.09%
Subsidies	5229.8		5229.8	5242.9		5242.9	13.1	13.1	9.3%	-37.8%	-14.36%
Total Transfers	103990.2	1000.0	102990.2	102568.5		101568.5	-1421.7	-1421.7	1.3%	13.8%	7.61%
Transfers for public entities	1632.8	850.0	782.8	1692.4		842.4	59.6	59.6	64.9%	-8.0%	3.50%
Other transfers	12265.7	150.0	12115.7	11785.4		11635.4	-480.3	-480.3	19%	5.7%	12.54%
Projects funded by external post-accession grants	17311.2		17311.2	16845.7		16845.7	-465.5	-465.5	-19.2%	71.9%	27.45%
Social assistance	69979.4		69979.4	69375.7		69375.7	-603.7	-603.7	1.6%	5.3%	3.47%
Other expenditure	2801.1		2801.1	2869.3		2869.3	68.3	68.3	16.4%	-18.1%	-3.31%
Expenditure funded from reimbursable funds	782.9		782.9	976.8		976.8	193.9	193.9	-33.3%	-43.9%	-39.50%
Capital expenditure	17669.5		17669.5	17848.5	618.0	17230.5	179.0	-439.0	-9.8%	-6.4%	-7.85%
Overall Balance	-13394.2		-13394.2	-14700.0		-14700.0	-1305.9	-1305.9	-2.4%	1.1%	-0.50%

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

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



Source: Ministry of Public Finance

VI. Fiscal Council's Opinion on the Second Supplementary Budget for 2013

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

1. General Considerations

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

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

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

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

2. The assesment of compliance with the fiscal rules

The Fiscal Council's opinion on the first budget amendment recorded the violation (by derogation) of the rules stipulated by article 6 letters b) and c) and article 16 of the Fiscal Responsibility Law no. 69/2010 (FRL) regarding the budget revisions. Although the current budget revision, through the spending cuts operated to partially offset the downward revision of the projections for budgetary revenue brings the total expenditure (excluding financial assistance from the European Union and other donors) within the expenditure ceiling set by Law no. 4/2013 and restores compliance with the provisions of article 6 letters c), a new violation of article 6 letter b) of Law 69/2010 is recorded. The latter provision of Law no. 69/2010 states that "the balance and respectively the primary balance of the general government for the next budget year shall not exceed the ceiling set by the fiscal strategy approved by the Parliament". Thus, the draft amendment foresees a deficit of 15.9 billion lei, up by 2.5 billion lei (0.4% of GDP) than the ceiling of 13.394 billion lei established by Law no. 4/2013, the deviation from the legal ceiling increasing by another 1.2 billion lei compared to the level considered in the first budget amendment. In addition, if the cash deficit increase operated on the occasion of the first budget revision did not lead, as assessed by the government, to an increase in the budget deficit target according to ESA95 (relevant in terms of relations with the EU), this does not happen now, the failure of the ESA95 deficit target initially set at 2.4% of GDP being probably unavoidable. In the opinion of the Fiscal Council, it is essential to ensure the compliance of the budgetary outturn in 2013 with the ceiling of 3% of GDP (even with an enough comfortable margin to accommodate potential future data revisions[13]) stated in the Stability and Growth Pact, so that entering into a new excessive deficit procedure will be avoided.

