CBR
COUNCIL FOR BUDGET RESPONSIBILITY

Evaluation of Medium-term Budgetary Objectives

May 2014

 The CBR thanks the Ministry of Finance and the Statistical Office of the Slovak Republic for the data provided.

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Summary

The government has published its budgetary objectives for the years to come. Apart from being important from the domestic fiscal perspective, these objectives are subject to EU-wide evaluation under the European Semester. The government's fiscal strategy is also important in the light of the effort to close the excessive deficit procedure to which Slovakia has been subject since 2009. The essential precondition has been to reduce the 2013 deficit below 3 % of GDP and keep it under this level also in 2014 and 2015 based on the Commission's forecast. In 2013 the deficit reached 2.8 % of GDP and the latest Commission forecast[1] assumes it could remain under 3 % of GDP also in 2014 and 2015. Based on these figures, **the excessive deficit procedure in respect of Slovakia is expected to be lifted.** The Council for Budget Responsibility evaluates the meeting of the medium-term objectives presented in the 2015-2017 Stability Programme from two perspectives. The first is to monitor and evaluate, pursuant to the Fiscal Responsibility Act, the development of public finances, with particular emphasis on identifying potential risks, and the second is to assess compliance with the Fiscal Compact, which has been transposed into the national legislation[2] and which defines the pace of consolidation towards the medium-term objective.

The Council views positively the fact that the government declares its intention to continue public finance consolidation at a pace necessary to ensure permanent deficit reduction after 2013 and put in place conditions for the abrogation of the excessive deficit procedure. Moreover, general government debt is expected to stabilise below 57 % of GDP and attain the medium-term objective (MTO) by 2017. **The meeting of these objectives will significantly improve the long-term sustainability of public finances in Slovakia.** On the other hand, a point needs to me made that, as of yet, **these plans are not supported in their entirety by concrete measures** a large number of which must be further specified. After the robust consolidation in 2013, the government is not planning to use the year 2014 to make permanent improvements in the general government balance; hence **the meeting of the MTO by 2017 will require an annual consolidation effort of the government of 1.2 % of GDP between 2015 and 2017.** The transgression of the third debt limit at 55 % of GDP in 2013 has triggered a set of sanction mechanisms which, among other things, entail a freeze on expenditures for 2015 at the level of the 2014 approved budget. The fiscal framework presented in the Stability Programme does not factor in these implications. In the medium-term, therefore, the 'debt brake' provisions should contribute towards reducing the deficit and bringing the debt growth to a halt.

The year 2013 closed with a deficit of 2.8 % of GDP, which is 0.2 % of GDP better than the budget target. From among the factors with medium-term budgetary impact we should particularly mention[3] the lower-than-planned drawing of EU funds and the ensuing national non-expenditures from the budget, which improved the balance in 2013 by 0.6 % of GDP. The local governments contributed to the improved balance mainly through significant cuts in capital

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1 The Spring Forecast of the European Commission of 5 May 2014 features a deficit of 2.9 % of GDP in 2014 and 2.8 % of GDP in 2015.
2 §30a of Act No 523/2004 on General Government Budgetary Rules.
3 A detailed description of differences against the budget can be found in Commentary 5/2004: Fiscal Performance of General Government in 2013.

expenditures by municipalities, which reached the lowest level since 2005. The shortfall in tax revenues has been offset by better VAT collection, thanks mainly to the measures adopted to combat tax evasion. The surplus in the budget of universities came as a positive surprise. The reclassification of *Železnice SR* (Slovak Railways) into the general government sector represented another unbudgeted positive factor contributing 0.1 % of GDP.

Certain positive and negative variations from 2013 will be spilling over to the years to come. The estimate for 2014 and the medium-term objectives already reflect the updated tax revenues. In spite of the positive surprise through the surpluses of universities and *Železnice SR,* their budgets in the next years are designed as nearly balanced. A lower drawing of EU funds may reduce expenditures on co-financing, which will negatively affect economic growth and/or the overall absorption of EU funds from the 2nd programming period. Higher current expenditures of municipalities may be partly offset by capital expenditures, yet the room for that has narrowed compared with the past.

In its evaluation of the approved budget at the end of the last year the CBR identified a number of risks, concluding that the ambition to reach the 2014 target was realistic, however, only if the planned one-off revenues indeed materialise. A substantial part of budgeted revenues relied on dividends carried over from 2013 and their increase, but, following a negative opinion by Eurostat, the Ministry of Finance already partly effected the transaction in 2013. Another risk relates to the amount of the ordinary dividend in 2014 which is conditional on the completion of a change in the SPP's ownership structure and the pay-out of a higher dividend than the dividend due to the state based on the government's stakes in SPP subsidiaries. The other identified risks included, in particular, local governments, healthcare sector, and the drawing of and financial corrections to EU funds. Since the better performance of municipalities in 2013 was mainly due to cuts in their capital expenditures, the CBR continues to perceive risks associated with higher current expenditures. The CBR does not yet have the actual budgets of municipalities for this year at its disposal. The healthcare sector may also come in as a negative surprise: although the debt of hospitals increased by over EUR 100 million in 2013, neither the budget nor the latest 2014 estimate by the Ministry of Finance foresees its further increase. The accelerated drawing of EU funds towards the end of 2013 slightly reduced the risk associated with the rollover of the corresponding co-financing expenditures to the following years to the level of EUR 140 million. On the contrary, the Ministry of Finance estimates that the amount of financial corrections in 2014 will reach approximately EUR 68 million. With the above-mentioned risks and the already adopted measures and potential reductions in the co-financing expenditures taken into account, including the positive impact of blocking 3 % of state-budget expenditures, **in the absence of additional measures** the 2014 deficit could reach **2.9 to 3.4 % of GDP.**

The drawing of EU funds has a considerable impact on the balance through the expenditures on co-financing; a higher drawing increases co-financing and, vice versa, non-drawing of EU funds reduces expenditures and thereby improves the balance. The actual figures on the drawing of EU funds until the end of 2013 and the 2014-2016 budget outline lead to the assumption that **from the total EU funds' allocation for the 2nd programming period, about EUR 1.6 billion might not be drawn.** The effort to absorb these funds creates a risk for the coming years in the order of EUR 137 million. On the other hand, the failure to draw the entire allocation would be a missed opportunity to boost the economic growth potential.

Structural deficit, as defined by the Fiscal Compact, reached 3.1 % of GDP in 2013 and is expected to deteriorate by 0.8 % of GDP in 2014 should the present deficit estimates prove to be correct. In such a situation, the deviation will most probably be considered significant under the Fiscal Compact rules and certain correction measures will need to be proposed. With the factors without long-term impact on the change of the fiscal position taken into account, the deterioration will be even more significant, reaching 1.1 % of GDP. This confirms the CBR's evaluation based on which the worse structural balance in 2014 **impairs the long-term sustainability of public finances. Provided that the fiscal targets are met, the fiscal restriction in 2015 - 2017 will have to be fairly tight, about 1 % of GDP annually,** which is in line with the requirements of the Fiscal Compact. This will be the case with the *proviso* that the necessary measures will not be of a one-off or temporary nature.

The consolidation effort of the government, which expresses the government's contribution to a permanent change of balance, **is estimated to be negative in 2014 at 0.7 % of GDP**. After the robust consolidation in 2013, whether in terms of improved structural balance or the consolidation effort of the government, **2014 is not planned to be a year of measures designed to make permanent changes in fiscal balance. Quite the contrary, the structural balance deterioration in 2014 means that in order to meet the medium-term objective by 2017, the average annual consolidation effort will have to reach 1.2 % of GDP**; the present framework anticipates the highest consolidation effort in 2015 at 1.6 % of GDP.

The meeting of the Ministry of Finance's deficit estimate for 2014 at 2.84% of GDP would require the adoption of **measures with an impact** representing 0.5 % of GDP. Provided that the measures have the same permanent impact over the entire medium-term horizon, the need to adopt additional measures for 2015 is quantified at 0.9 % of GDP[4].

The macroeconomic assumptions and estimates of revenues from taxes and social security contributions were approved by the respective committees in February 2014. Development hitherto does not indicate any significant risks for the assumptions used in the forecasts. There is a degree of uncertainty as far as the revenue from corporate income tax is concerned because its revised estimate based on the 2013 tax returns will only be available in June. The measures adopted to combat VAT evasion may have a positive impact on tax revenues.

The medium-term budget outline is the first step in the process of budget compilation. Since its main purpose is to specify budgetary objectives, the outline does not contain a detailed description of the measures designed to reach the objectives. The purpose of the measures on the revenue side is, in particular, to sustain the VAT revenue and expand the use of withholding tax and electronic cash registers. The expenditure side includes, in particular, cost reductions related to the ESO project (streamlined public administration), which the CBR is not in the

[4] The need for measures is usually higher than what this indicator suggests. It is due to the secondary effects of consolidation which impairs macroeconomic development; moreover, a part of the measures may negatively affect the expenditures of general government.

position to evaluate in the absence of detailed information. The remaining measures (about a quarter) will be defined at a later stage.

The medium-term budget outline presented in the Stability Programme does not yet reflect the sanction mechanisms embedded in the national fiscal rules. Although it quantifies the magnitude of the changes required under the Fiscal Responsibility Act, the budget outline has not yet incorporated them. Provided that the freeze on expenditures, as required by the Fiscal Responsibility Act, is fully reflected in the improved balance, most of the identified risks would be eliminated, helping the government to attain its fiscal targets. The slackening of the government's consolidation effort in 2014 may trigger (in 2015) the correction mechanisms arising from the implementation of the Fiscal Compact.

Introduction

The Fiscal Responsibility Act[5] obligates the Council for Budget Responsibility to monitor and evaluate the development of public finances. Two **phases of budget** preparation are of key importance to evaluation: The Medium-term Budget Outline and Stability Programme (submitted to the Cabinet in April) and the Budget Proposal, approved by the Cabinet and submitted to the Parliament (by 15 October). The Medium-term Budget Outline formulates the main fiscal policy objectives and the measures proposed to reach them, whereas the Budget Proposal is a detailed document containing specific measures. The purpose of CBR reports is to offer an independent view on the budget and assess whether the fiscal policy setup is sufficient in terms of achieving the targets set and, at the same time, to identify potential risks to be eliminated through the adoption of additional measures.

The present CBR opinion is based on the Stability Programme of the Slovak Republic for 2014-2017, approved by the Cabinet on 23 April 2014 and submitted to the European Commission as a binding document in line with the requirements of the Stability and Growth Pact. Although the draft Medium-term Budget Outline for 2015-2017 was on the Cabinet's agenda on the same day, the draft did not reflect the actual development in 2013, nor did it include specification of measures. The Cabinet suspended its discussion on the draft budget outline without approving it. This evaluation presents the development of fiscal position, the anticipated economic development, and a description of fiscal policy measures designed to meet the medium-term objectives. It is based on the 2014-2016 General Government Budget as approved in December 2013, on the estimate of the 2014 fiscal position, and on the 2015-2017 budgetary objectives proposed in the Stability Programme.

The document is divided into four chapters. Based on the preliminary figures for 2013 and the 2014 development, the **first chapter** updates the view on the risks of the approved budget for 2014[6]. The **second chapter** evaluates the budget from the perspective of the proposed objectives. The **third chapter** analyses the objectives in both the domestic and international contexts and evaluates the feasibility of the measures proposed. The **fourth chapter** monitors the budget from the perspective of the existing legislation at both the national and EU level, with particular emphasis on the consequences of transgressing (in 2013) the third debt limit laid down in the Fiscal Responsibility Act, which is connected with a number of budgetary restrictions.

Pursuant to the Fiscal Responsibility Act, the CBR will publish in November its second evaluation report scrutinising the 2015-2017 General Government Budget Proposal as approved by the Cabinet.

5 Act No. 493/2011 on Fiscal Responsibility, Article 4(1)(d).
6 The CBR identified risks in its evaluation report to the 2014-2016 General Government Budget Proposal of November 2013 and an addendum thereto of December 2013.

1. Risks to meeting the 2014 budgetary objective

The government set the target deficit value for the 2014 budget at 2.64 % of GDP. In its evaluation of the approved budget[7] the CBR identified several risks associated with this target and the potential sources for their elimination. **The publication of preliminary data for 2013, the revised 2014 deficit estimate by the Ministry of Finance to 2.84 % of GDP and the interim budget execution have enabled to update certain risks**[8].

The **main changes** compared to the approved budget include the non-materialised carry-over of dividends between 2013 and 2014, revision of the impacts of co-financing (risks and potential expenditure reductions) against the backdrop of developments in 2013, and identification of a new risk entailing the lower-than-planned dividend from the SPP gas company. On the other hand, the present estimate reflects the higher-than-expected tax collection and, in connection with the sanctions applicable under the Fiscal Responsibility Act, adds a new source covering the risks associated with the blockage of budget expenditures.

- **Revenues from taxes and social security contributions**

In comparison with the approved general government budget for 2014-2016, the **total revenue from taxes and social security contributions is expected to be higher**, which has been reflected in the forecast of revenues from taxes and social security contributions by the Tax Revenue Forecasting Committee ("TRFC") from February 2014. **The improvement represents EUR 189 million**.

In the case of **value added tax,** the new legislative measures which entered into force as of the beginning of this year (in particular the introduction of a VAT control statement) are expected to narrow the scope for tax evasions. The impacts of these measures have not been quantified and reflected in the forecast, but they represent a positive risk for VAT collection and a potential source from which other risks in the budget may be covered.

- **Non-tax revenues, including dividends**

The risk of the transfer of revenues from dividends not being recognised under ESA95 materialised when a Eurostat mission[9] confirmed that only the dividends paid from previous years' profits can usually be recognised as revenue[10]. As a consequence, the budgeted carryover of dividends from 2013 to 2014 did not take place. In 2013, a decision on payment of dividends from the 2012 profits of *SPP* and *SEPS* in the amount of EUR 254 million have been made which positively affected the general government balance in the same year. **Conversely, the impact in 2014 is expected to be negative at EUR 443 million**[11].

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7 The list or budget risks and reserves for the year 2014 was published in the [Addendum to the 2014-2016 General Government Budget Proposal].

8 The next part deals solely with the description of changes in the risks and the sources of their coverage in comparison with those identified in the evaluation of the approved general government budget. The risks are quantified against the approved 2014 budget.

9 Information from the Stability Programme, referring to a working version of the conclusions of a Eurostat mission, which have not been published yet.

10 Under ESA95 (Manual on Government Debt and Deficit, 2013), dividends may also be paid out from the profit from before two years, but only on the condition that such operation ensures smoothing of their flow over time. The intended carryover of dividends did not meet that condition.

11 Cash transactions did not take place, the shareholders issued the respective decision which, in this case, ESA95 considers decisive for the recording in the national accounts.

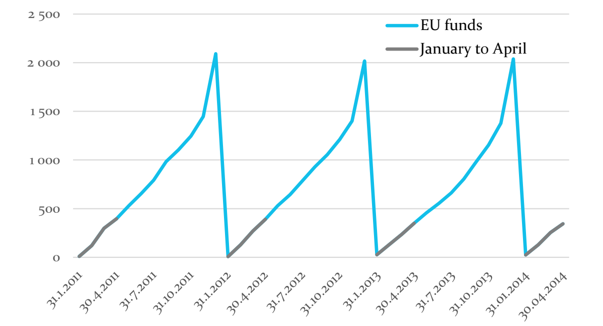
The **lower dividend from the 2013 SPP's profit** also represents a risk. The latest estimate of the 2014 balance is based on the revenue projection of EUR 370 million[12], which corresponds to a dividend payable to the state as a 100-percent shareholder. Hence the revenue hinges on the planned changes in the SPP's ownership structure being implemented[13]. Moreover, the plan for 2014 is based on a dividend from the total profit of subsidiaries where the state controls only 51 %[14]. The negative risk for the 2014 balance is represented by the amount of the dividend due to the minority stakeholder **at EUR 181 million.**

In the category of 'other non-tax revenues', the revenue from the **digital dividend** was lower than budgeted. The shortfall represents EUR 86 million. On the other hand, the balance will be positively influenced by a windfall revenue from a **fine** of EUR 45 million **imposed on construction companies engaged in a cartel agreement**. **The overall negative impact of both transactions on the balance represents EUR 41 million.**

- **Drawing of EU funds and co-financing**

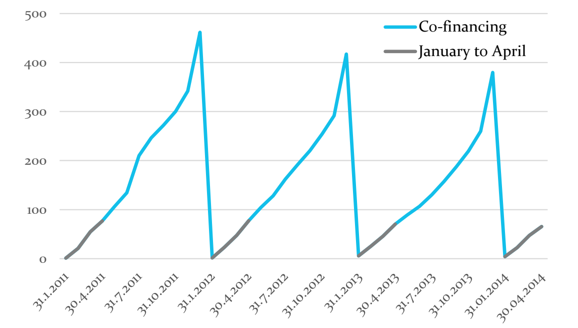
The total budgeted amount of EU funds for 2014 by far exceeds the average capacity to absorb them within a single year, which may lead to a potential **reduction in expenditures for co-financing in the amount of about EUR 200 million**. The CBR's estimate is based on the assumption that the uptake of EU funds in 2014 will be at the 2013 level, which the figures for the first four months of this year confirm. The reason may lie in the slower drawing of funds from the 3rd programming period, which is starting in 2014, or a potentially different structure of drawing in the 2nd programming period (lower in 2014 and higher only at a later point). The quantification does not include additional saving due to lower expenditures on accompanying investments from the national sources[15].

