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Budgeting in Bulgaria

by
Ian Hawkesworth, Richard Emery, Joachim Wehner *and* Kristin Saenger*

Bulgaria's budget management has seen a series of structural and procedural reforms, including in budget execution, treasury functions, internal audit, and programme and medium-term budgeting. This article discusses the use of modern budgeting techniques in Bulgaria such as top-down budgeting, multi-year budgeting perspectives and the use of performance information in the budget process, and makes recommendations for budget formulation, the role of Parliament, budget execution and management (including organisational questions and the role of municipalities), and accounting and audit.

* Ian Hawkesworth is an Administrator in the Budgeting and Public Expenditures Division, Public Governance and Territorial Development Directorate, OECD. Richard Emery is former Assistant Director for Budget Review, United States Office of Management and Budget. Joachim Wehner is a Lecturer in Public Policy at the London School of Economics. Kristin Saenger is an Economist at German Technical Cooperation (GTZ).

Preface

This review of the Bulgarian budget procedure was carried out as part of the work programme of the OECD Working Party of Senior Budget Officials. Budget reviews serve as a basis for the examination of the budget procedures of countries during the annual meetings of the senior budget officials from Central and Eastern Europe and enable the officials to discuss countries' budget procedures in depth. German Technical Cooperation (GTZ) is gratefully acknowledged for its contribution to the review.

A mission consisting of Mr. Ian Hawkesworth (Lead, OECD Secretariat), Mr. Dick Emery (Consultant), Dr. Joachim Wehner (London School of Economics) and Dr. Kristin Saenger (German Technical Cooperation) visited Sofia in February 2009 to carry out the review. During its visit the mission met with: Minister of Finance Dr. Plamen Oresharski; Deputy Minister of Finance Mr. Lyubomir Datzov; Budget Director Mr. Dobrin Pindjurov; and Senior Expert Mr. Iani Gueorguiev Ivanov; as well as a number of other senior Bulgarian officials of the Ministry of Finance and other ministries, the Parliament, and the National Audit Office.

The mission would like to express its gratitude and appreciation for the cordial reception by the Bulgarian authorities and the frankness and openness that characterised the discussions with all Bulgarian officials. Finally, the mission would like to thank Deputy Minister Mr. Lyubomir Datzov, Budget Director Mr. Dobrin Pindjurov and Senior Expert Mr. Iani Ivanov from the Ministry of Finance for the excellent organisation of the meetings, the unsparing help with the collection of information, and the hospitality during the mission's stay in Sofia.

The views expressed in this report are those of the OECD Secretariat and should not be attributed to any organisation or individuals consulted for this review.

1. Introduction

1.1. Recommendations

The Bulgarian budget preparation process is moving in a modernising direction. The procedure used for the 2009 budget exhibits many of the modern budgeting techniques found in OECD countries, such as top-down budgeting, multi-year budgeting perspectives, and the use of performance information in the budget process. Thus the real challenge for Bulgaria is to make these practices and procedures work by implementing them effectively and thoroughly. While there is no doubt that this process is under way, there are a few adjustments that should be considered:

- There has been progress in Bulgaria in making the budget more comprehensive of public activity. The overall goal should be to integrate all of the remaining separate budgets within a consolidated budget for the country. The extrabudgetary funds, state-sponsored enterprises, social insurance funds and autonomous budgets should all be integrated into the budget to enhance the transparency and public understanding of the budget.

- The programme budget format has been rolled out across all central government ministries, which is a major accomplishment. However, the traditionally used classifications and the new programme classification currently compete for attention. To some extent, the State Expenditure Directorate still regards the new format as a parallel system run by the Budget Directorate. In the medium term, the appropriations approved by Parliament should be put on a programme basis. For this to work, there must be a manageable number of carefully defined programmes in each ministry.
- Line ministries have produced a large number of performance targets that are attached to programmes. The number of targets is much too high to enable finance directorates in line ministries, as well as the Ministry of Finance and Parliament, to use this information systematically in budgetary decisions. The quality of performance information needs to be strengthened. Each first-level spending unit should have a small number of high-quality performance measures. Whether to focus on output or outcome measures should be carefully discussed, since both have advantages and disadvantages. While a clear link to outcomes is desirable, output-based performance measures are easier to define and their achievement easier to attribute for accountability purposes, which cautions against a premature move to outcome-based measures.
- The Bulgarian government should consider consolidating budget functions under one deputy minister in the Ministry of Finance. Having a single deputy minister with the lead responsibility for budgeting should simplify budget direction. The functions of some of the specialised directorates could be modified to focus on policy direction and shifting interaction with line ministries to a consolidated programme expenditure staff consisting of "key account managers". As Bulgaria moves toward programme and performance budgeting, it will make sense to integrate operating and investment budgeting on a programme basis. Similarly, as privatisation is finalised, programme review for state-sponsored enterprises and autonomous budgets could be integrated on a programme basis. Review of programmes administered by local governments should be consolidated with related centrally funded programmes, such as education or transport.
- Streamlining interaction with the line ministries with special "key account managers" would also help the Ministry of Finance support and upgrade the line ministries' central finance directorates. Just as a strong Ministry of Finance is conducive to the running of a prudent fiscal policy, so is a strong central finance directorate in line ministries conducive to sound budgeting and financial management practices in ministries and agencies. With a reformed budget process and the use of multi-year budget perspectives, top-down budgeting and the introduction of performance and programme budgeting, it is of paramount importance that the line ministry finance directorates are strong and relevant hubs in the working of the budget system. The overall structures and principles appear to be the right ones, but the true test of the practices lies in their implementation.

The Bulgarian Parliament (the National Assembly) has a role in the budget process perhaps similar to less active parliaments in the group of budget-influencing legislatures described below. Although members generate a number of amendment proposals, most of these have limited influence on the composition of the budget and fiscal policy. As long as the government has a secure majority, the National Assembly approves the budget with minimal changes.

The Budget and Finance Committee has an important role in the legislative budget process. Its review of the amendment proposals generated by sectoral committees and members sets the agenda for the discussion on the floor of the National Assembly. The committee exerts a disciplinary role and helps to contain pressures for spending increases during the parliamentary stage. Overall, the approval process is fairly effective, but there is potential for improvements in several areas:

- Parliamentary approval of expenditures is at a highly aggregated level. Moreover, the executive has substantial flexibility to adjust outlays during the fiscal year. In a number of OECD and non-OECD countries, legislatures approve the budget on a programme basis. The adoption of this approach in Bulgaria would create incentives for parliamentarians to scrutinise programme-level expenditures. As a result, line ministries would have to give a more central role to programmes and the associated performance information during the formulation process.
- The process for the judicial budget appears to be experiencing problems. In one-third of OECD countries (10 out of 30), the judiciary prepares its budget independently and its proposal is included in the draft budget without any changes by the central budget authority. In Bulgaria, there appears to be strong and persistent disagreement about the funding levels for the judiciary. Parliament may consider setting up an *ad hoc* cross-partisan committee to investigate the issue and to arrive at a more informed view on the current funding level for the judiciary.
- The Bulgarian Parliament does not have access to independent budget analysis capacity. A number of legislatures in OECD countries have created budget research offices which can support members with independent analytic work and contribute to transparency and accountability in the budget process. In particular, if the Bulgarian Parliament chose to strengthen its engagement with programme-level information, it might benefit from access to specialised policy and budgeting expertise.
- The duration of the parliamentary approval process does not comply with the "OECD Best Practices for Budget Transparency" (OECD, 2002), which stipulate that the legislature should receive the budget proposal no less than three months prior to the start of the fiscal year. It may be appropriate to extend the time available to the Bulgarian Parliament for its scrutiny of the budget.

Bulgaria's budget management has seen a series of structural and procedural reforms in budget execution, treasury functions, internal audit, and programme and medium-term budgeting. The assessment of the Ministry of Finance is that these reforms have resulted in stronger controls of budget aggregates and more delegation of budget details. Budget control, evaluation, and programme assessment and auditing still require attention:

- Budget execution in Bulgaria remains focused primarily on the legality and propriety of budget inputs. The culture of bureaucracy has not embraced a management focus on programme performance and results. As the programme budget is implemented, steps should be taken to shift greater responsibility for budgets to programme managers, and to reduce centralised control. Budget reporting will need to highlight programme results to a greater extent.
- The cash and debt management practices of Bulgaria reflect good practice principles. Efficiencies may be possible by including municipal finance in the treasury single account (TSA) system and the System for Electronic Budget Payments (SEBRA), rather than having municipalities develop their own cash management tools, but improved efficiency could involve a perception of the loss of local control.

- Strengthening the management culture within the line ministries is essential to greater accountability for programme performance. More planning is needed to tie personnel to performance. The changes in personnel compensation providing more discretion to spending units appear to be a step in the right direction, but emphasis should be increased on performance-related compensation.
- As the leaders of the Internal Control Directorate acknowledge, the transition to the distributed internal control system has been difficult. But it appears that the government of Bulgaria is taking appropriate action. Regular meetings with the heads of internal audit units in ministries are providing valuable input and creating a sense of ownership among the internal audit community. Substantial effort is being devoted to training. Consideration should be given to establishing consolidated internal audit offices for groups of smaller municipalities to insure that the offices are large enough to be effective.
- The accounting and internal audit reforms appear to be well designed; the challenge is in the implementation. Internal audit will require some time to further train the customers and the internal audit professionals to understand their respective roles. Continued collaboration between the National Audit Office and the internal auditors should result in improved public service for Bulgaria.

1.2. Fiscal performance and background information

Bulgaria, a former Communist country that entered NATO in 2004 and the EU in 2007, is located in southeast Europe, bordering the Black Sea, between Romania and Turkey. It is a parliamentary republic. The government is the main locus of executive power. After the parliamentary elections in June 2005, a coalition was formed with the former communist Bulgarian Socialist Party (BSP), the National Movement for Stability and Progress (NMSP), and the Movement for Rights and Freedoms (MRF). The centre-left governing coalition was headed by the Prime Minister, Sergei Stanishev, who is also leader of the BSP. New parliamentary elections were held in July 2009, and the centre-right party Citizens for European Development of Bulgaria (GERB) won the majority of seats. The new coalition is headed by Boyko Borisov, leader of the GERB party. The head of state is the president, who is directly elected every five years for a maximum of two terms. Georgi Parvanov, a previous leader of the BSP, won a second term as president in an election in November 2006.

By July 2009, the Bulgarian population was estimated at 7 204 687. Bulgaria is a predominantly urban society, with 70.6% of the population living in towns at the end of 2006. According to official statistics, less than one-third of the population lives in the three cities with more than 300 000 inhabitants – namely Sofia (1.15 million), Plovdiv (342 000) and Varna (312 000) (EIU, 2008). These larger towns are more affluent than most of the smaller ones, and there is also a contrast between the relatively poor northern part of the country, which mainly borders Romania, and the wealthier southern and coastal regions, which border the Black Sea, Turkey and Greece.

Bulgaria has experienced strong growth since a major economic downturn in 1996. Successive governments have demonstrated commitment to economic reforms and responsible fiscal planning, but have failed so far to rein in rising inflation and large current account deficits. For most of the period since 1996, output growth has been propelled by domestic demand. Investment has grown rapidly, but consumer spending has also grown strongly. The need to curb the increase in the current account deficit prompted the government to achieve a balanced budget in 2003 and, since 2004, strong budgetary surpluses. These have relied more on increased revenue due to better performance, rather than on spending cuts. Bulgaria has averaged more than 6% growth since 2004, attracting significant amounts of foreign direct investment. As seen in Table 1, Bulgaria has thus been able to reduce its general government consolidated debt as a percentage of GDP from 79.6% in 1998 to 14.1% in 2008, in marked contrast to the trend in EU and euro area countries.

Table 1. **General government debt: general government consolidated gross debt, as a percentage of GDP**

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Bulgaria	79.6	79.3	74.3	67.3	53.6	45.9	37.9	29.2	22.7	18.2	14.1
EU27	66.5	65.9	61.9	61.0	60.3	61.8	62.2	62.7	61.3	58.7	61.5
Euro area	72.8	71.5	68.7	68.4	68.2	69.3	69.7	70.4	68.6	66.2	69.6

Source: Eurostat (2009), *Eurostat Statistics Database*, Statistical Office of the European Communities, Luxembourg, *http://epp.eurostat.ec.europa.eu*.

When GDP per head is measured in terms of purchasing power parities, Bulgaria ranks ahead of only Romania among the 27 members of the EU.

A rise in the importance of services whose share in gross value added increased from 29.5% in 1989 to 62% in 2007 reflects a growth in this sector towards a modern, services-oriented economy as well as a decline of industry. These official figures ignore a thriving but unrecorded grey economy, the size of which is usually estimated at 20-30% of recorded GDP.

Table 2. **Real gross domestic product by sector, as a share of GDP**

	2003	2004	2005	2006	2007
Agriculture	11.7	11.0	9.4	8.5	6.3
Industry	29.1	29.2	29.4	30.9	32.3
Services	59.1	59.8	61.2	59.5	61.8

Source: Economist Intelligence Unit (2008), *Country Report Bulgaria 2008*, The Economist Intelligence Unit, London.

Foreign direct investment in Bulgaria has grown markedly in recent years and has been high even by the standards of other post-communist European countries. Having gradually moved away from its concentration on sales to former Soviet states, Bulgaria's trade is now predominantly directed towards OECD countries and, above all, to the EU, whose 26 other members accounted for 61% of all exports and 52% of all imports in the first 11 months of 2007.

High unemployment has been a significant social problem, but the unemployment rate has fallen steadily in recent years. At the end of 2007, the registered unemployment rate stood at 6.9%, down sharply from the rate of 14.3% recorded in 2003. However, employment growth is expected to turn negative in 2009-10, and the unemployment rate is expected to be close to 8% by the end of 2010.

In February 2007, the European Commission announced immediate and wide-ranging suspensions of pre-accession funding to Bulgaria, amid corruption concerns. In May 2008, the government appointed a new Deputy Prime Minister with responsibility for overseeing the administration of EU funds, and more anticorruption efforts are under way.

Table 3. **Unemployment rate in Bulgaria**

	1992-2004	2005	2006	2007	2008	2009	2010
Unemployment rate (Eurostat definition)	15.1	10.1	9.0	6.9	5.6	7.3	7.8

Source: European Commission (2009), "Economic Forecast – Spring 2009", *European Economy No. 3/2009* (May), Office for Official Publications of the European Commission, Luxembourg, doi: *http://dx.doi.org/10.2765/80609*, *http://europa.eu*.

Under the currency board scheme, where the Bulgarian lev is pegged to the euro, foreign exchange reserves at the Bulgarian National Bank (BNB) must cover at least 100% of base money. Controls on the money supply and on credit expansion are therefore tight. Overall, the currency board has proved successful in stabilising the economy.

Bulgaria's transport infrastructure is reasonably well developed but needs further investment. Improvement in communication routes should result from two factors: first, the development of European transport corridors (four of which are set to pass through Bulgaria); and, second, investment aided by an influx of EU funds, with EUR 6 billion to be invested in transport under the infrastructure programme for 2007-15. EU funds can play an important role in Bulgaria's development during the economic crisis, and it is important that available resources be utilised – not only because in the current environment they are one of the few remaining external financing sources, but also because high utilisation would boost the confidence of foreign investors.

1.2.1. The state of public finances at the beginning of 2009 and the road ahead

The general government surplus reached 1.5% of GDP in 2008, a result clearly affected by the financial crisis. However, for 2008 as a whole, real GDP grew by 6%, supported by still robust domestic demand. Since the beginning of 2009, economic sentiment and confidence indicators have deteriorated further, in line with the unfolding global economic crisis. This situation, together with falling industrial production and retail sales, points to a sharp slowdown ahead. Driven by weaker external demand and subdued credit growth, exports and domestic demand are expected to deteriorate significantly. For the first time since 1997, real GDP is projected by the European Commission to contract by around 1.5% in 2009 and to stagnate in 2010 (see Table 4). The IMF expects the Bulgarian economy to contract by around 3.5% in 2009 and 1% in 2010. The Economist Intelligence Unit (EIU, 2009), which is in line with the IMF for 2009, forecasts that real GDP will contract by 3.8% in 2009, but expects a modest rebound to 0.7% in 2010.

