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## Some considerations regarding budgetary priorities during crisis

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**Abstract:** In the first part of the paper are presented general aspects regarding budgetary priority establishment. The yearly achievable budgetary revenues cannot cover entirely the expenditures, being necessary the sorting of them in concordance with budgetary priorities from the Government's program. The budgetary priorities are established taking into account objective and subjective factors. Even if the author does not share the chronic deficit budgeting, however he accepts their existence in certain conditions. The deficit should be covered from state loans, and these to be used for financing investments (inclusively in human resources). In the second part of the article are presented the priorities in Romanian state budget for 2013. It is emphasized that the cumulated early deficits led to considerable interest expenditures with loans contracted by the administration. In 2013 these expenditures are 8.93% from total expenditures, exceeding with 1.52 pp all together education, health, culture and sport expenditures.

**Keywords:** budgetary priorities, current budgetary expenditures, investment expenditures, budgetary deficit

**JEL Classification:** H60, H62, H63

## **1. General issues concerning budget priorities**

Budget prioritization is always present even if it is done during the annual state budget drafting, and then during the discussion and approval by the legislative body. The novelty and importance of budget prioritization is determined by objective and subjective factors:

■ Practice shows that revenues which can be concentrated at one moment to state budget are limited. As such, the existing public financial resources fail to cover the needs of such resources as a result of the multiple requirements which should be financed. Consequently, a decision must be taken. We limit budget spending to incomes determined by the size of GDP, GDP per capita, shares of GDP for development and consumption and taxation rate or opt for a budget deficit. In case we opt for a budget deficit, it is necessary to know ex-ante what funding may be attracted to cover the deficit. Experience has shown that issuing paper money is not a solution to be retained to cover the budget deficit, as it leads to unmanageable rampant inflation.

It follows that to cover the budget deficit remains as solution which can be taken in consideration: state loans. This solution assumes, however, to know in time if the loans can be procured domestically, so in national currency, or it will turn to foreign loans. If the latter, it is necessary to know if they can be contracted from international financial institutions (IMF, World Bank, EIB , etc.) or other creditors. Regardless if it is preferred the domestic financial market, external market or both, there are required to be known and carefully analyzed the conditions set by lenders on loans destination , grace period , repayment term and various fees that are the responsibility of the borrower.

We believe that deficit budgets should not become a rule that is perpetuated year after year, given the consequences and costs involved with interest and annuities. The consequences are particularly serious as state loans are used for consumer spending. These expenses do not add value, and taxes or new loans will represent the source for reimbursement.

State borrowings for capital expenditures may have positive economic effects. We consider the use of loans for investments in various industries and sectors, with direct impact on labor productivity growth, creating new jobs and demand fulfilment for domestic goods from internal and/or external markets. It is acceptable also the idea of using loans to

make investments in human resources, namely education, health, culture and sports. Such investments should, however, help to obtain qualifications for a specific field, which will lead to growth in labor productivity and quality of goods, healthy environment which will permit sustained efforts for competitiveness, awareness and positive attitude on discipline and behavior in the workplace and in the family and respect for public order.

■ When budgetary priorities are set, it should be taken into account the objectives of the government program approved by Parliament. Normally, these objectives should lead to economic growth and raising living standards of the population and for this reason budget priorities will be determined so as to enable them. However, this entails establishing correlations to strive for an optimum, given the requirements are possibilities between personnel costs and expenses for goods and services, spending on economic development and social and cultural expenditures, between expenditure on public order and defense spending, etc.

If the government program is opting for a budget deficit than it is appropriate to link the budget deficit with the volume of total capital expenditures included in the budget. A possible difference between the higher fiscal deficit and lower capital costs can be interpreted by resorting to loans to cover consumer spending which have the consequences mentioned above.

■ The budget priorities will be taken into account the EU membership, which entails both rights and obligations to contribute to the coverage of the EU budget's expenses.

■ Budget prioritizing is made also by considering the state's obligations in relation to loans previously contracted. As such, in the budget appear also interest expenses and annuities that are due in the year for which the budget is drawn up.

■ Budgetary priorities cannot be determined without consideration of costs related to ongoing programs of previous periods. This includes both projects financed from post-accession EU funding and external refundable grants. Program based budgeting provide continuity and enable early decisions making for those measures which are necessary for the implementation of the investments.