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

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

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

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

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

October 30, 2013

Chairman of the Fiscal Council

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Annex I

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

Source: *The Ministry of Finance*

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

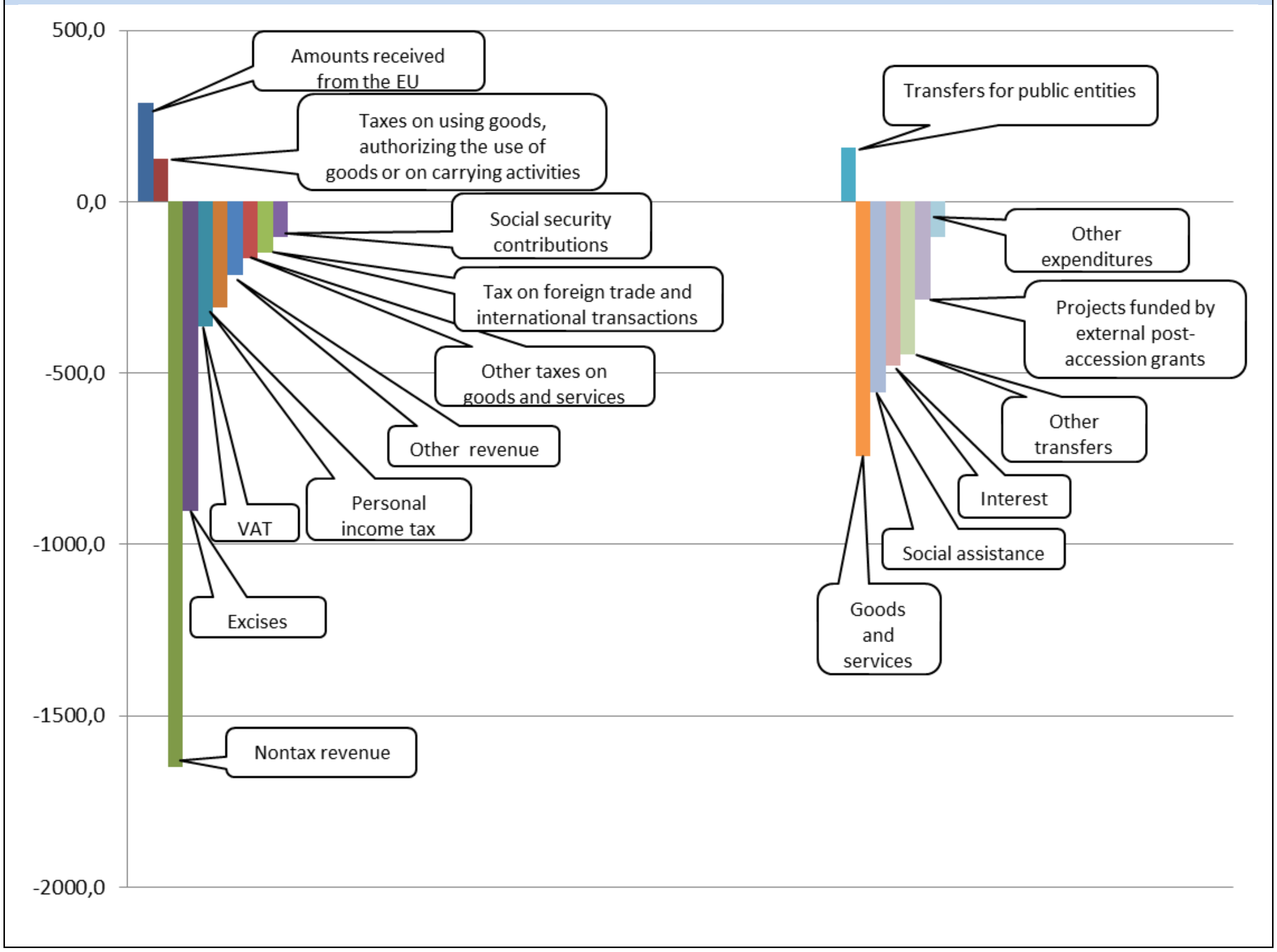
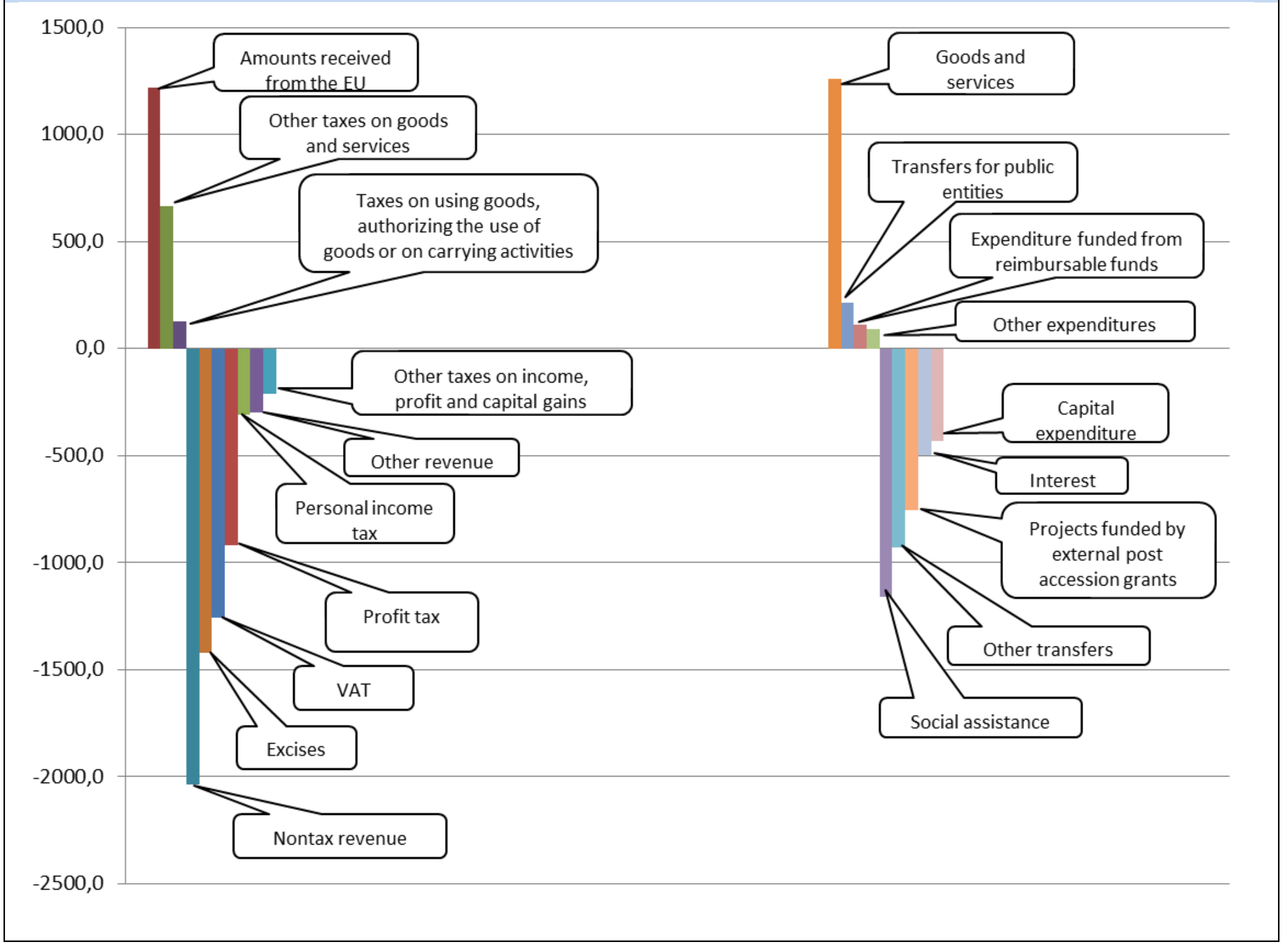