Despite the expenditure-reducing contingency buffer in the budget, the European Commission projects that the general government budget balance will deteriorate, resulting in a deficit of 0.5% of GDP in 2009 followed by a deficit of 0.3% in 2010. The EIU expects a

Table 4. **European Commission economic forecast for Bulgaria**

	1992-2004	2005	2006	2007	2008	2009	2010
GDP at previous year prices, annual percentage change	0.9	6.2	6.3	6.2	6.0	–1.6	–0.1
General government balance as a per cent of GDP	–	1.9	3.0	0.1	1.5	–0.5	–0.3
Current account balance as a per cent of GDP	–3.8	–11.5	–18.6	–22.5	–24.8	–18.8	–17.2
Structural budget balance as a per cent of GDP	–	1.0	1.9	2.0	0.2	0.3	1.6
General government gross debt as a per cent of GDP	–	29.2	22.7	18.2	14.1	16.0	17.3

Source: European Commission (2009), "Economic Forecast – Spring 2009", *European Economy No. 3/2009* (May), Office for Official Publications of the European Commission, Luxembourg, doi: *http://dx.doi.org/10.2765/80609*, *http://europa.eu*.

budget deficit of 1.5% in 2009. Much depends on the economic performance of the world economy and the EU area which is very uncertain and could lead to higher-than-expected revenue shortfalls. The European Commission expects the public debt level to increase to just above 17% of GDP in 2010.

As monetary policy is constrained by the fact that the lev is tied to the euro, the emphasis falls on fiscal policy to keep the economy on track. The 2009 consolidated budget targets a surplus of 3% of GDP, the same as was recorded in 2008, but allows for a narrowing to 1% of GDP in recognition of the government's aim of supporting the economy in the worsening economic climate. However, actual tax revenues depend on economic performance, which is looking bleak. According to the budget law, the government can easily restrict the implementation of the budget to 90% of what is appropriated, as discussed below. However, according to the IMF, the original 2009 budget – which envisaged 16% tax revenue growth – was too optimistic. The IMF suggests that if a surplus in 2009 is to be achieved, expenditures need to be cut further.

On the positive side, it should be noted that the IMF holds that Bulgaria has been shielded from some of the problems associated with the global financial crisis thanks to larger cushions and prudent policies (IMF, 2009). The banking system has remained stable and capital has been further increased without government money. The sharp exchange rate depreciations and associated private sector balance sheet pressures experienced by countries in the region with flexible exchange rates have been absent in Bulgaria. In addition, Bulgaria has entered the current downturn with strong buffers – the result of prudent policies during the boom years. The public finances are in surplus and the balance sheets of the central bank and the government are strong with considerable foreign reserves and substantial buffers accumulated in the fiscal reserve account.

2. Budget formulation

This section focuses on the budget formulation process and the issues surrounding it. The section begins by describing the public finance system, including the structure of the budget. The annual budget process is then described in detail followed by a description of the development of macroeconomic assumptions and the introduction of a programme budget structure as well as the initiatives to secure long-term fiscal sustainability. The section ends with a discussion of the internal organisation of the Ministry of Finance.

2.1. Design of the public finance system

The Consolidated Fiscal Programme (CFP) covers the state budget, local authority budgets, the budgets of the two social funds, and a number of extrabudgetary funds and accounts, and is similar to the GFS concept of general government (government finance statistics; see IMF, 2001). Figure 1 summarises the overall structure; the corresponding main aggregates for the 2008 fiscal year are shown in Table 5.

In addition to the state budget, there are several autonomous budgets, which accounted for 8.8% of GDP in 2008. The budgets of the 264 municipalities constitute most of the expenditures in this category (7.5% of the 8.8%). The remainder is made up of spending in other autonomous budgets, which cover the Bulgarian Academy of Science, state universities, Bulgarian National Radio and Bulgarian National Television. Local governments play a relatively minor role in the overall fiscal structure.

Figure 1. **Components of the Consolidated Fiscal Programme (*i.e.* general government)**

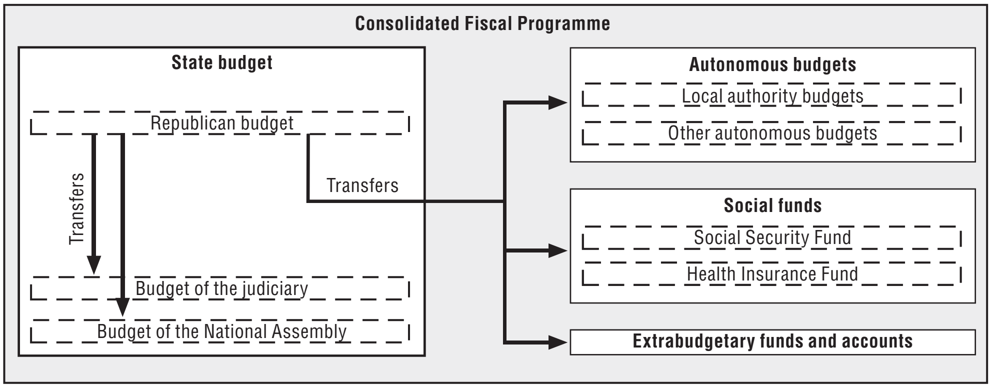


Table 5. **Total expenditures in the Consolidated Fiscal Programme[1] (2008)**

	Expenditure as a per cent of GDP
The state budget	15.5
The republican budget (line ministries, etc.)	*14.8*
The judiciary	*0.6*
The National Assembly	*0.1*
Autonomous budgets	8.8
Municipal budgets	*7.5*
Other autonomous budgets	*1.3*
Social security expenditures	9.7
Pensions	*8.4*
Social assistance	*1.1*
Employment-related assistance	*0.2*
Health insurance expenditures	2.5
Extrabudgetary funds and accounts	1.4
General government expenditure	37.9

1. State budget subsidy to social security: 41.6% of the total expenditure. State budget subsidy to national health insurance: 12.2% of the expenditure of the National Health Insurance Fund.

Source: Bulgarian Ministry of Finance.

The National Social Security Institute (NSSI) administers the mandatory insurance programmes for disability, old-age and survivors' benefits, sickness and maternity, work injuries and occupational diseases, as well as control and information services for citizens. In 2008, the expenditures administered by the NSSI amounted to 9.7% of GDP, most of which concerned pensions, while social assistance and employment-related assistance received small shares. From January 2009, the transfer for pensions from the state budget is 12% of the sum of all insured income of the insured persons for the relevant year. Costs have been increasing due to the ageing of the population and to adjustments to the annual cost-of-living indices.

The Health Insurance Fund provides for primary non-hospital medical care, specialised non-hospital medical care, hospital medical care, medicines and medical products for home treatment. The Health Insurance Fund has territorial divisions that consist of 28 regional funds. Health insurance premiums are financed by employers (60%) and employees (40%). The public sector is the principal health provider in Bulgaria; private health coverage is limited. In 2008, the expenditures of the Health Insurance Fund accounted for 2.5% of GDP. With an ageing society in Bulgaria, medical expenditures are increasing and, at the same time, there is a reduction in the number of contributing taxpayers. The hospital system is inefficient due to a number of reasons, such as unused capacity and hospital mismanagement resulting in arrears. The capacity issues are being addressed, for instance by consolidating hospitals and shifting responsibility for payments directly to the National Health Insurance Fund.

Budgeting for social security and national health insurance is on a pay-as-you-go basis. The systems are handled, respectively, by the NSSI and the National Health Insurance Fund on the basis of the general rules and guidelines for the preparation and implementation of the state budget as specified by the Ministry of Finance. The funds are autonomous budgets and have direct sources of revenue. Subsidies to the funds are included in the state budget as lump-sum transfers. The Law on the Budget of the State Social Security and the Law on the Budget of the Health Insurance Fund are approved separately from the state budget of the Republic of Bulgaria.

There are also a number of extrabudgetary funds and accounts, which amounted to 1.4 % of GDP in 2008. At the national level, there are: a fund for covering privatisation costs of the Privatisation Agency; the State Agricultural Fund; the extrabudgetary account of the National Fund for EU Resources under the control of the Minister of Finance; the Teachers' Pension Fund; and the Enterprise for the Management of Environmental Protection Activities. At the municipal level, extrabudgetary funds and accounts include: a special account for receipts from the privatisation of municipal enterprises; a fund for covering the costs of privatisation and post-privatisation control; and a special fund for investments and fixed assets. The number of extrabudgetary funds and accounts has been reduced over the past decade to the present eight.

Some of the extrabudgetary funds or accounts exist to manage funding from the European Union (EU). The extrabudgetary account of the National Fund was set up to ensure that co-financing requirements for the receipt of structural and cohesion funds from the EU are met. The National Fund within the Ministry of Finance is a central treasury authority responsible for transferring European Community funds to the respective beneficiaries.

The State Agricultural Fund was to act as the payment agency for EU agricultural subsidies. The European Commission suspended funding worth almost half a billion euros for a number of programmes in 2008, due to concerns over maladministration and corruption.

2.2. The annual budget process

The annual budget preparation process has three main stages:

- Development of a medium-term fiscal framework (MTFF) – an aggregate fiscal plan.
- Development of a three-year budget framework with expenditure ceilings for the line ministries (first-level spending units or FLSUs, excluding municipalities).
- Elaboration of the draft state budget law to be presented to the National Assembly.

The procedure for the preparation of the 2007 budget introduced a number of changes to the budget process. Notably, the first stage did not exist previously and was introduced for the first time for the 2007 budget procedure. The full integration of a procedure on major capital projects into the annual budget process happened in 2009. These capital projects are investment projects which require external or domestic borrowing and/or for which a state guarantee is to be issued.

At the beginning of the year, a decision of the Council of Ministers on the budget procedure sets out the timeline for the preparation, discussion and approval of the three stages listed above. The budget procedure is prepared by the Minister of Finance and submitted for approval in February. The procedure described below reflects the decision of the Council of Ministers on the budget procedure for the 2009 budget.

The **first stage**, which concerns aggregates for all of government, primarily takes place in March and April and involves the preparation of the macroeconomic assumptions and the MTFF. The Executive Agency for Economic Analysis and Forecasting (under the Ministry of Finance) develops a forecast for the main macroeconomic aggregates which the Budget Directorate uses to develop the aggregate state expenditure and revenue estimates. This forecast covers the current fiscal year, the upcoming budget year, and two out-years. On the basis of this information, the Minister of Finance develops and submits to the Council of Ministers an MTFF and main assumptions for the medium term, *i.e.* the upcoming budget plus two out-years. The Council of Ministers considers and approves the MTFF, including the main macroeconomic assumptions, and submits the approved documents to the National Assembly for information. In addition, line ministries develop and present to the Ministry of Finance a list with proposed major new investment projects, *i.e.* those involving borrowing and/or state guarantees.

The MTFF has several parts, including information about: the objectives of the medium-term fiscal plan; the macroeconomic framework; the mid-term economic perspectives; an analysis of fiscal risks; the objectives of economic and fiscal policy; the parameters of the fiscal framework and the major assumptions; the participation of Bulgaria in common EU policies; and an analysis of the long-term sustainability of public finances. An annex to the MTFF contains the aggregate parameters of the Consolidated Fiscal Programme for the respective three-year period. Revenues are broken down by type of tax (direct and indirect), non-tax revenues, and grants and donations. Spending is broken down by non-interest and interest expenditures. Non-interest expenditures include current expenditures (wages and salaries, scholarships, social security payments, maintenance and operations, subsidies, and social and health expenditures), capital expenditures and funds set aside for various contingencies. The MTFF is fully consolidated and comprises all on-budget and off-budget accounts of the government.

The **second stage** of the annual budget preparation process lasts from April to July and involves the preparation of a three-year budget framework. The objective of this framework is that the resources shall be allocated for the national strategic priorities in compliance with the general fiscal objectives and to assure a certain degree of budget predictability for the spending units.

At the end of April, the Minister of Finance issues guidelines to line ministries (first-level spending units, FLSUs) for the preparation of this framework and expenditure ceilings. The ceilings are sanctioned by the Council of Ministers. At the level of the line ministries, the different directorates and second-level spending units (SLSUs) prepare three-year estimates for investments; but for other types of spending, they only prepare figures for the upcoming budget while the figures for the two out-years are prepared centrally in the line ministry finance directorate. During May, the Ministry of Finance compiles a list of the major new investment projects proposed by line ministries and submits this to the Economic Policy Committee of the Council of Ministers for review. By the end of May, the line ministries submit to the Ministry of Finance their three-year budget framework, which includes information on policies and programmes for all line ministries.

Table 6. **Timetable for the formulation of the 2009 budget**

	Action
February	The Council of Ministers issues a decision on the annual budget procedure.
Mid March	The forecasting agency submits its macroeconomic forecast to the Ministry of Finance.
End March	Line ministries submit proposals for major new investment projects to the Ministry of Finance.
Early April	The Ministry of Finance submits the medium-term fiscal framework (MTFF), including the major macroeconomic assumptions, to the Council of Ministers.
Mid April	The Council of Ministers approves the MTFF and major macroeconomic assumptions and submits these to the National Assembly for information.
End April	The Ministry of Finance issues guidelines to line ministries (first-level spending units, FLSUs) for the preparation of the three-year budget forecasts and expenditure ceilings.
Mid May	The Ministry of Finance prepares a list of proposed major investment projects and submits it to the Economic Policy Committee of the Council of Ministers.
End May	The Economic Policy Committee of the Council of Ministers approves the major investment projects.
	Line ministries submit their three-year budget forecasts to the Ministry of Finance.
Mid June	The Ministry of Finance submits to the Council of Ministers the list of major investment projects.
End June	The Council of Ministers approves the list of major investment projects.
June	The Ministry of Finance analyses the three-year budget forecasts and consults with line ministries.
Mid July	The Ministry of Finance submits the three-year budget forecasts, expenditure ceilings and updated government debt management strategy to the Council of Ministers.
End July	The Council of Ministers approves the three-year budget forecasts, expenditure ceilings and updated government debt management strategy and submits these to the National Assembly for information.
	The Ministry of Finance issues guidelines for annual draft budgets to the line ministries (FLSUs).
End August	The line ministries (FLSUs) submit their draft budgets to the Ministry of Finance.
Mid September	The forecasting agency provides an updated macroeconomic forecast.
End September	The Ministry of Finance prepares the draft state budget law.
Mid October	The Ministry of Finance submits the draft state budget law to the Council of Ministers for approval.
End October	The Council of Ministers approves the draft state budget law.
	The draft budget is submitted to the National Assembly.

Source: Bulgarian Ministry of Finance.

Box 1. **Fiscal rules and adoption of the euro**

Bulgaria does not have a legally entrenched fiscal rule and instead relies on coalition agreements to provide the most fundamental guidelines for fiscal policy. Following the 2005 elections, the three largest groupings represented in Parliament signed a coalition agreement that spelled out a number of objectives. The document contained two fundamental fiscal policy rules. The government committed itself to: *i)* maintaining a balanced budget; and *ii)* keeping expenditures within a ceiling of 40% of GDP.

In addition, the Bulgarian government's wish to adopt the euro has resulted in certain fiscal targets. In order to enter the third stage of Economic and Monetary Union (EMU) and adopt the euro, Bulgaria has to meet several convergence criteria. In relation to public finances, the criteria in principle require a general government deficit not exceeding 3% of GDP as well as gross government debt not exceeding 60% of GDP. Every year since 2006, normally by 1 December, Bulgaria prepares its convergence programme and submits it to the European Commission and the European Council. The convergence programme spells out the country's fiscal and economic outlook and is used by the European Commission for the purpose of fiscal surveillance. In the 2008 convergence programme, the government reported full compliance with the EU fiscal criteria (Republic of Bulgaria, 2008, pp. 22-23).

During June, the Ministry of Finance evaluates the three-year budget submissions and holds a series of consultations with the line ministries as well as with the National Association of Municipalities in the Republic of Bulgaria (NAMRB). At the same time, the Ministry of Finance submits the list of proposed major investment projects to the Council of Ministers for final approval, which takes place at the end of June. Based on this information, the Minister of Finance prepares and submits to the Council of Ministers a final three-year budget framework for the government, as well as top-down expenditure ceilings for the medium-term period and an updated or new government debt management strategy.