The conclusion of those presented above is that budget priorities can take into consideration only those financial resources which remains from revenues after the following three categories of expenses are deducted: interest, reimbursements of previously contracted loans, respectively ongoing programs.

Budget prioritization during economic and/or financial crisis is an economic and political decision with high importance. Such budgetary decision is necessary to pursue in a way that not come to the deepening crisis. As such, fiscal measures that can hardly be avoided, for example, reductions in salaries for the staff working in public sector, increases of consumption taxes in bearable limits which does not lead to social conflicts. It is also desirable that such measures do not result in reduction of budget revenues by reducing consumption and income taxes. Also be considered and measures leading to a reduction in the administrative structures and reducing costs like those with phone calls, office materials, with displacement in the country and abroad that are not strictly necessary, etc.

If, however, budget revenues are decreasing due to the crisis and reduced expenditures as mentioned above must further be reduces, then reduction should minimally affect the correctly determined expenditures with education, health and social security. Practice shows that the reference without a rigorous analysis of employees in unemployment or early retirement has negative medium and long-term consequences both economically and financially.

## **2. Priorities in Romanian State Budget for 2013**

To see how the revenues are structured and, especially how priorities were expressed on expenses, we will focus at the beginning on the revenues from the state budget for the year 2013.

Total revenue of state budget is 98.182 billion lei. Of these, 93.12% are current incomes, 84.98% being tax revenues. Structure of the main tax revenue and non-tax revenue intake is presented in Table 1.

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Table 1. Romanian State Budget revenues for 2013

Revenue	Share in total revenues
Taxes on income, profits and capital gains from legal entities, including:	13.41
Tax on profit from economic organizations	11.44
Taxes on income, profits and capital gains from natural persons	7.78
Value added tax (VAT)	39.02**
Excises	21.26
Non-tax revenues	7.95

Source: Annex 2 to the Act No. 5 of 02.21.2013 the State Budget for 2013, published in Official Gazette No. 106 of 22.02.2013

\*) Represents only the difference remaining after deduction of allowances and amounts deducted from income tax for local budgets (15.260 billion lei). Income tax is 22.898 billion lei.

\*\*\*) Is the difference that remained from VAT (52.949 billion lei) after deduction of amounts deducted for local budgets (14.678 billion lei).

According to the data in Table 1 it is observed that indirect taxes, namely VAT and excise duties account for over 60% of budget revenues. Indirect taxes are inequitable because they do not take into account the purchasing power of consumers and are pressing harder on lower income taxpayers. As such, it can be envisaged some measures to ease the situation of people with modest incomes. Such measures may be: reduced VAT rates to some of the consumer products essential to everyday living, while increasing the rate at luxury objects and cars, alcoholic beverages and tobacco products.

Simultaneously, we consider reconsidering current tax system's revenues, especially for individuals. Flat rates violate the principle of tax equity, disregarding the power of contribution, respectively the amount of revenue and the personal wellness of taxpayers. By switching to progressive rate taxation (on income installments) will be removed inequities from the current system. Setting income installments and progressive rates can be designed such a way not to cause a gap in budget comparing with revenues obtained by using a flat rate of 16%.

Referring to the destination of spending set in the state budget for the 2013 we first consider grouping expenses according to economic classification presented in Annex 1.

Data from Annex 1 shows that the total spending in the amount of 116.360 million lei, 95 % are current expenses, 1.33% and capital expenditures and 3.51% are expenditures for loan reimbursement.

In current expenditures, transfers between government units represent 25.37% of them and 24.11% of total expenditures. It is followed, in order, by the personal expenses with 17.67% and 16.80% of total expenditures. Social expenditures are 12.79% and 12.16% of total expenditures. It should be noted that expenditures with projects funded by external post-accession grants represents over 12% of total spending, being on the 4th place in the structure of current expenditures.

The fact that, especially since 2000, borrowings to cover budget deficit increased has led to high spending on interest payments. Thus, in 2013, these expenses represent 8.93% of total spending, which is more than spending with education, health, culture and sport together (these three are totaling only 7.41% of total expenditures).

Moving to analyze budgetary expenditures given their functional classification, we note, as shown by the data in Annex 2, the top position is occupied by general public services expenses, which represent 41.36% of the total budget, or nearly double the spending on social and cultural activities that hold 22.8% of the total budget.

Important amounts of expenditures, over 12% of total transactions, are public debt and loans.