Figure 2: The main changes in expenditures and revenues compared to the initial budget (without the impact of swap schemes), million lei



VII. Fiscal Council's opinion on the State Budget Law, Social Insurance Budget Law for 2014 and the updated version of the 2014-2016 Fiscal Strategy

On November 7th, 2013, the Fiscal Council received from the Ministry of Finance the letter no. 82615, requesting, under art. 40, paragraph (2) of Law no. 69/2010, the opinions on the draft Budget Law for 2014, the Report on the macroeconomic situation for 2014 and the projections for the years 2015-2017, the draft of the Social Insurance Budget Law for 2014 and the corresponding explanatory note, and also the Revised Fiscal Strategy for 2014-2016, the explanatory note and the associated ceilings law of certain indicators specified in the fiscal framework. However, some of the necessary documents for the elaboration of the Fiscal Council's opinion (especially the report on the macroeconomic situation for 2014 and the projections for the 2015-2017 period and the latest version of the general consolidated budget projection for 2015-2017) were sent on November 12th, 2013, and the updated text of the fiscal strategy was received only during the day of 11/13/2013.

Given the Government's intention to approve the above documents on the meeting of 11/14/2014 (which implies an insufficient time to develop a rigorous analysis), the Fiscal Council is unable to issue an opinion on the updated Fiscal Strategy (FS) 2014-2016 and it reserves its right to issue a more detailed opinion afterwards.

The Fiscal Council is obliged to reiterate its previously stated recommendation to ensure a period of at least one week between the submission of the documentation by the Ministry of Finance and the adoption of the relevant legislation on the Government meeting, this interval being an absolute minimum required to elaborate an accurate analysis. In addition, ensuring such an interval would be consistent with the principle of transparency stated in the Law no. 69/2010, according to which "in setting the budgetary targets and objectives and in carrying out its fiscal and budgetary policies, the Government and the local authorities have the obligation to make public and maintain in public debate, for a reasonable period of time, all information necessary to allow the assessment of the implementation of fiscal and budgetary policies, the respective outcomes and the stance of central and local public finances."

Under the article 40, paragraph (2), letter d) of the Fiscal Responsibility Law (FRL) no. 69/2010, the Fiscal Council has the task "to analyse and issue opinions and recommendations on the annual budget laws before approval by the Government and before submission to Parliament, on the supplementary budgets and others legislative initiatives that may have an impact on the rules specified in this Law." Thus, considering its mandate, in accordance with Law no. 69/2010, the Fiscal Council issues the following opinions and recommendations on the draft budget for 2014 and its extension to the period 2015-2016:

The Fiscal Responsibility Law no. 69/2010 allows the revision of the fiscal strategy if occurs "a significant deterioration of the macroeconomic indicators and of the other assumptions that were used in developing the FS". However, the economic growth trajectory that underlies the budget projection in 2014-2016 does not record significant revisions – the forecast for 2.2% growth in 2014, 2.5% in 2015, and 3% in 2016 does not differ from those considered in the latest version of 2014-2016 FS (May 2013), only in 2015, when the previous forecast indicated 2.4%. Hence, the reason behind the revision of the budget prognosis is the large drop in the aggregate budgetary revenues, given the significantly below expectations performance corresponding to the starting point of the projection (year 2013): despite the revised forecast of a higher than initial GDP advance for 2013 (2.2% compared to 1.6%), revenues significantly lower than those projected were obtained given that the economic growth had a different composition compared to that originally envisaged (net exports instead of domestic demand, with a negative impact on revenues) and that the efficiency of collection has deteriorated. The evolutions mentioned above have been partially accommodated through the upward revision of the deficit target for 2013 (from 2.1% of GDP to 2.5% of GDP according to the cash methodology, and from 2.4% of GDP to 2.6% of GDP according to ESA95), revision over which the Fiscal Council has already issued an opinion at the budget amendments. The current update of the FS is therefore only a way to accommodate the fiscal rules violations already produced during the current year with the terms of the Law no. 69/2010 and it does not serve to the desideratum of anchoring the economic agents' expectations by providing a predictable stance of the fiscal policy.