The three-year budget framework builds on the MTFF by developing medium-term budget estimates for each line ministry. The Council of Ministers considers and approves these items and refers them to the National Assembly for information. The budget framework contains:

- the three-year budget forecast, consisting of updated data on the CFP;
- expenditure ceilings of line ministries (FLSUs), including total, current and capital expenditures and a reserve for the following three-year period;
- expenditure ceilings of the extrabudgetary funds;
- subsidies/transfers to the other autonomous budgets;
- expenditure ceilings of municipal budgets for state-delegated activities (education, health services, social assistance and care, and culture); and
- the updated government debt management strategy.[1]

The **third stage** of the annual budget preparation process takes place from July to October and involves the preparation of the draft annual budget. At the end of July, the Minister of Finance issues guidelines to line ministries for the preparation of draft budgets. The ministers in charge of education and science, health, labour and social policy, transport and culture, together with the Minister of Finance, issue guidelines to municipalities for the part of their budgets that concern state-delegated activities executed by the municipalities. By the end of August, the line ministries (FLSUs) elaborate and present to the Ministry of Finance their draft budgets for the upcoming year plus two additional years. The responsible ministers submit the autonomous budgets, the budgets of the extrabudgetary funds and of the Enterprise for the Management of Environment Protection Activities, and estimates regarding the financial assistance from the EU. Municipalities submit their draft budgets to the Ministry of Finance. At the end of September, the Executive Agency for Economic Analysis and Forecasting updates the forecast for the main macroeconomic aggregates for the current budget year, the upcoming budget year, and two out-years.

In many countries, the judiciary, the external audit body and the legislature have a slightly different budget formulation procedure than line ministries. In one-third of OECD countries (10 out of 30), the judiciary independently prepares a budget, which is then included in the draft budget without changes. In more than half of OECD countries (18 out of 30), the supreme audit institution either submits its proposal directly to the legislature or its budget is included in the draft budget without changes. Finally, the legislature prepares its own budget in almost two-thirds (19 out of 30) of OECD countries.[2] These arrangements grant additional autonomy to oversight institutions and can help to safeguard against politically motivated interference.

Similar arrangements apply in Bulgaria. The State Budget Procedures Act (Article 20) does not allow the Council of Ministers to make revisions to the draft budgets of the judiciary and of the National Audit Office. However, the Council of Ministers may prepare observations and submit these to the National Assembly. Unlike the judicial budget, the budget of the National Audit Office is part of the republican budget (see Figure 1 above), but the procedures do not differ substantively. An amendment to the State Budget Procedures Act (Article 16a) adopted in 2007 also introduced a special procedure for the budget of the National Assembly. The chairperson of the National Assembly must submit a three-year projection of the National Assembly budget and a draft budget disaggregated by programme to the Minister of Finance. The finance minister can submit observations on this draft. Disputes are to be settled between the Prime Minister and the chairperson of the National Assembly. Formally, these procedures are similar to the special arrangements for these bodies in a number of OECD countries.

In past years, there has been substantial conflict over the judicial budget. As a result, the National Assembly has had to decide between two versions of this budget, one prepared by the Ministry of Finance and another prepared by the Supreme Judicial Council. This process is discussed in more detail in the following section. A recent review of judicial public expenditure in Bulgaria carried out by the World Bank (2008) found that judicial resources, staffing and salary levels have increased steadily over the past few years, but highlights a number of challenges in areas such as capital spending, cash management, personnel management and expenditures as well as information technology. The report urges the Ministry of Justice, the Supreme Judicial Council and the Ministry of Finance to further strengthen their collaboration in the formulation of the judicial budget.

By the end of September, the Ministry of Finance finalises the draft of the state budget and comments on the draft budgets of the National Assembly, the Supreme Judicial Council and the National Audit Office. The Minister of Finance holds consultations with line ministries in order to reach agreement on the line ministries' draft budgets. Agreements are finalised in a memorandum for line ministries and a protocol with the local government association (National Association of Municipalities; see Section 4.8 below on municipal budgeting). The consultations are hosted by the Ministry of Finance and mostly happen at the level of vice-minister or director. In some rare cases, the consultations need to be taken to the level of the Minister of Finance and the relevant line minister. All such consultations are stipulated in the annual budget procedure. In cases of serious disagreement, a memorandum with reservations is signed which later goes to the Council of Ministers for final decision together with the draft state budget law.

Based on the revised estimates, all line ministries and state agencies update their draft budgets in programme format and present them to the Ministry of Finance to be included in the documents attached to the draft state budget law. In mid-October, the Minister of Finance prepares and submits to the Council of Ministers the draft state budget law with supporting documents, including programme budgets. The National Social Security Institute prepares the draft law on the social security budget, which the Minister of Labour and Social Policy presents to the Council of Ministers. The management council of the National Health Insurance Fund, through the Minister of Health, submits to the Council of Ministers the draft law on the budget of this fund. Following approval at the end of October, the draft laws are submitted to the National Assembly.

Box 2. EU funding in the Bulgarian budget

A number of EU funds aim to help less-favoured regions in Bulgaria by promoting competitiveness, fostering social cohesion and enhancing Bulgaria's economic performance. The most important funds are the regional and cohesion funds, the European Social Fund and the European Fisheries Fund.

EU funds are the primary resource for investment financing in Bulgaria. In 2009, approximately 30% of total investment funding within the Consolidated Fiscal Programme will be financed by EU funds, corresponding to BGN 1.607 billion (Bulgarian levs) (excluding agriculture and fisheries) or approximately EUR 820 million. Seven line ministry policy areas receive some of this financing. Each line ministry has an EU directorate that works with the Management of EU Funds Directorate of the Ministry of Finance and maintains a direct relationship with the EU.

Within the Republic of Bulgaria, all investments are part of strategic plans. The national development plan 2007-13, the national strategic reference framework 2007-13, and the national strategic plan for agricultural and rural development 2007-13 constitute the most important ones. In addition, Bulgaria develops operational frameworks for its investment programmes.

The investment process is part of the overall budget process which begins with the development of the medium-term fiscal framework. The Management of EU Funds Directorate of the Ministry of Finance outlines a general strategic investment programme. After its approval, a minimum level for investment expenditures is determined, which in 2008 amounted to 8% of total consolidated expenditures. Within given ceilings, and according to EU sector allocations, every line ministry/first-level spending unit is then responsible for developing an indicative annual investment programme containing different projects. Each first-level spending unit co-ordinates its investment activities with the EU, the respective division of the State Expenditure Directorate of the Ministry of Finance, and the Management of EU Funds Directorate. The latter is in charge of the overall co-operation with the EU and the prioritisation of projects according to the previously developed investment plans.

Although the determination of investments is part of the general budget process, only Bulgaria's own revenues used for investment are part of the state budget. EU funds are part of the consolidated fiscal plan. The implementation of all investment projects financed through EU funds is monitored by the Management of EU Funds Directorate in the Ministry of Finance.

The draft state budget law contains the appropriations for the upcoming budget year for each line ministry and other first-level spending units in the republican budget. The draft law includes a classification of the budget by policy and programme over the upcoming three-year period as a separate appendix. In addition, a budget report presents data classified according to the Consolidated Fiscal Programme.

2.2.1. Development of macroeconomic assumptions

The Executive Agency for Economic Analysis and Forecasting (under the Ministry of Finance) develops the macroeconomic assumptions for the budget. Set up in 1991 as the Agency for Economic Co-ordination and Development, this body initially reported to the Council of Ministers. It was later renamed and moved under the authority of the Ministry of Finance, and in 1999 it became an executive agency attached to the ministry. Its status

Box 3. **The Public Finance School**

The Public Finance School (PFS) was established in 2003 as a specialised unit within the Ministry of Finance. The mission of the PFS is to facilitate the creation of modern public financial management in accordance with the requirements for EU membership. The PFS aims to support the implementation of budget reforms and to improve the performance of financial officers through the provision of specialised training for Ministry of Finance officials as well as relevant staff in ministries, agencies, municipalities and other public sector organisations. The PFS training premises are in the building of the Ministry of Finance. The PFS currently has five staff members.

Between 2004 and 2008, the PFS conducted more than 200 training events with a total of over 6 000 officials. Most of the training has been on budgeting and financial management, with an increasing emphasis on internal control and the management of EU-funded programmes and projects. The trainers are practitioners with significant professional experience. The PFS has benefited from a close relationship with the Dutch Ministry of Finance which supported the development of its programmes. The PFS also interacts with a number of international organisations and training bodies, including the Center of Excellence in Finance in Slovenia.

reflects the practices in two-thirds of OECD countries (as shown in Table 7). The agency has a staff of about 30 economists. The head of the agency is a political appointee, but not the rest of the staff. The agency reports that its independence is respected in practice. In developing the assumptions, it does not co-ordinate with other government bodies, but interacts with economic think tanks, individual economists in various organisations and the private sector, as well as the central bank.

The agency provides forecasts for the government. Its first econometric estimates were based on a World Bank spreadsheet model, and the agency first developed its own econometric model in 1998. The current main macroeconomic model is used for the budget and medium-term forecasts. The agency also prepares long-term forecasts covering 50-60 years, based on European Commission methodology, which focus on the effects of demographic changes on social insurance, education and health care expenditures (Republic of Bulgaria, 2008). In addition, the agency has produced quarterly forecasts since 1994, and it carries out simulations of the effect of policy changes on the economy.

The agency provides input into budget formulation at two points in the annual budget process. It prepares a first forecast for the upcoming budget year as well as the medium-term forecast of key macroeconomic aggregates (GDP growth, inflation, unemployment, exchange rate, etc.) in February/March, depending on the availability of relevant end-of-year statistics from the Office of National Statistics and the Bulgarian National Bank (BNB). The agency's first forecast is used by the Ministry of Finance to prepare the medium-term fiscal framework and, later, the three-year budget forecast for the line ministries (first-level spending units, FLSUs). In September, the agency submits a second forecast that incorporates the latest macroeconomic developments and the consequences of the planned fiscal framework and that is published with the budget.

In developing the macroeconomic assumptions for the budget, the Executive Agency for Economic Analysis and Forecasting does not use prudency measures, *i.e.* the systematic and explicit downward revisions of key assumptions. However, the agency is satisfied with the accuracy of its forecasts, which it describes as cautious.

Table 7. **Formulation of the macroeconomic assumptions underlying the budget and its supporting documentation**

	Central budget authority/finance ministry	Independent government body	Private sector	Other
Australia	•			
Austria		•		
Belgium		•		
Canada			•	
Czech Republic	•			
Denmark	•			
Finland	•			
France	•			
Germany				•
Greece	•			
Hungary				•
Iceland	•			
Ireland	•			
Italy	•			
Japan				•
Korea	•			
Luxembourg		•		
Mexico	•			
Netherlands		•		
New Zealand	•			
Norway	•			
Poland	•			
Portugal	•			
Slovak Republic	•			
Spain	•			
Sweden	•			
Switzerland				•
Turkey				•
United Kingdom	•			
United States				•
Total	**19**	**4**	**1**	**6**

Source: OECD (2008), *OECD International Budget Practices and Procedures Database 2007*, Version 2.

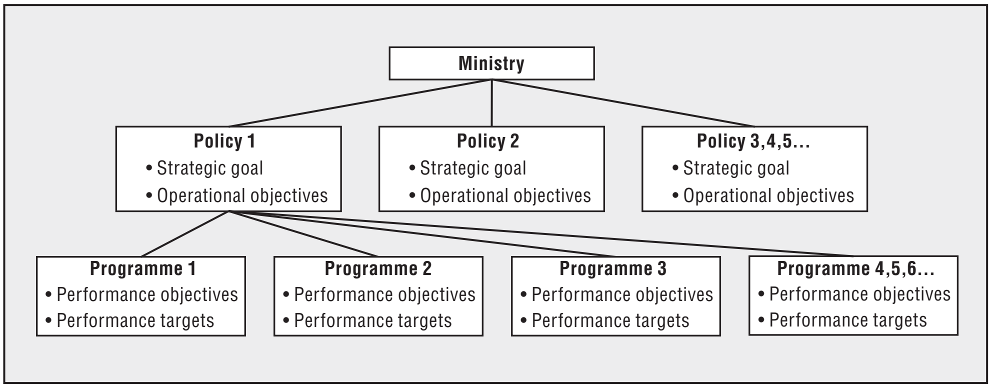
2.2.2. Programme budgets

After a pilot in 2003, a new programme format[3] was rolled out across central government ministries over the following years. There is no legal requirement to do so, but the 2005 government programme contained a commitment to introduce programme budgets across all line ministries. For the first time, all central government ministries submitted programme budgets as part of the formulation of the 2009 budget. The implementation of programme budgets has entailed the division of spending into policies and programmes, and the development of a large number of related performance measures and targets. Figure 2 outlines Bulgaria's programme-based budget structure, which is further illustrated with examples in the remainder of this section.

For example, the Ministry of Regional Development and Public Works has developed three policies and 15 programmes, one of which is for administrative and support functions. The three policies of this ministry are:

- territorial development and public works;

Figure 2. **The structure of the programme-based budget**



- the creation of conditions for balanced and sustainable development in the various regions of Bulgaria; and
- the management of state property and housing policy.

Each of these policies has a strategic goal with attached operational objectives. In the case of the policy "territorial development and public works", the strategic goal is to "create the conditions for an efficient investment process in the area of public works for the construction and maintenance of water supply and sewage systems and road infrastructure". Attached to this strategic goal are eight operational objectives, one of which is "improving the conditions of the water supply infrastructure and the management of water supply and sewage". Programmes are attached to these operational objectives, in this case the programme for building and managing water and sewage infrastructure.

Each programme in turn has a number of performance objectives. The programme "building and managing water and sewage infrastructure" has ten such objectives in total, *e.g.* to reduce leakage, to provide drinkable water that meets quality standards to all settlements, etc. Each of these objectives has at least one associated performance measure. In this case, the ten objectives are associated with 15 performance measures, each of which is associated with a concrete target. Examples of performance measures are: the number of kilometres of extended and rehabilitated sections of the water and sewage system (2008 target: 22 km), and the cubic metres of waste water subjected to primary treatment (2008 target: 125 000 m^3).

At present, the programme budget format is used simultaneously with the traditional approach on the basis of a unified budget classification. The Minister of Finance approves the format of the unified budget classification for each reporting year, although there have only been minor changes over the past few years. The unified budget classification includes detailed functional and economic classifications of expenditures using paragraphs and subparagraphs. While the programme format originated in the Budget Directorate of the Ministry of Finance, the unified budget classification is the traditional basis for budget negotiations between the State Expenditure Directorate and line ministries. Greater collaboration between the two directorates is required for the successful consolidation of the new approach.

The implementation of programme budgets and performance measures in Bulgaria has not been without challenges. One challenge described by line ministries is to reduce the number of policies and programmes. For example, the Ministry of Labour and Social

Box 4. Types of performance-oriented budgeting

The OECD broadly defines three categories of performance-oriented budgeting:

- Presentational performance budgeting necessitates the publishing of performance information in budget and/or other government documents (*e.g.* annual reports). The information can refer to targets, the results against them, or both. While it serves to disseminate information for greater transparency and accountability of government operations, presentational performance budgeting is not intended to play an explicit role in budget decision making.
- Performance-informed budgeting necessitates that the allocation of resources be informed by either proposed future or past performance. While performance information is important in decision making, it is not the sole factor determining the amount of allocation of resources. Performance information is used along with other information in the decision-making process. This practice is the most prevalent among OECD countries.
- Direct (or formula) performance budgeting necessitates the allocation of resources solely based on past performance outcomes and results. This form of performance budgeting is used only in specific sectors in a limited number of OECD countries. For example, the number of students who graduate with a Master's degree either in the current year, in the past or as a combination of the two will determine the following year's funding for the university running the programme.

Source: OECD (2007), *Performance Budgeting in OECD Countries*, OECD Publishing, Paris.