Figure 1: EU-funded expenditures from the state budget (€ million)



Source: State Treasury

Figure 2: National funds for the co-financing of EU funded projects (€ million)



Source: State Treasury

12 The budgeted revenue from SPP dividend in 2014 is €735m. If we take the impact of the non-effected dividend carryover in the amount of €365m into account, the remaining amount is €370m.

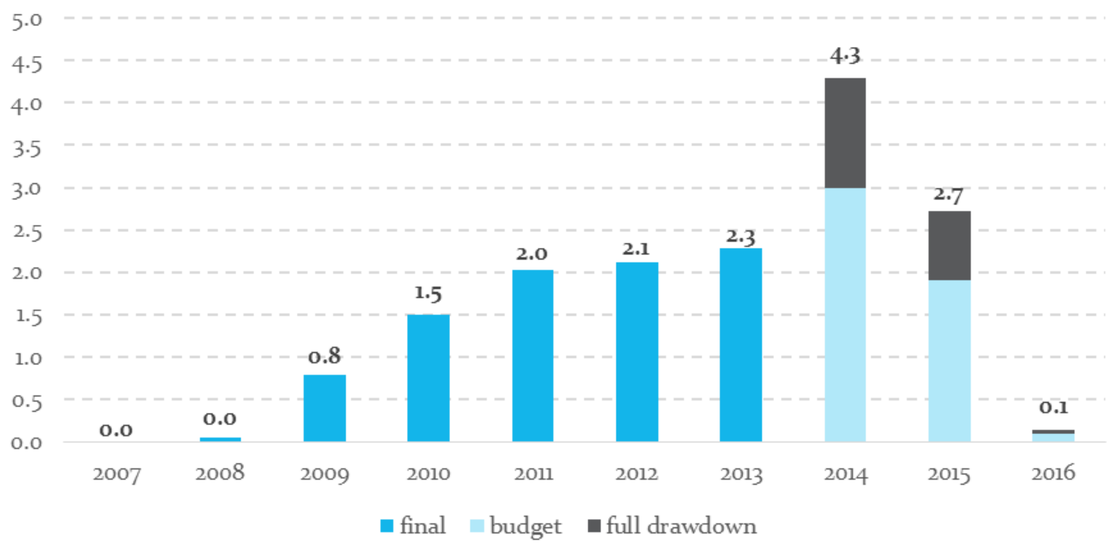
13 The purpose of the planned transaction is to put the loss-making SPP into the hands of the state (100% stake) and keep a 51-% stake in the other, profitable subsidiaries of SPP.

14 The CBR pointed out the problem in its Evaluation of the 2014-2016 General Government Budget Proposal of November 2013, p. 69.

15 These are national expenditures which need to be incurred in the implementation of certain major EU projects above and beyond the framework of co-financing, particularly in the development of the road and rail infrastructure.

However, in the case of **Structural Funds and Cohesion Fund in the 2nd programming period** (2007-2013)[16], the actual drawing until 2013 and the budgeted figure indicate that **funds worth EUR 1.6 billion from the total allocation would be left unused**. This would tantamount to a **permanent loss of opportunity to contribute positively towards boosting the economic growth potential.** If the funds were to be fully used[17], the potential risk for the 2014-2016 deficit due to higher expenditures for co-financing, amounts to **EUR 137 million**. At the same time, with the amount spread evenly between 2014-2016 in line with the planned drawing of EU funds (Figure 3), the **additional[18] risk to the 2014 balance would reach a maximum of EUR 82 million.**

Figure 3: Revenues from EU funds – 2nd PP, structural funds and Cohesion Fund (% of GDP)



* For 2014-2016, data from the approved 2014-2016 general government budget were used. The draft medium-term budget outlook for 2015-2017 assumes higher total drawing of EU funds both in 2015 and 2016. The increase is related to the updated assumptions on drawing of EU funds from the third programming period. *Source: CBR, MF SR*

If the planned reduction in expenditures for co-financing is reached and the risk associated with the full drawing of EU funds from the 2nd programming period is factored in, the CBR **estimates the total positive impact on the 2014 balance at EUR 118 million**. However, this in turn increases the risks[19] **in subsequent years by the same amount (from €137m to €255m)**.

The **financial corrections in connection with EU-funded projects had** a negative impact on the 2013 balance in the amount of EUR 125 million. They are expected to affect the balance negatively also in the years to come. For 2014, the Ministry of Finance estimates their amount at **EUR 68.4 million**.

16 Beneficiaries may draw these funds until 31 December 2015 and the expenditures may be declared to the Commission until 31 March 2017.

17 Based on the Budgetary Rules Act, unspent funds are transferred from 2013 to 2014 and thus represent additional resources above the framework of the approved budget.

18 This applies on the assumption that the actual drawing of EU funds in 2014 is higher than in 2013 by the amount of unbudgeted funds.

19 Subject to a full drawdown of the available EU funds.

- **Other expenditures from the state budget**

The risk of the negative impact of the carryover of expenditures from 2013 on the general government balance **has increased**. The 2013 budget expenditures in the amount of EUR 454 million (without EU funds and national co-financing) have been transferred to the year 2014. This considerable year-to-year expenditure carryover influenced the 2013 balance positively (EUR 203 million). The impact on the 2014 budget balance will depend on the amount of funds carried over from 2014 to 2015.

- **Local governments**

Based on the actual figures for 2013, the CBR updated its forecast of the **risk associated with the fiscal performance of local governments** (see Annex 1 for details). The higher risk is connected with the budgets of municipalities (risk of €194m), mainly due to their higher-than-budgeted expenditures on wages, goods and services. Their budgetary target can only be achieved at the expense of lower capital expenditures. However, given their low level in 2013 (deferred investments) and this year's communal elections, the room for offsetting the surge in current expenditures will be narrower (up to €100m, according to CBR estimates). The risk is lower in the case of the self-governing regions (about €15m); this tier of local government is expected to slightly overrun its budgeted payroll and operating expenditures. **The CBR estimates the overall risk associated with the fiscal performance of local governments, reflecting the likely decline in capital expenditures, to the tune of 100 to 200 million EUR.**

- **Other general government entities**

The impact on the balance of the reclassification of ***Železnice Slovenskej republiky*** **(Slovak Railways) into the general government sector** remains questionable. The budget for 2014 did not contemplate the reclassification (because the decision was taken later), yet the railway company had a positive impact on the balance in 2013. This change is likely to result in the revision of nominal GDP which, from the perspective of deficit-to-GDP ratio, represents a **positive risk**.

Based on the 2013 result (improved balance by €49m compared to the 2013 budget) **public universities represent a positive risk** for the balance.

The potential risk-covering sources now also include the blocked government expenditures (3 %) and the reserve funds of the prime minister and the government (described in detail in part 4.1) which have been blocked for spending due to the transgression of the debt limit defined in the Fiscal Responsibility Act. The maximum positive impact of this measure on the balance represents EUR 308 million, depending on which expenditure items will be affected by the blockage and whether or not any moneys will be disbursed from the reserve funds. The positive impact on the balance will be lower provided that the blockage affects the balance-neutral expenditures (transfers to other general government entities) or the reserve funds of the prime minister and of the government.

Based on the latest available information, the quantification of other risks remains unchanged -- in other words, development in 2013 confirmed the existence of these risks and their estimated impact. The final impact of transition to the new ESA2010 methodology is a question which remains unanswered.

Tab 1: Overview of budgetary risks and provisions for 2014 (€ million)

<table>
<tr><th rowspan="2">Risks to meeting budgetary targets</th><th colspan="2">December 2013</th><th colspan="2">May 2014</th></tr>
<tr><th>Risks</th><th>Risk coverage</th><th>Risks</th><th>Risk coverage</th></tr>
<tr><td>1. Unattained additional tax revenue from wage increases in the school sector</td><td>10</td><td rowspan="5">no quantification (better tax collection)</td><td>0[1]</td><td rowspan="4">189[3] (better tax collection), no quantification (better VAT collection)</td></tr>
<tr><td>2. Budgets of local governments</td><td>120-180</td><td>100-200</td></tr>
<tr><td>3. Underestimation of healthcare costs (unbudgeted increase in debts)</td><td>50-100</td><td>50-100</td></tr>
<tr><td>4. Contributions to registered capital (Eximbanka, SZRB)</td><td>max. 100</td><td>0[2]</td></tr>
<tr><td>5. Shortfall in revenues from the sale of emission allowances
6. Lower impact of the ESO reform (lower revenue from the sale of assets and lower cuts in expenditures)
7. Negative impact of the carryover of expenditures from 2013</td><td>50-100</td><td>50-100</td><td>200 (potential saving in co-financing)[4]</td></tr>
<tr><td>8. Carryover of unspent EU funds and the related co-financing to subsequent years [5]</td><td>400</td><td rowspan="6">200-300 (potential saving in co-financing)</td><td>max. 82[5]</td><td rowspan="3">max. 308 (saving due to sanctions under the Fiscal Responsibility Act)</td></tr>
<tr><td>9. Financial corrections to EU funds</td><td>no quantification</td><td>68</td></tr>
<tr><td>10. Non-recognition of the carryover of dividends under ESA95</td><td>437</td><td>443[3]</td></tr>
<tr><td>11. Lower revenue from SPP dividends</td><td>0</td><td>181</td><td rowspan="3">0 to 50 (impact of ŽSR and VVŠ)</td></tr>
<tr><td>12. Change of the ESA2010 methodology</td><td>no quantification</td><td>no quantification</td></tr>
<tr><td>13. Lower non-tax revenues (digital dividend, fine)</td><td>0</td><td>41[3]</td></tr>
<tr><th>Risk from a net-worth perspective without impact on budget balance</th><th>Risks</th><th>Risk coverage</th><th>Risks</th><th>Risk coverage</th></tr>
<tr><td>1. Reduced value of government assets due to the sale of state property (ESO)</td><td>54</td><td rowspan="4"></td><td>54</td><td rowspan="4"></td></tr>
<tr><td>2. Reduced value of government assets due to restriction on capital expenditures</td><td>no quantification</td><td>no quantification</td></tr>
<tr><td>3. Sale of assets of state corporations (CARGO) and the use of those revenues to cover current expenditures</td><td>98</td><td>98</td></tr>
<tr><td>4. Use of the revenue from the bank levy to finance current expenditures and occurrence of contingent expenditures</td><td>160</td><td>160</td></tr>
</table>

(1) The wage increase in the education system was reflected in the forecast issued by the Macroeconomic Forecasting Committee in February 2014. This means that also the present Tax Revenue Forecast reflects the measure.

Source: CBR

(2) The Ministry of Finance does not expect these transactions to take place.

(3) The Ministry of Finance took these risks into account in its latest deficit estimate for 2014 at 2.84 % GDP (Stability Programme for the Years 2014 to 2017).

(4) Without savings in related investments funded from national sources.

(5) It is a risk for 2014, calculated as a portion of the overall risk of €137m for 2014 to 2016. If the 2014 saving in the amount of €200m is attained and the risk of € 82m materialises, the risk for the following year will increase to €255m.

The presently identified risks and the sources of their coverage lead to the conclusion that, provided that no additional measures are taken, the 2014 general government deficit will reach 2.9 to 3.4 % of GDP.

2. Evaluation of budgetary objectives

The preparation of the budget for 2015 to 2017 is influenced by a number of factors. In April 2014, Eurostat notified the 2013 general government deficit in the amount of 2.8 % of GDP. The latest forecast by the European Commission[20] sees the deficit below the level of 3 % of GDP also in 2014 and 2015. These figures suggest to abrogate Slovakia from the **Excessive Deficit Procedure.** In the medium-term horizon until 2017, it will also be necessary to achieve the structural deficit target of 0.5 % of GDP in line with the requirements of the Fiscal Compact and the Stability and Growth Pact. General government debt in 2013 reached 55.4 % of GDP, triggering additional correction mechanisms prescribed by the Fiscal Responsibility Act based on which the government is obliged to **block 3 % of budget expenditures already in 2014** and, at the same time, submit to the parliament a budget which does not contemplate any increase in consolidated government expenditures in the years 2015 to 2017. For the first time, the sanctions will also affect the budgets of local governments which will have to freeze their spending at the 2014 budget level. The last factor is the negative impact of fiscal consolidation on economic growth.

The alignment of such mutually contradictory requirements calls for the adoption of a budgetary strategy that will mitigate the negative impacts on economic growth and ensure compliance with the requirements of the EU and national fiscal rules.

2.1 Fiscal framework

The 'general government budget outline' represents the first and fundamental step towards compiling government budget for the next three years, i.e., for 2015–2017 in this case. The outline provides initial information on the fiscal policy orientation, sets the target values for deficits during the outline period, and suggests the necessary of measures indispensible to meeting the defined budgetary objectives in a manner consistent with the rules of the Stability and Growth Pact at the EU level, and with the national fiscal responsibility rules, the compliance with which is monitored by the Council for Budget Responsibility.

The estimate of the 2014 deficit is a prerequisite for setting the 2015-2017 targets. According to the latest estimates by the Ministry of Finance, the **2014 general government deficit should reach 2.84 % of GDP.** The shortfall in revenues from dividends and other non-tax items (lower revenues from the digital dividend and additional income from a fine imposed on parties to a cartel agreement in the construction sector) is only partially offset by a higher estimate of tax revenues, including income from a special levy on operations in regulated industries.

The meeting of the 2014 target set at 2.64 % of GDP requires the adoption of measures in the amount of 0.20 % of GDP (€149m). **The key objective of the budget is to continue reducing, in a sustainable manner, general government deficit from 2.49 % of GDP in 2015 to 0.54 % of GDP in 2017.**

[20] Spring Forecast of the European Commission of 5 May 2014 features a deficit of 2.9 % of GDP in 2014 and 2.8 % of GDP in 2015.

Compared to the approved budget for 2014-2016, budgetary objectives have been modified. While for 2015 the draft budget outline expects the deficit to improve by 0.1 % of GDP, the fiscal target for 2016 deteriorates by 0.1 % of GDP.

Tab 2: General Government deficit targets (ESA95, % GDP)

	2014	2015	2016	2017
1. Approved general government for years 2014-2016	-2.6	-2.6	-1.5	
2. General government outline for years 2015-2017	-2.6	-2.5	-1.6	-0.5
3. Change (2-1) (% GDP)	**0.0**	**0.1**	**-0.1**	

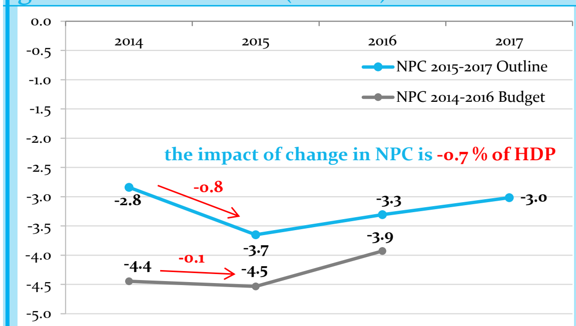
Source: MF SR

The following box presents the difference between the no-policy-change scenarios in the draft medium-term budget outline for 2015-2017 and the approved 2014-2016 budget, which identify the need to adopt measures aimed at reaching the objectives.

