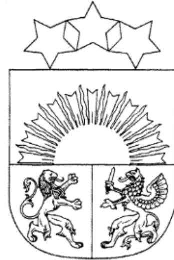

LATVIJAS REPUBLIKAS FISKĀLĀS DISCIPLĪNAS PADOME

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Fiscal discipline monitoring report 2014

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1. Summary

The fiscal policy of the Government of Latvia generally follows the principles and numerical fiscal rules stipulated in the Fiscal discipline law (further – FDL). The Draft medium term budget framework law (further – Draft Framework Law) and the Draft annual budget law (further – Draft Budget Law) comply with the three numerical rules stipulated in the FDL: (i) balance rule; (ii) expenditure growth rule; and (iii) continuity rule. To allow the Fiscal discipline council (further – Council) expanding the analysis of the Draft Framework Law and the Draft Budget Law a Memorandum of Understanding stipulating cooperation should be concluded.

The Council finds macroeconomic forecasts to be realistic if perhaps slightly optimistic given the current economic climate. The Council urges caution with respect to possible downside risks from the geopolitical environment and global energy prices suppressing the growth of nominal gross domestic product (further – GDP). There is a nontrivial risk of a higher than forecasted budget deficit and the Government should think about possible measures for additional revenues and/or lower expenditures as a backup plan.

The tax burden lags the government long-term objective of 1/3 of GDP causing risks for the government capacity to counter the needs for sustainable development of public services, facing security challenges, and the infrastructure development needs. A realistic plan for achieving the tax revenue objective is still to be developed. The tax measures for eliminating income inequality have not been sufficient so far. The Council sees potential in addressing the tax revenue gap through reducing the revenue losses through containing the "shadow" economy, broadening tax base, and increasing, if necessary the tax rates on capital not used for productive purposes.

The Council broadly agrees with the Fiscal risk declaration adopted by the Government, while it finds increasing risks of the expenditure estimates for pensions and social insurance benefits exceeding the state special budget estimates. The Council encourages the Government to improve the fiscal risk management and recommends that the Fiscal stability reserve is estimated in the framework law for 2017 in the amount of 0.13% of GDP, while the Fiscal stability reserve according to the transitional provisions of FDL is not being established for 2015 and is fixed at 0.1% of GDP for 2016.

According to the FDL the Council shall produce a Fiscal discipline monitoring report (hereinafter – the Monitoring report) to assess the compliance of the Draft Framework Law and the Draft Budget Law with the FDL.

2. Mandate of the Council

According to the FDL (Chapter III Monitoring of the fiscal discipline) the Council is an independent collegial institution, which has been established to monitor the compliance with FDL. Council's core competence is related to the assessment of fiscal discipline (see. Section 3 of the Monitoring report), and assess the fiscal policy and issues related to macroeconomic developments.

Specifically the Council has responsibility for:

- monitoring the compliance with the FDL provisions in the Draft Framework Law and the Draft Budget Law during their preparation, execution, and amendment;
- verifying, if the fiscal balance and the expenditure growth provisions have been properly applied, including an independent assessment of the potential GDP and nominal GDP, and the calculation of the structural balance;
- monitoring the compliance with the FDL conditions with the estimated summary fiscal indicators during the execution of the Annual state budget law, the consolidated local government budget, and derived public person budgets;
- preparing opinion regarding the major departures from the balance condition permitted during a severe economic downturn;
- preparing an opinion on the fiscal safety reserve to counter the prevailing fiscal risks for the state;
- preparing a monitoring report for fiscal discipline and, if necessary, an irregularity report;
- preparing and submit to the Saeima and the Government opinions regarding issues of fiscal policy and macro-economic development, as necessary to ensure the compliance with the FDL;
- preparing the reports stipulated by the FDL to assess and analyze the fiscal policy sustainability of the country.

3. Assessment of compliance with the numerical fiscal rules

According to the FDL the government shall comply with a number of numerical conditions to provide for a counter-cyclical and balanced economic development. According to Article 10 of the FDL – Balance condition, the general government structural balance in the Draft Framework Law for each year of the period should be set not lower than – 0.5% of the annual GDP. FDL also establishes a number of adjustments and deviations from the balance condition. The Government has applied the balance condition rule and assessed the general government deficit not to exceed 1% of GDP in 2015, 0.9% of GDP in 2016 and 0.7% of GDP in 2017 for the preparation of the Draft Framework Law. The Council agrees with the Government's balance condition calculations.