Policy reported that managers were initially very keen to create programmes to reflect their activities, but the number of programmes has since been cut by about one-third to 16 in the 2009 budget. At the end of 2008, this ministry convened an internal working group on the implementation of programme budgeting, which is tasked with reviewing and rationalising the programme structure. There remains scope to reduce the number of programmes. Another challenge has been the capacity of the line ministry and agency staff to understand and use the performance thinking. This also causes difficulties for the line ministry finance directorates.

The actual impact of the performance information on resource allocation decisions is still uncertain. There have been some examples of funding being moved away from programmes that fail to meet targets. However, it also appears that the number of targets is too large to allow line ministries, and in particular line ministries' finance directorates, to systematically monitor performance. Target inflation is a well-known potential problem, in particular during the early stages of a move towards performance-oriented budgeting. The use of performance information for monitoring and strategic decision making is only possible with a small number of well-defined measures for each programme.

Finally, the current targets are output-focused, whereas some line ministry officials were keen to include outcome-based targets. Outcome-based measures are theoretically appealing because they focus on the ultimate purpose of expenditures. However, they are also much more complex and difficult to design than output-based measures. Moreover, accountability for performance becomes much harder to attribute under an outcome-based system.

2.2.3. Long-term fiscal sustainability: contingent liabilities and other risks

The Bulgarian budget includes an analysis of fiscal risk (the Fiscal Risk Assessment) that reviews the economy and major policy risks and liabilities, and provides sensitivity analyses for key variables. In the 2007-09 budget, unfinished structural reforms and the demographic profile of the population were characterised as greater risks than the economic crisis. While the later economic events may have changed that assessment somewhat, Bulgaria has in recent years managed its fiscal policy soundly, reducing the potential concern.

Box 5. **Long-term fiscal projections**

Long-term fiscal projections estimate the cost and affordability of current policies factoring in a number of demographic, economic and other assumptions. These projections are one element of the "OECD Best Practices for Budget Transparency" (OECD, 2002). Projections should cover between 10 and 40 years and be prepared or updated at least every five years or following major changes in revenue and expenditure policies. Moreover, all key assumptions underlying the long-term fiscal projections should be made explicit, together with a range of plausible scenarios. In addition, the IMF *Manual on Fiscal Transparency* (IMF, 2007) states that projections should focus on more than just demographic change. Long-term projections, however, do not provide a means to assess the efficiency or desirability of such policies compared to alternative policies, or a means to identify clear solutions to address the fiscal challenges discussed.

Over the past ten years, Bulgaria has reduced its outstanding public debt. The Government Debt Law requires the establishment of three ceilings per year: on new state debt, on the issuing of state guarantees, and on the overall stock of state debt. Loans for investment projects are included in the total of state debt. New sovereign guarantees were estimated to be EUR 0.9 billion in 2009. A majority of the guarantees were for energy (75%) and transportation (16%). The Municipal Debt Act limits local borrowing to cover infrastructure investments and repayment of existing debt. Total municipal debt in 2008 was 4.5% of the consolidated debt. Bulgaria has had a budget surplus for the past ten years. Its budget assumed a surplus of 3% in 2009. While the revenue estimates may prove to have been too optimistic, Bulgaria's fiscal policy should provide a cushion for fiscal risk.

Pensions and health care are funded on a pay-as-you-go basis. The ageing population is causing increased costs for both social supports. The government is reducing premiums in an attempt to broaden coverage within the grey economy. It is also reducing costs where possible. Notwithstanding these changes, the extended outlook is for increasing state contributions to the social insurance programmes.

2.3. Overview of the Ministry of Finance with special focus on the budget function

The Ministry of Finance is one of 16 ministries that make up the central government. The political hierarchy consists of the Minister of Finance and five deputy ministers who are affiliated with different political parties constituting the governing coalition. The incumbent deputy ministers are experienced civil servants and have a long history of working together; this is also the practice in all other central government ministries. In addition, there is a secretary general responsible for administrative functions, and a state treasurer. The Ministry of Finance has about 670 staff distributed across 21 directorates, 64 divisions and 7 agencies.

The Ministry of Finance has a number of agencies – second-level spending units – some of which have well-developed regional structures. These are: the National Revenue Agency, the National Customs Agency, the Public Financial Inspection Agency, the State Receivables Collection Agency, the Executive Agency for Economic Analysis and Forecasting, the State Commission on Gambling and the Executive Agency for the Audit of EU Funds.

This subsection discusses the organisation of the part of the Ministry of Finance that is responsible for preparing the budget, monitoring its execution, and accounting – in essence what is known as the "central budget authority" (CBA). A CBA is a public entity, or several co-ordinated entities, responsible for the custody and management of all (or the majority) of the public money. It is often part of the central government Ministry of Finance. The CBA has the leading role in maintaining aggregate fiscal discipline, ensuring compliance with the budget laws, and enforcing effective control of budgetary expenditure. The CBA regulates budget execution but does not necessarily undertake the treasury function of disbursing public funds. Moreover, it shapes the practices and procedures – and reforms – of the national budget system in order to achieve sound budget outcomes.

In Bulgaria, these functions and tasks are the responsibility of the directorates listed below. The result is that budget functions are spread among several directorates and under five deputy ministers and several agency heads, which will be discussed in more detail below.

The main actor in the budgetary process is the Budget Directorate which has overall responsibility for co-ordinating the budget process and developing budget methodology. In the annual budget process, the State Expenditure Directorate is the main negotiating partner of first-level spending units (FLSUs) – principally line ministries and state agencies. The Budget Directorate and the State Expenditure Directorate report to different deputy ministers, with different party political affiliations. Despite the political nature of their appointment, there is a tradition of appointing deputy ministers with relevant work experience in the Ministry of Finance.

There are two principal budget directorates and other key budget functions dispersed across the Ministry of Finance:[4]

- The **Budget Directorate**, with a staff of 29, is responsible for developing fiscal and budgetary policies, budget methodology and training. The Budget Directorate has been the driving force behind implementing the programme budget. It has performed various analyses on social sector policies and programmes with impact on financing mechanisms and allocation of funds.
- The **State Expenditure Directorate**, with a staff of 41, is the main counterpart of the line ministries. It is responsible for developing estimates at the level of the economic classification for the line ministries (first-level spending units) and overseeing execution of the budgets by first-level spending units. Staff is organised by broad policy areas of government; each analyst has the lead in working with one or more line ministries.
- The **Executive Agency for Economic Analysis and Forecasting**, an agency attached to the Minister of Finance with a staff of 30-35 economists, is responsible for macroeconomic assumptions and analysis. The Agency reports to the Minister of Finance. Its head is a political appointee, but all other staff are experts without regard to political affiliation. The Agency uses the EC, the IMF and the OECD as sources for its key assumptions. The only source of independent comparisons within Bulgaria is the central bank.

- The **Management of EU Funds Directorate**, with a staff of 57, takes the lead in co-ordinating investment budgeting.
- The **National Fund Directorate**, with a staff of 75, operates as a certifying authority to verify the legality and propriety of spending for EU programmes.
- The **Executive Agency for the Audit of EU Funds** has a staff of 40, including 19 auditors, which functions as the audit authority for EU funds.
- The **Local Government Financing Directorate**, with a staff of 22, co-ordinates state and municipal budgets, negotiates with the National Association of Municipalities on subsidy allocations to municipalities and, jointly with the State Expenditure Directorate, works with key ministries and the National Association of Municipalities on funding allocations for locally administered programmes such as primary and secondary education for the Ministry of Finance.
- The **Real Sector Finance Directorate**, with a staff of 21, oversees budget policy for state-owned enterprises, concessions and the State Agricultural Fund. The Directorate is responsible for: analysing and planning the budget revenues and expenditures from concessions and privatisation; the structural reforms in the economy; the planning and control of state subsidies and capital transfers to the state and municipal companies and compensations in the transport sector; and preparing forecasts for budget planning and monitoring of the expenditures from the European agricultural funds and the national programmes for financing in agriculture.
- The **Tax Policy Directorate**, with 34 employees, has a unit for analyses and forecasts and reports on the revenues in the state budget, proposes solutions regarding the bases for determining taxes and amendments to the tax rates, evaluates the overall tax and insurance burden, assesses and forecasts the amount of tax revenues, and participates in the preparation of the revenue part of the short and medium-term fiscal framework. The directorate helps determine the contributions of the Republic of Bulgaria to the EU general budget.
- The **Government Debt and Financial Markets Directorate**, with a staff of 26, develops forecasts for debt financing and the required funds for debt service, which are updated when necessary. It also prepares provisions to be included in government debt regulatory documents and reports. Another major function is implementation of the procedure for considering and approving investment projects financed by government loans and projects applying for financing by government guarantee as part of the budget procedure.
- The **EU Affairs Directorate**, with a staff of 12, prepares and updates the forecasts for the total amount of the annual payment of the Bulgarian contribution to the general budget of the European Communities for the purpose of the national budget procedure.

The organisational structure of the Ministry of Finance creates added burdens for the first-level spending units in that they are required to work with multiple offices within the Ministry of Finance on the budget and thus without one "key account manager". Their primary contact is with the State Expenditure Directorate for state budget issues. If they are addressing issues involving local funding, investment programmes or the real sector, they interact with other offices within the ministry.

Development efforts like the current initiative to establish programme budgeting are led by the Budget Directorate. The State Expenditure Directorate did not appear to be actively involved in this effort. Issues of co-ordination and disagreement among the directorates of the Ministry of Finance regarding the budget process are resolved by informal discussions between deputy ministers, by the Minister's Cabinet (consisting of the Minister, the five deputy ministers, the Head of Office, and the Secretary General), or by the Minister.

The flow of information between the Ministry of Finance and the first-level spending units is quite complicated, with different directorates requesting similar information from line ministries. For investment budgeting, three directorates are involved. Programmes administered through the municipalities involve at least two directorates, as do the real sector activities. Decisions on allocations among these categories require input from several deputy ministers. This structure can also create conflict between various Ministry of Finance units trying to further "their" subject areas.

Performance budgeting is in the process of being implemented. The primary focus of the majority of the Ministry of Finance's staff is on input budgeting rather than budgeting for particular programmes and focusing on their performance. Shifting this focus will require central leadership and the co-ordinated efforts of all of the directorates with budget responsibilities.

Table 8. **Staff in budget functions**

Unit	Staff
State Expenditure Directorate	41
Tax Policy Directorate	34
Executive Agency for Economic Analysis and Forecasting	30
Budget Directorate	29
Government Debt and Financial Markets Directorate	26
Local Government Financing Directorate	22
Real Sector Finance Directorate	21
EU Affairs Directorate	12
Subtotal (non EU-related budget functions)	**215**
National Fund Directorate	75
Management of EU Funds Directorate	57
Executive Agency for the Audit of EU Funds	40
Subtotal (EU-related budget functions)	**172**
Total	**387**

Of the roughly 650 persons working in the Ministry of Finance, approximately 400 staff are involved in central budget functions, broadly defined. Budget staff report to four deputy ministers and the State Treasurer. A large number of the staff (172) is allocated to the management and oversight of EU funds. About 215 staff are in the directorates for Budget, State Expenditure, Local Government Financing, Real Sector Finance, Forecasting, etc. When comparing these figures to selected OECD countries (see Table 9), the EU management directorates should only be counted to a limited extent. It would thus seem that Bulgaria is placed close to the norm in OECD countries with regards to the size of the central budget authority. The political structure of the Ministry of Finance's budget tasks – *i.e.* having a number of deputy ministers – is unusual compared to OECD countries, where most have a single head (either a senior civil servant or a political appointee).

The importance of a powerful central budget authority in achieving sound budget outcomes – particularly fiscal discipline – has received much attention in the literature on budget institutions. Dimensions of a strong central budget authority are the political

Figure 3. **Organisation of the Bulgarian Ministry of Finance**

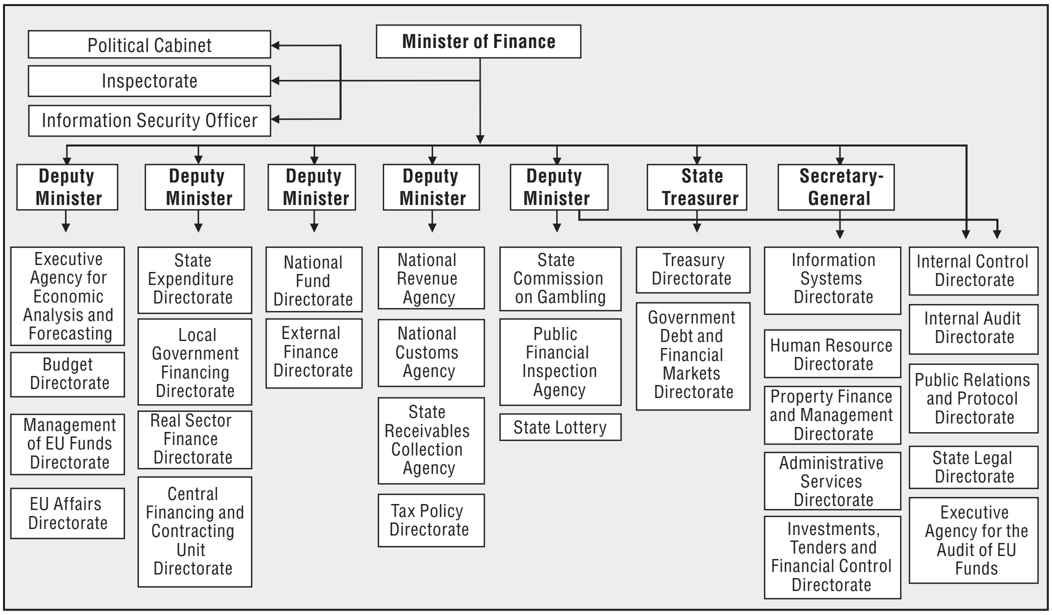


Table 9. **Head and staff size of the central budget authority in selected OECD countries**

	Head of the central budget authority		Amount of personnel
	Senior civil servant	Political appointee	Full-time equivalent[1]
Austria		•	110
Czech Republic		•	504
Denmark	•		100
Finland	•		35
Greece		•	50
Hungary		•	136
Netherlands	•		175
New Zealand	•		320
Norway	•		45
Poland		•	170
Slovak Republic	•		100
Sweden	•		80
Switzerland	•		220

1. The full-time equivalent should not be mistaken to refer to the total staff of the Ministry of Finance, only to the tasks undertaken by the central budget authority as defined above.

Source: OECD (2008), *OECD International Budget Practices and Procedures Database 2007*, Version 2.

strength of the Ministry of Finance, the resources available to it, but also importantly the internal organisation of the central budget authority. Organisations must always adapt institutionally to reflect the main priorities of the government of the day. In addition, many finance ministries are faced with the question of how best to organise staff resources in order to maximise their utility. Many OECD countries have organised their finance ministries on the basis of the following principles:

- The Ministry of Finance should reflect the organisation of the government at large by having units shadowing each line ministry or policy area.

- These units should be the "key account managers" of the relevant line ministry. All dealings between the Ministry of Finance and the line ministry should be co-ordinated by the relevant unit.
- The unit's core task should be to prepare the budget proposals for the line ministry in collaboration with the line ministry's budget office. This task entails that the unit has a number of experts who thoroughly understand the line ministry's budget as well as the line ministry's political goals.
- All key account managers should ultimately refer to the budget director, who should be able to have the final say on all technical aspects of the budget and be the finance minister's senior advisor on all budget matters.

An example of a movement towards these principles, but by no means the only one, is the United States. This example also illustrates that, although an organisation might have functioned well at a certain time, it can evolve over time in ways that may weaken the finance ministry's ability to control the budget process. At the beginning of the administration of President Clinton, roughly in 1993, the United States Office of Management and Budget (the central budget authority) found that line ministries had too many entry points to the organisation. It was therefore decided to shift staff from certain directorates within the Office of Management and Budget that had thematic responsibility across many line ministries (such as accounting practices) to directorates that were responsible for specific line ministries and programmes. Thus the Office of Federal Financial Management, the Office of Procurement Policy, and the Statistical Policy Office shifted staff to the OMB line directorates such as Health, Education and National Security. Subsequently all contact with line ministries took place via designated desk officers ("key account managers"). The directorates with general responsibilities focused on establishing policy and issuing guidelines, which were then implemented via the desk officers.