It is worrying that the proportions of transfers from the state budget to social security budget, because it represents 11.52% of total expenditures. Social security budget have deficit for several years, and this is a consequence of the large number of retirements approved under questionable conditions.

The second position in total spending, respectively 22.8%, occupy expenditure on social and cultural activities. More than half of these expenditures are social assistance. This means that the number of people in material need and health is significant. Unfortunately, the amounts allocated to education, health and culture represent only 7.41% of total expenditures.

Expenditures for economic activities are 18.8% of total spending, ranking the third place. Within these expenses, the larger amounts are allocated to transport which counts 11.15% from total expenditures. While funds are allocated for roads and bridges representing 5% of total

spending, no amounts are provided for the construction of highways. Agriculture, forestry, fishing and hunting are allocated only 5.2% of total spending, for agriculture being allotted 1.44 % of total expenditures. We believe that agriculture, by all means and importance in providing products on daily life and thus affecting the health of the population deserves greater financial effort from the state.

The following item in total budget expenditures is occupied with defense, public order and national security expenses which are totalizing 14.49% of the grand total. Prevalled are spending with public order and national security, which represents 10.65% of the total budget. Defense expenditures represent 3.83% of total expenditures. We do not have enough information to say that too much money is allocated for defense, especially since it costs and membership in NATO. We try, however, a sense of regret when we see that the budget amounts allocated to education is only 3.4%.

In light of appropriations, the last category of expenditure is the expenditure with development services, housing, environment and water, which represents 2.49% of total expenditures. Housing, public services and development benefit from 1.07% while environmental expenditures are 1.42% of total spending.

Finally, note that summing percentage of total budget expenditure as it is shown in Annex 1, capital expenditure plus expenditure with projects financed from post-accession funding and expenses from grant programs resulting 15.34%. Comparing the budget deficit relative to total budget expenditures representing 15.62% of the three components above, we note that the values are very close. To say, however, that the budget deficit has his whole nature of investment spending, we lack data on which to see the programs to which I referred above translates into actions that directly support the economic and social development.

### **3. Conclusions**

We note that summing percentage of total budget expenditure as it is shown in Annex 1, capital expenditure plus expenditure with projects financed from post-accession funding and expenses from grant programs



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**Romanian state budget expenditures in 2013 – economic classification**

Indicator	Thousands lei	Share from total expenditures (%)
Total expenditures in 2013	116,359,817	100
•Current expenditures	110,556,298	95
-staff expenditures		16.80
-expenditures with goods and services		3.74
-interests		8.93
-subsidies		3.0
-transfers between government units		24.11
-other transfers		10.62
-projects financed from EU budget		12.04
-projects financed from reimbursable funds		1.97
-social assistance		12.16
•Investments	1,552,404	1.33
•Loan reimbursements	4,083,769	3.51

Source: Annex 2 to the Act No. 5 of 02.21.2013 the State Budget for 2013,  
published in Official Gazette No. 106 of 22.02.2013

<sup>)</sup> Calculated by the author

**Romanian state budget expenditures in 2013 – functional classification**

Indicator	Thousands lei	Share from total expenditures (%)
Total expenditures in 2013	116,359,817	100
General public services	48,190,084	41.36
- Executive authorities		3.94
- Contributions to the EU budget		5.77
- Fundamental and development research		1.66
- Transactions on public debt and loans		12.1
- Transfers to social security budget		11.52
- Transfers to health insurance fund		3.97
Defense, public order and national security	16,860,288	14.49
- Defense		3.83
- Public Order and National Security		10.65
- Judicial authorities		1.76
Social and cultural expenditures	26,531,483	22.8
- Social assistance		12.16
- Education		3.4
- Health		2.25
- Culture, recreation and religion		1.5
- Recreational and sporting services		0.26
Public services and development, housing, environment and water	2,896,993	2.49
Economic activities	21,940,492	18.8
- General economic, commercial and labour actions		1.92
- Fuel and energy		0.15
- Mining, processing and construction		0.11
- Agriculture, forestry, fishing and hunting		5.2
- Transports		11.15
- Communications		0.17
- Economic research and development		0.09
- Other economic actions		0.06
<b>DEFICIT</b>	<b>-18,176,810</b>	
Deficit/Total expenditures		15.62

Source: Annex 2 to the Act No. 5 of 02.21.2013 the State Budget for 2013,  
published in Official Gazette No. 106 of 22.02.2013

<sup>)</sup> Calculated by the author