Box 1: Explanation of changes in the NPC scenarios developed by the Ministry of Finance

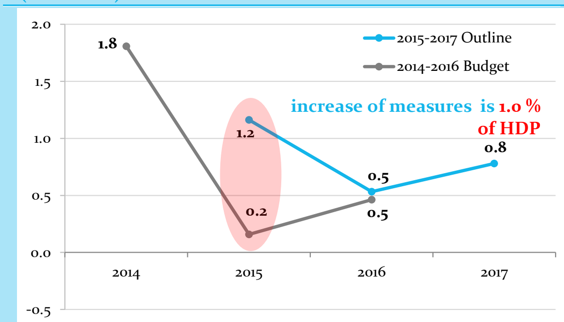
Compared to the approved 2014-2016 budget, the need to adopt measures in 2015 has risen by 1.0 % of GDP[21]. The difference lies mainly in the dynamics of NPC scenarios. While the one developed at the stage of budget preparation expected a slight deterioration of balance between 2014 and 2015 by 0.1 % of GDP, the present NPC indicates deterioration by 0.8 % of GDP. The NPC update has increased the need for additional measures by 0.7 % of GDP. The second factor is the change of budgetary objectives, which necessitates the adoption of measures amounting to 0.3 % of GDP[22]. The general government budget contemplated deficit reduction from 2.64 % of GDP in 2014 to 2.57 % of GDP in 2015. The present document assumes a change from the estimated 2.84 % of GDP to 2.49 % of GDP over the same period of time.

Figure 4: NPC development of general government balance (% GDP)



Source: MF SR, CBR

Figure 5: Need to adopt measures (% GDP)



Source: MF SR, CBR

The NPC scenario, developed at the time of the 2014-2016 budget preparation, was based on estimate for 2013. The updated scenario is based on the figures expected for 2014. The main difference, which

[21] Calculations are based on the 2014 deficit of 2.84 % of GDP, estimated by the Ministry of Finance. If the deficit target of 2.64 % of GDP is met through permanent measures, the need for measures in 2015 would decline to 1.0 % GDP. The change compared to the 2014-2016 budget would thus reduce to 0.8 % of GDP (0.7 % of GDP as a consequence of the NPC scenario update and by 0.1 % of GDP as a consequence of revised budgetary objectives).

[22] Comparison of YoY changes in deficits (% of GDP): (2.84-2.49) – (2.64-2.57) = 0.35 – 0.07 = 0.28.

may change the view on medium-term budget development, is the update of revenues and expenditures based on the latest macroeconomic forecast, adopted legislation and updated estimates of those items which are not estimated in the NPC by way of indexation (e.g., amount of non-tax revenues).

The need to adopt measures due to the NPC update (0.7 % of GDP) is a consequence of lower revenues by 0.9 % of GDP and expenditures by 0.2 % of GDP. On the revenue side, the decline in non-tax revenues is particularly considerable (0.6 % of GDP). On the expenditure side, the change is caused mainly by a decline in expenditures for goods and services, which is partly offset by an increase in capital expenditures.

Tab 3: No-policy-change development of general government balance (% GDP)

	NPC Budget 2014-2016			NPC Outline 2015-2017			comparison of changes
	2014	2015	change	2014	2015	change	
Total revenue	**32.91**	**31.85**	**-1.06**	**35.72**	**33.74**	**-1.98**	**-0.92**
Tax revenue	14.93	14.45	-0.48	16.12	15.34	-0.78	-0.31
Social security contributions	13.01	12.88	-0.13	13.18	13.09	-0.09	0.04
Nontax revenue	3.15	2.91	-0.24	4.32	3.53	-0.80	-0.56
Grants and transfers	1.83	1.61	-0.22	2.10	1.78	-0.31	-0.10
of which: from EU	*1.58*	*1.57*	*-0.01*	*1.86*	*1.75*	*-0.11*	*-0.09*
Total expenditure	**37.36**	**36.39**	**-0.97**	**38.56**	**37.39**	**-1.17**	**-0.20**
Gross wages	6.15	6.09	-0.07	6.43	6.37	-0.06	0.01
Goods and services	10.57	10.65	0.08	10.79	9.87	-0.92	-0.99
Current transfers	16.43	15.95	-0.48	16.34	15.97	-0.36	0.12
Interest	1.86	1.84	-0.02	1.88	1.80	-0.08	-0.06
Capital expenditure	2.35	1.86	-0.48	3.12	3.37	0.25	0.73
Balance	**-4.45**	**-4.53**	**-0.09**	**-2.84**	**-3.65**	**-0.81**	**-0.72**

Source: MF SR, CBR

The government defines its targets in the form of general government balance under the ESA95 methodology. A mere comparison of the year-on-year change in these deficits is insufficient to assess whether the government tightens up or relaxes its fiscal discipline and what is the government's contribution to the change. At the same time, they cannot be used to unequivocally determine the size of measures through the adoption of which the budgetary objectives can be met. These questions can be answered through short-term and medium-term analytical indicators[23] featured in the following table.

[23] More in CBR's Discussion Paper No. 02/2014: How to Measure Consolidation in Public Finances (currently available only in Slovak, the English version is under preparation). The discussion paper states that the government consolidation effort indicator is linked exclusively to the contribution of government measures towards permanent fiscal change. The indicator is therefore different than the consolidation effort presented by the Ministry of Finance.

Tab 4: Change in structural balance of general government in 2014 - 2017 (ESA95, % GDP)

	2013	2014E	2015O	2016O	2017O
1. Net lending/borrowing	**-2.8**	**-2.8**	**-2.5**	**-1.6**	**-0.5**
2. Cyclical component	-0.4	-0.3	-0.2	-0.1	0.1
3. One-off measures	0.7	1.4	0.4	0.4	0.1
4. Structural balance (1-2-3)	**-3.1**	**-3.9**	**-2.7**	**-2.0**	**-0.7**
5. Change in structural balance (Δ4)/ Fiscal compact	**1.8**	**-0.8**	**1.2**	**0.7**	**1.2**
6. Change in fully-funded pillar	0.4	0.0	0.0	0.0	0.0
7. Change in interest payments	-0.1	0.1	0.1	-0.1	0.1
8. Change in construction of motorways	-0.1	0.1	0.0	0.0	0.0
9. Change in decommissioning scheme of nuclear facilities	0.1	0.0	0.0	0.0	0.0
10. Change in structural balance (5-6-7-8-9)/ National concept	**1.6**	**-1.1**	**1.1**	**0.8**	**1.2**
11. GG balance in NPC scenario	**-2.8**	**-3.4**	**-4.0**	**-3.8**	**-3.9**
12. Change in structural balance in NPC scenario/ National concept	**-**	**-0.4**	**-0.5**	**0.0**	**-0.2**
13. Size of measures (1-11)	**0.0**	**0.5**	**1.5**	**2.2**	**3.4**
14. Change in size of measures (Δ13)	-	0.5	0.9	0.7	1.2
15. Consolidation effort of government (10-12)	**-**	**-0.7**	**1.6**	**0.8**	**1.4**

Source: CBR

The 2013 structural deficit, as defined by the fiscal compact's requirements, reached 3.1 % of GDP and is expected to deteriorate by 0.8 % in 2014, which is based on the latest government deficit estimate at 2.8 % of GDP. This development – given the almost unchanged general government balance – is due to the large number of one-off measures in 2014. **The meeting of the budgetary objective for 2014 (deficit at 2.64 % of GDP) may lead to a change in structural balance, depending on which measures will be used to meet the objective**[24].

Assuming that the change in structural balance reflects also other factors which, from a long-term perspective, do not have an impact on the change of fiscal position, but have either a positive or negative impact on the budget horizon, **its deterioration in 2014 will be even more significant (amounting to 1.1 % of GDP)**. In other words, the debt interest payments which are not under direct government control and the construction of motorways implemented outside the general government's balance, contribute to the 2014 deficit improvement by 0.3 % of GDP.

If the budgetary objectives are to be met, the 2015–2017 fiscal restriction will have to be fairly tight, about 1 % of GDP annually. This will apply on the assumption that the measures will not be of a one-off nature and will not affect the budget components which are neutral in the long term (e.g., impact of the fully-funded pillar, nuclear decommissioning scheme) and that there will be no transfer of expenditures outside the government balance (impact of motorway construction).

[24] Provided that the 2014 budgetary objective is reached solely through measures of a permanent nature and other indicators (e.g., impact of economic cycle on public finances) remain unchanged, the deterioration of structural balance will reach 0.6 % of GDP.

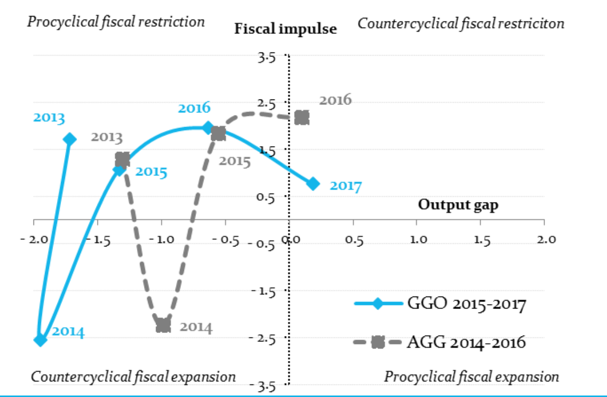
If the NPC scenario developed by the CBR (for more information, see Annex 3) is taken into account, the planned fiscal policy can be evaluated from two additional points of view. The first one is the **government consolidation effort**, which expresses the government's contribution to the permanent change of balance. **In 2014, it is estimated to be negative at 0.7 % of GDP**. In comparison with the change of structural balance, the negative impact is lower, which is connected with public finance development under the assumption of unchanged policies. In the absence of any government intervention, the 2014 structural balance would deteriorate by 0.4 % of GDP. The meeting of the medium-term budgetary objectives will require an average government consolidation effort at 1.2 % of GDP annually.

The second is the **size of measures**, which expresses the overall impact of the measures necessary to attain the budgetary objectives compared with the no-policy-change scenario. It does not distinguish measures based on whether they change the balance on a one-off or permanent basis. In 2014, measures with an impact of 0.5 % of GDP had to be adopted to for the forecasted figures to be reached. Provided that the measures have the same permanent impact over the entire medium-term horizon, the need to adopt additional measures for 2015 is quantified at 0.9 % of GDP[25].

After the robust consolidation in 2013, whether in terms of improved structural balance or the government's consolidation effort, 2014 is not planned to be a year of measures designed to make the changes in fiscal balance permanent. On the contrary, the structural balance deterioration in 2014 means that in order to meet the medium-term objective by 2017, the average annual consolidation effort will have to reach 1.2 % of GDP. The present fiscal framework assumes the greatest consolidation effort of the government in 2015, at 1.6 % GDP, which the CBR views as ambitious.

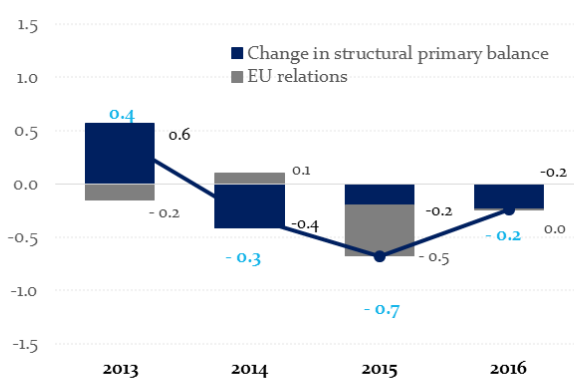
In the forthcoming period, the fiscal position will be restrictive with a negative impact on economic growth. Only in 2014 the pace of consolidation relaxes. However, the expansive counter-cyclical position in 2014 is caused by the year-on-year increase in EU funds by 1.4 % of GDP. If fully drawn[26], EU funds may contribute towards reviving economic growth and, at the same time, attenuate the adverse consequences of consolidation under a negative output gap. The effect of deficit reduction will prevail in subsequent years.

Figure 6: Fiscal impulse in 2013-2017 (% GDP)



Source: CBR

Figure 7: Change in fiscal impulse GGO[27] (2015-2017) vs AGG (2014-2016) (% GDP)



Source: CBR

[25] The need for measures is usually higher than on the basis of this indicator. This is connected with the secondary effects of consolidation which deteriorate macroeconomic development; at the same time, some of the adopted measures may negatively affect general government expenditures.

[26] In 2004-2012, the average drawing of EU funds reached approximately 62% of the budgeted amount.

[27] GGO (medium term general government budget outline), AGG (approved general government budget).

2.2 General government debt

Subject to meeting the defined budgetary objectives, the Stability Programme assumes that the debt will increase from 55.4 % of GDP in 2013 and to culminate at 56.2 % of GDP in 2015. In the years after, it should decline to 53.4 % of GDP at the end of 2017. Thus, in the medium-term, the debt is expected to fall by 2.0 % of GDP.

Tab 5: Gross general government debt (% GDP)

	2013	2014	2015O	2016O	2017O
Gross general government debt (EUR mill.)	39 975	41 110	43 711	44 824	46 021
Gross general government debt (% of GDP)	**55.4**	**55.2**	**56.2**	**54.9**	**53.4**
Structure of debt					
1. Existing debt (end-2012)	**47.3**	**47.5**	**47.0**	**46.4**	**45.5**
- debt level	47.3	45.8	43.9	41.8	39.6
- cumulated interest from existing debt	0.0	1.6	3.2	4.6	5.9
2. New debt - fiscal policy in 2013-2016	**0.0**	**1.5**	**2.8**	**2.9**	**2.3**
- primary balance (cumulated) + other impact	0.0	1.5	2.8	2.8	2.1
- cumulated interest from primary balances	0.0	0.0	0.1	0.1	0.2
3. Liabilities related to EFSF and ESM	**3.4**	**3.6**	**3.5**	**3.4**	**3.2**
- EFSF liabilities	2.6	2.7	2.6	2.5	2.3
- paid capital into ESM	0.7	0.9	0.8	0.8	0.8
- cumulated interest payments (only ESM)	0.0	0.0	0.1	0.1	0.1
4. Cash reserve for debt management	**4.7**	**3.2**	**4.7**	**4.1**	**4.2**
- cash reserve	4.7	3.0	4.5	3.7	3.7
- cumulated interest related to cash reserve	0.0	0.2	0.3	0.4	0.5
5. Extraordinary debt repayments*	**0.0**	**-0.6**	**-1.9**	**-1.9**	**-1.8**
- extraordinary repayments	0.0	-0.6	-1.9	-1.8	-1.7
- cumulated int. related to extraord. repayment	0.0	0.0	0.0	-0.1	-0.1
p.m. implicit interest rate	-	3.4%	3.3%	3.4%	3.3%

** reduction in debt of Emergency Oil Stocks Agency, revenues from the privatisation of Slovak Telekom* *Source: MF SR, CBR*

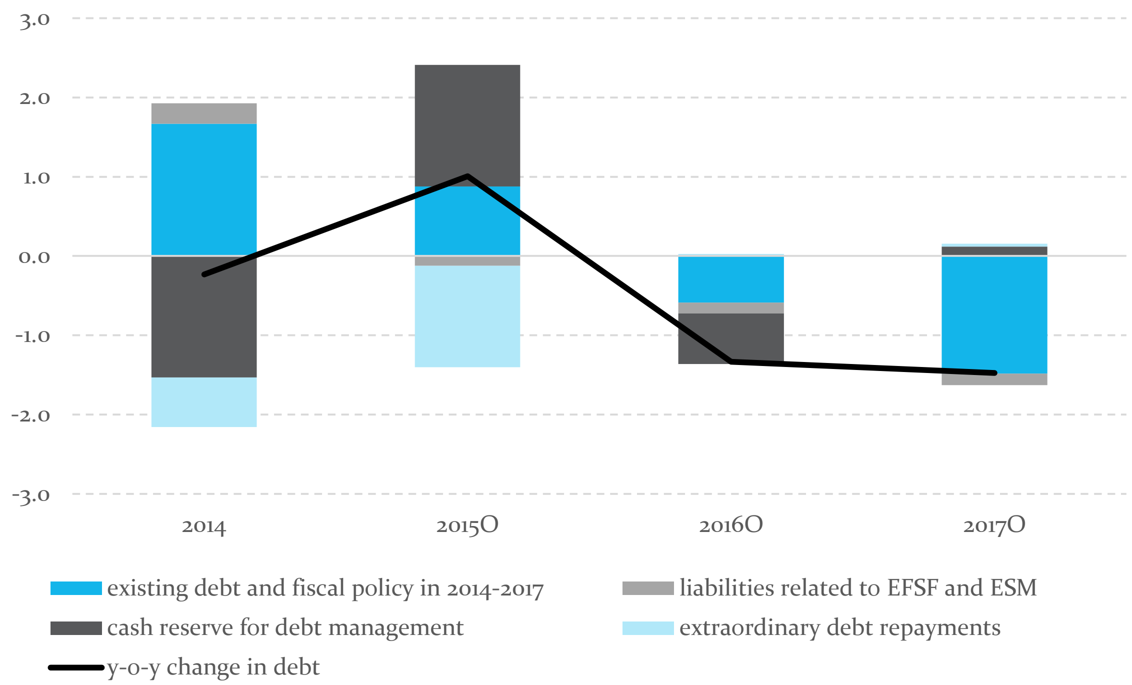
In terms of contribution towards debt reduction from its 2013 level, it is necessary to distinguish between two contradictory groups of factors:

- The debt growth in 2014-2015 is driven by primary fiscal deficits, that is, by expenditures exceeding revenues after deduction of debt interest payments. In 2016, this negative effect is slightly offset by primary fiscal surplus. Another factor affecting the debt negatively is that the surpluses of certain entities (municipalities) may not be used in the State Treasury system, which increases the need to finance cash deficits through new debt. Slovakia's **international commitments under the EFSF guarantees and contributions to the ESM** will have a slightly negative impact in 2014.