2.4. Conclusions and recommendations

The Bulgarian budget preparation process is moving in a modernising direction. The procedure used for the 2009 budget exhibits many of the modern budgeting techniques found in OECD countries, such as top-down budgeting, multi-year budgeting perspectives, and the use of performance information in the budget process. Thus the real challenge for Bulgaria is to make these practises and procedures work by implementing them effectively and thoroughly. While there is no doubt that this process is under way, there are a few adjustments that should be considered:

- There has been progress in Bulgaria in making the budget more comprehensive of public activity. The overall goal should be to integrate all of the remaining separate budgets within a consolidated budget for the country. The extrabudgetary funds, state-sponsored enterprises, social insurance funds and autonomous budgets should all be integrated into the budget to enhance the transparency and public understanding of the budget.
- The programme budget format has been rolled out across all central government ministries, which is a major accomplishment. However, the traditionally used classifications and the new programme classification currently compete for attention. To some extent the State Expenditure Directorate still regards the new format as a parallel system run by the Budget Directorate. In the medium term, the appropriations approved by Parliament should be put on a programme basis. For this to work, there must be a manageable number of carefully defined programmes in each ministry.

- Line ministries have produced a large number of performance targets that are attached to programmes. The number of targets is much too high to enable finance directorates in line ministries, as well as the Ministry of Finance and Parliament, to use this information systematically in budgetary decisions. The quality of performance information needs to be strengthened. Each first-level spending unit should have a small number of high-quality performance measures. Whether to focus on output or outcome measures should be carefully discussed, since both have advantages and disadvantages. While a clear link to outcomes is desirable, output-based performance measures are easier to define and their achievement easier to attribute for accountability purposes, which cautions against a premature move to outcome-based measures.
- The Bulgarian government should consider consolidating budget functions under one deputy minister in the Ministry of Finance. Having a single deputy minister with the lead responsibility for budgeting should simplify budget direction. The functions of some of the specialised directorates could be modified to focus on policy direction and shifting interaction with line ministries to a consolidated programme expenditure staff consisting of "key account managers". As Bulgaria moves toward programme and performance budgeting, it will make sense to integrate operating and investment budgeting on a programme basis. Similarly, as privatisation is finalised, programme review for state-sponsored enterprises and autonomous budgets could be integrated on a programme basis. Review of programmes administered by local governments should be consolidated with related centrally funded programmes, such as education or transport.
- Streamlining interaction with the line ministries with special "key account managers" would also help the Ministry of Finance support and upgrade the line ministries' central finance directorates. Just as a strong Ministry of Finance is conducive to the running of a prudent fiscal policy, so is a strong central finance directorate in line ministries conducive to sound budgeting and financial management practices in ministries and agencies. With a reformed budget process and the use of multi-year budget perspectives, top-down budgeting and the introduction of performance and programme budgeting, it is of paramount importance that the line ministry finance directorates are strong and relevant hubs in the working of the budget system. The overall structures and principles appear to be the right ones, but the true test of the practices lies in their implementation.

3. Parliamentary approval

The parliamentary approval process in Bulgaria takes only about two months. It involves hearings on the budget by various committees, a first reading, the review of amendment proposals by the Budget and Finance Committee, and a second reading that concludes with the adoption of the budget. The process results in few changes to the budget proposed by the executive.

This section first outlines the legal framework for the parliamentary stage, before summarising the processes leading up to the first reading and to the second reading. The section concludes with several recommendations relating to the enhancement of parliamentary engagement with programme-level information, the judicial budget, the creation of independent analytic capacity, and the timing of the legislative budget process.

Box 6. The National Assembly of Bulgaria

Bulgaria has a unicameral National Assembly that was established in 1991. It has 240 members, elected for a four-year term by proportional representation in multi-seat constituencies with a 4% threshold for political parties. Following the 2005 legislative elections, seven parliamentary groups (which require a minimum of ten members) were formed in the National Assembly. The governing coalition comprised the three largest groups: the Coalition for Bulgaria (82 seats), the National Movement Simeon II (53 seats), and the Movement for Rights and Freedoms (34 seats).

The National Assembly has the authority to enact laws, approve the budget, schedule presidential elections, select and dismiss the Prime Minister and other ministers, declare war and deploy troops outside of Bulgaria, and ratify international treaties and agreements. Members serve on standing and *ad hoc* committees. At the time of the review, there were 25 standing committees and 20 *ad hoc* committees. In addition, there were five subcommittees which are part of one of the standing committees. The composition of the standing committees is based on the principle of proportional representation of the parliamentary groups.

3.1. Legal framework and parliamentary powers

After each election, one of the first tasks of Parliament is to approve its rules, including for the approval of budget bills. Since 2007, the rules contain a separate appendix on the budget of the National Assembly with detailed provisions on members' remuneration, expenses and gifts. There is a single legislative procedure, but an important exception is enshrined in Article 87(2) of the Constitution, which stipulates that only the Council of Ministers can initiate the budget.

According to Article 20(5) of the State Budget Procedures Act, the Council of Ministers must submit the draft state budget to the National Assembly not later than two months before the commencement of the relevant budget year, *i.e.* by 31 October of the preceding year. Should the budget not be approved in time, the act allows for spending in accordance with existing laws and "not exceeding the amount of outlays for the same period of the preceding year" (Article 26[1]).

Article 21(2) of the act also limits parliamentary amendment authority: "Upon consideration of the bill, the standing committee in charge of the budget shall consolidate the observations of the other standing committees of the National Assembly and the motions of the national representatives and shall pass on the said observations and motions without revising the balance of receipts and outlays as moved." This means that amendment proposals should not affect the budget balance.

3.2. The stages of the parliamentary process

3.2.1. Submission and first reading

The stages of the parliamentary budget process are summarised in Table 10. The submission of the draft state budget by the Minister of Finance receives substantial media coverage. Once entered into a register, the Speaker has to issue a special order within three days and specify the lead committee to consider the bill and which other committees are involved. The Budget and Finance Committee is the lead committee for the annual budget, but usually all other standing committees are secondary committees and also receive the

Table 10. **The stages of the parliamentary process**

Date	Action
End October	The Minister of Finance submits the draft budget to the National Assembly.
Early November	The Budget and Finance Committee and the Economic Policy Committee hold joint hearings. Sectoral committees also hold hearings and report to the Budget and Finance Committee, which produces a summary report.
Mid November	First reading of the state budget bill. The National Assembly votes on whether to proceed with the bill.
End November	Members submit amendment proposals.
Early December	The Budget and Finance Committee deliberates and adopts a report with its decision on each amendment proposal, which is distributed to all members of the National Assembly.
Mid December	Second reading of the state budget bill. The National Assembly votes on each amendment proposal and adopts the bill.

bill. The Economic Policy Committee is involved in considering macroeconomic aspects, while sectoral committees focus on the parts of the budget that are relevant to their specific policy area. All standing committees are composed of members of the different parliamentary groups proportionate to their share of seats in the National Assembly.

The Budget and Finance Committee has 23 members, including the chairperson and three deputy chairpersons. A small number of staff supports the work of the committee: two experts, one senior expert assistant, and one senior expert. There is no independent budget research office attached to Parliament. The mandate of the Budget and Finance Committee covers annual budgets as well as legislation relating to municipal budgets, the central bank, external audit, financial supervision, taxation, financial audit, accountancy, and national and municipal debt. Committee sessions are, in principle, open to the public. Since 2007, the Budget and Finance Committee has a Public Sector Accountability Subcommittee, consisting of seven members, which assists with the scrutiny of government accounts.

After receiving the budget documents, the Budget and Finance Committee and the Economic Policy Committee hold joint hearings in preparation for the first reading. They invite the Minister of Finance and budget officials, as well as representatives of the judiciary and the social funds. Representatives of trade unions and some professional organisations are also invited. This meeting discusses the three-year budget forecast, the macroeconomic framework and the draft law on the state budget, and it usually lasts about three hours.

Following these discussions, the Economic Policy Committee votes on the state budget bill. The Budget and Finance Committee usually does not vote on the bill at this first meeting, as it reserves the right to hold two or three further meetings with other participants. For these further meetings, the Budget and Finance Committee invites other organisations, and the opposition usually asks more detailed questions that the executive is obliged to answer. The Minister of Finance can be asked to provide additional material as required. If all issues have been sufficiently clarified, the Budget and Finance Committee votes on the bill and concludes its first hearing.

In the meantime, other standing committees also meet to discuss parts of the budget related to their policy area, *e.g.* the Health Care Committee looks at the health budget, the Defence Committee considers defence spending, etc. Each of the sectoral committees submits opinions to the Speaker and to the Budget and Finance Committee, containing an analysis of proposals for the relevant sector as well as proposals. Some sectoral committees recommend spending increases, and occasionally a committee proposes not to accept the budget. The chairperson of the Budget and Finance Committee must prepare a report to the National Assembly that conveys the outcome of the discussions in the committee as well as a summary of the discussions in other committees.

At this stage, one of the more problematic issues to be dealt with relates to the judicial budget. During the formulation stage, the Minister of Justice submits a budget proposal to the Supreme Judicial Council. The minister chairs this council, but has no voting rights. The council discusses the draft judicial budget, changes and approves it, and sends it to the Ministry of Finance and the Council of Ministers to be included in the draft budget (see the previous section). Usually, the Ministry of Finance considers this funding proposal to be too generous and comes up with its own, reduced proposal. Parliament receives both versions of the judicial budget. The report by the Budget and Finance Committee must include a recommendation on which of the two judicial budgets should be supported, so the first vote of the committee is on whether to proceed with the budget prepared by the Supreme Judicial Council or with the government version. Officials do not recall an instance where the government was defeated on this issue.

In mid-November, after receiving the report on the state budget by the chairperson of the Budget and Finance Committee, Parliament schedules a session for the first reading of the state budget bill. The first reading usually lasts a whole day and sometimes longer. Every member has a right to intervene, and opposition members tend to be particularly keen to do so. At the end of the first reading, when each parliamentary group has used up its allotted time, Parliament votes on whether to proceed with the bill.

3.2.2. Amendment proposals and second reading

After the first reading, members are given a deadline (usually seven days) by which they must submit any amendment proposals. A working group chaired by the chairperson of the Budget and Finance Committee and including other parliamentarians and executive branch representatives reviews all amendment proposals. The working group prepares a substantial report of about 150-170 pages with an opinion on each proposal. The Budget and Finance Committee considers this report. Members of other committees can defend their proposal(s), but they may not vote. The Budget and Finance Committee can decide to accept, reject or amend a proposal. After the end of this meeting, a report with the decisions of the committee is submitted to the administration of the National Assembly and distributed to members.

The number of amendment proposals by members or parliamentary groups is affected by membership turnover and changing committee assignments following elections. In the first budget after elections, there are usually fewer proposals, but they proliferate in subsequent years and it is possible that several dozen bundles of amendments can be proposed. The Budget and Finance Committee has tended to observe the balancing requirement in the State Budget Procedures Act when it considers these proposals, which is one reason why there are not many major changes to the budget. However, there are examples of spending increases that were financed by an increase in tax revenues and by decreasing one of the reserves in the budget (for structural reform). According to officials, parliamentarians have used the significant surpluses in recent years to some extent.

At the second reading, which takes place around mid-December, Parliament considers and votes on each proposal. After that, the state budget bill is submitted to the legal directorate of the National Assembly, which checks whether the text corresponds with all deliberations. Once drafted, the chairperson of the Budget and Finance Committee signs off and the Speaker sends the draft law to the President for promulgation. The President has 14 days for review and is entitled to return the bill to Parliament or to sign the draft law as passed. The President has never refused to sign budget bills.

With the State Budget Act, Parliament approves the budget of each first-level spending unit broken down by: *i)* own revenues; *ii)* gross expenditures; *iii)* net transfers; *iv)* subsidies from the national budget; *v)* the balance; and *vi)* borrowing. The newly developed policy and programme-based classification is contained in a separate appendix of the State Budget Act. The policies discussed in the previous section have binding force, but not the programmes. This implies that Parliament exercises slightly more control over public spending than under the traditional approach, where the only binding decision was on the total of each first-level spending unit. Nonetheless, as the previous section illustrated, each policy bundles a large number of programmes in a typical line ministry. As a result, parliamentary approval remains at a highly aggregated level.

Box 7. **Parliamentary influence in OECD countries**

There is substantial variation in terms of the role of legislatures in the budget process in OECD countries and elsewhere. Broadly speaking, it is possible to distinguish three groups of legislatures in terms of their influence on budget policy.

The most powerful are budget-making legislatures, which have the capacity to amend or reject the budget proposal of the executive and to formulate and substitute a budget of their own. World wide, there are very few legislatures that fall into this category; those of Korea, Mexico and the United States are arguably the only examples among OECD countries. Budgets approved by the United States Congress often differ fundamentally from the proposals submitted by the President. Government agencies have to shut down unless their funding is approved, as happened during the winter of 1995/96.

Less dominant are budget-influencing legislatures, which have the capacity to amend or reject the budget proposal of the executive, but lack the capacity to formulate and substitute a budget of their own. Many parliaments of OECD countries fall into this category, including those in the Nordic countries as well as in several continental European countries, *e.g.* Germany, Poland and Switzerland. Amendments to the executive budget proposal are not uncommon in most of these countries, but fundamental changes would be exceptional.

Finally, legislatures with little or no budgetary effect lack the capacity to amend or reject the budget proposal of the executive and to formulate and substitute a budget of their own. As a result, these legislatures typically approve the budget without any changes. Most Westminster-type parliaments fall into this category. The last time the British Parliament voted down a request for money was in 1919, when the Lord Chancellor was refused funding for a second bathroom. The New Zealand Parliament last reduced an allocation in 1930 when it cut the vote for the Department of Agriculture by five pounds.

Sources: P. Norton (1993), *Does Parliament Matter?*, Harvester Wheatsheaf, New York, United States; A. Schick (2002), "Can National Legislatures Regain an Effective Voice in Budget Policy?", *OECD Journal on Budgeting*, 1(3); J. Wehner (2006), "Assessing the Power of the Purse: An Index of Legislative Budget Institutions", *Political Studies*, 54(4).

Parliamentary approval does not guarantee that funding is actually disbursed. Parliament approves non-interest expenditures and transfers in Article 1 of the State Budget Act, *i.e.* expenditures in the republican budget and transfers to other budgets. However, Articles 17 and 18 of the 2009 State Budget Act allow the Council of Ministers to withhold 10% of the total amount, providing the executive with a discretionary buffer during the financial year. In principle, this allows the executive to withhold any voted expenditures, up to a maximum of 10% of the total amount approved by Parliament. These provisions give the Council of Ministers substantial authority over total disbursements as well as the composition of actual spending. This aspect is discussed further in the following section.

The same procedure outlined above for the state budget bill applies to the budgets of the two social funds, the only difference being that the Health Care Committee and the Labour and Social Policy Committee are the secondary committees. In addition to the annual State Budget Act, Parliament approves the National Health Insurance Fund Budget Act as well as the Public Social Insurance Budget Act.

3.3. Conclusions and recommendations

The Bulgarian National Assembly has a role in the budget process perhaps similar to less active parliaments in the group of budget-influencing legislatures described in Box 7 above. Although members generate a number of amendment proposals, most of these have limited influence on the composition of the budget and fiscal policy. As long as the government has a secure majority, the National Assembly approves the budget with minimal changes.