However, before these calculations are used in the drafting of the Framework law other numerical fiscal condition parameters should be verified. FDL provides that the lowest value derived comparing different numerical criteria should be selected, including the criteria on expenditure growth condition and continuity condition. According to Article 5 of the FDL the continuity condition does not apply in case if the difference with the other condition (balance or expenditure growth) exceeds of 0.1% of GDP.

During the examination of macroeconomic forecasts and the general government sector's financial performance projections the Government has been dealing with various the levels of expenditure forecasts. The Government approved Draft Budget Plan of the Latvian General Government for 2015 (further – Draft budgetary plan) on 15 October 2014, assessing the fiscal space for introducing new revenue-decreasing or cost-increasing measures at zero. Moreover, ministries and other central government authorities submitted requests for new policy initiatives (further – NPI) amounting to EUR 567.7 million in 2015, EUR 942 million in 2016, and EUR 1 199.5 million in 2017. At this meeting the ministries were requested to review their medium-term plans and to submit proposals that postpone the previously announced NPI.

The Government approved updated macroeconomic forecasts on 10 November 2014 increasing the fiscal space from zero to EUR 18.3 million. 12 November 2014 the Government approved the revenue measures with impact of EUR 62.6 million in 2015. The fiscal space increased to EUR 133.2 million from the adjustments of line ministry medium-term plans (http://www.fm.gov.lv/files/fmbudzets/newnode/Izdevumi_pamatfunkcijas.pdf) to support NPI.

The Council provisionally concludes that the Ministry of Finance (further – MoF) has applied correctly the numerical fiscal rules on the fiscal balance, the expenditure growth and the continuity conditions as of the 10 November 2014. The further adjustments related to the additions to the fiscal space including the specified macroeconomic forecasts, revenue measures, and adjustments ministries have brought to the medium-term plans exceed 0.1% of the 2015 GDP estimate at current prices therefore and the conditions of FDL Article 5 part two apply. Therefore, the provision of Article 15 of the FDL applies stipulating that the expenditure ceiling for the 2015 budget is established according to the balance rule establishes (please see Table 1 cells highlighted for 2015), based on lower value compared to the expenditure growth rule in the amount of EUR 7,470.6 million. Based on the adjustments introduced by the Government not exceeding 0,1% of GDP in 2016 brings the continuity rule as the lowest value of the expenditure ceiling to be applied in the amount of EUR 7,598.7

million. However, expenditure ceiling for 2017 should be established alike 2015 according to the balance rule and the value of EUR 7,969.9 million.

Numerical fiscal rule assessment allows to conclude that the Government budget expenditure forecasts as of November 22, 2014 comply with FDL numerical condition assessments (please refer to Table 1, the trailing lines).

The Council would like to note that it has not made comprehensive independent assessment of the government projections of individual indicators. Meanwhile, it would like to mention that the projections for the cost of paying pensions and other social insurance benefits appear to be underestimated in the draft budget based on the current trends in 2014, which may contribute to deterioration of the general government balance by 0.2-0.3 percent of GDP.