  Above the framework of the present debt forecast, the prepared change in the Eurostat methodology (ESA 2010) may also have a negative impact, particularly due to the reclassification of some state-controlled corporations into the general government sector.

- On the other hand, the debt will decline through **extraordinary instalments** by reducing the debt assumed from the Emergency Oil Stocks Agency in 2014[28] and through a revenue from the privatisation of *Slovak Telekom* in 2015.The **government's liquidity stock is expected to decline moderately**. At the same time, **accelerating economic growth** will also contribute towards reducing the share of debt to GDP.

Figure 8: Contributions to y-o-y change in general government debt (% GDP)



Source: CBR, MF SR

At the end of 2013, the amount of debt exceeded the third limit laid down in the Fiscal Responsibility Act. This triggered new sanctions which should lead to debt stabilisation in the medium term (see Part 4.1 for more).

28 Based on a Eurostat decision, the sale of emergency oil reserves to the Emergency Oil Stocks Agency, which took place in 2013, increased the gross government debt by the amount of the transaction (€465.2m). The Ministry of Finance intends to adjust the modus operandi of the Agency in order to eliminate this negative impact on debt in 2014.

3. Evaluation of the likelihood of meeting the budgetary objectives

The proposed medium-term objectives for 2015-2017 are based on the macroeconomic assumptions approved by the Macroeconomic Forecasting Committee and on the forecast of revenues from taxes and social security contributions approved by the Tax Revenue Forecasting Committee. Given the initial phase of budget preparation, the Stability Programme provides only a limited overview and description of the measures designed to reach the objectives. This part of the evaluation focuses on the identification of risks arising from different-than-expected macroeconomic development, tax revenue forecasts, and the size and nature of measures.

3.1 Macroeconomic assumptions

The macroeconomic framework based on which the preparation of the budget for the next three years has begun[29] is based on the latest predictions of the Macroeconomic Forecasting Committee ("MFC") which its members in February 2014 classified as realistic. Given the fact that the forecasts were published three months ago, the following section evaluates their underlying assumptions in the light of actual developments in both domestic and international contexts.

Following a moderate increase in 2013 (0.9 %), the pace of economic growth in 2014 is expected to step up and reach 2.3 %. The acceleration is also confirmed by the Q4 figures for 2013 observing a growth of 1.5 % of GDP year-on-year. Gradual revival of domestic consumption, in combination with the rising global demand, create conditions for growth acceleration also in the years to come. Compared to the approved 2014-2016 budget, the expectations have changed only moderately (Table 6). While unemployment is likely to develop more positively than expected, the price growth will be lagging behind the original expectations quite substantially.

Tab 6: MFC macroeconomic forecasts

Indicator (in %)	Actual	Forecast (February 2014)				Change compared to September 2013 (2014-2016 Budget)			
	2013	2014	2015	2016	2017	2013	2014	2015	2016
GDP, real growth	0.9	2.3	3.0	3.2	3.4	0.1	0.1	0	0
Inflation, year average; CPI	1.4	0.8	2.1	2.3	2.4	-0.2	-0.9	0	0
Nominal wage, growth	2.4	2.5	3.5	4.1	4.5	-0.2	-0.2	0.1	0.6
Real wage, growth	1.0	1.7	1.5	1.8	2.1	0.1	0.6	0.2	0.6
Employment (ESA), growth	-0.8	0.3	0.6	0.7	0.9	0.2	0.1	0	0.1
Unemployment rate (ILO)	14.2	14.0	13.2	12.3	11.3	-0.3	-0.3	-0.3	-0.3
Private consumption, real growth	-0.1	1.2	2.2	2.4	2.9	-0.6	0.3	0.1	0.1
Investments, real growth	-4.3	1.8	2.4	0.8	2.1	1.5	-1.1	2.4	2.3
Export of goods and serv., real growth	4.5	4.0	4.5	4.8	4.8	-0.4	-0.3	0	-0.3

Source: NBS, SO SR, MF SR

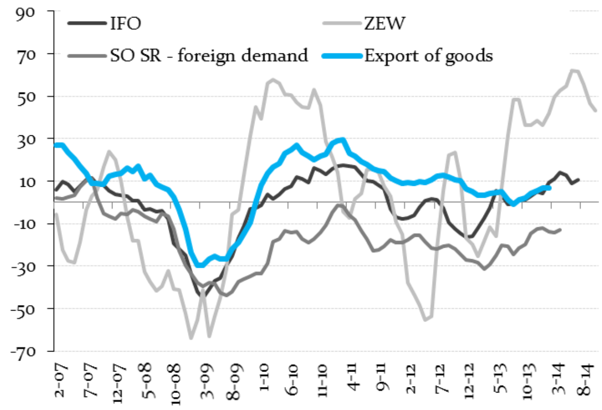
[29] The 2015-2017 budget proposal will be submitted to the Cabinet for discussion in August 2014 and will be based on the updated MFC macroeconomic forecasts of June 2014.

EU Member States will continue to implement their fiscal consolidation programmes, which will have negative ramifications for their economic growth. Nevertheless, with Greece and Portugal back on financial markets, the uncertainty connected with sovereign debt financing in the eurozone is ebbing[30]. Gradual implementation of the banking union project is bound to underpin the confidence of financial markets in the eurozone, however, in the interim, the sector remains uncertain, with negative ramifications for investments.

Compared with the original assumptions of the forecast, the inflation estimate for 2014 looks overrated, yet the tensions behind the EU's eastern border represents an additional upward risk (commodities – energy, foodstuffs)[31].

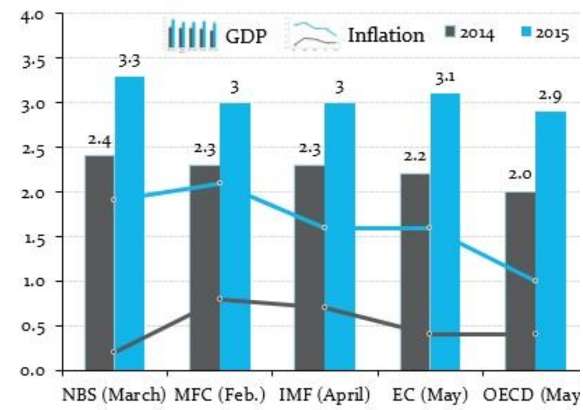
This year's acceleration of growth in the eurozone and the Czech Republic gives an additional impetus to the real economy, and export statistics indicate that Slovakia is maintaining its export markets also outside the EU. Exports in the first half of 2014 are likely to develop positively, although there is a degree of uncertainty because some of the leading indicators (ZEW) suggest that the trend may reverse later (Figure 9).

Figure 9: Slovak export leading indicators[32]



Source: ZEW, CESifo, SO SR, NBS

Figure 10: Latest inflation and economic growth forecasts



Source: IMF, EC, MF SR, NBS, OECD

MFC predictions published in February are very much in line with the latest predictions by international institutions (Figure 10) with **macroeconomic risks balanced both upwards and downwards.**

30 Slovakia's position on sovereign bond markets is momentarily favourable, however, nominal rates are expected to increase as the German Bund yields rise to long-term averages. Risk premia are declining under increased interest of non-residents (ARDAL, 2014), which, however, brings about negative risks of higher volatility under external shocks (Ebeke, Lu, 2014).

31 Energy prices have been the main reason behind stagnating inflation in the past 12 months.

32 IFO, ZEW – balance of future expectations (lead of 3 or 6 months), Statistical Office of the Slovak Republic – expected international demand in industry (balance, 3-month average), Export of goods – year-on-year growth at current prices (3-month average).

3.2 Forecast of revenues from taxes and social security contributions

The forecast of revenues from taxes and social contributions contained in the Stability Programme is based on the TRFC forecast published in February 2014. In comparison with the approved budget, the forecast is influenced by a better-than-expected development of the macroeconomic environment. In addition to the February forecast, it also reflects the new legislative measures with positive impact. However, these measures have not been yet approved by the Tax Revenue Forecasting Committee (except for changes in health-insurance premiums payable on dividends), nor have they been notified to the Committee.

In terms of the impact of macroeconomic assumptions, the downward revision of the deposit interest rate estimate, which undercut the revenue from withholding tax, influenced the update most adversely. Since 2016, the lower withholding tax revenue will be counterbalanced by a higher collection of income taxes and social security contributions as the wage base develops more positively.

There are three main reasons to forecast increased revenues beyond the framework of macroeconomic development and new legislation. In the category of excise taxes, the better-than-budgeted collection towards the end of 2013 led to the revision of forecast in the years to come. As far as the corporate income tax is concerned, based on the preliminary figures released by the statistical office, the forecast reflects a higher profitability of the corporate sector in 2013. The collection of VAT surpassed original expectations and hence the revenue forecast has been revised upwards throughout the budget period.

In comparison with the approved general government budget for 2014-2016, the following new legislative measures have been reflected:

- Sustained revenue and increased collection of VAT[33] from 2015 in the amount of +230 million EUR;
- Introduction of VAT cash registers in doctors' offices and other professions from 2015 in the amount of +70 million EUR;
- Changes in health insurance premiums payable from dividends (single annual settlement, common assessment base) from 2015 in the amount of –8 million EUR;
- Introduction of a withholding tax on in-kind benefits provided by pharmaceutical companies to doctors and income from the sale of scrap metal from 2015 in the amount of +5 million EUR;
- Introduction of a single annual settlement system for the Social Insurance Agency from 2016 in the amount of +60 million EUR.

Above the framework of the new legislation, the Ministry of Finance expects a one-off revenue in 2014 from a levy payable by market operators in regulated industries at +176 million EUR. This revenue is subject to implementing certain transactions and recognising it as government revenue under ESA95.

[33] For the purposes of this evaluation, the CBR assumes that the basic VAT rate will remain unchanged at 20 % from 2015, since the impact corresponds to the impact of this measure.

Tab 7: Taxes and SSC – to – GDP ratio development

	2012	2013 E	2014 B	2015 B	2016 B
1. Tax revenue – baseline scenario	**25.6**	**27.6**	**27.1**	**26.5**	**26.3**
2. New legislation (compared to 2013-2015 Budget)	0.0	0.0	0.2	0.5	0.4
- *of which: permanent measures*	0.0	0.0	0.0	**0.5**	**0.4**
- *of which: temporary measures* [1)]	0.0	0.0	**0.2**	0.0	0.0
3. Other one-off effects	0.0	0.0	0.0	0.0	0.0
TOTAL	**25.6**	**27.6**	**27.3**	**26.9**	**26.7**

1) One-off increase of temporary entrepreneurial levy in regulated industries (€ 176 million in 2014)

Source: CBR, MF SR

In comparison with the approved general government budget for 2014-2016, the overall **revenue from taxes and social security contributions is expected to increase**. The Tax Revenue Forecast, except for the legislative changes specified in the Stability Programme, was discussed by the Tax Revenue Forecasting Committee on 12 February 2014. The new measures need to be specified in a greater level of detail, including the proposed legislative wording, and submitted to the Tax Revenue Forecasting Committee for assessment.

3.3 Consolidation measures

In order to be credible, the budget strategy must be supported by specific measures, including changes in legislation, and the quantification of their likely impact on government revenues and expenditures. Since the medium-term budget outline is the first phase in the budgeting process, the government has not yet drawn up a list of all the measures necessary to meet the objectives. The impacts of the measures incorporated into the outline are quantified; in addition, the Stability Programme lists also other potential measures. As in the past, all the measures should be specified at the latest in the budget proposal to be submitted to the Parliament this autumn. However, for the sake of transparency, it would be desirable for the potential measures to be at least roughly quantified already in this phase of the budgeting process.

The overall need of these measures, compared to the no-policy-change scenario compiled by the Ministry of Finance, reaches 1.2 % of GDP in 2015 and increases to 2.5 % of GDP in 2017[34]. **The measures amounting from 0.9 % of GDP in 2015 to 1.7 % of GDP in 2017 are already reflected in the draft medium-term budget outline.** Some of these measures are specified in detail. They include revenue-side measures in the area of taxes and social security contributions and expenditure-side measures through cost saving under the ESO programme (for more information, see Box 2). The medium-term budget outline also includes measures, although without detailed specification, resulting from the slower indexation of certain expenditure items (mainly wages in public administration and capital expenditures) compared with the economic assumptions used in the NPC scenario.

34 These calculations do not reflect the potential impact of the measures necessary to meet the 2014 budgetary target. Provided that the measures adopted for 2014 have a permanent impact also in subsequent years, the need for the adoption of measures in 2015 to 2017 will decline.

The meeting of the 2015 budgetary objective will require, in addition to the already incorporated measures and other changes compared to the NPC scenario, the specification of additional measures amounting to **0.3 % of GDP**. Provided that they are of a permanent nature, the need for additional measures in 2016 represents **0.1 % of GDP**. Assuming that also these measures are structural, further measures worth **0.3 % of GDP** will need to be adopted in 2017.

Tab 8: Overall need for consolidation measures in 2015-2017

	2015O	2016O	2017O	2015O	2016O	2017 O
	€ million			% GDP		
1. Total measures needed	904	1 385	2 134	1.2	1.7	2.5
2. Measures incorporated in 2015-2017 Outline	686	1 072	1 507	0.9	1.3	1.7
a. Detailed measures	409	470	489	0.5	0.6	0.6
b. Other (particularly the impact of indexation in NPC scenario)	277	602	1 018	0.4	0.7	1.2
3. Measures beyond 2015-2017 Outline (1-2)	218	313	627	0.3	0.4	0.7
- annual change	-	94	314	-	0.1	0.3

Source: MF SR, CBR

According to the Stability Programme, other potential consolidation measures include changes in the real estate tax, namely the introduction of a minimum tax depending on the location and other characteristics of the real estate. The government will also consider changes in tax expenditures in the area of direct taxes.

Box 2: Proposed consolidation measures in 2015 – 2017

On the revenue side, the government expects to preserve the level of revenues and increase the collection of value added tax in 2015 to 2017. Another measure affecting medical doctors, the sectors of professional, scientific and technical activities, and the providers of accommodation services, is the obligation to use electronic VAT cash registers. These operators will have to append payment confirmations (cash register slip or electronic transfer confirmation) to the official documents issued by private persons (e.g., notaries, lawyers, medical doctors, experts). The withholding tax base will be expanded to include the income of healthcare providers from pecuniary and in-kind considerations provided by pharmaceutical companies and the income from the sale of scrap metal. The single annual settlement of social security contributions, introduced as of 2015, will also increase government revenues. The new system is expected to discourage transactions designed to optimise payers' liability through one-off bonuses exceeding the maximum assessment base in a given month. The measures on the revenue side should generate 303 to 383 million EUR throughout the budget outline period.

The entire **expenditure-side consolidation** is connected with the ESO programme, thanks to which the government will save more than EUR 100 million annually through reduced wage costs and intermediate consumption.

Tab 9: Proposal of consolidation measures in 2015-2017 (ESA95)*

	2015O	2016O	2017O	2015O	2016O	2017O
	€ million			% GDP		
Revenue	303	368	383	0.39	0.45	0.44
- same or higher VAT collection	227	236	248	0.29	0.29	0.29
- VAT cash registers (doctors, other professions)	71	71	71	0.09	0.09	0.08
- withholding tax – healthcare providers, scrap metal	5	5	5	0.01	0.01	0.01
- annual settlement of SSC	0	56	59	0.00	0.07	0.07
Expenditure	106	102	107	0.14	0.12	0.12
- savings on wages (ESO)	66	66	66	0.08	0.08	0.08
- savings on intermediate consumption (ESO)	40	36	41	0.05	0.04	0.05
Total measures	409	470	489	0.53	0.57	0.57

* Compared to NPC scenario based on the current estimate of GG balance in 2014 *Source: MF SR*

The table containing consolidation measures shows that the quantified consolidation reflected in the 2015-2017 budget outline (until additional specific measures are presented) is mostly concentrated on the revenue side of the budget.

