

## ROMANIA’S PUBLIC FINANCES: WHERE ARE WE NOW?

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**Abstract:** The outbreak of the Covid-19 pandemic could be a good opportunity for the implementation of structural measures that would lead Romania to a new paradigm of economic growth, more resilient to external shocks.

The budget constructions for 2021 and the following years are and will be marked by the year of 2020, which through its particular exposition, brings to the fore the need for a new economic approach and the preparation of conditions for a new way of formulating public policies, strengthening the concept of sustainability, of the balances between macro and microeconomics, strengthening governance, orienting future investment projects towards reducing/eliminating structural vulnerabilities (transport infrastructure, health infrastructure) in the context of the challenges of a profoundly changing society.

**Keywords:** *public finances, crisis, the excessive deficit, the inflation*

Currently, we live in moments when the problems seem to become easier to identify, to conceptualize. The government was deposed with the highest score in the history of censorship motions in the last 30 years, and, in this state of affairs, the country is sinking into crisis every day. The government that will be formed already has a very busy agenda<sup>1</sup>.

Also, we cannot neglect the impact of the pandemic in the area of finance, which is a very severe one, increasing the uncertainty and placing the recovery on a difficult trajectory. The health crisis has effects on the Romanian economy and, as it can be seen, unfortunately, the presence of vaccines is not enough to eliminate the “civilizational” gaps between Romania and the developed countries of the West.

The pandemic, from a financial perspective, passes through societies, economies bringing changes for a long time, and in this context, financiers are called to analyze the possibilities through which states, unions of states, various other decision-makers can fight against and mitigate the negative effects of the crisis.

In addition to the financial problems caused by the Covid-19 pandemic, the high costs of managing the health crisis, we are also facing another threat, namely, the

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<sup>1</sup> We specify that at the date of the conference there were only negotiations regarding the structure of the new government of Romania. Meanwhile, after a period of political crisis, on November 25, 2021, the government led by Nicolae Ciucă was invested.

climate change that can destabilize the public budget. The impact of the climate change can far outweigh that of the pandemic, it can cause devastating effects for communities, society, and these effects will also affect public budgets, communities and individuals in general. The economic impact of the pandemic is considered to be transitory (even if long-term), but public budgets would not need to be destabilized in general if pre-pandemic levels of economic activity are reached in a sustainable way. The climate change, an extreme event and an existential threat, transposes us into another paradigm, in the sense that the effects on the economic activity and on the public, firm and individual budgets will be permanent.

History reminds us that, as in 1931, when Romania was struggling with the raging waves of the economic crisis, researching the organization of Romanian public finances, it was found that, unlike the states with extensive experience in public administration (France, England), our competent ministry did not have sufficient resources to carry out its important mission (Stan, 1937, p. 71). The same aspects can be felt today in the context in which the quality of public services is among the lowest in the European Union, the level of taxpayer satisfaction regarding the government's fiscal policy, the activity of the National Agency for Fiscal Administration and the trust in the civil servants is very low in the surveys conducted.

During the previous economic crisis (2007–2009) many member states of the European Union entered the excessive deficit procedure, now Romania is in this situation again, the letter from Brussels arriving in April – after the outbreak of the pandemic.

The Council adopted the recommendation under the excessive deficit procedure for Romania and the recommendation establishes that Romania should put an end to the excessive deficit situation by 2024 at the latest<sup>2</sup>.

The Council found that an extension to the current deadline for Romania to correct its public deficit would be important in order not to compromise the economic recovery after the Covid-19 pandemic. The new deadline for correcting the excessive deficit allows for a more gradual effort and a balance between fiscal consolidation and the economic recovery.

The recommendation indicates that, in order to meet this new deadline, Romania would need to achieve a general government deficit target of 8.0% of GDP in 2021, 6.2% of GDP in 2022, 4.4% of GDP in 2023, and 2.9% of GDP in 2024, which is in line with the Romanian government's objectives.

The Council has taken into account the changes in the Romanian fiscal situation, budgetary developments in 2020 and the new budgetary strategy put in place and calls for reforms, including in the management of public finances. In this context, the Recovery and Resilience Facility can provide an opportunity for Romania to improve its fiscal situation while still supporting growth and job creation.

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<sup>2</sup> See <https://www.consilium.europa.eu/en/press/press-releases/2021/06/18/excessive-deficit-procedure-council-adopts-recommendation-for-romania/>, consulted (Accessed: 1 October 2021).