Table 1. FDL numerical conditions for 2015-2017 Draft Framework Law

	2015		2016		2017	
	10.11.2014	22.11.2014	10.11.2014	22.11.2014	10.11.2014	22.11.2014
Theoretical CG expenditure in accordance with the FDL, in million euro –						
(1) Balance rule	7,394.5	7,470.6	7,465.3	7,616.8	7,889.4	7,969.9
(2) Expenditure rule	7,537.2	7,654.9	7,548.3	7,709.7	7,907.8	7,972.1
(3) Previous budget amount rule	7,326.6	7,351.2	7,575.1	7,598.7	–	–
GDP, million euro, at current prices	25,365.6	25,365.6	26,859.0	26,859.0	28,513.3	28,513.3
0,1% of GDP	25.4	25.4	26.9	26.9	28.5	28.5
Rule that applies for the ceiling for establishing the CG expenditure	(1)	(1)	(1)	(3)	(1)	(1)
Central government budget revenue, million euro	7,156.7	7,255.6	7,191.6	7,324.1	7,407.8	7,484.1
Local government budget balance, million euro	-55.4	-55.4	-0.2	-0.2	0.9	0.9
Derived public persons budget balance, million euro	-13.9	-13.9	-0.2	-0.2	-0.4	-0.4
ESA corrections, million euro	59.1	36.4	25.1	44.2	269.6	273.8
Minimal structural balance, % of GDP	-1.021	-1.021	-0.909	-0.909	-0.750	-0.750
One-off, % of GDP	–	–	–	–	–	–
Cyclical component, % of potential GDP)	0.043	0.043	-0.018	-0.018	0.009	0.009
Cyclically-adjusted balance, % of GDP	-1.0	-1.0	-0.9	-0.9	-0.7	-0.7

	2015		2016		2017	
	10.11.2014	22.11.2014	10.11.2014	22.11.2014	10.11.2014	22.11.2014
Structural balance, % of GDP	-1.0	-1.0	-0.9	-0.9	-0.8	-0.8
Central government expenditure, million euro	not assessed	7,469.2	not assessed	7,594.1	not assessed	7,655.4
FDL rules compliant (yes/no)	not assessed	yes	not assessed	yes	not assessed	yes

Due to the limited time frame to prepare the numerical fiscal conditionality assessment of the Council had to rely on the Government's analytical material without further independent evaluation. In the future the model of cooperation should be developed to allow the Council to obtain the necessary information at the earliest possible stage.

The Council recommends:

1. To adopt a Memorandum of Understanding with the MoF for the exchange of information and cooperation in the monitoring of fiscal discipline.
2. Follow closely the 2015 general government balance level for the need of correction mechanism for 2016 due to estimated overshooting the 2014 budget deficit target (i.e. -1,0% of the GDP structural balance objective instead of the current forecast of -1,3%).

4. Macroeconomic outlook and output gap

The macroeconomic outlook has worsened during 2014 and the Council welcomes the downward adjustment of Latvia's GDP growth forecasts in the Draft budgetary plan compared to the more optimistic figures in Latvia's Stability Programme for 2014 – 2017 published earlier in the year (further – Stability programme).

Table 2. GDP growth and output gap estimates, fall 2014

	2014	2015	2016	2017
Nominal GDP growth, %				
Ministry of Finance	3.8	5.2	5.9	6.2
Bank of Latvia	4.0	4.8	5.9	6.4
European Commission	4.2	5.1	6.2	-
IMF	3.9	4.8	5.4	6.2
Real GDP growth, %				
Ministry of Finance	2.9	2.8	3.3	3.6
Bank of Latvia	2.8	2.7	3.5	4.0
European Commission	2.6	2.9	3.6	-
IMF	2.7	3.2	3.4	4.1
Output gap, % of potential GDP				
Ministry of Finance	0.7	0.1	0.0	0.0
Bank of Latvia	1.2	0.3	0.2	0.3
European Commission	1.0	1.2	1.6	-

The Government's forecasts of GDP growth are largely in line with those of the European Commission, IMF and the Bank of Latvia, but given multiple downside risks – slow growth in Europe in general and in the Eurozone in particular coupled with geopolitical uncertainty and continuing sanctions/ counter-sanctions vis-à-vis Russia – actual growth is, however, very likely to be lower. This is seen in the GDP data so far available for 2014, i.e. real GDP in the first three quarters is up 2.5% compared to the same period last year and the last quarter of the year is most unlikely to be strong enough to yield the forecasted 2.9% annual growth for the whole of 2014. Downside risks for the economic growth pick up in 2015 are also substantial.

The Government forecasts inflation to pick up from its current very low level. The Council has a similar opinion although with oil prices substantially down it is very likely to lead to less inflationary pressure than forecasted in the Draft budgetary plan. Altogether, the risk of a somewhat lower real GDP growth rate coupled with the possibility of a lower inflation rate may lead to a less optimistic development of nominal GDP, and thus a potentially smaller tax base. Additional measures for boosting the government's capacity to tax the economy might be needed to ensure that the revenue targets can be achieved.