The Budget and Finance Committee has an important role in the legislative budget process. Its review of the amendment proposals generated by sectoral committees and members sets the agenda for the discussion on the floor of the National Assembly. The committee exerts a disciplinary role and helps to contain pressures for spending increases during the parliamentary stage. Overall, the approval process is fairly effective, but there is potential for improvements in several areas:

- Parliamentary approval of expenditures is at a highly aggregated level. Moreover, the executive has substantial flexibility to adjust outlays during the fiscal year. In a number of OECD countries and elsewhere, legislatures approve the budget on a programme basis. The adoption of this approach in Bulgaria would create incentives for parliamentarians to scrutinise programme-level expenditures. (See Box 8 for an example.) As a result, line ministries would have to give a more central role to programmes and the associated performance information during the formulation process.
- The process for the judicial budget appears to be experiencing problems. In one-third of OECD countries (10 out of 30) the judiciary prepares its budget independently and its proposal is included in the draft budget without any changes by the central budget authority (OECD, 2008).[5] In Bulgaria, there appears to be strong and persistent disagreement about the funding levels for the judiciary. Parliament may consider setting up an *ad hoc* cross-partisan committee to investigate the issue and to arrive at a more informed view on the appropriateness of the current funding level for the judiciary.
- The Bulgarian Parliament does not have access to independent budget analysis capacity. A number of legislatures in OECD countries have created budget research offices which can support members with independent analytic work and contribute to transparency and accountability in the budget process. In particular, if the Bulgarian Parliament chose to strengthen its engagement with programme-level information, it might benefit from access to specialised policy and budgeting expertise.
- The duration of the parliamentary approval process does not comply with the "OECD Best Practices for Budget Transparency" (OECD, 2002) which stipulate that the legislature should receive the budget proposal no less than three months prior to the start of the fiscal year. It may be appropriate to extend the time available to the Bulgarian Parliament for its scrutiny of the budget.

Box 8. South Africa's switch to voting on programmes

South Africa fundamentally modernised its public financial management system with the adoption of the Public Finance Management Act (PFMA) in 1999. Among the many reforms taken forward with this legislation, there is now a requirement for the annual budget to be structured by "vote" (departmental budgets) and broken down into main divisions (programmes) with attached "measurable objectives" (Section 27).

Once approved by Parliament, the accounting officer in a department may only shift a saving of up to 8% of the amount appropriated for a programme to another programme within the same vote (Section 43). In addition, amounts that are specifically and exclusively allocated for a purpose mentioned under a main division within a vote may not be reduced, transfers to institutions may not be adjusted, and capital expenditure may not be reduced in order to defray current expenditure.

As a result, the South African Parliament now votes on programmes, rather than only on total departmental funding as in the past.

Source: Republic of South Africa (1999), "Public Finance Management Act", Pretoria.

4. Budget execution and management

Bulgaria's budget management has benefited from a long-term relationship with the IMF, the OECD SIGMA programme (Support for Improvement in Governance and Management), and the EU. Overall this has been a positive experience that has led to a series of structural and procedural reforms in budget execution, treasury functions, internal audit, and programme and medium-term budgeting. The assessment of the Ministry of Finance is that these reforms have resulted in stronger controls of budget aggregates and less attention to budget details. Budget control, evaluation, and programme assessment and auditing still require attention.

This section reviews the implementation of the budget in eight subsections: organisation of government, structure of appropriations, budget flexibility, budget execution, cash and debt management, human resources, procurement, and the role of municipalities.

4.1. Organisation of government

The government of Bulgaria is divided among first and second-level spending units and lower-level organisations. The first-level spending units (FLSUs) include the ministries, establishments and other budget organisations: 16 ministries, 2 ministers without portfolio (one for EU integration and the other for management of EU funds), 31 other establishments, and 264 municipalities. The 16 ministries are responsible for the great majority of the central government functions of Bulgaria and are divided along programmatic lines, such as defence, health, agriculture and food supply, interior, transport, etc. Examples of the other establishments are the National Assembly and the Council of Ministers. Each of the first-level spending units receives funds from the central budget and bears the responsibility for management of its budget. Second-level spending units (SLSUs) are a broad array of organisations that receive their budgets through allocations from the first-level units. The second-level spending units of the Ministry of Finance are listed in Section 2. State-owned schools are second-level spending units of the

Ministry of Education which allocates them budgetary resources; municipal schools are second-level spending units of municipalities. (A list of the first-level spending units and examples of second-level spending units are included as an annex to this report.)

The 2009 State Budget Act of Bulgaria identifies the extrabudgetary funds operating during 2009, a substantial reduction from earlier years. The authorising legislation for each of these activities provides for its extrabudgetary status. These activities include: the fund for covering privatisation costs of the Privatisation Agency; the State Agricultural Fund; the extrabudgetary account of the National Fund for EU resources under the Minister of Finance; the special account for municipal revenues from privatisation and post-privatisation control; the special fund for municipal councils' investments and fixed assets; and the Teachers' Pension Fund. Expenditures for these funds totaled BGN 3.1 billion in 2009, or EUR 1.6 billion. All extrabudgetary funds are included in the consolidated budget and subsidies from the state budget are recorded in the State Budget Act as discussed in Section 2.

State-sponsored enterprises: Public funds are also used in state-owned enterprises and commercial companies carrying out quasi-fiscal activities. The Bulgarian government follows Eurostat requirements in determining which operations to cover in the budget. These requirements are established to prevent impediments to open trade and may preclude state assistance that the EU determines as non-competitive. In the past years, examples of these entities were the Bank Consolidation Company, which controls the implementation of the privatisation process in the banking sector, and the Public Infrastructure Projects joint-stock company (known also as the National Investment Company) which was created to develop, construct, and overhaul public infrastructure projects. Another example is the Enterprise for the Management of Environmental Protection Activities, a state-owned company that is treated as extrabudgetary for reporting and statistical purposes. The budget also includes subsidies provided to a broad range of utility and transportation companies. Gas, electricity, heat, water, sewerage, long-distance communications, and the postal service are all regulated by the state. Subsidies and capital transfers are provided to the two state-owned railway companies, a railway operator and a railway infrastructure company. Limited subsidies are provided for services that are not financially viable, such as bus service to remote rural areas. EU regulations establish restrictions on public subsidies and guidance on regulations. Budgeting for the real sector follows the requirements of the general budget process. The Real Sector Finance Directorate in the Ministry of Finance oversees these budgets.

Social insurance funds: The budgets of the Social Security Fund and Health Insurance Fund are approved by the National Assembly separately from the annual state budget law. Transfers from the republican budget to the two funds are included in the state budget.

Autonomous budgets: Public universities, the Bulgarian Academy of Science, Bulgarian National TV and Bulgarian National Radio have autonomous budgets. Since 1998, their budgets have been executed outside of the state budget. Parliament approves only transfers from the central government while separate laws govern their revenues, expenditures, transfers and financing.

The relationship between the state budget, the Social Security Fund, the Health Insurance Fund and autonomous budgets is explained in Section 2 above.

4.2. Structure of appropriations

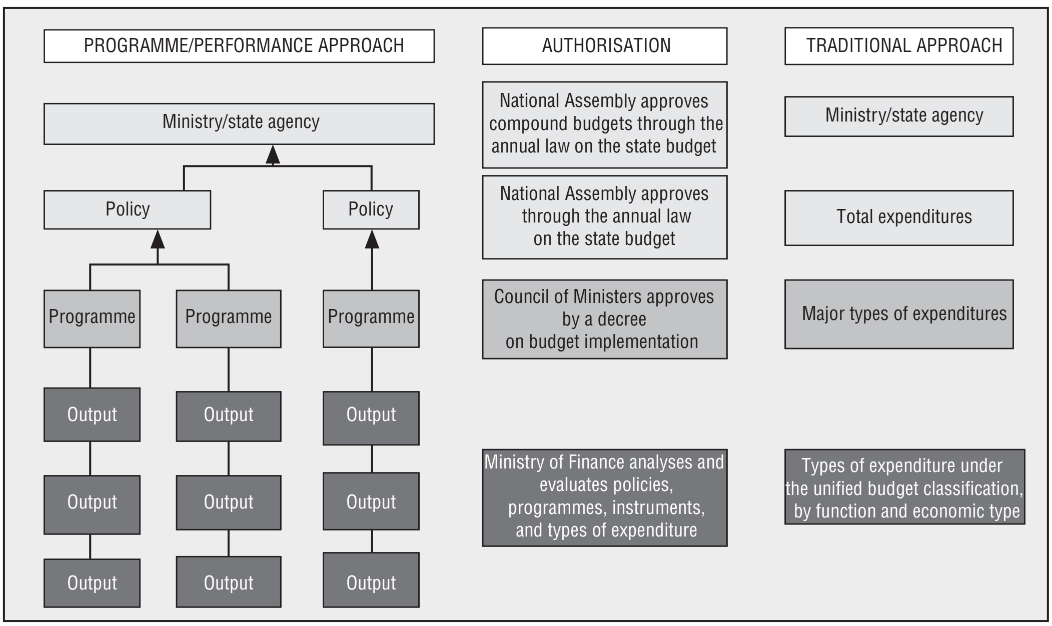
In Article 1 of the State Budget Act for 2009, the National Assembly appropriates the revenues, expenditures, transfers, contribution to the European Union budget, balance and financing of the republican budget by economic classification. In separate articles, the National Assembly appropriates the autonomous budgets of the judiciary, the National Assembly, the National Audit Office and the Financial Supervision Commission by economic classification. Article 6 appropriates revenues, expenditures, transfers, subsidies/payments, budget balance and financing of designated first-level spending units. Parliament directs the Council of Ministers to specify the greater detail required for the budgets of the public authorities, ministries and administrations.

Parliament appropriates the expenditures by policies of the Council of Ministers and directs the Council of Ministers to approve the budgets of the entities mentioned in the preceding paragraph by programmes within the expenditures approved in more detail in Appendix No. 2 to the law. On the basis of the budget law approved by Parliament, the Council of Ministers issues a decree on the implementation of the state budget (implementing decree) which consists of a further breakdown of the line ministries' appropriations by economic classification as well as by policy and programme. The expenditures per programme are further broken down by department (personnel, maintenance, and capital expenditures) and administered item (subsidies, etc.).

The budget of Bulgaria consists of:

- A **summary document** – approximately 85 pages long – that presents an analysis of the economy and a summary of the spending and the revenue policies. The document is easy to read and uses tables and graphs effectively.
- The **appropriation law** that provides aggregate revenue, spending, financing and major economic type such as transfers or subsidies or investment for the first-level spending units.
- **Annexes** that contain expenditure details and explanations by sub-unit, including all individual programme budgets of the line ministries and state agencies.

Figure 4. **Link between performance budgeting and authorisation**



Within 30 days of the budget law's approval by the National Assembly, the appropriation law is further broken down by the Council of Ministers decree that allocates the approved aggregates by programme and by economic classification (for example, salaries, maintenance, and capital).

4.3. Budget flexibility and contingency and reserve funds

As discussed above, the Bulgarian budget is currently approved by the legislature at paragraph level which means by line ministry (institutional) and major economic classification. The breakdown is further disaggregated in the Council of Ministers decree at subparagraph level which is by economic classification (such as salaries, transfers and subsidies). The budget law does not allow carryover or borrowing from next year's appropriations. The Organic Budget Law (Articles 34 and 35) stipulates transfer authority between the first-level spending units as well as within the first-level spending units in the following situations:

- The Minister of Finance can transfer appropriations from one paragraph of the budget to another, if the budget totals are not changed.
- The Minister of Finance can shift appropriations from one paragraph of the budget to another with the agreement of both organisations as long as the transfer does not change the amount or purpose.
- The Minister of Finance is authorised to approve the request of a line ministry or other first-level spending unit to reallocate funding among the components of the budget classification of their budgets, as long as the totals for the first-level spending unit are not changed.
- Line ministries/first-level spending units are authorised to move money among second-level spending units within subparagraphs – for example, to shift funding for maintenance from one project to another within the ministry.
- The Council of Ministers is authorised to approve spending up to 1.5% of estimated revenues under the Consolidated Fiscal Programme in the event of own revenues being larger than expected. Also, revenue from the sale of assets such as property or land does not require a supplementary budget to be submitted in Parliament. The revenue can be spent under a Council of Ministers decree.
- All of these actions are limited to those that do not worsen the budget balance. Supplemental appropriations in excess of the amount mentioned above (1.5%) may be requested from the National Assembly.
- In practice, internal reallocations within the line ministries/first-level spending units occur quite frequently; other changes occur less frequently. The Ministry of Labour and Social Policy, for example, mentioned 30 to 40 reallocations per year requiring approval by the Ministry of Finance.

If the budget is not approved by the beginning of the fiscal year, revenues shall be collected consistent with the tax law currently in effect and expenditures shall be made in amounts not to exceed those in the corresponding period of the previous fiscal year. This procedure is to be used for no more than three months. If the state budget has not been approved within the first quarter of the year, the National Assembly must provide a temporary extension of budget authority. There has only been one instance of the need for a short-term extension, in 1997 when the budget was enacted on 1 July.

For 2009, Bulgaria is executing the budget under a 90% rule, under which the non-interest expenditure and transfers from the republican budget are reduced by 10% to ensure that revenues are sufficient to meet fiscal policy requirements. The only exclusion from this requirement concerns the social security expenditures on pensions. The reduction is implemented through the Council of Ministers decree, not the budget approved by the National Assembly, by reducing the monthly appropriation allotment by 10%. If the mid-year report that is presented to the National Assembly in September shows revenues meeting targets, the remaining 10% can be released. In recent years, budgets have been held to a 93% rule. The 93% and 90% rules have been used for six of the past seven years (*i.e.* 2003-07; 2009). The reserve requirement was not used in 2008, but was reinstated in 2009 due to the financial crisis. In practice, revenues have consistently come in above expectations, allowing the release of the reserves. Non-interest expenditures and transfers under the republican budget may be further reduced if the underperformance of the consolidated fiscal revenues reaches a level that may jeopardise the balance of the Consolidated Fiscal Programme.

A second source of potential spending constraint involves co-financed EU-funded projects that could be delayed, providing another buffer of up to 7% of the consolidated budget. The budget also includes reserve funds for the social and health insurance programmes of 0.4% of GDP to cover shortfalls in revenues or unanticipated expenses. This reserve is part of an overall reserve of EUR 456 million budgeted for unexpected and urgent expenditures.

4.4. Budget execution

The State Expenditure Directorate and the Treasury Directorate have the lead on budget execution within the Ministry of Finance. Budget execution is based on the appropriations law and the Council of Ministers decree. The decree is prepared by the Ministry of Finance and subdivides the appropriations by economic classification and by programme. Upon approval of the Council of Ministers decree allocating the budget, the Ministry of Finance issues guidelines for budget execution, including monthly allocations. These guidelines serve as the basis for payments from the treasury system for line ministries and first-level spending units and for transfers to municipalities. For 2009, the monthly allocations are based on the 90% rule.

The State Expenditure Directorate reviews reallocation proposals of the line ministries and other first-level spending units who in turn review requests for reallocations among their second-level spending units. The criteria followed are the legal context, the government priorities, economy and efficiency. The regularity of expenditure is also reviewed, particularly with regard to the need for large procurements. Expenditures are monitored on an ongoing basis against the financing plan of the budget and to ensure that arrears are not built up. Line ministries are required to have approved internal control systems and to appoint financial controllers (see Section 5.2 below on internal control).

The Ministry of Finance (*i.e.* the Treasury Directorate) receives substantial reports on budget execution:

- Data on cash execution four times per month from the Bulgarian National Bank, used by the Ministry of Finance for cash management, not for public release.
- Monthly reports from line ministries providing files broken down by paragraph, 10 days after the end of the month, consolidated within 30 days after the end of the month, provided to the Council of Ministers and released to the public.

- Quarterly and annual cash reports by detailed budget classification (by subparagraph), 90 days after the reference period, consolidated within 45 days. They also include information on the expenditures of the first-level spending units by function, group and activity, as specified in the unified budget classification.
- Trial balances of first-level spending units accounting data, 45 days after the end of the period, not for public release, consolidated and used for fiscal notification and GFS purposes, where the methodology of ESA 95 (European System of Accounts; see Eurostat, 1996) and GFSM 2001 (see IMF, 2001) is used.
- Annual reports that have been produced in the GFSM 2001 framework since 2003.

4.5. *Cash and debt management*

The Ministry of Finance began implementing the treasury single account (TSA) in 1999 with support from SIGMA, the EU, the IMF, and the World Bank. On 18 June 2000, all funds – either on budget, extrabudgetary or in accounts in the Bulgarian National Bank (BNB) – were centralised in the TSA system. In 2003, the Ministry of Finance was reorganised to create the Treasury Directorate under an appointed State Treasurer.