Regarding the inflation, we start from the reports of the National Bank of Romania (August 2021) which showed that the annual inflation rate continued to increase in the second quarter of 2021 exceeding the upper limit of the range associated with the stationary target and reaching the level of 3.94% at the end of the analyzed period (+0.89 percentage points compared to March 2021)<sup>3</sup>. But the annual inflation rate continued its upward trend, rising to 6.3% in September, according to the data released by the National Institute of Statistics.

The inflation perspectives must also be analyzed in terms of keeping the epidemiological situation under control. The annual inflation rate is expected to continue its upward trajectory seen in the first half of this year and in the second half, being forecast at 5.6% in December 2021, a level above the upper limit of the target range.

Lifting most of the restrictions and restoring confidence in the summer of 2021 supported the revival of the economic activity, but activities involving physical interaction have not yet fully recovered the losses associated with the restrictive measures and the population's prudence. Additionally, the strong manifestation of the new pandemic wave tempers the encouraging evolution of the Romanian economy.

In Romania, the health and financial crisis brought the public debt to record values, however, below 50%. As a share in GDP, Romania's debt decreased in July 2021, to 49.3% compared to 49.5% in June 2021, the explanation being that of significant economic growth, even though the government added another 20 billion lei in a month to the total amount of public debt.

Although the above-mentioned figures are worrying, the reports of the National Bank of Romania emphasize that the big problem is the country's ability to pay its loans. The additional indebtedness must have a counterpart in assets or changes in the structure of the economy, which will allow the payment of debts without generating the particular burden of future generations.

If we follow the reports on budget execution<sup>4</sup>, we notice that in the second quarter of this year the budget registered a deficit of 19.17 billion lei (1.68% of GDP), and in the third quarter, the budget recorded a deficit of 10.48 billion lei (approx. 0.89% of GDP). Let's not forget that, during all this time, every effort has been made to combat the effects of the Covid-19 pandemic.

Budget revenues have increased, but this increase is mainly due to the fact that in the previous period / year the revenues had to "suffer" due to the effects of fiscal measures instituted in order to support taxpayers.

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<sup>3</sup> See <https://insse.ro> (Accessed: 1 October 2021) and The inflation report August 2021, <https://www.bnr.ro/PublicationDocuments.aspx?icid=3922> (Accessed: 1 October 2021).

<sup>4</sup> *Report on the implementation of the budget for the third quarter of 2021*. <https://mfinante.gov.ro/domenii/bugetul-de-stat/informatii-executie-bugetara> (Accessed: 30 October 2021).

In the third quarter of 2021, the tax revenues amounted to 46.93 billion lei (approx. 4% of GDP), a positive trend, recording revenues from profit tax, income, VAT, social contributions<sup>5</sup>.

There is also a significant increase in the local tax collection. This upward trend was mainly due to some legislative changes, such as the annual indexation of taxes for freight vehicles with a total authorized mass of 12 tones or more, as well as for combinations of freight vehicles with goods with the maximum total authorized mass equal to or greater than 12 tones, depending on the exchange rate of the euro in force on the first working day of October of each year and published in the Journal of the European Union and the minimum levels laid down in Directive 1999/62/EC<sup>6</sup>.

If things were to recover and keep up, it would be time for the economy to support the state again.

Let's also look at the evolution of the general consolidated budget expenditures. They accounted for 8.9% of GDP in the same reference period, in the third quarter of this year, respectively. The expenditures related to this quarter compared to the volume of expenditures in the third quarter of 2020 increased by approx. 0.86 billion lei<sup>7</sup>.

Thus, we notice that the personnel expenses represent 2.3% of GDP, those with goods and services 1.3% of GDP, the interest rates approx. 0.3% of GDP, the subsidies 0.1% of GDP, the social assistance expenditures 3.1% of GDP and the capital expenditures approx. 0.5%.

Despite all the positive aspects revealed, in the third quarter of 2021, the level of budget revenues did not reach the programmed level in the conditions in which the revenues received from the internal economy exceeded the programmed level for the analyzed period.

The situation is also caused by the fact that the revenues expected to be collected from non-reimbursable external funds registered a lower degree of achievement than the level scheduled for the third quarter of 2021, which led to the non-realization of the scheduled budget revenues for the analyzed period.

In the next period, the pace of revenue collection in the domestic economy should increase. This must also be the main objective of ANAF (NAFA – National Agency of Fiscal Administration n.t.), achievable through<sup>8</sup>:

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<sup>5</sup> During this reference period, the revenues from the profit tax represented 0.4% of the GDP, from the income tax 0.6% of the GDP, from the VAT approx. 1.8%, from insurance contributions 2.7%.

