

**Bulgaria: Report on the Observance of Standards and Codes—
Fiscal Transparency Module**

This Report on the Observance of Standards and Codes on Fiscal Transparency for Bulgaria was prepared by a staff team of the International Monetary Fund as background documentation for the periodic consultation with the member country. It is based on the information available at the time it was completed on August 4, 2005. The views expressed in this document are those of the staff team and do not necessarily reflect the views of the government of Bulgaria or the Executive Board of the IMF.

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**International Monetary Fund
Washington, D.C.**

INTERNATIONAL MONETARY FUND

BULGARIA

**Report on the Observance of Standards and Codes (ROSC)
Fiscal Transparency Module**

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August 4, 2005

Executive Summary

This report provides an assessment of fiscal transparency practices in Bulgaria in relation to the requirements of the IMF *Code of Good Practices on Fiscal Transparency* based on discussions with the authorities and other organizations, the authorities' response to the IMF fiscal transparency questionnaire, and other sources of information. The IMF *Manual on Fiscal Transparency* (<http://www.imf.org/external/np/fad/trans/manual/>) should be consulted for further explanation of the terms and concepts discussed in this report.

Bulgaria has made considerable progress in improving fiscal transparency since the 2000 ROSC, much of it linked to European Union accession requirements. Areas of improvement include closure of most extrabudgetary funds, publication of arrears data, clarification of procurement, customs, and privatization legislation, strengthening of tax and customs administration, reductions in quasi-fiscal activities of public corporations, and development of a more medium-term approach to budgeting. Bulgaria meets the requirements of the Code in a number of areas, including the consistent use of the general government as the basis for fiscal management, clear definition of the fiscal roles of the branches of government, and independence of external audit. Areas where Bulgaria approaches best practice include the timeliness of within year fiscal reporting and reporting on the final general government outturn, and debt reporting.

Effective implementation of recently-enacted laws will, however, be crucial to achieving the level of transparency stipulated in legislation. This will be a challenge given long-standing weaknesses in public administration and control systems.

There remain many other areas, however, where further improvements are needed to meet the requirements of the Code. The key areas where action is recommended are:

(1) elimination of provisions permitting the government to spend, without prior parliamentary appropriation, revenues that exceed those forecast in the budget; (2) publishing the budget execution report promptly at the time of its tabling in parliament; (3) significantly expanding the information provided to parliament with the annual budget (e.g., full medium-term fiscal forecasts, expanded information on fiscal risks, details of concessions, financial asset holdings); (4) discontinuing the use of company structures to carry out predominately government fiscal activities; (5) strengthening the independence of the procurement agency; (6) modernizing internal control; (7) further strengthening tax and customs administration; (8) appropriating spending in the budget to a more disaggregated level of administrative units, and reducing the discretionary ability of the government to transfer funds between appropriations during budget execution; and (9) presenting a mid-year report to parliament on budget execution.

A number of the above recommendations should, as a matter of priority, be included in the Organic Budget Law.

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ABBREVIATIONS AND ACRONYMS

AEAF	Agency for Economic Analysis and Forecasting
BNB	Bulgarian National Bank
CFP	Consolidated Fiscal Program
CoA	Chart of Accounts
CoM	Council of Ministers
CSO	Community Service Obligations
EBF	Extrabudgetary Fund
ESA95	European System of Accounts 1995
FMIS	Financial Management Information System
GFS	Government Finance Statistics
LoBNB	Law on Bulgarian National Bank
MoF	Ministry of Finance
NAO	National Audit Office
NGOs	Nongovernmental Organizations
NSI	National Statistical Institute
NRA	National Revenue Agency
NFPCs	Nonfinancial Public Corporations
NSSI	National Social Security Institute
OBL	Organic Budget Law
PIFCA	Public Internal Financial Control Agency
PIP	Public Investment Project
QFAs	Quasi-fiscal Activities
ROSC	Reports on the Observance of Standards and Codes
SDDS	Special Data Dissemination Standard
TSA	Treasury Single Account
VAT	Value-added Tax

WEBSITES

MoF	www.minfin.bg
Agency for Economic Analysis and Forecasting	www.aeaf.minfin.bg
PIFCA	www.advfk.minfin.bg
Privatization Agency	www.priv.government.bg
General Tax Directorate	www.taxadmin.government.bg
Customs Agency	www.customs.government.bg

I. INTRODUCTION¹

1. This report provides a reassessment of fiscal transparency practices in Bulgaria against the requirements of the IMF *Code of Good Practices on Fiscal Transparency*. It replaces the fiscal transparency ROSC prepared in August 1999 and reissued in March 2000. The assessment has two parts. The first part is a description of practice, prepared by the IMF staff on the basis of discussions with the authorities and their responses to the fiscal transparency questionnaire, and drawing on other available information. The second part is an IMF staff commentary on fiscal transparency in Bulgaria.