The treasury single account is an account or set of linked accounts in the BNB through which the government transacts all payments. Under the TSA system, each second-level spending unit (agencies, etc.) has two accounts: a transit, or zero-balanced, account for centralisation of revenues in the line ministries/first-level spending units' accounts in the BNB, and a cash account for payments of cash. The central government has about 4 000 accounts in the BNB and commercial banks. The TSA in the Bulgarian National Bank covers all line ministries/first-level spending units, autonomous budget accounts, social security and national health insurance, and some second-level spending units served by the BNB. It does not cover municipal governments' own finances and some universities in the country. There was an attempt to include municipalities in the TSA, but this was not realised.

The System for Electronic Budget Payments (SEBRA) was developed for automated management and control of payments initiated by the spending units included in the treasury single account system within the spending limits of line ministries/first-level spending units' accounts determined by Ministry of Finance. The approved allocations are recorded in the SEBRA system and spending units authorise payments that are administered by a network of the bank system. The SEBRA system verifies that each payment is within the authorised budget allocation. SEBRA allows the Ministry of Finance to monitor the daily expenditures of the FLSUs and the FLSUs to control the expenditures of the lower-level spending units. To summarise, the different steps are as follows:

1. Order issued by line manager.
2. Order approved by head of organisation or designee.
3. Order checked by accountant to verify within budget and cash-flow forecast.
4. Review by financial controller to verify signatures of manager, head of organisation and accountant.
5. Payment request presented to commercial bank.
6. Request entered into SEBRA system, verifying availability of funds (the Treasury Directorate and the State Expenditure Directorate have access to the SEBRA system to facilitate monitoring of cash transactions).
7. Payment issued.
8. *Ex post* review by the Public Financial Inspection Agency.

The cash management staff in the Treasury Directorate monitors liquidity, payment limits in the TSA for first-level spending units, ceilings on transfers to municipalities, daily forecasts for receipts and payment for the central budget, and other daily reports.

Over the past ten years (1999-2008), the ratio of general government debt to GDP has dropped from 79% to 14% of GDP. Interest expense has consequently dropped from 3.8% in 1999 to 0.9% of GDP in 2008 (a reduction of 86%). The ratio of interest to overall expenditure has been reduced from 9.6% in 2000 to 2.3% in 2008. This impressive improvement in the government debt of Bulgaria has been the result of strict fiscal policies and the resulting government surpluses over the past several years, as well as high GDP growth. The restraint in government spending has allowed Bulgaria to repay the IMF, Brady Bonds, and most World Bank debt. Current outstanding debt is roughly two-thirds external debt and one-third internal debt.

Debt management is the responsibility of the Government Debt and Financial Markets Directorate under the State Treasurer. Bulgaria has developed a debt management strategy for 2009-11. The State Debt Law establishes requirements for three debt ceilings: limitations on new state debt, new sovereign guarantees, and debt outstanding at year-end. Guarantees for individual investment projects are included under the debt limit as sovereign guarantees.[6] Sovereign guarantees are estimated to be EUR 0.6 billion. The Municipal Debt Act limits municipal borrowing to borrowing for infrastructure investment and borrowing to roll over debt. Municipal borrowing accounts for about 4.2% of consolidated debt.

The debt management strategy for 2009-11 took into account the economic downturn. Forecasts were based on parameters prepared by the Executive Agency for Economic Analysis and Forecasting. The strategy includes scenarios about needed funds for debt service, ranging from pessimistic to optimistic. Bulgaria has arranged a credit agreement with the World Bank to provide USD 300 million annually if needed to support structural reforms. Bulgaria has also arranged a loan of EUR 700 million with the European Investment Bank.

4.6. Human resources

As of end 2008, the total number of administrative entities in the central administration is 107 (16 ministries, 24 entities subordinated to the Council of Ministers, 61 entities under ministers, and 6 state institutions reporting to the National Assembly). There are 28 regional administrations, 264 municipal administrations, 35 district municipal administrations, and 113 specialised territorial administrations.

Data for 2008 show that there are 86 877 established positions in the central state administration; 47.5% of the employees work under civil service contracts and 52.5% under labour contracts.

Bulgarian public salaries are among the lowest in the EU. Until 2008, control of personnel compensation was quite rigid in Bulgaria. The Council of Ministers annually approved the average gross salary for each category of public employee. Since the beginning of 2009, the average gross salary constraint was eliminated; managers were given some flexibility to reduce the number of employees so as to free up resources and allow an increase in salaries for the remainder of their employees. Compared with the private sector, the public sector has higher average salaries, but the numbers are misleading due to the size of the "grey" sector of unreported income in Bulgaria that results in understating the compensation of private

Table 11. **Numbers in public and private employment**

Sector	Full-time employees
Employees in the public sector	618 120
of which:	
Employees on budget	*401 232*
Employees working under civil service contract	*35 991*
Employees in the private sector	1 735 756
Total	**2 353 876**

Source: Ministry of Finance, Bulgaria.

employees. Salaries for groups of specialised employees may show larger differences between public and private sectors – for example, salaries of public internal auditors are substantially less than comparable private sector salaries. Base salaries in government are augmented by "fringe" payments for longevity, education, and performance. Performance is only one criterion for determining compensation, not the major determinant.

The positions in the administration are defined at various levels according to the type of contract, the professional experience and the educational requirements, as stipulated in the Unified Classification of Positions in the Administration (UCPA). Salaries of employees in the state administration are defined according to the Council of Ministers decree on salaries in public sector organisations and functions. An annex to the decree sets forth a table on the amount of minimum and maximum monthly salaries by position levels.

Human resource management is the responsibility of the Ministry of State Administration. The ministry has been implementing reforms in recruitment and personnel appraisal to enhance transparency and increase emphasis on staff performance. Beginning in 2003, greater competition has been implemented for recruitment. A central process was launched for recruitment of junior personnel: 2 000 candidates took competitive exams and 600 candidates were approved, of which 60 to 70 now work for the government. The approved candidates are listed in a database, but ministries are not required to hire from the approved list if they use competitive procedures to recruit staff. A British model of personnel evaluation has been adopted to strengthen the performance content of evaluations which involves a three-step process:

- An annual performance plan is developed jointly between the employee and the manager.
- Interim meetings are held mid-year to review performance.
- A formal evaluation is conducted annually to review the degree to which objectives are met, the level of competence of the employee, and the fulfillment of tasks.

4.7. Procurement

The Bulgarian procurement policy was established by the Public Procurement Act of 2004. Rules for its implementation and ordinances for small procurement and special purpose procurement (all drafted according to EU guidelines) expand upon this authority. The Public Procurement Agency (PPA) of the Ministry of Economy and Energy is responsible for procurement management under the responsibility of the minister. The PPA issues guidelines, monitors public procurement including *ex ante* control for large-scale procurement,[7] and maintains a procurement register. The register lists all procurement tenders and announces procurement awardees. It is intended to enhance the competitiveness of the procurement system and provide greater transparency for the procurement process. Although some of the infrastructure has been put in place, at this point Bulgaria does not use e-procurement to any significant extent, but does use central procurement for some ministries – for example, for computer purchases. The Italian government has provided technical support for centralised procurement procedures.

In 2006, a commission was established to respond to appeals of procurement actions: the Commission on Protection of Competition. The Commission reports to the National Assembly. In 2007, the first year of the Commission's operations, about 400 appeals were heard, about half of which were dismissed. About 30 cases were appealed to the Supreme Administrative Court. In 2008, roughly 500 to 600 cases were heard. The results of these reviews are not known at present.

4.8. The role of municipalities

According to the Bulgarian Constitution, the territory is divided into regions and municipalities. In 2009, 28 regions and 264 municipalities covered the needs of about 5 330 settlements and their respective citizens. While a region is defined as an administrative unit "entrusted with the conduct of a regional policy, the implementation of state government on a local level, and the ensuring of harmony of national and local interest", the municipality is the basic administrative territorial unit where self-government is practised. Thus municipalities are characterised as follows:

- They are defined as legal entities.
- Citizens participate in government, directly and through elected bodies.
- The municipal council as a body of self-government is directly elected.
- The mayor, elected by the citizens, is the main executive power.
- Municipalities, in contrast to regions, possess their own budgets and are entitled to permanent revenues by law.

In 2008, the size of total municipal spending amounted to 7.6% of GDP and about 20% of the expenditures of the Consolidated Fiscal Programme. Municipalities, as the lowest government level, are responsible for resolving issues relating to municipal property, finance and administration, as well as relating to culture, including theatres, museums, libraries or public works such as water and sewerage or local public transport. In addition, municipalities execute and budget for activities delegated by the state, especially in the sectors of education, health care and social support.

The municipal budgeting procedure follows the general budgeting timetable and adopts the general procedure (see Section 2). Each municipality is in charge of its own budget. All 264 municipal budgets are part of the state's autonomous budgets and are included in the Consolidated Fiscal Programme. The Municipal Budgets Act – introduced in 1998 and since modified several times – defines the basic regulatory framework for the municipal budgeting process. It bases the process on the principles of legality, appropriateness of purpose, efficiency, effectiveness, and public openness. Other regulations like the Municipal Debt Act or the Local Administration Act complete the judicial framework.

The municipal budget formulation process takes place in the following way:

- The mayor – the chief executive of a municipality – establishes a first draft of the municipal budget, taking into account the municipality's strategy, its development plan, the financing obligations for municipal debt, and the division of local and delegated activities. The mayor considers the proposals of the competent ministries regarding structural changes in activities delegated by the state as well as information from the Ministry of Finance concerning the expected transfers from the state budget. The revenue administration at the national level co-operates with the municipality in the estimation of the annual amount and monthly proceeds from the revenues (Article 11[2], Municipal Budgets Act).

- The own revenue and local expenditure estimates are submitted to the Ministry of Finance. At the same time, the mayor delivers a proposal for the amount of *ad hoc* grants needed from the state budget for capital expenditure purposes. Finally, the mayor also submits the municipality's intended level of borrowing (Articles 11[3] and [4], Municipal Budgets Act).
- The draft budget should consider proceeds from subsidies from the central budget as well as general assumptions on the development of delegated activities by the state as set in the national budget (see also subsection 4.8.1 on state budget subsidies to municipalities).
- The draft budget is made available for public discussion under procedures established by the municipal council.
- The municipal council discusses and reviews the budget proposal and finally adopts the municipal budget.
- Within one month following its adoption, the municipal budget is submitted to the competent regional office of the National Audit Office as well as to the Ministry of Finance.

The budget formulation process shows the institutional independence of the municipal budget from the central state. An exception nevertheless exists for the delegated activities: during the budgeting process for preparing the draft national budget, the National Association of Municipalities is supposed to make a proposal concerning the total amount of financial support from the central budget to municipal budgets which is presented to the Ministry of Finance's Local Government Financing Directorate. A draft bill is then developed by the Ministry of Finance and discussed with the National Association of Municipalities. Any differences in opinion should be reflected in a protocol and be reviewed by the Council of Ministers which finally has to adopt the amount of financial assistance that the state budget gives to the municipal budgets. All transfers and subsidies provided by the state are thus included in the state budget and are subject to the National Assembly's approval. The National Audit Office audits the implementation of the financial support from the state budget and municipal budgets.

Municipal budgets are supposed to show all revenues and expenditures for a given period. According to law, municipal revenues in Bulgaria consist of own revenues such as fees, taxes and revenues from municipal property. About 32.6% of the total municipal expenditures and their extrabudgetary funds' expenditures are financed through own revenues (if grants are included as own revenue, the amount is 35.4%). Local fees, such as fees for sewerage, rubbish removal or kindergartens, and the sale of non-financial assets cover about two-thirds of these own revenues. Local taxes, such as the property or transport vehicle tax, cover about one-third of the total amount of own revenues. About 50% of municipal expenditures in 2008 are financed by transfers and subsidies from the central government.

Although municipal own revenues are relatively low and revenue arrears exist in most of the municipalities, municipal debt is not used as an alternative. The total amount of municipal debt is insignificant. According to the Municipal Debt Act, municipalities are allowed to borrow from banks and other financial institutions There are no limits to the amount of borrowing, but there are limits to the amount of payments, as follows (Article 12, Municipal Debt Act):

- The annual amount of payments on the debt during each particular year may not exceed 25% of the sum total of revenues from own sources and the block equalising grant under the last audited report on the implementation of the budget of the municipality.
- The nominal value of the municipal guarantees issued may not exceed 5% of the sum total of revenues from own sources and the block equalising grant under the last audited report on the implementation of the budget of the municipality.

4.8.1. State budget subsidies to municipalities

In 2008, about 45% of total municipal expenditures were mandatory – they are governed by a national law other than the budget, and include education and health care. The execution of these laws has been delegated to municipalities by the central government, which also finances these mandates via transfers and subsidies of the following categories:

- Subsidies to fund-delegated activities: Since 2008, all mandated activities are financed by subsidies. Previously mandated activity had also been financed by a municipal share in the personal income tax. Due to a very unequal division of the personal income tax, this financing instrument was given up in 2008.
- An equalisation grant for local activities: The equalisation grant is designed to ensure a minimal level of local service provision in municipalities. Criteria for the distribution of grants to municipalities are determined by the Minister of Finance and the National Association of Municipalities. Among other factors, they take into account the municipal expenditures for child care and home care as well as revenues from local taxes, and provide inflationary compensation.
- An *ad hoc* grant allocated for capital expenditure (as local or delegated activity): The Minister of Finance and the National Association of Municipalities are responsible for determining the amount of *ad hoc* grants for capital expenditures as well as the criteria for their distribution.
- An *ad hoc* grant can be allocated for the implementation of the state policy to promote the development of municipalities and for the implementation of national, regional or international programmes and for co-financing under EU programmes.

4.9. Conclusions and recommendations

Bulgaria's budget management has seen a series of structural and procedural reforms in budget execution, treasury functions, internal audit, and programme and medium-term budgeting. The assessment of the Ministry of Finance is that these reforms have resulted in stronger controls of budget aggregates and more delegation of budget details. Budget control, evaluation, and programme assessment and auditing still require attention:

- Budget execution in Bulgaria remains focused primarily on the legality and propriety of budget inputs. The culture of bureaucracy has not embraced a management focus on programme performance and results. As the programme budget is implemented, steps should be taken to shift greater responsibility for budgets to programme managers, and to reduce centralised control. Budget reporting will need to highlight programme results to a greater extent.

- The cash and debt management practices of Bulgaria reflect good practice principles. Efficiencies may be possible by including municipal finance in the TSA and the SEBRA systems, rather than having municipalities develop their own cash management tools, but improved efficiency could involve a perception of the loss of local control.
- Strengthening the management culture within the line ministries is essential to greater accountability for programme performance. More planning is needed to tie personnel to performance. The changes in personnel compensation providing more discretion to spending units appear to be a step in the right direction, but emphasis should be increased on performance-related compensation.

5. Accounting and audit

Within the past several years, Bulgaria has made substantial progress in strengthening its accountability systems, including strengthened public accounting, restructuring the internal audit system to distribute internal audit among the first-level spending units and, a little over ten years ago, the establishment of the National Audit Office. This section is presented in three subsections: accounting, internal control, and the National Audit Office.

5.1. *Accounting*

In accordance with the Bulgarian budget and accounting legislation, budget units apply a unified chart of accounts (for reporting on an accrual basis), a unified budget classification (for reporting on a cash basis), and the related instruction of the Minister of Finance. The framework for reporting by budget entities was developed on the basis of:

- The EU requirements for the accounting, the statistics and the budgeting of the public sector.
- The accounting framework, principles and concepts of the GFSM issued by the IMF.
- The international public sector accounting standards.
- The requirements of the Bulgarian legislation concerning budgeting, execution and reporting of the Consolidated Fiscal Programme, and management and control of funds and expenditure of the budget units.

