Fiscal Council's preliminary opinion on the State Budget Law and Social Insurance Budget Law for 2017

On January 23, 2017, the Fiscal Council received from the Ministry of Public Finances (MPF) the letter no. 5408 dated to January 21, 2017, requesting under art. 53, paragraph (2) of the Fiscal Responsibility Law no. 69/2010 republished (FRL), the opinion on the draft of the Budget Law for 2017, the draft of the Social Insurance Budget Law for 2017, the Report on the macroeconomic situation for 2017 and the projection for the period 2017-2020, the Fiscal Strategy for 2017-2019 and the corresponding explanatory note and the draft of the ceilings law of certain indicators specified in the fiscal framework for the year 2017. However, the set of documents necessary for the elaboration of the Fiscal Council's opinion was incomplete in the absence of Fiscal Strategy for 2017-2019 and the Fiscal Council requested additional information and clarifications from MPF under the letter no. 7 dated 23 January 2017. Meanwhile, the draft budget has undergone significant changes compared to the version originally notified to the Fiscal Council, the updated construction budget being sent by MFP (with the text of the Fiscal Strategy) on the morning of January 27, 2017.

Under article 53, paragraph (4) of the FRL, the Government and Parliament are required to consider the opinions and recommendation of the Fiscal Council when **elaborating and approving the Fiscal Strategy and the annual budgets, as well as in the preparation of other measures triggered by the implementation of this law.** Given the Government's intention to approve the above documents at the meeting on 27.01.2017, which clearly involves an insufficient time for analysis, development and approval of the requested opinion and the lack of the full set of documents and the required clarifications, the Fiscal Council is unable to develop a complete opinion on the above documents. In the preliminary opinion, written in order to avoid the delaying of budget adoption in the government meeting and submission to Parliament, the Fiscal Council will only write some general considerations, following that development of the complete opinion to be finalized in the week 30 January-3 February 2017. After its completion, the Fiscal Council will notify the Parliament and publish the opinion on the website of the institution.

Therefore, the Fiscal Council considers appropriate the following preliminary general considerations:

- The State Budget Law targets a deficit below the reference level of 3% of GDP corresponding to the corrective arm of the Stability and Growth Pact (SGP), but, regardless of the output gap used (there are major differences between the estimates of the National Commission for Economic Forecasting and the latest available estimates of the European Commission), the budget confirms a very large slippage (and widening until 2018) from the requirements of the SGP's preventive arm, adopted in the national legislation through FRL;

- The macroeconomic scenario behind the budget construction appears as significantly more favorable than the earlier assessments of the National Commission for Economic Forecasting. Such a development is justified to a certain proportion by the new measures introduced by the government but, given the information available at this time, the Fiscal Council considers this scenario as optimistic and inappropriate from the perspective of a prudent budget construction. The preliminary assessment of the Fiscal Council, however, shows that the MPF's revenue projection does not appear to fully incorporate the more favorable evolution of the macroeconomic scenario. However, the Fiscal Council has reservations about the revenues projected in the draft budget, the preliminary analysis indicating their potential overestimation.

- The estimated developments of the revenue aggregate " Amounts received from the EU in the account of payments made and pre-financing" and its expenditure counterparty (projects funded by EU non-reimbursable funds) are not comparable with the historical ones, in the context of the agricultural subsidies transiting the 2017 budget (the European Agricultural Guarantee Fund (EAGF) - 8.1 billion lei, the European Agricultural Fund for Rural Development (EAFRD) - 4.1 billion lei, whose final beneficiary is the private sector). Moreover, these amounts will not transit the general consolidated budget in terms of the European methodology (ESA 2010).

- The Fiscal Council had concerns regarding the projected development of some expenditure aggregates included in the budget construction received on the 23 of January - especially at the level of goods and services and the personnel expenses who appeared as potential undersized in the context of an preliminary analysis performed without having the detailing sources of savings (relative to the impact of the announced fiscal measures). The updated projection of the budget expenditures received by the Fiscal Council on the morning of 27st January brings major changes at the level of some expenditure aggregates, changes that are likely to increase significantly the concerns already existing in regard to the possible under dimension of personnel expenses and adding to these new concerns regarding potential under budgeted aggregates "social assistance", "interest expenses" and "other transfers". Compared to the initial version remitted to the Fiscal Council, the second one includes current expenditure cuts worth around 5 billion lei localized in a descending order, at the level of "other transfers" (-1.7 bn. lei, with an unexplained reduction of the Romania's due contribution to the EU budget), "interest" (-1.5 bn. lei), "personnel expenses" (-867 mil lei) and "social assistance" (-821 mil lei). In return, the capital expenditures are increased by 5 billion lei, the source of the increase being localized at the level of Ministry of Defense's capital expenditures. In this context, it is worth mentioning the further development of this aggregate after 2017, the supplementation of allocations to the Ministry of Defense appearing as temporary because the allocations return in 2018 to levels comparable to the historical ones.

The Fiscal Council’s preliminary assessment therefore indicates a potential over-estimation of budget revenues and a probable under-estimation of current expenditure, which is likely to strongly tilt the balance of risks in the sense of recording in execution a deficit higher than projected in the absence of corrective measures.

The above opinions and recommendations of the Fiscal Council were approved by the Chairman of the Fiscal Council, according to article 56, paragraph (2), letter d) of Law no. 69/2010, republished, after being approved by the Council members through vote, on 27th of January, 2017.

27th January 2017 **Chairman of the Fiscal Council,**

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