The review of the deficit target for 2013 occurred concurrently with the revaluation of the potential GDP trajectory by the European Commission (if in the spring forecast and in the latest update of the Convergence Programme the growth pace of the potential GDP was estimated at 2.1% in 2013 and 2.6% in 2014, the revaluation indicates values of 1.6% in 2013 and 1.8% in 2014), which implies a downward revision of the absolute values of the cyclical component (negative) of the budget balance (by 0.3 pp. of GDP in 2013, respectively 0.5 pp. of GDP in 2014). Thus, the size of the structural fiscal consolidation for 2013 is lower by 0.4 pp. of GDP compared to the original plan (0.7 pp. of GDP compared to 1.1 pp. of GDP), the difference being explained in roughly equal proportions by the actual deficit target revision and by the reassessment of its cyclical component. The current structural budget deficit (2% of GDP) implies a consolidation effort of about 1% of GDP in the next two years to comply with the commitment to achieve the medium-term objective (MTO) in 2015, described by a level of the structural deficit of 1% of GDP.

The Fiscal Council has no significant objections regarding the macroeconomic scenario that substantiates the budgetary projection. Any macroeconomic forecast involves risks, but we consider that their next year balance is relatively balanced.

The draft budget for 2014 aims a deficit target of 14.49 billion lei, respectively 2.2% of GDP. According to ESA95 the budget deficit is also assessed at a level of 2.2%, given that the budgeted wage bill includes a 25% tranche of the amount related to final court rulings regarding the historical wage obligations of the state (2.06 billion lei, respectively 0.3% of GDP), their total being already included in the budget execution according to ESA95 in 2011 (according to accrual accounting principles), which is likely to lead to a significant approximation of the cash and ESA95 deficit values. From the perspective of the fiscal rules, their evaluation is irrelevant, given that the budget law comes bundled with the updated version of the FS and of the associated ceilings law of certain indicators specified in fiscal framework.

In the Convergence Programme elaborated by the Government, the possibility to achieve the MTO in 2014 was specified with an adjustment effort measured at 0.6 pp. of GDP. Given the equivalent reduction of the actual deficit (0.4 pp. of GDP, from 2.4% of GDP to 2% of GDP in the Convergence Programme, respectively from 2.6% to 2.2% of GDP in the current budget projection), the downward revision of the potential GDP trajectory involves a smaller size in absolute value of the budget balance cyclical component (negative) and, consequently, a downward revaluation of the associated structural adjustment effort, from 0.6 pp. to 0.3 pp. of GDP, the achieving of MTO being postponed for 2015.

The total general government revenues for 2014 are estimated to reach a level of 216.81 billion lei (32.92% of GDP), of which 850 million lei represent a swap scheme designed to clear outstanding obligations to the state budget with equivalent impact both on revenues and on expenditures. Excluding the impact of swaps in 2013-2014, the revenues are forecasted to increase by 12.11 billion lei, or 5.94%, compared to the level estimated for the end of 2013, a level that includes a temporary income of 2.1 billion lei from the mobile operators for renting frequency bands. Beyond the impact of the known fiscal measures (the increase of tobacco excise from April 1st and the additional transfer of 0.5 pp. to the second pension pillar from the contribution paid by employee, both according to the calendar), the draft budget includes a discretionary package of measures amounting 4.27 billion lei, which includes:

- additional excise duty of 0.07 euro / liter for energy products used as motor fuel (impact assessed by the Government to +2.28 billion lei, of which 1.84 billion lei on excises and 0.44 billion lei on VAT);
- Abandoning the practice of using the reference rate from October 1st EUR/RON announced by the European Central Bank and indexing the excises with the average inflation rate in October 2012 - September 2013 (+4.77%) (impact assessed by the Government to 1.1 billion lei, of which 0.89 billion lei on excises and 0.21 billion lei on VAT);

- broadening the tax base for property taxes for companies by including special structures (impact assessed by the Government to 0.49 billion lei);
- indexation in two tranches of the minimum monthly wage to 900 lei (impact assessed by the Government at 344 million lei, of which 300 million lei on social contributions and 44 million lei on personal income tax);
- The increase of royalties for mineral resources others than oil and natural gas with 25% (impact assessed by the Government at 50 million lei at the level of non-tax revenues).

The Fiscal Council considers as realistic the estimates for the additional income, excluding the impact of broadening the tax base for the property tax in the companies' case, where it is unable to decide because the measure's parameters are not clear yet. Based on the available data from the balance sheets of companies from Romania, the broadening of the tax base for the property taxes by including special structures and therefore taxation of all buildings present in the companies' balance sheets seems to have a much greater impact than that considered by the Government in the budget construction.