In terms of the output gap, the Council lacks persuasive economic/intuitive explanation in the Budgetary plan for why this was revised for 2013 from slightly negative (- 0.1% of potential GDP) to quite positive (+ 0.8% of potential GDP), i.e. from roughly balance to somewhat above equilibrium. The Council is aware of the discrepancy between the output gap estimates of the MoF and the European Commission (see Stability programme, p. 16) and supports the Ministry's opinion that the economy is not experiencing a strong and positive output gap, and the output gap is closing rather than widening as the estimates of the European Commission

suggest. The Council's view is that with the current slowdown and continued subdued growth outlook, there is no major positive output gap and if growth would disappoint going forward, a negative output gap could appear.

Overall, the Council finds macroeconomic forecasts to be acceptable as the basis for the budget preparation for 2015, if perhaps slightly optimistic given the current economic climate. The projections for 2016-2017 would need to be scrutinized separately, particularly if the downside risks in economic development outweigh the upside ones. The Council finds that the Budget plan complies with the Balance rule and Expenditure rule, but at the same time urges caution with respect to possible downside risks. There is a nontrivial risk of a higher than forecasted budget deficit and the government should think about possible measures for additional revenues and/or lower expenditures as a backup plan.

The Council would like to comment on the following macro issues:

1. The Council would like to invite the MoF providing better explanation of the output gap calculation.

2. Drafting budget with deficits in years of positive output gap does not comply with the FDL's 2nd principle (the principle of savings) according to which "fiscal policy shall be implemented so that the budget is planned and implemented with surplus if the economic situation allows" or, for that matter, the Law's Section 1 "[to] ensure balanced budget over the economic cycle".

3. Exhausting the estimated fiscal space for 2016 and 2017 already now is likely to be imprudent if economic growth was to turn out to be lower than forecasted and thus deficit targets will be overshot unless expenditures are cut. The medium term budget of 2014 and then exhausted fiscal space for 2015 serves as an example.

4. Fiscal sustainability and ability to raise expenditures is dependent on the economy growing. For this, structural reforms and other forward-looking policy choices are crucial and the government would serve it right to honour the promises made on these issues, e.g. see the letter of the Latvian authorities to European Commission http://www.fm.gov.lv/files/eiro/2013-06-20_Apnemsanas-vestule-euro-grupai.PDF

5. Fiscal policy challenges

Broader society expects the government to assume an increasing role in addressing a number of serious challenges over the next few years, including the support to structural reform effort for achieving better outcomes of the education and health sectors, countering security challenges, and improving infrastructure. All these require more effective management effort and additional resources. Moreover, promoting sustainable economic growth and reducing public debt accumulated during the crisis of 2008-2010 are also important considerations.

The structural reforms should focus on improving the quality and access to government services, while it is highly unlikely that Latvia would manage to achieve the service levels of EU countries public sector (building a welfare). Therefore, in offering public services a balance should be found between the charges for services from the public in order to encourage responsible consumption of these services and the support for the vulnerable part of the population to have access to essential services.

A major challenge for fiscal policy is having sustainable public finances in Latvia, while ensuring sufficient public services. It means to have enough resources for meeting the needs for both – adequate social services and the development of the country. In the current projections the expenditure side of the medium term budget outlook is not properly covered by the revenues. Therefore, the Council welcomes the target assumed by the new Cabinet of HE Laimdota Straujuma of moving towards the ratio of tax revenue to GDP – 1/3. Meanwhile, the Council notes that there is no documented path to achieve this objective within the mandate for the current Saeima. The current level of the tax share to GDP lags the target by over five percentage points – the tax burden in 2015-2017 is declining below the current 27.7-27.9 percent level maintained since 2012. The drive for the reduction of payroll taxes over the past few years has increased the deviation from the target as there has been a lack of effective compensatory measures.