The expenditures reflected in the medium-term budget outline, adjusted for those which are balance-neutral or do not relate to the present economic policy, are growing throughout the term of the budget (for more information, see Box 3). The growth is driven mainly by the expenditures incurred as a consequence of legislative requirements or economic development (social benefits, social insurance benefits, etc.). The operational expenditures of the state will be growing at a slower pace. On the other hand, the government's **capital expenditures will be declining throughout the period.** This effect is mainly due to the increased share of the EU funds planned for this category[35], as a consequence of which capital expenditures, adjusted for EU funds and co-financing, will be declining.

35 In 2014, EU funds represent 31 % of capital expenditures, growing further to 39 % in 2015, 49 % in 2016 and 57 % in 2017. The share of co-financing spans from 13 % to 15 % of the total. The share of own resources thus declines from 54 % in 2014 to 46 % in 2015, 38 % in 2016 and 29 % of planned capital expenditures in 2017.

Box 3: Structure and development of expenditures in the medium-term budget outline

A basic overview of development in the structure of general government expenditures can be obtained after their adjustment for those items that do not affect the balance or are not linked with the current economic policy. Such items may include:

- **Expenditures financed from EU funds** – they are balance neutral
- **National co–financing - the amount of expenditures is directly proportional to the EU funds drawn**
- **Payments to the EU budget – made in line with the agreed mechanism**
- **Debt interest payments – reflect the previous policy and conditions on financial markets which the government cannot significantly influence in a given year**
- **Insurance premiums paid by the state** – this item is also included on the revenue side in the same amount (net of premiums paid to the fully-funded pillar) and is not consolidated under the ESA95 methodology

The thus adjusted expenditures can be further categorised. The table below categorises current expenditures into those which are mandated by the applicable legislation (social benefits, social security payments, ...) and those which can be affected by government decisions (wages, goods and services, subsidies, other current transfers). Capital expenditures constitute a separate category.

Tab 10: Structure of general government expenditures (ESA95, € million)

	2014	2015	2016	2017
Total expenditures	28 310	28 404	28 537	29 347
- EU Expenditures	1 388	1 365	1 090	1 390
- Co-financing	640	586	426	480
- Interest paid	1 367	1 366	1 476	1 494
- Social contr. on behalf of certain groups	1 477	1 458	1 490	1 542
- Transfers to the EU budget	671	658	731	690
Adjusted expenditures	22 767	22 971	23 324	23 751
annual change (%)		0.9	1.5	1.8
of which: mandatory	9 840	9 866	10 051	10 087
annual change (%)		0.3	1.9	0.4
of which: facultative	11 911	12 137	12 614	13 097
annual change (%)		1.9	3.9	3.8
of which: capital	1 015	967	659	567
annual change (%)		-4.8	-31.8	-14.1

Source: MF SR, CBR

A detailed overview of all general government expenditures, including their categorisation, is provided in Annex 3.

A glance at the structure of expenditures indicates that unless additional cuts in connection with the ESO programme are made in line with the government's intentions, significant savings can only be achieved through changes in the legislation governing welfare benefits, social security benefits and health care provision. An alternative to cutting expenditure is to look for additional sources on the revenue side of the budget which the government intends to generate through the adoption of new measures. Similarly as in the approved budget for 2013-2015, also the present budget proposal assumes a decline in investments funded from national sources (non-EU funds). **By 2017, their amount is expected to decline by 44 % compared to 2014[36].**

3.4 Risks to meeting the medium-term objectives

As of yet, the measures designed to reach the medium-term objectives have not been sufficiently specified. These measures will be introduced at the latest in the budget proposal submitted to the Parliament. The CBR will publish (in November) its second evaluation report scrutinising the 2015-2017 General Government Budget Proposal as approved by the Cabinet.

The risks to meeting the MTOs will largely depend on the development in 2014. At this stage, the CBR has identified the following medium-term risks:

- After having taken into account the latest available information, the overall perspective on the economic development forecasts does not change considerably compared to the assumptions used in the medium-term budget outline and in the Stability Programme, **the risks – in comparison with the situation before the adoption of the 2014-2016 budget – are balanced.**

- The **revenue from corporate income tax for 2013,** to be revised in June when the missing data become available, represents an uncertainty in the Tax Revenue Forecast. The deviation in estimates automatically spills over to the following years of the forecast. The new measures in the area of taxation have been quantified only indicatively and have not yet been discussed in Tax Revenue Forecasting Committee.

- Given the existing risks in 2014 (overrun of current expenditures), **the budgets of municipalities and self-governing regions** also represent a risk to meeting the medium-term budgetary objectives. This risk may be partly attenuated by the obligation under the Fiscal Responsibility Act for municipalities and self-governing regions to adopt their 2015 budgets with expenditures not exceeding the 2014 level (for more information, see Part 4.1).

- In the **healthcare sector,** the government is considering taking over liabilities of hospitals worth EUR 50 million in 2015. In view of the actual development in 2013 and given the persisting risks and the absence of measures, this amount may not suffice.

- The **financial corrections to the projects financed from EU funds,** which may have a negative impact in 2015, represent another risk. These corrections come as

[36] Both the budget itself and the medium-term budget outline assume growing expenditures covered from EU funds, which mitigates the decline in the overall decline of capital expenditures in general government.

a consequence of decisions taken in 2013 and we can assume that EU funds will be drawn also in 2014 and 2015 in respect of the projects affected by financial corrections.

- Similarly as in 2014, the **revenues from SPP dividends** planned for 2015 and 2016 represent a risk. Also in these two years the plan is to pay out dividends from the total profit of SPP subsidiaries in which, however, the state controls only 51 %.

- The prepared **change in the methodology of reporting (transition to ESA2010)** may negatively affect balances in individual years which, unless the budgetary targets are adjusted, may require the adoption of additional measures.

- The **sanctions applicable under the Fiscal Responsibility Act** constitute a positive risk. The freeze on general government expenditures at the 2014 budget level may significantly contribute towards reaching the budgetary objectives.

4. Evaluation of the budget in terms of fiscal rules

Apart from respecting domestic fiscal rules, the preparation of Slovakia's general government budget must also respect the budgetary restrictions applicable to eurozone members. The most important domestic piece of legislation is **Constitutional Act No. 493/2011 on Fiscal Responsibility** and the amended Budgetary Rules Act, which implements the fiscal rule of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (the Fiscal Compact is a part of the Treaty) into the national legislation. At the EU level, compliance with the requirements of the **Stability and Growth Pact** (and related regulations) is of particular importance.

4.1 National fiscal rules

The Fiscal Responsibility Act defines the domestic fiscal responsibility rules. The most important provision sets out the **general government debt limit**. Although the upper debt limit is 60 % of GDP, the sanction brackets are activated as soon as the debt exceeds 50 % of GDP. Apart from the "debt brake" the Act contains specific provisions applicable to municipalities and self-governing regions, which will enter into force as of 1 January 2015, and also foresees a public expenditure ceiling to be defined at a later stage.

In 2013, general government debt reached 55.4 % of GDP, **trespassing the third debt limit**, which carries the following sanctions:

- The Ministry of Finance is obliged to block 3 % of defined government expenditures. The blockage applies to the cash expenditures of the state budget approved by the 2014 State Budget Act[37], excluding expenditures for government debt service, EU funds, national funds earmarked for the financing of joint EU projects, transfers to the EU budget, transfers to the Social Insurance Agency and expenditures to remedy damages caused by natural disasters. Specifically, the blockage affects expenditures worth EUR 305 million (calculation is presented in Annex 4). Given the existing derogations, the blockage will take effect as of 16 May 2014[38].

  The impact of the blockage on government balance may be different also in relation to the way in which reserves are budgeted. If a reserve is budgeted within the existing revenue framework a large part of which is subject to approval by the Tax Revenue Forecasting Committee, its budgeting fulfils two functions. On the one hand, the reserve covers unforeseen negative risks which may occur during the budgeted period. On the other hand, it facilitates compliance with those sanctions of the Act which oblige the

37 Act No. 473/2013 on 2014 State Budget.

38 According to the Fiscal Responsibility Act, the blockage should take effect as of the first calendar month following the debt publication, i.e., as of May 2014. At the same time, however, the transitional period of 24 months from the approval by the parliament of the government's manifesto and the vote of confidence is still running; during this period, the sanctions for transgressing the 55-% debt limit do not apply. The parliament approved the government's manifesto and voted confidence in the government on 15 May 2012, which means that the sanction becomes applicable as of 16 May 2014.

government to block expenditures, because the government, already in the budgeting process, had knowingly restricted its expenditures by the amount of the reserve created. However, if a reserve is created to revenues which, at the time of budgeting, cannot be assessed as realistic and the actual development during the year does not confirm them as being realistic, the reserve fails to fulfil either of the two purposes. It artificially inflates the base for the calculation of sanctions under the Act, which does not really sanction or force the government into adopting additional measures. The budgeting of such reserves ultimately undermines the effectiveness of fiscal rules[39] and reduces the transparency[40] of budgeting.

- The reserve fund of the prime minister and the reserve fund of the government are also blocked for spending. This sanction applies as of the same date as the blockage of expenditures and may save up to EUR 3 million[41]. Since these funds are part of state budget expenditures and represent a potential source for blockage, they do not necessarily have to lead to additional savings (in addition to those expenditures that are blocked).

- The Government may not submit to the Parliament its 2015-2017 budget proposal which would entail a year-on-year nominal increase in consolidated expenditures of general government compared to the 2014 budget, except for expenditures on debt servicing, EU funds, national funds earmarked for the financing of joint EU projects, transfers to the EU budget and expenditures to remedy damages caused by natural disasters. This means that the adjusted expenditures of the general government budget in 2015 to 2017 should not exceed EUR 24,177 million. If this expenditure ceiling is respected, the share of expenditures in GDP would fall from 37.7 % of GDP in 2014 to 32.7 % of GDP in 2017.

  The Stability Programme did not reflect this requirement in the 2015-2017 government expenditures which in fact exceed the 2014 level. In order words, compliance with the expenditure ceiling will require additional consolidation measures on the expenditure side in the amount of 0.4 to 1.3 % of GDP. Such an adjustment would go beyond the size of the measures needed to meet the targets quantified in the Stability Programme, which would substantially eliminate identified risks and help the government to meet the fiscal objectives.

- Municipalities and self-governing regions are obliged to adopt their 2015 budgets with expenditures not exceeding the 2014 budget level, except for expenditures to remedy the consequences of damages caused by natural disasters and expenditures for co-financing. The freeze on local government expenditures for 2015 is likely to reduce the need to cut

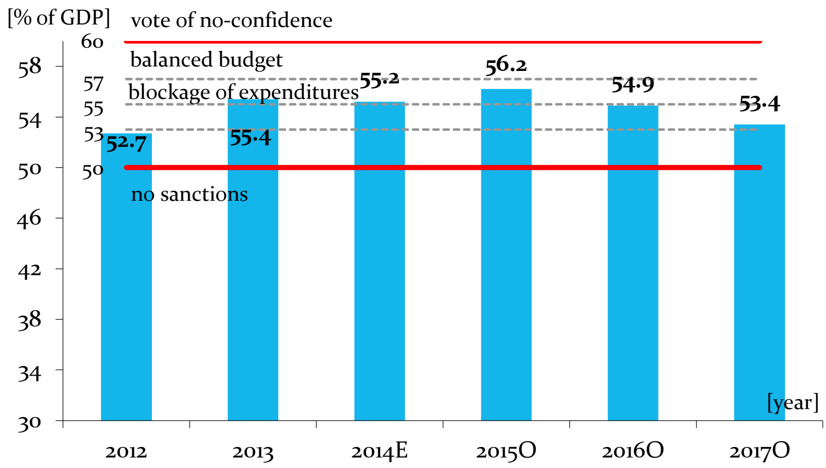
39 This applies not only to the rules of the Fiscal Responsibility Act, but also to the rule of 1-percent increase in state budget expenditures if covered by revenues. More in Box 8 of the CBR's document: Evaluation of the General Government Budget Proposal for 2014-2016.
40 For example, in relation to the obligation to use the tax forecasts approved by Tax Revenue Forecasting Committee.
41 The amount of savings is calculated based on the balance in the two reserve funds as of 30 April 2014 (Annex 4). Since expenditures from these reserve funds may be incurred until 15 May 2014, the amount may be lower.

the expenditures of other government entities in order to ensure that the expenditures of the general government sector as a whole do not increase.

- Moreover, similarly to what happens when the 53-percent debt limit is exceeded, the Government will submit to the Parliament a proposal for debt-reduction measures and, at the same time, reduce the salaries of cabinet members to the 2013 level.

Provided that the budgetary objectives are met, the debt forecast for 2014 to 2015 spans from 55 to 57 % of GDP. In the two subsequent years, the debt should fall to 53-55 % of GDP. **Should the outlined budget scenario materialise, the sanctions described above will be invoked again in 2015 and 2016** (except for blocking 3 % of state-budget expenditures, because the blockage applies only in the first year when the 55-% limit is exceeded). The prepared change in the Eurostat methodology (ESA 2010) may also affect the debt negatively, particularly as a consequence of sectoral reclassification of non-financial entities.

Figure 11: Debt forecast and debt brake limits (% of GDP)



Source: CBR

A new fiscal rule entered into force as of 1 January 2014. An amendment to the Budgetary Rules Act[42] implemented a part of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (the **Fiscal Compact** is a part of the Treaty) into the national legislation.

It is a structural balance rule, through which public finances should reach their medium-term budgetary objective. The rule also contains a correction mechanism which is triggered if a significant deviation from the planned adjustment path toward meeting the MTO occurs, unless caused by exceptional circumstances[43] (for example, a severe economic downturn). The Act obligates the Ministry of Finance to publish, each year by 30 June and 30 November, whether,

[42] §30a of Act No. 523/2004 on the General Government Budgetary Rules

[43] The beginning and end of the duration of extraordinary events is declared by the Cabinet at the proposal of the Ministry of Finance; before the Cabinet issues such declaration, the proposal is assessed by the Council for Budget Responsibility.

based on the data notified by Eurostat, a significant deviation has occurred. If such deviation is identified, the Ministry will propose to the Government correction measures (in the form of expenditure ceilings). The role of the CBR will then be to assess such proposal. In reaction to the opinion of the Ministry of Finance, the CBR will prepare its evaluation of compliance with this rule for the year 2013.

Even though the compliance with the fiscal compact rules is evaluated only once actual figures become available, the assessment of planned figures in the light of these rules suitably complements the analysis of the government's fiscal objectives. Based on the latest estimates, the CBR expects the structural balance to deteriorate by 0.8 % of GDP in 2014 (Ministry of Finance expects deterioration by 0.3 % of GDP). The meeting of the budgetary objective may change this value, however, the deviation from the Fiscal Compact requirements will most likely be significant[44], necessitating the adoption of correction measures.

Provided that the budgetary objectives are met through measures of a permanent nature, the fiscal restriction in 2015- 017 will have to be fairly tight, at about 1 % of GDP annually, which is in line with the requirements of the Fiscal Compact.

4.2 EU fiscal rules

In relation to the rules of the Stability and Growth Pact, the main commitment of Slovakia in 2013 and 2014 **has been to reduce and keep the deficit of public finances below 3 %of GDP, paving way for abrogation of the excessive deficit procedure**. The 2013 deficit reached 2.8 % of GDP and the latest Commission forecast[45] assumes that it will remain under 3 % of GDP also in 2014 and 2015. Slovakia also meets the debt-to-GDP reference value set at 60 % of GDP. Based on these figures, the excessive deficit procedure in respect of Slovakia is expected to be abrogated.

The abrogation of the excessive deficit procedure would also mean that Slovakia's public finances will be subject to the preventive arm of the Stability and Growth Pact. The basic precondition is to meet the **medium-term budgetary objective (MTO), expressed as structural deficit, in the amount of 0.5 % of GDP**. In line with CBR recommendations and the government plan presented in the Stability Programme, Slovakia should meet this objective **in the year 2017**. The SGP rules set the pace of adjustment towards meeting the MTO at 0.5 % GDP annually; the pace may be faster in better economic times and slower in times of downturn.

[44] According to the rules of the Stability and Growth Pact, a significant deviation is a deviation by 0.5 % of GDP (or higher) from the recommended structural balance change which for a country under the preventive arm of the Pact not meeting the medium-term budgetary objective, with debt below 60 % of GDP and output gap between -1,5 and 1,5 % of potential GDP, represents 0.5 % of GDP annually. It means that any negative change in structural balance would meet the criterion of significant deviation.

[45] Spring Forecast of the European Commission of 5 May 2014 features a deficit of 2.9 % of GDP in 2014 and 2.8 % of GDP in 2015.