The Fiscal Council deplores the fact that once again a significant set of amendments to the Tax Code will entry into force without being subjected to a minimal public debate for a reasonable period of time, contrary to the spirit of the provisions of article 4, paragraph (1) of the Tax Code, which states that „the present code can be modified and supplemented only by law, after being typically promoted for 6 months before the date of its entry into force", and without an impact assessment of those measures. Also, the Fiscal Council draws attention to the interpretation difficulties regarding the new rules for conversion of the excise duties (defined in euro) in national currency, especially in terms of excise revenue projection in the coming years. By default, the exchange rate EUR/RON used for transformation in 2014 is 4.5223 x 1.0477 = 4.7380 EUR /RON. It is easy to imagine a situation in which the exchange rate published by the European Central Bank for 1 October 2014 would have a value of, for example, 4.47 EUR/RON, more appreciated than the level from 1 October 2012 (4.5223 used in the calculation of excise duty in 2013), but depreciated than that from 1 October 2013 (4.4585, inferior to the anterior one, that entails under the new rules the inflation indexing) and perfectly consistent with the average exchange rate hypothesis used in the budget foundation for 2014 (4.45). If for 2015 the excise calculation had been done at this rate, it would imply, *ceteris paribus*, a decrease in revenues from excises with 4.47/4.7380 X 100-100 = -5.65% compared with their level projected for 2014, with losses of income taking place for any exchange rate in the range (4.4585, 4.7370), and hence also for values of the exchange rate even more depreciated compared to the October 1st 2012 level, used for transformation in 2013. The Fiscal Council calls on the Ministry of Finance to clarify the assumptions used in the construction of the excise projection for 2015, given that their level is projected to rise by 5.9% in that year.

In conclusion, the Fiscal Council considers as realistic the revenue projections for 2014, appreciating that they are consistent with the dynamics of the relevant macroeconomic bases and with the assessed impact of discretionary measures (see, in this line Annex III), with reservations about the lack of precision on taxation parameters for special structures. Also, given the stated intention of the Government to reduce social security contributions during the year 2014, the Fiscal Council finds that the impact of such measure is not in the current budget projection for 2014 and even in that on the long term (*ceteris paribus*, the annualized net impact of a 5 pp. reduction for SSC at the employer would imply a higher deficit by about 0.5 - 0.6% of GDP). The Fiscal Council considers that the adoption of such a measure, although clearly desirable from the perspective of the business environment, it is not possible while respecting the commitment to assumed fiscal consolidation (which come out from the European Treaties) without identifying equivalent compensatory measures (therefore large), represented either by increasing/broadening of the tax base for other taxes or by reducing some expenses. In the opinion of the Fiscal Council, a large reduction in the statutory levels of SSC, required in terms of reducing the tax burden on labour, can be achieved to the extent that it reduces/eliminates the current high differences in tax treatment between different forms of income (wages, copyright, freelancers, microenterprises, etc.). Alternatively, the Government may consider a strong commitment to a path of gradual implementation of multi-annual reductions in social contributions (e.g. 0.5 to 1 pp. per year), which could be easily compensated by equivalent discretionary measures or possibly covered ex-ante by an improvement in the efficiency of collection, reflected in higher budget revenues (and hence smaller deficits) than those scheduled, identified with the occasion of the mid-year assessment of the fiscal policy (particularly in the context of the analysis associated to the Half-year report on economic and budgetary situation). Such a multi-year plan would have the advantage of anchoring the expectations of economic agents and, if accumulation of credibility, could produce favourable effects in the economy even before the effective implementation.

Regarding expenditure, the draft budget considers a level of 231.298 billion lei (of which 850 million lei represents a new compensation (swap) scheme designed to clear outstanding obligations to the state budget), higher by 4.87% compared to the previous year (adjusting the amount of expenditure for swaps included in 2013 and 2014), mainly due to expenses related to projects funded by external pro-accession grants (+3.7 billion lei, respectively 22.3%, while the Government expects a growth of annual inflows of EU funds by about 2.4 billion lei). The projected growth rate of spending in 2014, and also 2015 and 2016 (4.25% in 2014, 3.85% in 2015 and 5.18% in 2016, without adjusting the aggregates with the amount of swaps in the years 2013 and 2014), respects the rule stated in article 6, letter d) of the Fiscal Responsibility Law no. 69/2010, that states "*for each of the three years covered by the FS, the annual growth rate of total expenditure of the consolidated general budget will be kept under the annual rate of nominal GDP growth projected for that budget year, until the consolidated general budget* *balance is in surplus in the previous year for which the draft budget is elaborated* ", given that the evolution of nominal GDP is described by growth rates of 5.27% in 2014, 5.09% in 2015 and 5.5 % in 2016. In the context of clarifying the assumptions about wage and pension indexation, the Fiscal Council has no reservations about the projected trajectory of expenses, however, a slight overestimation being identified at the level of interest expense (their level involves a buffer stock that can be used in case of failures of scheduled income or occurrence of unexpected expenses). The Fiscal Council notes the recent inclusion in the text of the Report on the macroeconomic situation for 2014 and its projection for the 2015-2017 period of certain graphs representing the time evolution of the share of different spending aggregates in the budget deficit (see page 10 , pages 57-60) and appreciates the plus of transparency, but also warns that those weights have no relevance for assessing the government's priorities in allocation of resources, all the more so as, as fiscal consolidation will progress and the budget balance will inevitably approach the equilibrium, they inherently tend to increase for any budgetary expenses aggregate, without any economic significance for this phenomenon. Highlighting the weight of the expenses aggregates in total expenditure or total revenues, possibly comparing them with the other European countries in the same stage of development (peer- countries) would be more relevant.