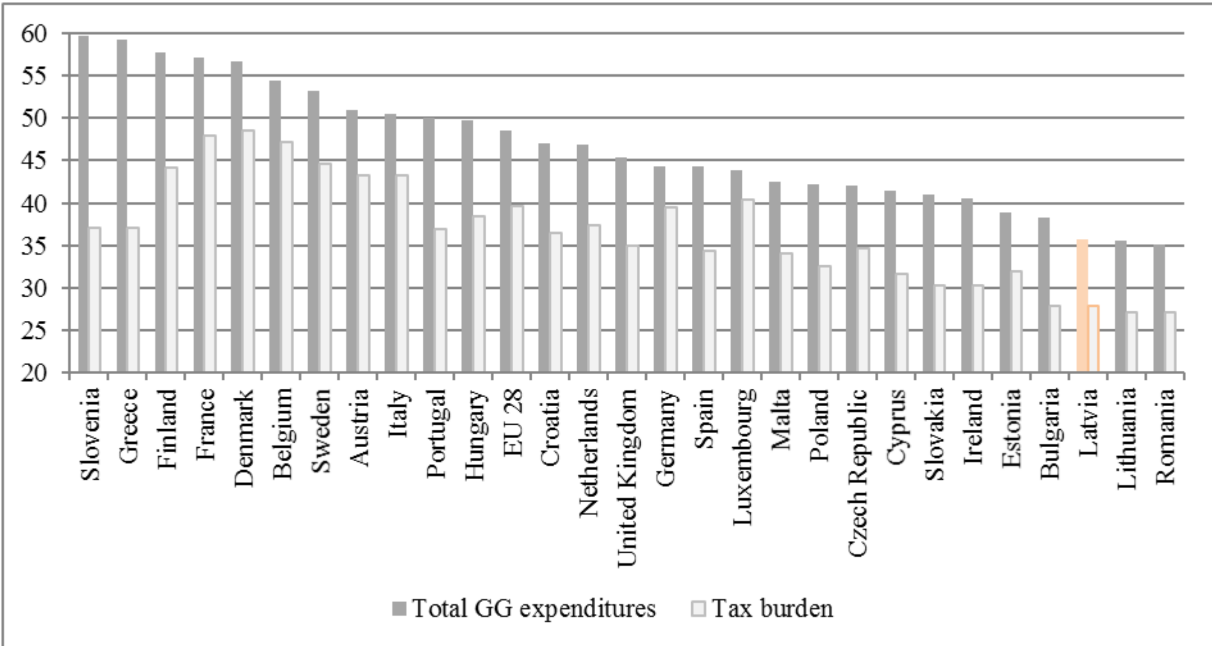

Figure 1. Total general government expenditure and tax burden, 2013, % 0f the GDP, Source: Eurostat

The Latvian tax share to GDP is one of the lowest in EU28 with third lowest tax revenue to GDP ratio bypassing Lithuania and Romania and trailing Bulgaria. The current policies do not offer improvement until 2017. The Council finds that shrinking the tax burden and thus shrinking public spending as a share of GDP embodies risks to the ability to carry out (often basic) public services and public investment in sufficient volumes and quality. Currently EU funds are the major source of funding the public investments, while not all priority projects, e.g. regional roads, are eligible for the EU support and require the resources raised from the taxation.

The tax rates in Latvia are broadly comparable with those in Estonia, which has achieved a tax revenue intake amounting to 32.5% in 2012– close to Latvia's objective, while our revenue outcomes lag behind. Not all of this could be attributed to the effectiveness of the revenue authorities. The impact to large extent comes from much broader tax exemptions and larger economic sectors enjoying these exemptions. For instance, Estonian companies are subject to income tax only in respect of distributed profits. A single personal income tax rate applies to all types of income – all labour and personal capital income (dividends, interests, capital gains, royalties, etc.).

Moreover, the draft budget for 2015 and the 2016-2017 budget framework does not outline effective measures for progress towards achieving the revenue target. The measures for fighting the shadow economy very unlikely would achieve the revenue target without further elimination of loopholes in the tax laws and reduced tax rates. Furthermore, broadening the tax base and rate increases should have been considered to strengthen the fiscal position and to counter the challenges the country faces – improved social and human security, the need for better education outcomes, infrastructure, and business environment.