In connection with the consolidation requirements under the Preventive Arm of the Stability and Growth Pact, the Commission has recently introduced so-called "investment clause" that allows temporary deviations for Member States from the adjustment path towards their medium-term objectives (MTOs) amidst the ongoing economic crisis. The clause should apply to expenditures that foster sustainable economic growth. The government intends to invoke the investment clause in connection with the planned relaxation of fiscal discipline in 2014 when structural deficit is expected to deteriorate. The Commission will assess the application of the clause after the end of 2014, however, only if the EDP in respect of Slovakia is indeed abrogated[46].

The CBR does not quantify the change in structural balance strictly according to the methodology defined in the Stability and Growth Pact. For this reason, the CBR does not evaluate the government's budgetary objectives in terms of their compliance with EU fiscal rules. Nevertheless, it may be concluded that the reduction of government deficit in 2013 has brought structural balance closer to the MTO, yet the reaching of this objective will require that the consolidation of public finances continue also in the years to come.

[46] More in Box 5: Application of the Investment Clause in the CBR's document: Evaluation of the General Government Budget Proposal for 2014-2016.

Annex 1 – Fiscal performance of local governments in 2014

The Council for Budget Responsibility, as part of risk identification, has assessed the fiscal performance of local governments as risky, with potential negative impact on general government balance in 2014. Decree of the Ministry of Finance No. MF/21513/2012-31, which entered into force in 2012, changed the methodology for the reporting[47] of certain transactions of municipalities and self-governing regions which used to be recorded in extra-budgetary accounts in the past. This method of recording has a number of negative effects for the evaluation of 2012 and 2013: 1) the annual comparison of performance of municipalities and self-governing regions is distorted because these revenues and expenditures were neither reported nor budgeted in the past (MoF is not budgeting them for 2014, either); 2) at the same time, duplicities may occur in the recording of certain transactions (recording in Parts I and III) without the possibility of effective control. In 2012, the amount of the balance of municipalities and self-governing regions in Part III of the State Treasury reporting form was EUR 3.1 million; in 2013, the balance declined to -1.6 million. In terms of the overall impact on the balance of local governments the amount is relatively low. For this reason, the **CBR has quantified the risk only for the transactions budgeted by the Ministry of Finance.**

The following table illustrates the actual development of selected revenue and expenditure categories in 2009 to 2013[48]; the years 2014 to 2016 represent the budget of municipalities and self-governing regions as approved by the Parliament in December 2013.

Tab 11: Selected budgetary items of municipalities in 2009-2016

(ths €)	2009	2010	2011	2012*	2013*	2014B	2015B	2016B	2014 CBR	risk
nontax revenues	414 260	439 305	411 852	415 416	434 354	478 000	473 000	480 000	454 155	-23 845
grants and transfers	1 148 097	1 425 801	1 453 242	1 309 531	1 256 826	1 097 911	1 059 924	822 500		
gross wages	1 209 227	1 247 587	1 278 602	1 307 153	1 372 623	1 275 821	1 275 821	1 275 821	1 372 623	96 802
goods and services	948 484	946 540	940 606	946 193	947 768	874 228	901 632	916 233	947 768	73 540
subsidies and transfers	360 296	361 199	354 451	371 871	390 287	375 791	383 307	390 973		
capital spending	860 169	1 105 384	861 541	665 802	576 384	750 578	553 149	508 882		
(growth in %)	2009	2010	2011	2012*	2013*	2014R	2015R	2016R		
nontax revenues	-30.3	6.0	-6.2	0.9	4.6	10.0	-1.0	1.5		
grants and transfers	20.2	24.2	1.9	-9.9	-4.0	-12.6	-3.5	-22.4		
gross wages	7.0	3.2	2.5	2.2	5.0	-7.1	0.0	0.0		
goods and services	4.4	-0.2	-0.6	0.6	0.2	-7.8	3.1	1.6		
subsidies and transfers	5.3	0.3	-1.9	4.9	5.0	-3.7	2.0	2.0		
capital spending	12.4	28.5	-22.1	-22.7	-13.4	30.2	-26.3	-8.0		
Estimated risk of municipalities for 2014										**194 188**

*only part I FIN 1-12 is included

Source: CBR

47 Under this Decree, municipalities and self-governing regions record their business activities in a "special" reporting form (Part III of the State Treasury reporting form FIN1-12).

48 The years 2012 and 2013 contain only revenues from Part I of the State Treasury reporting form.

Based on the development in recent years and, in particular, based on the actual figures for 2013, the CBR considers the budgeted amount of non-tax revenues of municipalities for 2014 as overrated and the growth at the level of 10% as not very likely[49]. Similarly, the CBR does not expect the saving in compensations and purchases of municipalities in 2014 to reach the budgeted amount; the upcoming local government elections slated for June 2014 should also be taken into account. Due to this, the CBR expects that these expenditure items will reach the levels comparable with the year 2013. The decline in current transfers and, partly, also purchases of goods and services by municipalities, will probably reflect the expected reduction in received grants and transfers. **The CBR has quantified the risk for the balance of municipalities at EUR 194.2 million.**

Tab 12: Selected budgetary items of self-governing regions in 2009-2016

(ths €)	2009	2010	2011	2012*	2013*	2014B	2015B	2016B	2014 CBR	risk
nontax revenues	71 537	71 206	78 793	84 010	87 914	84 000	85 000	87 000		
grants and transfers	433 627	506 909	485 977	481 147	478 155	416 885	409 481	404 384		
gross wages	346 818	344 897	340 667	344 756	357 721	334 222	334 222	334 222	344 285	10 063
goods and services	223 306	204 662	210 422	208 067	205 910	201 226	201 346	210 351	205 910	4 684
subsidies and transfers	388 843	387 654	409 408	421 090	409 679	403 316	407 382	419 610		
capital spending	158 886	108 881	122 376	134 336	106 907	111 400	136 570	122 656		
(growth in %)	2009	2010	2011	2012*	2013*	2014R	2015R	2016R		
nontax revenues	-24.6	-0.5	10.7	6.6	4.6	-4.5	1.2	2.4		
grants and transfers	10.6	16.9	-4.1	-1.0	-0.6	-12.8	-1.8	-1.2		
gross wages	6.2	-0.6	-1.2	1.2	3.8	-6.6	0.0	0.0		
goods and services	-2.1	-8.3	2.8	-1.1	-1.0	-2.3	0.1	4.5		
subsidies and transfers	10.8	-0.3	5.6	2.9	-2.7	-1.6	1.0	3.0		
capital spending	-19.0	-31.5	12.4	9.8	-20.4	4.2	22.6	-10.2		
Estimated risk of self-governing regions for 2014										**14 747**

*only part I FIN 1-12 is included

Source: CBR

In the case of the self-governing regions, the CBR has reduced its estimate for saving in compensations of employees; the CBR's estimate for 2014 reflects the average development of this item during 2009-2012, since 2013 was the year of regional elections, so the disbursement of compensations could have been higher. The CBR is also expecting a slightly higher risk related to current expenditures, namely at the 2013 level. **The risk for the self-governing regions has been quantified at EUR 14.7 million.**

The CBR has quantified the risk of an overrun in the current expenditures of municipalities and self-governing regions in 2014 at EUR 208.9 million. The increase in current expenditures may be partly offset by cuts in capital expenditures. However, given their low level in 2013 (deferred investments) and this year's communal elections, the room for offsetting will be narrower and may reach, according to CBR estimates, up to EUR 100 million. **On the whole, the negative risk to the 2014 local government balance spans from 100 to 200 million EUR.**

[49] The CBR has adopted a conservative assumption whereby the 2014 increase in non-tax revenues will not exceed the 2013 rate of increase.

Annex 2 – List of one-off measures

This part describes the one-off measures which are taken into account calculating the general government's structural balance. The following Box contains 10 principles which the CBR considers in assessing the one-off measures[50].

Box 4: 10 principles of one-off measures according to CBR definition

The CBR assesses one-off measures particularly in the context of their impact on net worth (in contrast, the Commission takes into account the impact of measures on the medium-term fiscal position). According to the CBR, it is essential that the identification of one-off measures is made in a transparent and consistent manner in time. For this reason, the CBR has defined a set of rules facilitating clearer categorisation of these measures into one-off and temporary.

1. **Time horizon** – measures applicable in the medium term.
2. **Transaction value** – account will be typically taken of the measures which, in at least one year, exceed 0.05 % of GDP .
3. **Type/nature of transaction** – changes in the government balance, such as the sale of assets, revaluation of assets, workout of historical debts, remission of debts.
4. **Sign of budgetary impact** – deficit-improving impacts will be scrutinized more rigorously.
5. **Consistency in time** – several transactions relating to the same event should be recorded consistently in time.
6. **Legal power** – measures defined in constitutional acts will be considered as more permanent than measures defined in ordinary acts of parliament (adopted by a simple majority) or subordinate legislation.
7. **Implicit and contingent liabilities** – measures which change the present balance, but have no impact on long-term sustainability.
8. **Capital expenditures** – considered permanent.
9. **Accrual treatment** (period of transaction) – recording in time is more important than cash payment.
10. **Political risk** – shifts of impacts across political cycles.

1. **Possibility opt–out from the fully-funded pillar of the pension system**[51] – In response to the changes made in the fully-funded pillar at the turn of 2012 and 2013 (effective from 1 September 2012 until 31 November 2013), the government temporarily 'opened' the fully-funded pillar of the pension system allowing citizens to either exit or enter the scheme. The total effect in 2013 represented EUR 239.7 million.

   Reflected principles: 1, 7
   In the case of the opening of the fully-funded pillar of the pension system, this measure does not have impact on the long-term sustainability of public finances because the higher revenues at present will be counterbalanced by higher expenditures in the future. The present government balance (through the revenues of the Social Insurance Agency) is influenced positively. The expenditures related to population ageing represent implicit liabilities for the government and the change has had a significant impact on the balance in the order of

[50] For details, please consult the CBR's document "The 'True' Deficit".
[51] Under the new ESA2010 methodology, revenues from the transfers of pension liabilities will not have impact on the government balance.

0.3 % GDP. For similar reasons, this transaction will no longer be considered, pursuant to ESA2010, as a revenue for public finances.

2. **Temporary levy on business operations in regulated sectors** – Effective from 1 October 2012, a levy on business operations in regulated sectors was introduced as one of the consolidation measures designed to reach the fiscal objectives. It applies to companies with revenues from regulated activities accounting for least 50% of their overall revenues and with profits in excess of EUR 3 million. The measure is effective in the 2012-2016 period. Its impact in 2013 was EUR 75.0 million. In 2014, the revenue from the levy is exceptionally increased by the amount of EUR 176 million from the *SPP* company. The positive impact of this measure in 2015 and 2016 is estimated at about EUR 90 million.

   Reflected principles: 1, 2
   The originally adopted legislation limited the applicability of this measure only to 2012-2013, but the 2014-2016 general government budget proposal extended it through 2016.

3. **Taxation of retained profits from before 2004** – The effect of the one-off withholding tax on retained profits from before 2004 (at the rate of 15 %) only applies to the 2013 tax period. This measure will yield about EUR 4.0 million in 2013 and about EUR 5.2 million in 2014.

   Reflected principles: 1, 3
   Since this is clear one-off measure laid down in the law, the CBR takes it into account despite its relatively low yield.

4. **Extended bank levy** – As of 1 January 2012 the government introduce a levy on selected financial institutions in the amount of 0.4 % of liabilities, net of equity and deposits covered by the Deposit Protection Scheme. As of 1 September 2012, the levy calculation base was extended to also include the value of protected deposits, which were initially exempt. Depending on the aggregate amount of the levy collected and the total assets of the banking sector, the bank levy rate could even drop to zero. In 2013, the levy increased revenues by EUR 157.1 million. Its positive contribution to the government balance in 2014 is expected to reach EUR 126 million, and then the revenue will be gradually falling to reach about EUR 50 million in 2017.

   Reflected principles: 1, 2, 7
   The bank levy, and the associated government revenue, is classified as a revenue of State Financial Assets and recorded on a separate extra-budgetary account. The revenue is specifically bound to cover the costs associated with the consequences of financial crises and stabilisation of the banking sector. For this reason, the bank levy can be considered a one-off measure; in substance, it is a contingent liability which will be paid in the future should need arise. Moreover, once the set amount of assets in the sector is attained, the rate of levy is reduced to zero and thus the revenue is temporary.

5. **VAT receipt from a PPP project** – In 2011, the imputation of a claim towards the *Granvia* company as a consequence of VAT payment in connection with a PPP project for the R1 motorway in the amount of EUR 174 million had a positive effect on the deficit. In the next

30 years, the balance of the advance payment will be reduced every year by an aliquot portion amounting to EUR 5.79 million. This amount will have a negative effect on the general government budget during the 30-year period.

Reflected principle: 5
In 2011 and 2012, the investor paid VAT (on completion of the R1 motorway sections), which caused an increase in tax revenues. This income is considered as a one-off revenue. The payment of VAT by the government will be evenly recorded throughout the period of concession, together with the availability payments made by the state. Hence the impact of this measure is neutral throughout the entire period.

6. **JAVYS** – In the 2014-2016 general government budget the CBR has identified, among the revenues of the National Nuclear Fund, a one-off contribution from *JAVYS, a.s.* in 2013 in the amount of EUR 30 million.

   Reflected principles: 1, 3
   This is a one-off contribution which is unlikely to recur (time horizon).

7. **Loan instalment paid by *Cargo, a.s.*** – On 4 March 2009, the government approved the use of state financial assets for the provision of a loan to Cargo Slovakia a.s. in the amount of EUR 166 million. Under a contract with the Ministry of Finance and the Ministry of Transport, Post and Telecommunications, Cargo used the loan to finance its payroll and personnel expenditures, charges for the use of the railway infrastructure, and its own financial expenses. The payment of interest was set to begin in 2009, the payment of the principal in 2011, and the entire loan matures in 2020. In 2013, the instalment represented EUR 19.5 million.

8. **Loan instalment paid by *Vodohospodárska výstavba, š.p.*** - In 2002 and 2006, the state provided to *Vodohospodárska výstavba, š.p.* two loans which, due to the anticipated inability of the recipient to pay them back, were classified as capital transfer. The moneys were intended to restructure the debts of *Vodohospodárska výstavba* (VVB), š.p., Bratislava. EUR 160 million was repaid by 2011 and the remaining debt amounting to EUR 105 million is expected to be repaid in the following years, with the last instalment scheduled for 2015. In 2013, the company paid EUR 30.3 million.

   Reflected principle: 5
   The provision of loans to companies VVB and Cargo and their subsequent reclassification into capital transfer had a one-off negative impact on the balance and debt of general government debt (in 2002 and 2006 in the case of VVB, and in 2009 in the case of Cargo). The fact that these companies are repaying their debts has a positive impact on the balance (under the ESA95 methodology). In both cases, these transactions are recorded as one-off transactions.

9. **Financial corrections to EU funds** – These are moneys which the Slovak Republic must return to the EU budget due to the irregularities identified in the use of EU funds by general government entities. On the whole, these financial corrections are expected to have a negative impact on the balance in the amount of EUR 257 million in 2013-2015. In 2013 alone, financial corrections to EU funds reached EUR 124.5 million.

Reflected principles: 1, 2
Financial corrections to EU funds occur every year, but the present corrections are likely to have a significant impact on the government balance, which will be probably spread over three years. Moreover, corrections are imposed in reaction to concrete irregularities which are unlikely to be repeated soon.

10. **Recording of hospital debts** – In 2011-2012, the deficits of general government subsumed higher debts of hospitals than the hospitals themselves reported, which deteriorated general government balances in both 2011 and 2012. On the other hand, the 2013 government balance was, for this reason, "improved" for the incorrectly recorded amount of the debts incurred by hospitals in the amount of EUR 93.8 million. The CBR considers the recording in time, which assigns the debt to the period when it was incurred, as having a one-off impact.

Reflected principles: 2, 9
The recording of the debt in time meets the principle of proper accrual accounting.

Tab 13: Impact of takeover of debt of healthcare facilities on the GG deficit (€ million)

	2011	2012	2013
1. liabilities included in the debt according to ESA95 (impact on deficit)	100.1	130.0	18.5
2. liabilities recorded by Ministry of Healthcare (impact on deficit)	67.2	69.2	112.3
3. difference in liabilities (one-offs) (1-2)	**-33.0**	**-60.8**	**93.8**

Source: MF SR

11. **Refund of EU finds in the transport sector** – In the past, these projects were financed from national resources. In line with the EU rules, the projects were then reclassified as EU-funded projects, as a consequence of which the EU reimbursed, in 2014, the actually incurred expenditures in the amount of EUR 50 million.