Regarding the medium term developments, fulfilment of the medium-term objective (structural deficit 1% of GDP) according to the schedule agreed with the European Commission involves a significant structural adjustment in 2015 (by 0.7 pp. of GDP), equivalent to a reduction by 0.8% of GDP of the effective deficit, to a level of 1.4% of GDP (cash and ESA95). However, it is difficult to identify the effective measures leading to a structural adjustment of this size in 2015 starting from the current budget projection, especially that adjustments of the same size could be implemented in the past only through introducing packages of discretionary measures on the revenue side (tax increases or the introduction of new ones, widening the tax base) or by significantly reducing spending, especially in the area of public investment. Therefore, the structural adjustments come in most from the components:

- "other transfers" (-0.16% of GDP); the reduction comes from smaller allocation by 474 million lei compared to the budgeted level for 2014, and 2015 level appears inexplicably small, considering that these allocations are projected to grow before this time (eliminating the impact of swaps in 2012 and 2013 on this component, increases would be 842.3 million lei in 2012, or respectively 636.1 million lei in 2013) and after (in 2016 and 2017 increases are 241.5 million lei, respectively 700.7 million lei);

- "social assistance" (-0.17% of GDP, while the nominal advance of the aggregate, by 3.5%, is lower than envisaged for nominal GDP, 5.1%): if the projected decrease in the amount of unemployment benefit expenditure is in line with the hypothesis of an accelerating growth, it is difficult to explain why the expected growth rate of pension expenditure is only 4.1%, while under the application of current indexing algorithm (as in the pension Law, amended in January 2013) would generate an indexation of the pension point with 5%, derived from the amount of average inflation projected for 2013, 4.1%, to which is added half of real wage growth projected for 2013, namely 1.8%);

- "Projects financed by external post-accession grants", whose nominal advance, only 996.1 million lei, is substantially lower than projected additional inflows for post-accession funds (+2.2 billion lei), which lowers the projected deficit with the difference between them. Moreover, such a phenomenon (additional inflows of post-accession funds, accompanied by a lower advance of costs with projects funded by post-accession grants) is not scheduled before 2015, or in the projection of future developments after this year.

The above opinions and recommendations of the Fiscal Council were approved by the Chairman of the Fiscal Council, according to article 43, paragraph (2), letter d) of Law no. 69/2010, after being adopted by the members of the Council through vote, on November 14th, 2013.

November 14th, 2013

Chairman of the Fiscal Council

IONUŢ DUMITRU

ANNEX I		- million lei
	Budgetary impact	Revenue category
Discretional fiscal policy measures:	4268,7	
Excise duty indexation with the inflation rate (4.75%)	1106,8	**Total impact on revenue, out of which:**
	892,6	**Excises**
	214,2	**VAT**
The increase of the excise duty on fuel with 0.07 euro / liter.	2279,9	**Total impact on revenue, out of which:**
	1838,6	**Excises**
	441,3	**VAT**
The tax base for the property taxes that will be broadened by the inclusion of special structures.	488,0	**Property tax**
The increase by 25% of royalties for mineral resources other than oil and natural gas	50,0	**Non-tax revenue**
The increase of the minimum gross salary from 800 lei/month to 850 lei/month starting with January 2014 and to 900 lei/month starting with July 2014	344	**Total impact on revenue, out of which:**
	300	**Social security contributions**
	44	**Personal income tax**