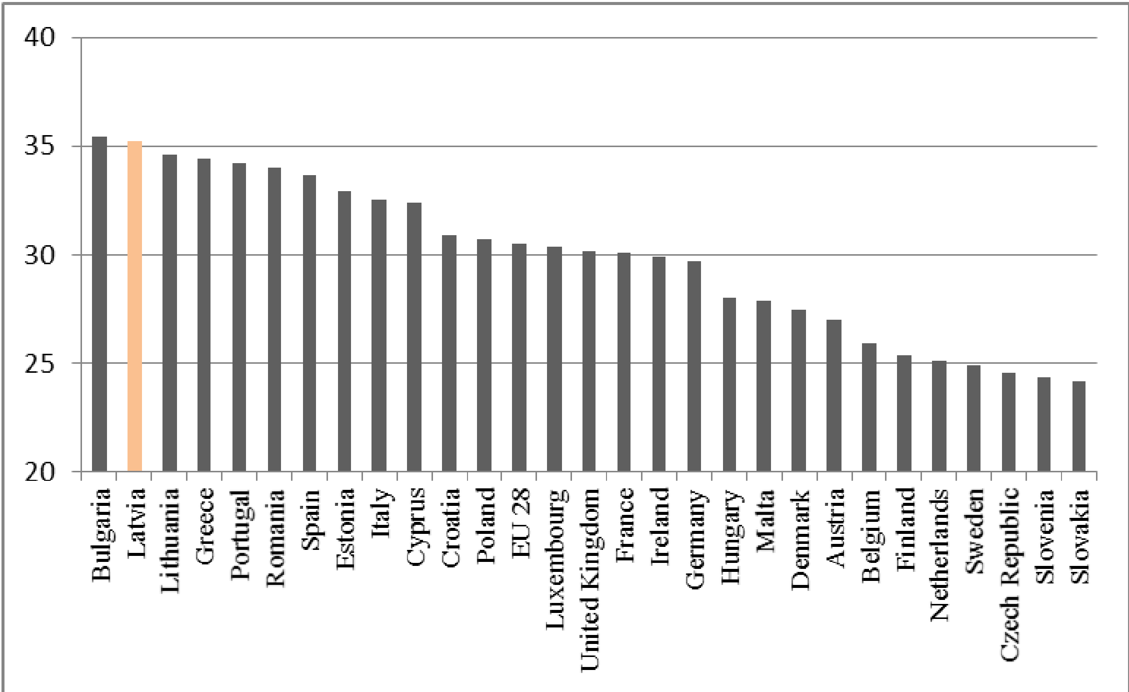

Figure 2. Gini coefficient, EU28, 2013, Source: Eurostat

Income inequality in Latvia (see chart above providing a comparison of Gini coefficients in EU countries) is one of the highest in EU28. High income inequality may have negative implications for the growth potential of the economy (via lack of adequate skills, poor health,

emigration etc.) and thus for income growth and improvements of standards of living. To address this, tax policy has been geared towards reducing payroll taxes, especially for those with lower incomes where the labour tax wedge has been particularly high. *Eurostat* has assessed that the payroll tax burden in Latvia is by 6 percentage points lower than the average in the EU, while the tax wedge for the workers receiving salaries at the level of 67 percent of the average salary exceeds the average in the EU by 6.4 percent. The Council does support the policy choice of reducing payroll taxes, yet we see that the scheduled lowering of the labour tax wedge over the medium term budget of 2015 – 2017 could be geared more towards raising tax exempt minimums and similar measures (to support those with lower incomes and support elimination of the so-called “envelope wages”) rather than straightforward reductions in the flat personal income tax rate.

The Latvian tax system is particularly lenient towards the taxation of capital. Property tax revenues in Latvia in relation to GDP in 2012 of 0.9 % were well below the EU28 average of 2.3 % according to Eurostat (*http://ec.europa.eu/taxation_customs/resources/documents/taxation/gen_info/economic_analysis/tax_structures/2014/report.pdf*).While maintaining low tax rates on productive capital, taxation of fixed assets used for consumption, including housing, should be considered at higher levels to promote efficiency in the resource allocation. Revisions to the property taxation have been rejected on the grounds that the cadastral values have come out of line with the market values for the properties and some vulnerable groups of population dwelling in the areas of high cadastral values would be hurt particularly hard in case of increases of tax rates. IMF has recommended to consider increasing the tax burden on properties as having lesser impact on economic growth. (*http://www.imf.org/external/pubs/ft/scr/2014/cr14115.pdf*)

To counteract such risks, the Council suggests the government to consider:

1. Formulate tax policy strategy by the time of preparing the Stability program for 2015-2018 allowing the government to achieve its set objective of reaching tax revenue ratio of 1/3 to GDP by 2018.