Reflected principle: 1
The refund is linked to concrete projects from the past, hence it is a one-off income which will not recur.

12. **Digital dividend** – The sale of frequency bands through auction, the so-called digital dividend, had a one-off positive impact on non-tax revenues in the amount of EUR 163.9 million in 2014.

Reflected principles: 1, 2, 3
This is a one-off receipt from the sale of assets (nature of transaction) which will not recur.

13. **Transfer of funds resulting from the cancellation of bearer deposits** - In 2006, bearer deposits were cancelled and subsequently transferred under the management of State Financial Assets. The deposit claims expired at the end of 2013, which is expected to bring EUR 26 million in revenues in 2014.

Reflected principles: 1, 3

Similarly as the taxation of retained profits, this is one-off measure laid down in the law and the CBR takes it into account despite its relatively low yield.

14. **Revenues from the sale of state property (assets)** - As part of the second stage of the ESO reform focusing, in particular, on streamlining the system of public administration, one-off revenues totalling EUR 54 million should be cashed in from the sale of redundant state assets in 2014.

    Reflected principles: 1, 3
    This is a one-off receipt from the sale of assets (nature of transaction) which will not recur.

15. **Fine imposed by the Antimonopoly Office** - In October 2006, the Antimonopoly Office ruled that the companies of Strabag a.s., Doprastav, a.s., BETAMONT s.r.o, Inžinierske stavby, a.s., Skanska DS a.s., and Mota – Engil, Engenharia e Construcao, S.A. concluded a carter agreement in conflict with the provisions of the Antimonopoly Act and the Treaty on the Functioning of the European Union . The cartel agreement concerned a public tender for the construction of the first section of the D1 motorways (Mengusovce – Jánovce). The Supreme Court of the Slovak Republic confirmed the legality of the fine in the amount of EUR 44.8 million on 30 December 2013. The fine will increase the 2014 non-tax revenues.

    Reflected principles: 1,2
    This is a significant one-off revenue which will not recur in the future (time perspective).

16. **Dividends**[52] – These are one-off transfers of revenues from dividends unrelated to the respective fiscal year, and/or special agreements on the payout of dividends between the state and other shareholders which do not have to be recognised under the ESA95 methodology.

    The proposed MTOs of the general government budget are still based on revenues from dividends from the *SPP* company which correspond to a 100-% government stake in *SPP* subsidiaries. However, the CBR takes into consideration only the payout of dividends from ordinary activities in the current year, corresponding to a 49-% state ownership. It considers all additional revenues (for example, from retained profits from previous years) as one-off revenues.

Tab 14: One-off dividends of SPP

	(mill. €)	2014	2015	2016
1	GGP 2014-2016	370*	300	300
2	51 % share (ordinary dividends)	189	153	153
	one - offs (1-2)	**181**	**147**	**147**

**General government budget proposal for 2014-2016 originally expected dividends in the amount of € 735 million. of which dividend transfer was estimated by € 365 million, however this transaction is already incorporated in actual 2014 deficit estimate .*

Source: CBR

[52] More detailed description can be found in Annex 6 of the CBR's document Evaluation of the General Government Budget Proposal for 2014-2016.

Along similar lines, the CBR also identified one-off dividends from *Slovak Telecom* in 2014 and 2015, however, their impact is negligible. In aggregate, the dividends will increase the government's non-tax revenues by EUR 185 million in 2014, EUR 150 million in 2015, and EUR 147 million in 2016.

Reflected principles: 1, 2, 9
This is a one-off revenue with significant impact on deficit, where accrual recording is of essence.

Tab 15: One-off measures in 2013-2017 (ESA95, % GDP)

	2013	2014	2015	2016	2017
exit from the fully-funded pension pillar	0.3	-	-	-	-
VAT revenue/payment from a PPP project (Granvia)	0.0	0.0	0.0	0.0	0.0
accrualisation of hospitals´ liabilities	0.1	-	-	-	-
temporary entrepreneurial levy in regul. industries (incl. CIT)	0.1	0.3	0.1	0.1	0.0
taxation of retained earnings before 2004	0.0	0.0	-	-	-
digital dividend (transfer from 2012)	-	0.2	-	-	-
special levy in the banking sector (incl. CIT)	0.2	0.2	0.1	0.1	0.1
cancelled "bearer" deposits	-	0.0	-	-	-
dividends	0.0	0.2	0.2	0.2	0.0
revenues from sales of state property (ESO)	-	0.1	-	-	-
JAVYS (voluntary grant)	0.0	-	-	-	-
reimbursement of EU sources in transport sector	-	0.1	-	-	-
EU corrections	-0.2	-	-	-	-
Penalty of the Antimonopoly Office of the Slovak Republic	-	0.1	-	-	-
repayment of loans of Cargo	0.0	0.1	0.0	0.0	-
repayments of loans Water-management development	0.0	0.1	-	-	-
TOTAL	**0.7**	**1.4**	**0.4**	**0.4**	**0.1**

Source: CBR

Annex 3 – General government balance under baseline scenario – CBR estimate

As a part of its Report on the Long-term Sustainability of Public Finances from April 2014, the CBR prepared a baseline scenario of public finance development. It is a projection of general government revenues and expenditures assuming unchanged policies and taking into account the applicable legislation. The medium-term part of the scenario, based on the actual figures for 2013, may be viewed (with certain adjustments) as an NPC scenario of public finance development in the years covered by the three-year government budget.

The main difference between these scenarios lies in the applicable legislation reflected. While the baseline scenario, as an estimate based on the actual figures for 2013, reflects the legislation applicable as of 31 December 2013 (i.e., including the legislative changes approved in the course of 2013 which will take effect during 2014), the NPC scenario necessary to estimate the medium-term indicators should not reflect such legislation in order to capture the impact of the government in individual years. In other words, the NPC scenario for the calculation of medium-term indicators based on the 2013 figures should reflect only such legislation which took effect until the end of 2013. In the case of those legislative effects which spread over several years, only their aliquot portion should be reflected in the years covered by the budget[53].

For this reason, the balance in the baseline scenario in individual years has been adjusted for the impact of such legislative changes which, albeit adopted during 2013, bring effects only in 2014 (Table).

Tab 16: Balance adjustment in baseline scenario (ESA95, % GDP)

	2014	2015	2016	2017
1. General government balance in baseline scenario	-3.2	-3.8	-3.6	-3.9
2. Effect of changes in tax revenues & SSC (approved in 2013, effective from 2014)	0.2	0.2	0.2	0.0
3. Adjusted GG balance in NPC scenario (1-2)	**-3.4**	**-4.0**	**-3.8**	**-3.9**

Source: CBR

In the next step, the thus adjusted balance of the NPC scenario was cleared of the factors necessary for the quantification of structural balance under the national methodology. Individual data differ quite considerably from those used for the structural balance estimate based on budgetary targets mainly in the case of one-off effects. This is because these measures have a short-term impact and they are decided on every year; hence they the NPC scenario features them only to a very limited extent. There are also smaller differences in the amount of debt interest payments, since the deficits in the NPC scenario are considerably worse than the budgetary targets and their financing thus entails higher cost.

53 The reduction in contributions to the fully-funded pillar as of September 2012 can be used as an example. This legislation was adopted and entered into force in 2012. However, in order to correctly quantify the government's contribution to the reduction of deficit in 2013, it is necessary to take into account the 2013/2012 difference in impact on the balance, i.e. approximately ¾ of the annual impact.

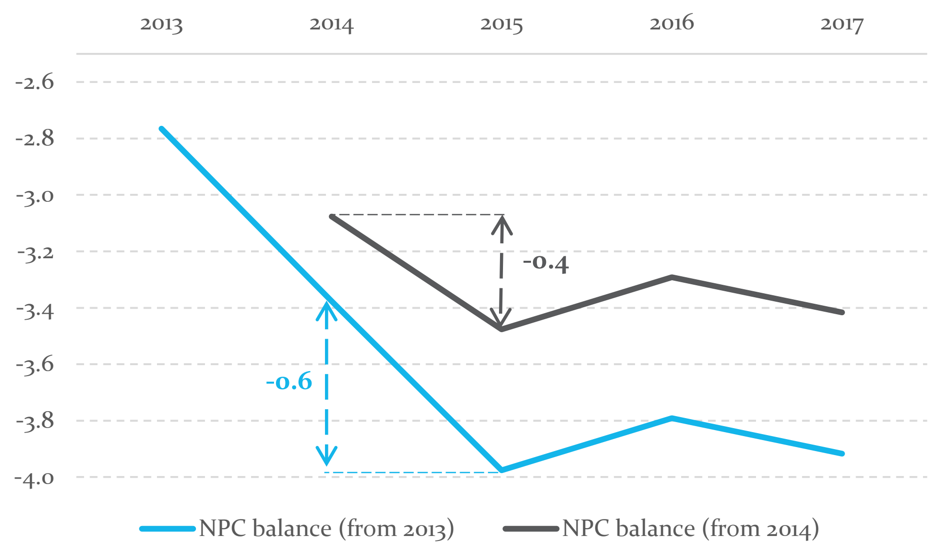
Tab 17: Change in general government structural balance in NPC scenario (ESA 95, %GDP)

	2013	2014	2015	2016	2017
1. General government balance - NPC scenario	**-2.8**	**-3.4**	**-4.0**	**-3.8**	**-3.9**
2. Cyclical component	-0.4	-0.3	-0.2	-0.1	0.1
3. One-off measures	0.7	0.3	0.1	0.1	0.1
4. Structural balance (1-2-3)	**-3.1**	**-3.3**	**-3.8**	**-3.9**	**-4.1**
5. Change in fully-funded pillar	-	0.0	0.0	0.0	0.0
6. Change in interest payments	-	0.0	0.0	0.0	-0.1
7. Change in construction of motorways	-	0.1	0.0	0.0	0.0
8. Change in decommissioning scheme of nuclear facilities	-	0.0	0.0	0.0	0.0
9. Change in structural balance (Δ4-5-6-7-8) / National concept	**-**	**-0.4**	**-0.5**	**0.0**	**-0.2**

Source: CBR

When interpreting the results of the medium-term indicators based on such NPC scenario (government's consolidation effort and size of measures), one should bear in mind that the first year of the scenario captures them most precisely. Subsequent years are rather indicative and depend on the impact of the measures adopted in the previous year. This can be illustrated on the change of the NPC balance in 2015. At present, the deficit is expected to deteriorate by 0.6 % of GDP year-on-year (from 3.4 % of GDP to 4.0 % of GDP). Assuming that a measure is taken for the year 2014 with a permanent positive impact in the amount of 0,3 % of GDP in 2014 and 0.5 % of GDP in 2015, the balance in the NPC scenario for the year 2015 based on the year 2014 will deteriorate only by 0.4 % of GDP (from 3.1 % of GDP to 3.5 % of GDP). This is caused by the impact of the measure adopted for the year 2014.

Figure 12: Illustration of changes in NPC scenario (% of GDP)



Source: CBR

Annex 4 – Calculation of sanctions applicable when the 55 % debt limit is exceeded

A. Blocking of 3 % of state-budget expenditures

Table 18 shows the expenditure items which, in determining the amount of blocked funds, are adjusted pursuant to Article 12, paragraph 5(a) of the Fiscal Responsibility Act. These items have either no impact on the general government balance, but they increase revenues and expenditures, or are not under the direct control of the government.

State debt interest payments include the transfer from the state budget to the so-called "balance account" (through which difference between interest expenditures and revenues related to state debt management are covered) and the expenditures for fees connected with the state debt.

European Union funds represent transfers from the EU budget. They are part of the state budget revenues and expenditures with neutral impact on general government balance . **Co-financing from the state budget** is directly related to the drawing of these funds from the EU budget. These expenditures are thus not under the direct control of the government.

Contributions to the European Union represent Slovakia's contributions to EU budget. At present, these are expenditures from a source based on VAT, a source based on gross national income, and Slovakia's share in the UK rebate[54].

Transfers to the Social Insurance Agency represent transfers from the state budget to cover the deficits of the pay-as-you-go pillar of the pension systems, plus the social contributions paid by the state to the pay-as-you-go pillar on behalf of certain categories of citizens. Both transactions have a neutral impact on the balance, since the increase in state-budget expenditures increases the revenues of the Social Insurance Agency (which is also a part of the general government).

The definition of **expenditures to remedy damages caused by natural disasters** is met by the *budget reserve for crisis situations*, which is created based on Act No. 387/2002 on the Management of the State in Crisis Situations outside the Times of War and State of War. This reserve also serves to cover expenditures incurred as a consequence of floods and natural disasters, and damage compensations in extraordinary and crisis situations.

The calculation is based on cash data contained in the 2014 State Budget Act (cash expenditures from the state budget, EU funds and expenditures for co-financing) and in the approved general government budget for 2014-2016 (remaining data). **The amount of blocked expenditures will reach EUR 305 million.**

54 Contributions from traditional own resources are not a part of state budget expenditures.

Tab 18: Blocking of 3 % of state budget expenditures (€ million)

	2014
1. Cash expenditures of state budget for 2014	**17 392**
2. State debt interest payments	1 398
3. Funds from the European Union budget	3 173
4. Co-financing to EU funds from the state budget	640
5. Contributions to the European Union budget	727
6. Transfers to Social Insurance Agency	1 280
7. Damages caused by natural disasters	11
8. Adjusted expenditures (1-2-3-4-5-6-7)	**10 163**
9. Amount of blocked expenditures (3 % of adjusted expenditures)	**305**
% of GDP	**0.41**

Source: CBR, MF SR

B. Suspended disbursement from the reserve funds of the prime minister and the government

The 2014 State Budget Act set up the reserve fund of the prime minister in the amount of almost EUR 1.5 million and the reserve fund of the government in the amount of EUR 5 million. By 30 April 2014, the total amount disbursed from the two reserve funds reached EUR 3.5 million, which means that the **maximum**[55] **saving** by the year-end may reach **EUR 3 million.** Depending on whether or not these unspent funds are included in the blockage, this amount may contribute towards reducing the overall government expenditures above the frameworks of blocking.

Tab 19: Overview of reserves (€ ths.)

	2014 B	as of 30.4.2014	difference
1. Government reserve fund	5 000	2 050	-2 950
2. Prime minister reserve fund	1 495	1 443	-52
3. Total (1+2)	**6 495**	**3 493**	**-3 002**

Source: MF SR

C. Freeze on the budgeted expenditures of general government

Table 20 shows the amount of adjusted general government expenditures for 2014 under ESA95 based on the figures published in the approved General Government Budget for 2014-2016. The General Government Budget for 2015-2017 should contain adjusted expenditures in the same or lower amount.

The expenditures are adjusted for the same items as in the case of their blocking (except for the transfer to the Social Insurance Agency), but the figures corresponding to these items are different for a number of reasons:

55 The suspension of disbursement from the reserve funds, as well as the blocking of expenditures from the state budget, as defined by the Fiscal Responsibility Act, apply as of 16 May 2014. This means that the disbursements from the reserve funds effected until 15 May 2014 may reduce the balance left.

- **State debt interest expenditures** relate solely to the state debt, are accrualised, consolidated for interest transfers to other general government entities and are expressed in ESA95 classification (code D.41 pay). This item also includes the interest paid to other general government entities for the use and appreciation of their available funds. Since at the time when the balance for the entire general government is prepared, these flows are consolidated, it is important that also this item contains consolidated data.

- The consolidated expenditures of general government in the ESA95 methodology contain only those **funds of the European Union** the final beneficiary of which is a general government entity. For this reason, expenditures are adjusted on for this part of EU funds.

- **Contributions to the EU budget** are, under ESA95, reduced by the source based on VAT, because this part of the contribution reduces the revenues of general government under ESA95.

- **Expenditures for co-financing and expenditures to remedy damages caused by natural disasters** are identical with those listed in the quantification of the 3-% blockage of government expenditures. The reason is that they are exclusively a part the state budget and are not subject to any adjustment in the transition to ESA95.

Tab 20: Freeze on the budgeted expenditures of general government (ESA 95, € million)

	2014B	2015B	2016O	2017O
1. Nominal consolidated expenditures of GG	**28 050**	**28 404**	**28 537**	**29 347**
2. Debt management	1 341	1 333	1 442	1 459
3. Funds of European Union	1 198	1 365	1 090	1 390
4. Co-financing to EU funds from the state budget	640	586	426	480
5. Contributions to the European Union	683	658	731	690
6. Damages caused by natural disasters	11	11	11	11
7. Adjusted expenditures (1-2-3-4-5-6)	**24 177**	**24 452**	**24 838**	**25 317**
8. Necessary change in expenditures		**275**	**661**	**1 140**
- in % GDP		**0.4**	**0.8**	**1.3**

Source: CBR, MF SR

The expenditures of general government in the years 2015 to 2017 should be lower by 0.4 % to 1.3 % GDP than those presented in the Stability Programme.