In agreement with the IMF, a uniform chart of accounts (CoA) for the budget sector was developed in 2000. The development of the CoA corresponds to the commitments made to the EU for improving budget resources management, strengthening fiscal discipline, and increasing transparency in planning, execution and reporting of the state budget. During the work process, the structure of the CoA was discussed and agreed with advisers from the European Commission, SIGMA, and the IMF technical assistance missions. The State Budget Act for 2001 required budget entities to use the chart of accounts approved by the Minister of Finance. The structure of the accounts and the principles and rules for recognition, valuation and classification of assets, liabilities, revenues and expenditures in the chart of accounts are on the whole established in harmony with the accounting framework of the new IMF *Government Finance Statistics Manual* (GFSM 2001) and the European System of Accounts (ESA 95) (Eurostat, 1996). The transition to the new chart of accounts makes possible consolidation of the financial reports on an accrual basis in order to ensure availability of financial information for the purposes of macroeconomic and fiscal analysis. The State Treasurer is the officer within the Ministry of Finance responsible for accounting standards and reporting methodology.

The unified budget classification continues to exist as the public sector accounting framework for cash basis purposes. This is necessary in view of the legally stipulated practice of preparing and reporting, on a cash basis, the state budget, the municipalities' budgets, the autonomous budgets and the extrabudgetary accounts and funds, and in order to provide cash-based public finance data to international institutions and organisations as well.

According to the Organic Budget Law, monthly, quarterly and annual reports are prepared on a cash basis. Quarterly and annual financial reports are also prepared on an accrual basis, consolidated and used for ESA 95 and GFS purposes and for the purposes of macroeconomic and fiscal analysis as well. Depreciation is not included in the accounting.

5.2. Internal control

In 2005, recognising weakness in the management of ministries and other first-level spending units, Bulgaria launched an effort to shift responsibility for internal audit from central government to the spending units. Three laws were enacted in early 2006 to shift functions from the centralised public internal financial control system to the ministries:

- Financial Management Control Law.
- Internal Audit Law.
- Financial Inspection Law.

The Internal Control Directorate was created in the Ministry of Finance to support this initiative. The legislation established a decentralised model of internal control based on the Professional Practices Framework of the Institute of Internal Auditors. Internal auditors were to report directly to heads of organisations, were to be independent and were subject to qualification requirements necessitating successful passage of an examination and certification by the Ministry of Finance.

Internal audits' tasks are to identify and assess risks in ministry/municipality processes, evaluate the efficiency and effectiveness of financial management and control systems, and make recommendations for improvements in the effectiveness of the government's activities. The reports of the internal auditors are presented to ministry/municipality/agency managers. The managers are required to respond to the reports in writing with action plans for correcting identified problems. Shifting the focus of internal audits from financial inspection to management improvement is a major challenge. The primary focus in the past has been the legality and propriety of public expenditure emphasising budgetary inputs. The goal of the internal audit processes it to strengthen management, not identify wrongdoing.

At the time of the decentralisation of these functions, the central Public Financial Inspection Agency (PFIA) under the Ministry of Finance had 1 300 staff. These staff were reassigned to the first-level spending units. Only 166 people remain in the Public Financial Inspection Agency. The primary function of the remaining central staff is to perform *ex post* financial inspections on request, potentially leading to action by the public prosecutor or Public Procurement Agency. A total of 463 internal auditors have been hired by first-level spending units: 16 ministries, 34 agencies and administrations, and 108 municipalities have internal audit offices staffed with a minimum of two to ten auditors, 149 smaller municipalities and agencies are to have at least single auditors according to the Internal Audit Law. Many of these small offices may be too small to be effective. Of this group, at present approximately 50 have vacancies. The number of internal auditors depends upon the size of the budget and the staff of the organisation. Six hundred of the original staff members of the agency have not yet been reassigned.

The reorganisation has been a difficult process. Some of the previous staff of the Public Financial Inspection Agency did not pass the qualification exams. Others were reluctant to relocate to distant municipalities. Still others have not been selected by offices or municipalities with vacancies. Finally, many of the smaller municipalities do not pay wages at the same level as the central government or the agency.

The Internal Control Directorate of the Ministry of Finance has been responsible for implementing this reorganisation, which it is doing by providing a framework rather than a hands-on, top-down approach. This office prepares guidelines for internal audits, provides training, conducts qualification examinations, provides professional support and monitors the quality of internal audit reports. It also maintains a website that presents the results of the internal audits, maintains a roster of vacancies for internal auditors, and lists candidates available for posting. The Internal Control Directorate has organised a networking group consisting of internal auditors from the ministries that spend EU funds to implement new guidelines on a pilot basis. The networking group has provided active support in the development of procedures and training, and has generally strengthened the process.

The Internal Control Directorate maintains a close working relationship with the National Audit Office, commenting on audit standards and consulting on issues of shared concern. The Anti-Corruption Committee of Parliament is active in its review of the findings of the internal audits, as is the Subcommittee for EU Management for EU-related projects.

There are still a number of problems hindering the full implementation of the distributed internal control system. There has been a relatively high turnover of staff. Some staff lack the skills or do not have the capacity to pass the exams and be certified as internal auditors. Some of the managers of small agencies or municipalities lack a good understanding of the potential benefits of having their own internal auditors; the heads do not know how to use them or might not wish to. There are other cases where the internal auditors and management do not communicate well, leading to frustration on both sides. Internal auditors lack the job security to be able to exercise independence in carrying out their responsibilities. Finally, there is a danger that internal audit will be converted to internal inspection, identifying wrongdoing rather than systematic improvements.

5.3. National Audit Office

The National Audit Office was established as an institution by the Constitution of 1991. It began operations in 1995, and was formally authorised by the National Audit Office Act of 2001. The office was created as the external audit body for all budget funds and state authorities; it was not given judicial powers. It is collective body with a president and ten members. The members have a nine-year mandate; the term for the current office began in 2005. Members are appointed on a non-partisan basis. The Office has a total staff of 520 with from 350 to 370 auditors. It is organised into ten audit divisions, one headed by each member, each with a staff of 15 to 25 people. Approximately 200 staff members are located in Sofia. The NAO has six regional offices that cover the rest of the country. The model adopted in Bulgaria reflected a review by the Bulgarian authorities of the German, Dutch, British and European courts of auditors.

The National Audit Office regulates its own powers and functions. It establishes national audit standards, prepares an audit handbook, and maintains internal guidelines covering a code of ethics, approval of its budget and strategic plans. The Board approves an annual work plan based on risk assessment, public interest, and historical work. The Board is completely independent in developing its plan, but does not ignore issues brought to its attention by the government. Parliament is authorised to request up to five audits per year, but rarely uses this authority. In 2008, Parliament requested two audits of EU fund management systems. Some audits address internal control of ministries and municipalities, others the disposal of state-owned properties, rental of state-owned properties, or administration of municipal revenue. The judiciary and Parliament have both been audited. During 2008, 491 audits were assigned, 41 of which (8.4%) were performance audits.

The Board of the National Audit Office approves the audit report findings and conclusions. A summary of each report is published on the website. The report is sent to the entity that was audited. The audited entity is given a deadline to comply with the recommendations. The National Audit Office follows up on implementation: first through a written response by the entity, then by a visit from a National Audit Office team. Recommendations to second-level spending units are also provided to relevant line ministries and first-level spending units. Issues concerning procurement are brought to the attention of the Ministry of Finance; criminal findings to the prosecutor. An annual report to Parliament covers everything done during the year, including summary statistics of audits.

The National Audit Office certifies the annual financial reports of the line ministries (FLSUs) every year and does an audit of the report of the state budget.

5.4. Conclusions and recommendations

As the leaders of the Internal Control Directorate acknowledge, the transition to the distributed internal control system has been difficult. Nevertheless, it appears that the government of Bulgaria is taking the appropriate actions. Regular meetings with the heads of internal audit units in ministries are providing valuable input and creating a sense of ownership among the internal audit community. Substantial effort is being devoted to training. Consideration could be given to establishing consolidated internal audit offices for groups of smaller municipalities to insure that the offices are large enough to be effective.

The accounting and internal audit reforms appear to be well designed; the challenge is in implementation. Internal audit will require some time to further train the customers and the internal audit professionals to understand their respective roles. Continued collaboration between the National Audit Office and the internal auditors should result in improved public service for Bulgaria.

Notes

1. The Ministry of Finance prepares a new government debt management strategy every three years, and it is updated after the first and second year following its adoption. The most recent strategy covers the period 2009 to 2011.
2. Questions 29 to 31 in the *OECD International Budget Practices and Procedures Database* (OECD, 2008).
3. Broadly, a programme is a grouping of government activities in relation to a specific set of policy objectives.
4. Note that cash management (24 staff), debt management (26 staff), tax policy (34 staff), and internal control and audit (24 staff) are in other directorates in the Ministry of Finance.

5. Twenty OECD countries responded that the judiciary is subject to the same procedures and policies as any other governmental organisation included in the executive budget proposal.
6. A separate ceiling is enacted for guaranteed debt to limit the programme expenditures through guaranteed borrowing. Many OECD countries have similar limits.
7. As of January 2009, the PPA carries out *ex ante* control of: *i)* procedures for the award of public contracts, financed by EU funds, which comply with specific requirements; and *ii)* negotiated procedures without notice, awarded by contract authorities.

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ANNEX A1

Table A1.1. **First-level spending units (FLSUs)**

1	National Assembly
2	National Audit Office
3	Supreme Judicial Council
4	Office of the President
5	Council of Ministers
6	Constitutional Court
7	Ministry of Finance
8	Ministry of Foreign Affairs
9	Ministry of Defence
10	Ministry of Interior
11	Ministry of Justice
12	Ministry of Labour and Social Policy
13	Ministry of Health
14	Ministry of Education and Science
15	Ministry of Culture
16	Ministry of Environment and Water
17	Ministry of Economy and Energy
18	Ministry of Regional Development and Public Works
19	Ministry of Agriculture and Food
20	Ministry of Transport
21	Ministry of State Administration and Administrative Reform
22	Ministry of Emergency Situations
23	State Agency National Security
24	State Forestry Agency
25	The Committee for Disclosing and Announcing Affiliation of Bulgarian Citizens to the State Security and the Intelligence Services of the Bulgarian National Army
26	Commission for Protection against Discrimination
27	Commission for Personal Data Protection
28	State Agency for Information Technology and Communications
29	State Agency for Youth and Sport
30	The Commission for Establishing of Property Acquired from Criminal Activity
31	National Protective Services
32	National Intelligence Service
33	Ombudsman
34	National Statistical Institute
35	Bulgarian Patent Office
36	Communications Regulation Commission
37	Council for Electronic Media
38	State Energy and Water Regulatory Commission
39	Nuclear Regulatory Agency
40	Financial Supervision Commission
41	State Commission on Information Security
42	National Tourism Agency
43	National Agency Road Infrastructure
44	National Social Security Institute
45	National Health Insurance Fund
46	Bulgarian National Television
47	Bulgarian National Radio
	Municipalities = 264

Table A1.2. **Examples of second-level spending units (SLSUs)**

SLSUs of the Ministry of Finance	
1	National Revenue Agency
2	National Customs Agency
3	Public Internal Financial Control Agency
4	State Receivables Collection Agency
5	Executive Agency for Economic Analysis and Forecasting
6	State Commission on Gambling
7	Executive Agency for the Audit of EU Funds
SLSUs of the Ministry of Transport	
1	Executive Agency “Maritime Administration”
2	Executive Agency “Railway Administration”
3	Executive Agency “Maintenance and Study of the Danube River”
4	Executive Agency “Automobile Administration”
5	General Directorate “Civil Aeronautical Administration”
6	Air Squad 28
SLSUs of the Ministry of Labour and Social Policy	
1	National Employment Agency
2	Social Assistance Agency
3	Executive Agency “General Labour Inspectorate”
4	State Agency for Child Protection
5	Agency of People with Disabilities
6	“Work Conditions” Fund
7	Social Investment Fund
8	National Institute for Conciliation and Arbitration
9	Centre for Human Resources Development and Regional Initiatives
10	Bulgarian-German Vocational Training Centres (5): Pazardjik, Pleven, Smolyan, Stara Zagora, Tzarevo
11	Social Assistance Fund

Table A1.3. **Unified classification of positions in the administration**

Position level	Name of position	Minimum educational requirements for holding a position	Minimum rank for holding a position	Minimum professional experience for holding a position	Type of employment contract
1	2	3	4	5	6
A.	**Management positions**				
A1	Secretary general of the Council of Ministers, of the administration of the National Assembly and of the President	Master's degree	III senior	10 years	Civil service
A2	Secretary general of a ministry, administrative secretary of the Ministry of Foreign Affairs; director within the administration of the National Assembly, of the President and of the Council of Ministers (CoM)	Master's degree	IV senior	9 years	Civil service
A3	Head of unit in the administration of the National Assembly, of the President and of the CoM	Master's degree	V senior	8 years	Civil service
A4	Secretary general of a second-level administration; state treasurer of the Ministry of Finance; secretary of Sofia (metropolitan) municipality	Master's degree	V senior	7 years	Civil service
A4	…	Bachelor degree	I junior	7 years	Civil service
A5	Secretary of a municipality having over 50 000 inhabitants	Bachelor degree	I junior	6 years	Civil service
A5	Director of a directorate; chief director of a chief directorate of a second-level administration; deputy director of a directorate in the National Revenue Agency; head of unit in a ministry or in a first-level administration;…	Master's degree	I junior	6 years	Civil service
A6	Secretary of a municipality having less than 50 000 inhabitants…	Bachelor degree	II junior	6 years	Civil service
A6	Head of unit; deputy head of a customs authority…	Master's degree	II junior	6 years	Civil service
A6	Head of section in a ministry or in a first-level administration…	Bachelor degree	II junior	6 years	Civil service
A7	…	Bachelor degree	III junior	5 years	Civil service
A8	…	Bachelor degree	III junior	4 years	Civil service
A9	…	Bachelor degree	III junior	3 years	Civil service
B.	**Expert positions having analytical and/or control functions**				
B1	Adviser in the administration of the National Assembly, of the President and of the CoM	Master's degree	I junior	8 years	Civil service
B2	State expert; state internal auditor; chief accountant; chief legal adviser; … in the administration of the National Assembly, the President and the CoM; government interpreter/translator	Master's degree	I junior	6 years	Civil service
B3	State expert; state internal auditor; chief accountant; chief legal adviser in a ministry and first-level administration…	Master's degree	II junior	5 years	Civil service
…	….	…	…	…	…
B11	Junior expert in a town/village council	Occupational bachelor	V junior	Not required	Civil service
C.	**Expert positions having auxiliary functions**				
C1	Chief specialist; senior accountant in the National Assembly, of the President and of the CoM	Secondary education		3 years	Labour contract
…..	…	…	…	…..	…
C9	Junior specialist in a town/village council	Secondary education		Not required	Labour contract
D.	**Technical staff**				
D1	Clerk	Secondary education		Not required	Labour contract
D2	Clerk			Not required	Labour contract
D3	Clerk	Not required		Not required	Labour contract

Table A1.4. **Consolidated Fiscal Programme of Bulgaria**

	t	t + 1	t + 2	t + 3
Total revenues				
Tax revenues				
Direct taxes				
Corporate taxes				
Income tax				
Social insurance contributions				
Pension and unemployment contributions				
Health Insurance Fund				
Indirect taxes				
Value-added tax				
Excise duties				
Customs duties				
Others				
Non-tax revenues				
Bulgarian National Bank transfers				
Others				
Grants and donations				
Domestic grants				
Grants from abroad				
Total expenditure with the EU contribution				
Total expenditure				
Total non-interest expenditure				
Current non-interest expenditure				
Compensation				
Wages and salaries				
Scholarships				
Social security payments from employers				
Social security contributions				
Health social insurance paid by the employers				
Additional compulsory social security contributions				
Maintenance and operations				
Subsidies – Total				
Subsidies				
Subsidies for health care and medical assistance				
Social expenditures				
Pension fund				
Social assistance and unemployment				
Health Insurance Fund				
Capital expenditures				
Contingency				
Structural reform, fiscal sustainability				
Budget				
Health Insurance Fund				
Parliament				
Judiciary authority				
Pension fund				
Natural disaster				
Interest				
External				
Domestic				
EU contribution				
Primary balance				
Overall balance				
GDP				