ANNEX II

	2014 Budget projection (from 2014-2016 Fiscal Strategy)	2013 Budget projection (2013 Budget after the second rectification)	2014 Budget draft	2014 Budget draft / FS 2014	2014 Budget draft / 2013 Budget after the second rectification	FS 2014	2013 Budget after the second rectification	2014 Budget draft	2014 Budget draft - FS 2014	2014 Budget draft - 2013 Budget after the second rectification
GDP	660600	625617	658683							
	without swaps			without swaps, percentage change		without swaps, % of GDP			without swaps, difference, pp. of GDP	
	1	2	3	8=7-1	9=7-4	10	11	12	13=12-10	14=12-11
TOTAL REVENUE	223769,3	203846,3	215958,3	-3,49%	5,94%	33,87%	32,58%	32,79%	-1,09%	0,20%
Current revenue	208299,0	190166,0	200481,2	-3,75%	5,42%	31,53%	30,40%	30,44%	-1,10%	0,04%
Tax revenue	128468,0	118451,9	125312,2	-2,46%	5,79%	19,45%	18,93%	19,02%	-0,42%	0,09%
Corporate income tax	13879,0	12070,0	12710,0	-8,42%	5,30%	2,10%	1,93%	1,93%	-0,17%	0,00%
Profit	12343,8	10805,0	11378,0	-7,82%	5,30%	1,87%	1,73%	1,73%	-0,14%	0,00%
Capital gains and other taxes	1535,2	1265,0	1332,0	-13,24%	5,30%	0,23%	0,20%	0,20%	-0,03%	0,00%
Personal income tax	24662,9	22851,0	24014,9	-2,63%	5,09%	3,73%	3,65%	3,65%	-0,09%	-0,01%
Wages, dividends, capital gains, rent	24649,3	22838,1	24000,9	-2,63%	5,09%	3,73%	3,65%	3,64%	-0,09%	-0,01%
Other (local) taxes	13,6	12,9	14,0	3,24%	8,50%	0,00%	0,00%	0,00%	0,00%	0,00%
Property tax	4665,7	4452,8	5040,7	8,04%	13,20%	0,71%	0,71%	0,77%	0,06%	0,05%
Taxes on goods and services	84069,4	78096,1	82512,6	-1,85%	5,66%	12,73%	12,48%	12,53%	-0,20%	0,04%
VAT	55864,0	50692,0	53771,6	-3,75%	6,08%	8,46%	8,10%	8,16%	-0,29%	0,06%
Excises	23644,7	20942,1	24102,0	1,93%	15,09%	3,58%	3,35%	3,66%	0,08%	0,31%
Other taxes on goods and services	1940,9	1622,9	1807,1	-6,90%	11,35%	0,29%	0,26%	0,27%	-0,02%	0,01%
Taxes on using goods, authorizing the use of goods or on carrying activities	2619,8	4839,1	2831,9	8,10%	-41,48%	0,40%	0,77%	0,43%	0,03%	-0,34%
Tax on foreign trade and international transactions	785,5	591,8	623,0	-20,69%	5,27%	0,12%	0,09%	0,09%	-0,02%	0,00%
Other tax revenue	405,5	390,1	411,0	1,36%	5,35%	0,06%	0,06%	0,06%	0,00%	0,00%
Social security contributions	58199,6	54325,2	57779,0	-0,72%	6,36%	8,81%	8,68%	8,77%	-0,04%	0,09%
Non-tax revenue	21631,4	17389,0	17390,0	-19,61%	0,01%	3,27%	2,78%	2,64%	-0,63%	-0,14%
Capital revenues	731,4	607,1	621,0	-15,09%	2,29%	0,11%	0,10%	0,09%	-0,02%	0,00%
Subsidies	0,0	0,0	0,0	-	-	0,00%	0,00%	0,00%	0,00%	0,00%
Grants	337,7	631,9	14,6	-95,68%	-97,69%	0,05%	0,10%	0,00%	-0,05%	-0,10%
Amounts received from the EU	14401,2	12441,4	14841,5	3,06%	19,29%	2,18%	1,99%	2,25%	0,07%	0,26%

ANNEX II

	2014 Budget projection (from 2014-2016 Fiscal Strategy)	2013 Budget projection (2013 Budget after the second rectification)	2014 Budget draft	2014 Budget draft / FS 2014	2014 Budget draft / 2013 Budget after the second rectification	FS 2014	2013 Budget after the second rectification	2014 Budget draft	2014 Budget draft - FS 2014	2014 Budget draft - 2013 Budget after the second rectification
GDP	660600	625617	658683							
	without swaps			without swaps, percentage change		without swaps, % of GDP			without swaps, difference, pp. of GDP	
	1	2	3	8=7-1	9=7-4	10	11	12	13=12-10	14=12-11
TOTAL EXPENDITURE	235957,4	219746,4	230448,4	-2,33%	4,87%	35,72%	35,12%	34,99%	-0,73%	-0,14%
Current expenditure	217087,8	202508,8	212652,8	-2,04%	5,01%	32,86%	32,37%	32,28%	-0,58%	-0,08%
Personnel	48663,0	46152,0	47786,1	-1,80%	3,54%	7,37%	7,38%	7,25%	-0,11%	-0,12%
Goods and services	36971,2	38522,6	39361,5	6,47%	2,18%	5,60%	6,16%	5,98%	0,38%	-0,18%
Interest	12218,4	10885,3	11223,5	-8,14%	3,11%	1,85%	1,74%	1,70%	-0,15%	-0,04%
Subsidies	5801,0	5213,8	5742,3	-1,01%	10,14%	0,88%	0,83%	0,87%	-0,01%	0,04%
Total Transfers	112594,8	100473,2	107262,3	-4,74%	6,76%	17,04%	16,06%	16,28%	-0,76%	0,22%
Transfers for public entities	2211,1	998,7	549,1	-75,17%	-45,02%	0,33%	0,16%	0,08%	-0,25%	-0,08%
Other transfers	10815,5	11188,7	11817,1	9,26%	5,62%	1,64%	1,79%	1,79%	0,16%	0,01%
Projects funded by external post-accession grants	22879,7	16558,3	20250,9	-11,49%	22,30%	3,46%	2,65%	3,07%	-0,39%	0,43%
Social assistance	73927,3	68819,4	71512,7	-3,27%	3,91%	11,19%	11,00%	10,86%	-0,33%	-0,14%
Other expenditure	2761,2	2908,1	3132,5	13,45%	7,72%	0,42%	0,46%	0,48%	0,06%	0,01%
Reserve fund	107,0	365,7	197,0	84,11%	-46,13%	0,02%	0,06%	0,03%	0,01%	-0,03%
Expenditure funded from reimbursable funds	732,4	896,3	1080,1	47,47%	20,51%	0,11%	0,14%	0,16%	0,05%	0,02%
Capital expenditure	18869,5	17237,6	17795,6	-5,69%	3,24%	2,86%	2,76%	2,70%	-0,15%	-0,05%
Overall Balance	-12188,1	-15900,0	-14490,0	18,89%	-8,87%	-1,85%	-2,54%	-2,20%	-0,35%	0,34%