Provided that the necessary change in expenditures is reflected in the general government budget in a manner ensuring that these changes fully improve the deficit, such a change will exceed the size of the measures necessary to meet the objectives defined in the Stability Programme. In this case, the freeze on expenditures would substantially eliminate the identified risks and facilitate the meeting of the government's fiscal objectives.

Tab 21: Potential impact of expenditure freezing on GG balance and debt (ESA 95, € million)

	2015O	2016O	2017O
1. Necessary change in expenditures (compliance with expenditures freezing)	275	661	1 140
2. Measures necessary to meet targets of SP 2014-2017	218	313	626
3. Assumption of change in targets (1-2)	57	348	514
- in % GDP	0,07	0,43	0,60
4. New targets for GG balance (3+p.m.)	-1 880	-967	49
- in % GDP	**-2,42**	**-1,18**	**0,06**
5. Estimated impact on GG debt	-58	-415	-957
- in % GDP	**-0,1**	**-0,5**	**-1,1**
p.m. targets set in Stability Programme	*-1 937*	*-1 316*	*-466*
- in % GDP	*-2,49*	*-1,61*	*-0,54*

Source: CBR

D. Freeze on the budgeted expenditures of local governments

Municipalities and self-governing regions are obliged to adopt their 2015 budgets with expenditures not exceeding their 2014 budget level, except for expenditures to remedy the consequences of damages caused by natural disasters and expenditures for co-financing. The freeze on local government expenditures for 2015 is likely to reduce the need to cut the expenditures of other government entities in order to ensure that the expenditures of the general government sector as a whole do not increase.

At this point, it is still impossible to quantify the impact of this sanction on local government expenditures because the figures from the 2014 approved budgets are not yet available.

Annex 5 – Balance of general government revenues and expenditures

Tab 22: General government (ESA95, € million)

	2012	2013	2014B	2014E	2015B	2016B	2017B
Total Revenue	**23 974.1**	**25 925.8**	**26 049.2**	**26 194.3**	**26 249.2**	**26 908.4**	**28 254.7**
Tax revenue	11 009.3	11 739.2	12 024.2	12 124.5	12 348.1	12 811.8	13 308.7
Taxes on Production and Imports	7 046.6	7 518.4	7 634.2	7 546.3	7 720.6	7 945.3	8 216.4
- VAT (excl. VAT the EU)	4 243.8	4 596.5	4 816.6	4 674.4	4 874.1	5 062.5	5 352.9
- Excise taxes	1 973.3	1 984.8	1 944.1	1 993.8	2 008.3	2 024.8	2 046.2
- Import duty	0.1			0.0	0.0	0.0	0.0
- Taxes on Land, Buildings etc.	215.3		233.2	233.2	241.4	249.9	249.9
Current Taxes on Income, Wealth	3 962.6	4 220.8	4 390.0	4 578.2	4 627.5	4 866.5	5 092.3
- PIT	1 863.7	1 893.7	1 967.0	1 951.0	2 075.0	2 195.9	2 342.1
- CIT	1 714.8	1 808.2	1 913.0	1 943.9	2 036.9	2 121.8	2 265.6
- Withholding Tax	167.1	177.8	154.1	151.4	150.8	175.3	218.5
- Income Tax - emissions	0.0	0.0		0.0	0.0	0.0	0.0
- Property Taxes and Others	100.5		107.7	107.7	111.6	115.5	115.5
Social Security Contributions	9 039.9	9 931.5	9 927.3	9 909.8	10 211.5	10 703.8	11 230.5
Actual Social Security Contr.	8 928.9	9 800.6	9 818.7	9 801.2	10 112.6	10 601.8	11 128.4
Imputed SSC	111.0	131.0	108.6	108.6	98.8	102.0	102.0
Nontax revenue	2 051.5	2 014.4	1 943.4	1 778.1	1 761.0	1 750.4	1 807.8
Sales	1 242.3	1 352.0	842.2	1 106.6	1 185.0	1 196.6	1 237.3
Property Income, of which	809.2	662.3	1 101.2	671.6	576.1	553.8	570.5
- Dividends	623.7	459.9	997.4	566.9	484.9	437.9	432.8
- Interest	137.2	149.3	50.5	50.2	36.6	60.5	82.4
Grants and transfers	1 873.4	2 240.7	2 154.3	2 381.9	1 928.6	1 642.4	1 907.7
of which: from EU	806.7	817.7	1 197.9	1 387.9	1 365.0	1 089.6	1 389.6
Total Expenditure	**27 164.8**	**27 918.4**	**28 049.6**	**28 309.6**	**28 404.1**	**28 536.8**	**29 346.7**
Current expenditure	24 977.8	25 999.9	26 563.4	26 431.6	26 290.1	26 793.9	27 404.9
Compensation of employees	5 224.1	5 488.1	5 015.3	5 216.3	5 217.6	5 267.0	5 308.4
Intermediate Consumption	3 308.5	3 319.4	3 438.9	3 431.9	3 349.6	3 284.1	3 338.2
Taxes	69.0	91.7	122.8	122.8	23.3	23.5	23.5
Subsidies and transfers	718.2	812.0	989.1	716.6	686.0	687.7	695.7
Interest	1 297.6	1 411.1	1 375.0	1 367.2	1 366.3	1 476.3	1 493.7
Total Social Transfers	13 306.5	13 660.8	13 757.9	13 718.6	13 917.3	14 428.9	14 961.6
Social benefits other than in kind	9 805.0	9 996.3	9 996.0	9 979.9	10 135.5	10 452.2	10 802.7
Active Labour Market Measures	57.1	38.2	20.9	20.9	13.2	2.3	2.3
Sickness benefits	428.5	399.7	432.0	423.8	446.9	464.7	480.7
Old-age and disability pensions	5 639.5	5 893.8	6 112.2	6 111.0	6 259.2	6 514.2	6 784.8
Unemployment benefits	175.8	174.3	179.2	173.4	170.7	164.0	163.2
State social allowances	1 375.4	1 381.3	1 402.2	1 402.2	1 422.9	1 444.4	1 457.2
Insurance premiums	1 598.5	1 541.3	1 476.6	1 476.6	1 458.2	1 490.3	1 542.3
Social transfers in kind	3 501.5	3 664.5	3 761.9	3 738.8	3 781.8	3 976.7	4 158.9
Other subsidies and transfers	1 053.9	1 216.8	1 864.6	1 858.2	1 730.0	1 626.3	1 583.8
o/w: Levies to the EU budget	556.4	645.5	683.1	671.3	657.8	730.6	690.4
Capital Expenditure	2 187.0	1 918.6	1 486.1	1 878.1	2 114.0	1 742.9	1 941.8
Capital Investment	1 543.0	1 461.5	829.9	1 395.1	1 545.2	1 484.6	1 720.3
Capital transfers	644.0	457.0	656.3	482.9	568.7	258.2	221.4
Net lending/borrowing	**-3 188.0**	**-1 994.9**	**-2 000.4**	**-2 115.3**	**-2 154.9**	**-1 628.4**	**-1 092.0**
Measures needed to reach the target				148.7	218.0	312.9	626.5
Targeted balance	**-3 188.0**	**-1 994.9**	**-2 000.4**	**-1 966.6**	**-1 936.9**	**-1 315.5**	**-465.5**

Source: MF SR

Tab 23: General government (ESA95, % GDP)

	2012	2013	2014B	2014E	2015B	2016B	2017B
Total Revenue	33.7	35.9	34.4	35.2	33.7	32.9	32.8
Tax revenue	**15.5**	**16.3**	**15.9**	**16.3**	**15.9**	**15.7**	**15.4**
Taxes on Production and Imports	9.9	10.4	10.1	10.1	9.9	9.7	9.5
- VAT (excl. VAT to the EU)	6.0	6.4	6.4	6.3	6.3	6.2	6.2
- Excise taxes	2.8	2.8	2.6	2.7	2.6	2.5	2.4
- Import duty	0.0	0.0	0.0	0.0	0.0	0.0	0.0
- Taxes on Land, Buildings and Other Structures	0.3	0.0	0.3	0.3	0.3	0.3	0.3
Current Taxes on Income, Wealth etc.	5.6	5.9	5.8	6.1	5.9	6.0	5.9
- PIT	2.6	2.6	2.6	2.6	2.7	2.7	2.7
- CIT	2.4	2.5	2.5	2.6	2.6	2.6	2.6
- Withholding Tax	0.2	0.2	0.2	0.2	0.2	0.2	0.3
- Income Tax - emissions	0.0	0.0	0.0	0.0	0.0	0.0	0.0
- Property Taxes and Others	0.1	0.0	0.1	0.1	0.1	0.1	0.1
Social Security Contributions	**12.7**	**13.8**	**13.1**	**13.3**	**13.1**	**13.1**	**13.0**
Actual Social Security Contributions	12.6	13.6	13.0	13.2	13.0	13.0	12.9
Imputed SSC	0.2	0.2	0.1	0.1	0.1	0.1	0.1
Nontax revenue	**2.9**	**2.8**	**2.6**	**2.4**	**2.3**	**2.1**	**2.1**
Sales	1.7	1.9	1.1	1.5	1.5	1.5	1.4
Property Income, of which	1.1	0.9	1.5	0.9	0.7	0.7	0.7
- Dividends	0.9	0.6	1.3	0.8	0.6	0.5	0.5
- Interest	0.2	0.2	0.1	0.1	0.0	0.1	0.1
Grants and transfers	**2.6**	**3.1**	**2.8**	**3.2**	**2.5**	**2.0**	**2.2**
of which: from EU	**1.1**	**1.1**	**1.6**	**1.9**	**1.8**	**1.3**	**1.6**
Total Expenditure	38.2	38.7	37.0	38.0	36.5	34.9	34.0
Current expenditure	**35.1**	**36.0**	**35.1**	**35.5**	**33.8**	**32.8**	**31.8**
Compensation of employees	7.3	7.6	6.6	7.0	6.7	6.4	6.2
Intermediate Consumption	4.7	4.6	4.5	4.6	4.3	4.0	3.9
Taxes	0.1	0.1	0.2	0.2	0.0	0.0	0.0
Subsidies and transfers	1.0	1.1	1.3	1.0	0.9	0.8	0.8
Interest	1.8	2.0	1.8	1.8	1.8	1.8	1.7
Total Social Transfers	18.7	18.9	18.2	18.4	17.9	17.7	17.4
Social benefits other than in kind	13.8	13.9	13.2	13.4	13.0	12.8	12.5
Active Labour Market Measures	0.1	0.1	0.0	0.0	0.0	0.0	0.0
Sickness benefits	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Old-age and disability pensions	7.9	8.2	8.1	8.2	8.0	8.0	7.9
Unemployment benefits	0.2	0.2	0.2	0.2	0.2	0.2	0.2
State social allowances	1.9	1.9	1.9	1.9	1.8	1.8	1.7
Insurance premiums	2.2	2.1	1.9	2.0	1.9	1.8	1.8
Social transfers in kind (healthcare facilities)	4.9	5.1	5.0	5.0	4.9	4.9	4.8
Other subsidies and transfers	1.5	1.7	2.5	2.5	2.2	2.0	1.8
o/w: Levies to the EU budget	0.8	0.9	0.9	0.9	0.8	0.9	0.8
Capital Expenditure	**3.1**	**2.7**	**2.0**	**2.5**	**2.7**	**2.1**	**2.3**
Capital Investment	2.2	2.0	1.1	1.9	2.0	1.8	2.0
Capital transfers	0.9	0.6	0.9	0.6	0.7	0.3	0.3
Net lending/borrowing	-4.48	-2.77	-2.64	-2.84	-2.77	-1.99	-1.27
Measures needed to reach the target				0.2	0.3	0.4	0.7
Targeted balance	-4.48	-2.77	-2.64	-2.64	-2.49	-1.61	-0.54

Source: MF SR

Annex 6 – Structure and development of general government expenditures

Tab 24: Structure of adjusted general government expenditures (ESA95, € million)

	2014E	2015O	2016O	2017O
Adjusted expenditures	**22 766.8**	**22 970.8**	**23 324.2**	**23 751.1**
Mandatory	**9 840.0**	**9 866.4**	**10 051.2**	**10 087.0**
Compensation of employees	5 176.0	5 187.0	5 264.0	5 306.1
- Wages	3 792.4	3 816.5	3 875.3	3 906.8
- Employer social security contributions	1 383.5	1 370.5	1 388.7	1 399.2
Intermediate consumption	2 466.5	2 781.3	3 004.4	3 007.7
Taxes	122.8	23.3	23.5	23.5
Subsidies	574.6	571.0	583.4	583.4
- Agricultural subsidies	7.4	7.3	7.3	7.3
- Transport subsidies	430.6	436.4	452.6	452.6
- Rail transport	205.0	205.5	205.4	227.9
- Bus transport	224.6	229.9	246.3	223.8
- Other	136.7	127.3	123.5	123.5
Social transfers	371.9	364.3	372.3	372.3
Other current transfers	1 128.3	939.5	803.5	794.0
Facultative	**11 911.4**	**12 137.3**	**12 613.7**	**13 097.4**
Social benefits	11 861.6	12 084.5	12 566.3	13 047.1
- Social benefits other than transfers in kind	8 122.9	8 302.6	8 589.6	8 888.1
- Active labour market policy	12.4	2.9	2.3	2.3
- Sickness benefits	423.8	446.9	464.7	480.7
- Old-age and disability pensions	6 111.0	6 259.2	6 514.2	6 784.8
- Unemployment benefits	173.4	170.7	164.0	163.2
- State benefits and social assistance	1 402.2	1 422.9	1 444.4	1 457.2
- Child allowance	319.2	322.2	328.5	328.5
- Allowance for newborns	9.3	9.2	9.2	9.2
- Parental allowance	361.0	363.0	371.8	371.8
- Material needs benefits	274.5	270.3	267.6	267.6
- Cash subsidies on compensation	246.7	258.6	263.0	263.0
- Other	191.5	199.6	204.2	217.0
- Social transfers in kind (Healthcare)	3 738.8	3 781.8	3 976.7	4 158.9
Other current transfers	49.7	52.9	47.4	50.3
of which: 2% of income tax to 3rd sector	49.7	52.9	47.4	50.3
Capital expenditures	**1 015.4**	**967.1**	**659.4**	**566.7**
Capital investment	693.4	576.3	513.0	468.3
Capital transfers	322.0	390.8	146.4	98.3

Source: CBR, MF SR

Annex 7 – Fiscal performance of general government entities

Tab 25: General government performance (ESA95, ths €)

	2013E	2014B	2015O*	2016O*	2017O*
A. State Budget	-2 477 014	-2 353 824	-2 510 230	-2 021 213	-1 581 471
B. Other subjects of GG	482 096	353 430	355 332	392 815	489 485
Municipalities	121 791	22 357	52 176	52 122	123 981
Higher teritorial units	50 975	15 019	6 681	17 242	37 400
Social Insurance Agency	41 034	44 340	23 167	25 435	23 533
Health insurance companies	5 167	28 317	8 529	10 355	12 152
Nuclear decommissioning fund	145 028	128 192	150 021	170 238	170 238
National Property Fund	-147 325	-15 795	-11 417	-5 172	-4 447
Environmental fund	23 104	39 126	38 943	38 953	38 953
State fund for housing development	93 326	81 553	80 167	80 282	80 417
Healthcare Surveillance Authority	2 833	185	39	246	909
Slovak Land Fund	9 931	7 824	5 259	5 259	5 853
Slovak consolidation agency	5 096	2 680	1 817	157	122
Public universities	49 235	1	100	101	101
Broadcasting and televison	3 326	1 072	730	285	24
TASR	-2	434	175	175	175
Audit Surveillance Authority	77	-12	-5	4	4
Audiovisual Fund	-238	50	0	0	
Council for Budget Responsibility	214	60	5	-4	7
Railways	58 251	-	0	0	0
RTVS	143	-	-	-	-
Nation's Memory Institute	-21	-	-	-	-
Slovak National Centre for Human Rights	-1	-	-	-	-
Danubiana	-371	-	-	-	-
Contributory organisations	20 523	-1 973	-1 055	-2 863	63
General government	-1 994 918	-2 000 394	-2 154 898	-1 628 398	-1 091 986
(% GDP)	-2.77	-2.64	-2.77	-1.99	-1.27
GDP at cur.p. (mill. eur)	*72 134*	*75 773*	*77 787*	*81 710*	*86 210*

** without measures*

Source: CBR, MF SR

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