2. Consider broadening the tax base, especially VAT, while the support to vulnerable groups of population could be provided through specifically targeted social assistance schemes, which should be devised and implemented simultaneously.

3. The Council would encourage tightening the legal provisions with the objective of reducing the “shadow” economy more effectively.

4. Consider eliminating all tax exemptions. Simplification of the tax system through reduced number of different rates and exemption rules could support more efficiency in the operation of the State Revenue Service.

5. Consider replacing the reduction in the personal income tax with the increase in non-taxable minimum income to reduce the tax wedge of low paid workers, encouraging legalization of employment and reducing income inequality. The Council supports the plans for the progressive tax-exempt minimum income.

6. Consider increasing property taxes in conjunction with the revision of cadastral values as a measure of increasing equity in the income distribution. Long-term residents in

locations with high cadastral values of properties (when objectively needed) should be allowed to capitalize the increment of increased property taxes, which could be settled later during the transfer of the property title (either due to inheritance or sales).

7. Consider shifting some public services to the private sector and therefore have a clear strategy for lowering public expenditures in the medium term: e.g., research the possibility of using more targeted tools to support specific groups of the society and thus raise the efficiency of the existing support tools.

6. Assessment of fiscal risks and the adequacy of the Stabilization reserve

The Council has made assessment of the Declaration of Fiscal Risks as approved by the Cabinet of Ministers on 10 November. The Government has the responsibility for a comprehensive assessment of the fiscal risks and the requirements for setting up a separate reserve in the budget to counter the risks.

The government assesses a fiscal risk emerging in case, if there is probability of the fiscal aggregates substantially depart from those included in the approved annual budget and budget framework.

The Council understands that the Constitution (Satversme), the FDL, and the Budget and financial management law determine key legal boundaries for the budget management, including the legal responsibilities of officials ensuring that no commitment of budget funds happens without explicit budget authorization. This assumes that:

- The Cabinet has arrived responsibly to the key projected amounts in the macroeconomic framework, and realistically assessed the budget revenues and expenditures,
- No increases in the budget expenditure or reduction in revenue may occur without offsetting compensation by additional revenue or reduction on other expenditure, and
- Budget managers ensure responsible assumption of commitments not exceeding appropriations authorized by law.

FDL assumes that the risks are quantified to the extent possible and a Fiscal Safety Reserve is established to compensate for the impact on the general government fiscal balance. The transitional clauses of FDL assume that the Fiscal Stability Reserve would not be established for 2015, the reserve would be established in the amount of 0.1% of GDP in 2016 and the reserve would be estimated based on the assessed risks for 2017.

The government estimate suggests that the fiscal risks in 2017 and associated required allocations to the Fiscal Safety Reserve would be limited to the following:

- 3.6 million euros for the balance of loan guarantees issued to 14 state corporations based on the assessment of outstanding amounts;
- 0.9 million euros for the balance of government loans repayment risks related to 11 borrowers in the education, waste recycling, transportation, not including local governments, where the loan recovery risk has been assumed nonexistent;
- Not assessed – for the direct and indirect exposure to the agreements on public-private partnerships (further – PPP) and concession agreements as the data has not been centralized on PPPs concluded before the effectiveness of the law on PPPs and concession agreements from 2009, while no such agreements have been concluded since the effectiveness of the PPP Law;
- Not assessed – for the corporations with state capital classified to the general government sector because the government estimates their financial results are already a component for the general government fiscal balance, therefore in case of change,

the impact on the general government balance should be recorded instead of separate risk assessment;

- Not assessed – for the penalties awarded or other expenditure ruled by international courts or the Constitutional Court (Satversmes tiesa) because of unpredictability, while some risks associate with substantial claims;
- Not assessed – for the social insurance benefits and pension cost estimates, while substantial risks of underestimating separate benefits exist;
- Other risks, where the probability of occurrence is negligible.

