CROATIAN PARLIAMENT
Fiscal Policy Commission
Class: 021-19/16-10/02
Ref. No.: 6521-05-1-16
Zagreb,14 March 2016

7th Position paper of the Fiscal Policy Commission on the the Draft Budget of the Republic of Croatia for 2016

In line with the provisions of item IV subparagraph 1 and item V paragraph 5 of the Decision on the Establishment of the Fiscal Policy Commission, at its 13th meeting held on 14 March 2016, the Croatian Parliament Fiscal Policy Commission discussed the Draft Budget of the Republic of Croatia for 2016 along with the projections for 2017 and 2018 and the proposal of financial plans of extra-budgetary users for 2016 along with the projections for 2017 and 2018, that were submitted to the Croatian Parliament by the Government of the Republic of Croatia on 10 March 2016. The Commission adopted the following position:

The budget indicates an intention to accelerate fiscal consolidation, which is at present a reasonable course to take regarding fiscal and economic policy. It shows the intention of reducing the budget deficit by planning to reduce the central government budget deficit to 2.2% of GDP in 2016, as opposed to 3.7% of GDP planned in 2015.

The budget clearly expresses the ambition to control expenditure growth, since when provided for, expenditure growth is either associated to previous commitments or to the use of EU funds. The budget includes fairly conservatively projected tax revenues. The Commission believes nevertheless that the 2016 budget has probably significantly overestimated revenues from the EU. However, this automatically means that expenditures have been overestimated as well, so as a rule this should not affect the achievement of the deficit target, although it is not excluded that some expenditures expected to be covered from the EU funds will eventually have to be covered from domestic funds. As for the projections of revenues from corporate income tax for 2016, only a small decline in relation to the achievement in 2015 is expected. In addition, it has not been explained how the losses of commercial banks due to the conversion of loans in Swiss francs into euros will affect revenues from corporate income tax. There is a risk that the decrease of revenues from corporate income tax will be higher than planned.

Unfortunately, the budget does not mention to which extent it complies with the fiscal rules, which would undoubtedly be absolutely necessary. Although the Explanatory Statement relating to the Draft Budget mentions some risks with regard to implementing the fiscal rules, they are neither sufficiently emphasized nor complete. The Commission has identified two key risks that could affect the achievement of the planned deficit target. First, the macroeconomic risks, and second the risk of the trends of expenditures for employees.

We should point out the weaknesses of the fiscal framework in Croatia indicated by the European Commission's In-Depth Review[1] and by the Council of the EU's Special Recommendations[2]. These are for instance: the low correlation with previous plans, the lack of information about the plans for extra budgetary units or at the level of general government, incoherence between the budgetary plans and the accounting standards used in reporting for the purposes of the Excessive Deficit Procedure (EDP) or for compliance with the fiscal rules, or weaknesses in planning certain revenues and expenditures. It is particularly worth to point out the part of the recommendations concerning desirable amendments to the Fiscal Responsibility Act in order to strengthen the role and independence of the Fiscal Policy Commission and to advance the fiscal rules. The government should seriously consider taking appropriate steps for the improvement of the fiscal framework and for the efficient implementation of structural measures.

[1] **http://ec.europa.eu/europe2020/pdf/csr2016/cr2016_croatia_en.pdf**
[2] **http://ec.europa.eu/europe2020/pdf/csr2015/csr2015_council_croatia_en.pdf**