ANNEX III	2013			2014						
	2013 Budget after the second rectification	The influence of the two compensation schemes	2013 Budget after the second rectification exluding schemes effect	The influence of the compensation schemes in 2013	Discretional fiscal policy measures in 2014	Explanations	Relevant macroeconomic basis	Revenue projection 2014 Fiscal Council	CGB revenues according to the 2014 budget draft	Differenc es
	1	2	3 = 1-2	4	5	6	7	8=3*7+4+5	9	10=9-8
TOTAL REVENUE	205964,3	2118,0	203846,3	850,0	4268,7			217177,6	216808,3	369,2
Current revenue	192284,0	2118,0	190166,0	850,0	4268,7			201699,8	201331,2	368,6
Tax revenue	120569,9	2118,0	118451,9	850,0	3918,7			126290,2	126162,2	128,0
Corporate income tax	12070,0		12070,0					12707,3	12710,0	-2,7
Profit	10805,0		10805,0				Nominal GDP (+5,28%)	11375,5	11378,0	-2,5
Capital gains and other taxes	1265,0		1265,0				Nominal GDP (+5,28%)	1331,8	1332,0	-0,2
Personal income tax	22851,0		22851,0		44,0			24352,3	24014,9	337,4
Wages, dividends, capital gains, rent	22838,1		22838,1		44,0	The increase of the minimum wage should be included in the projection for the dynamics of earnings and therefore will not be considered separately in our forecast.	The average number of employees(+1,33%) Average gross earnings (+5,17%)	24338,7	24000,9	337,8
Other (local) taxes	12,9		12,9				Nominal GDP (+5,27%)	13,6	14,0	-0,4
Property tax	4452,8		4452,8		488,0	The local taxes are supposed to remain at the current level to which is added the impact of the tax base broadening.		4940,8	5040,7	-99,9
Taxes on goods and services	80214,1	2118,0	78096,1	850,0	3386,7			83248,2	83362,6	-114,4
VAT	52810,0	2118,0	50692,0	850,0	655,5	Although the excise increases (which implies price increases) generate additional revenue from VAT, their impact should be included in the deflator's projection for the relevant macroeconomic base considered. However, considering the information available at this moment, the excise increases were not included in consumption deflator and the calculation reported here will include both the variation of the nominal consumption and the additional revenues resulted from these measures.	Household's final consumption expenditure excluding self consumption and the related market (+4,74%)	54602,1	54621,6	-19,5
Excises	20942,1		20942,1		2731,2	The indexation of excises with the average inflation rate from the October 2012 - September 2013 period (+4.77%) and the extra excises of 0.07 euro / liter for energy products used as motor fuel.	Household's final consumption expenditure excluding self consumption and the related market, in real terms (+1,75%)	24039,6	24102,0	-62,4
Other taxes on goods and services	1622,9		1622,9			This amount includes the revenues from the clawback tax. According to the projection of the Ministry of Public Finance.		1807,1	1807,1	0,0
Taxes on using goods, authorizing the use of goods or on carrying activities	4839,1		4839,1			The starting point of the extrapolation (the projected revenues for 2013 from the second budget rectification) is adjusted excluding the extraordinary income from renting the frequency bands to mobile operators during 2013 (2100 million lei).	Real GDP (+2,2%)	2799,4	2831,9	-32,6
Tax on foreign trade and international transactions	591,8		591,8				Imports of goods and services (+6,6%)	630,9	623,0	7,9
Other tax revenue	390,1		390,1				Nominal GDP (+5,28%)	410,7	411,0	-0,3
Social security contributions	54325,2		54325,2		300,0	The starting point of the extrapolation (the projected revenues for 2013 from the second budget rectification) is adjusted by adding the compensatory transfers to affected persons regarding the amounts collected under a provision declared unconstitutional. These transfers were recorded as negative revenue, negatively affecting the execution of the first 9 months of 2013 (by 796 million lei). Also, the increase of the minimum wage should be included in the projection for the dynamics of earnings and therefore will not be considered separately in our forecast.	The average number of employees(+1,33%) Average gross earnings (+5,17%)	58019,7	57779,0	240,6
Nontax revenue	17389,0		17389,0		50,0	According to the projection of the Ministry of Public Finance. Revenues are projected to increase slower than the average inflation forecasted for the next year.		17390,0	17390,0	0,0
Capital revenues	607,1		607,1				The average rate of inflation forecasted for 2014 (2,4%)	621,7	621,0	0,7
Subsidies	0,0		0,0					0,0	0,0	0,0
Grants	631,9		631,9			According to the projection of the Ministry of Public Finance		2,8	14,6	-11,8
Amounts received from the EU	12441,4		12441,4			According to the projection of the Ministry of Public Finance		14853,3	14841,5	11,8