The Council has assessed the fiscal risks under the assumption that the Fiscal stability reserve is not formed for 2015 and the allocation for the reserve for 2016 is established in the amount 0.1% of GDP in line with the FDL. Meanwhile, the Fiscal stability reserve for 2017 should be formed according to the risk assessment.

Meanwhile, the challenging circumstances may result into deviations from the original assumptions. 2014 has experienced added pressures on the government to finance additional expenditure for agriculture to mitigate the African swine fewer as well as compensating farmers for the consequences of the Russia's trade sanctions targeting major food stapes that have led to major market distortions in Latvia. The Council expects that addressing such adverse events could be normally financed from the Emergency Reserve of the government or budget shifts from expenditure categories with lesser priority. The public information on implicit government obligations to counter such emergencies is not clear, especially, where the public should acquire adequate insurance to protect their properties and businesses from risks.

The Council finds that the risks associated with the operation of corporations with state capital substantial, especially taking into account that the monitoring of operations of these corporations is not always sufficient by respective line ministries. This specifically concerns the lack of forward warning of actions of these corporations that may cause substantial impact on the general government fiscal balance.

The Council has conducted a survey of the Social insurance budget expenditure performance over 2008-2013 against the originally adopted budgets. In consultation with the authorities of the Ministry of Welfare and the State social insurance agency it has been determined that the impact of policy changes influencing the number of beneficiaries and the average amount of pensions or benefits should be adjusted to ensure comparability of the data. Policy decisions are usually made by decision of the Cabinet with full responsibility for evaluating the fiscal impact of such changes.

Table 3. Deviation of actuals from budgeted for the social insurance budget by fund, excluding policy measures adopted during the fiscal year

	2008	2009	2010	2011	2012	2013
Employment	-10.50	-61.24	41.44	43.39	7.20	-5.19
Disability, maternity, sickness	-40.90	16.17	6.16	23.75	15.06	-9.29
Work injury	-1.16	-1.15	-1.98	-2.66	-0.35	-0.78
Pensions	-17.31	38.25	-9.96	-8.44	-21.82	-20.92
Total millions LVL	-69.87	-7.97	35.65	56.04	0.10	-36.18

Total millions EUR	-99,42	-11,35	50,72	79,73	0,14	-51,48
Total as Share to GDP	-0,41%	-0,06%	0,28%	0,39%	0,001%	-0,22%

The assessment indicates that the budget overruns for the reasons not related to the policy changes adopted during the fiscal year in three out of the past six years. The average expenditure in excess of the originally approved budget has been 0.23 percent and the probability of occurrence of such risk is 50 percent. This would require estimating the associated allocation to the Fiscal stability reserve for 2017 in the amount of 0.115 percent – equivalent of 32.8 million euros. The Council would support establishing the Fiscal stability reserve for 2017 in this amount, while the amount of the reserve could be corrected, if the performance of the pension and social insurance benefit expenditure improves against the appropriation in 2014 and forthcoming years.

In regard to the fiscal risks declaration the Council recommends the following:

1. Accept the fiscal risks declaration assessed by the Government.

2. Provide adequate information to the public and encourage businesses and households acquiring adequate insurance to counter the fiscal risks associated with the natural calamities and business risks.

3. Improve the management of risks associated with the corporations classified to the general government sector to ensure receiving timely information regarding their actions that may cause impact on the fiscal balance.

4. Consider estimating the Fiscal stability reserve for 2017 in the amount of 37.3 million euros or equivalent of 0.13 percent of GDP.

5. Local governments' deficits are expected to be close to zero from 2016 onwards although historically there has been a substantial deficit. The Council sees significant risks that such deficits are likely to be higher, e.g., close to past averages.

7. Abbreviations

EU	European Union
FDL	Fiscal discipline law
FM	Ministry of Finance
GDP	Gross domestic product
IMF	International Monetary fund
NPI	new policy initiatives
PIT	private income tax
VAT	value added tax