<sup>6</sup> See Law no. 296/2020 which amended and supplemented art. 491 Fiscal Code, an article that regulates the method of updating inflation set in fixed amounts. The indexation procedure can be done either by adopting a decision of the local council or by the effect of the law. Law no. 296/2020 for the amendment and completion of Law no. 227/2015 on the Fiscal Code, published in the Official Gazette of Romania no. 1269 of December 21, 2020.

<sup>7</sup> In the third quarter of 2020, the expenditures amounted to 103.6 billion lei, and in the similar period of 2021 they increased to 104.46 billion lei (by about 0.8%).

<sup>8</sup> See [https://www.anaf.ro/anaf/internet/ANAF/info\\_publice/plan\\_masuri\\_colec\\_venit\\_bgc](https://www.anaf.ro/anaf/internet/ANAF/info_publice/plan_masuri_colec_venit_bgc) (Accessed: 30 October 2021).

- simplification of tax administration procedures to support voluntary compliance with the declaration of tax obligations;
- supporting the compliance with the payment of tax obligations;
- measures to prevent and fight against tax evasion;
- ensuring a differentiated tax treatment depending on the tax behavior of the taxpayers.

It is also necessary to take measures at the level of the main authorizing officers to increase the absorption of non-reimbursable external funds, as well as to increase the rigor in the quarterly programming of public expenditures.

We are once again in a moment when the revival of economic growth in the EU requires urgent measures, a trend that our country is also in line with (Lazăr, 2016, p. 151). Thus, although quite late, the actors involved in the procedure of drafting the budget state that they are preparing a balanced budget construction, responsible for stimulating the economy and for correctly distributing the public money for the welfare of the Romanians.

The government program in the field of public finances does not suggest the introduction of new taxes, as a source of revenue. Instead, the new government assumes the control of the budget deficit by applying fiscal-budgetary responsibility, preparing in this regard, as we have shown, a balanced budget with the role of stimulating the economy. In outlining the budget projection for the next year, the government is also considering the possibility of increasing the budget revenues by fighting against tax evasion.<sup>9</sup>

Obviously, given the exceptional character of the budget years during the Covid-19 pandemic, which also determines the prolongation of measures to eliminate the multiple effects of the health crisis, in the next budget year a credible budget construction is required, avoiding pro-cyclical policies and creating fiscal space. It is intended that the budget correction be an exception, not a solution to a crisis<sup>10</sup>.

Let us not forget that this difficult budgetary context of 2021 also requires measures to accelerate the digitization of the tax administration. The approach will be materialized by reporting in digital format the fiscal and accounting information

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<sup>9</sup> Take into account the role of the tax record in preventing and fighting against tax evasion and in streamlining the administration of taxes and duties owed to the state. In this regard, see Coștaș, 2021, p. 91.

<sup>10</sup> See the situation of the budget corrections from the current year – at the beginning of September 2021, the Emergency Ordinance no. 97/2021, published in the Official Gazette of Romania no. 858 of September 8, 2021, which aimed to allocate resources to finance unforeseen expenses to combat the spread of Coronavirus, such as: providing the necessary funds for the purchase of vaccines, medicines, the implementation of national health programs and the implementation of incentives for Covid vaccination; ensuring the necessary amounts to finance the expenses with medicines and medical services, the remuneration rights for the personnel from the public health units and for the payment of the indemnities related to medical leaves. Also, on November 24, 2021, the Ministry of Finance sent to the Fiscal Council a draft budget rectification requesting its preliminary opinion on this proposal.

(standard audit and tax file system – SAF – T)<sup>11</sup>. From 1 January 2022, SAF-T reporting will become mandatory for large taxpayers, and the others will be enrolled in the subsequent reporting system in 2022 and 2023, respectively.

The construction of the budget for 2022 will be a severe test given the need to reconcile the management of the very difficult situations facing Romania (the health crisis, the energy price shock, the effects of the tensions on international markets), which require adequate resources, with the need for budget consolidation, the visible reduction of the budget deficit. In this context, we emphasize that it is mandatory to strictly control the spending of public money, public spending that provides basic public goods for citizens (such as health, education) and at the same time to take into account the constraints imposed by the budget consolidation. All these measures will have to be combined with the increase in tax revenues. Without a substantial increase in tax revenues, it will be virtually impossible to meet current and future challenges regarding the public budget, the public finances and the Romanian society.

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<sup>11</sup> [https://www.anaf.ro/anaf/internet/ANAF/despre\\_anaf/strategii\\_anaf/proiecte\\_digitalizare/saf\\_t/](https://www.anaf.ro/anaf/internet/ANAF/despre_anaf/strategii_anaf/proiecte_digitalizare/saf_t/) (Accessed: 15 September 2021).

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