II. DETAILED DESCRIPTION OF PRACTICE

A. Clarity of Roles and Responsibilities

Definition of government activities

2. **General government is largely defined consistently with Government Finance Statistics (GFS) principles, and is well covered in the budget process.** The Budget Report which is presented to the National Assembly in conjunction with the annual budget appropriations presents fiscal activity on a “Consolidated Fiscal Program” (CFP) basis the institutional coverage of which is largely consistent with the GFS concept of general government. Thus the consolidated fiscal program covers not only general government bodies directly governed by the annual budget appropriations, but also extrabudgetary funds and the municipalities. Fiscal reporting is on the same basis. This represents significant progress from the position as at the time of the 2000 ROSC, when there were a large number of extrabudgetary funds which were not encompassed by fiscal reporting. Concerns have, however, arisen in relation to the recent establishment outside the budget of a Public Infrastructure Projects (PIP) company, the purpose of which is to carry out public infrastructure projects with national and local significance. Because most of the capital expenditure which it will undertake will be general government in nature, PIP constitutes an extrabudgetary fund.

¹ Discussions on fiscal transparency were held in Sofia during March 22–April 5, 2005. The staff team, comprising Mr. Robinson (head), Ms. Jacobs (FAD), and Mr. Petrie (a member of the FAD Panel of Experts), was supported by the IMF Resident Representative, Mr. Roaf, and his staff in the IMF office in Bulgaria. The team met with Deputy Finance Ministers Lingorski, Ziya, and Datzov, as well as with Mr. Katzarchev (Advisor to the Minister), and other officials and agencies from the Ministry of Finance (including the Agency for Economic Analysis and Forecasting; the General Tax Directorate and the National Customs Agency). It also met with officials from the Bulgarian National Bank, the Ministry of Economy, the Ministry of Transport and Communications, the Ministry of Health, the National Audit Office, the Public Procurement Agency, the Privatization Agency, the National Statistical Institute, the State Administration Directorate in the Council of Ministers, Sofia Municipality, the World Bank, the EU delegation in Bulgaria, the Union of Employers in Bulgaria, the Center for the Study of Democracy, and Ernst and Young (tax division). The mission was unable to meet with the members of the budget committee of the National Assembly.

Box 1. General Government in Bulgaria		% GDP
General government in Bulgaria comprises the following :		year 2004, preliminary expenditure and GDP data
Central Government Units Covered by the Central Budget:		18.9%
1. National Assembly, President's Office, Council of Ministers' Office, Constitutional Court, National Audit Office, ministries (16) and government agencies.		
2. Central Government Authorities: Judiciary Authorities; Bulgarian Academy of Sciences; State Universities; Bulgarian National TV and Bulgarian National Radio.		
Central Government Units outside the Budget:		14.8%
3. Extrabudgetary funds: Social Security Funds; Health Insurance Fund; Teacher Pension Fund; Privatization Expenditures Fund; Agricultural Fund; National Fund; State Enterprise for Management of Environmental Activities, Employees' Guaranteed Claims Fund.		
Local Government:		6.3 %
4. Local government units: 264 municipalities		
5. Municipal Extrabudgetary funds: Privatization Expenditures Fund; Special Fund for Investments and Fixed Assets; Special Account for Privatization Receipts with the Municipalities.		

3. **Relationships between government and nonfinancial public corporations (NFPCs) are being progressively clarified.** Public corporations are registered under the general Commercial Code. The size of the enterprise sector is considerably smaller with the privatization of many enterprises over the last decade. The Council of Ministers exercises ownership control, with individual ministers acting as shareholders with respect to commercial enterprises in their respective sectors, and line ministries having responsibility for policy advice and monitoring. The management boards of individual corporations are appointed by the relevant minister, and may include officials from the supervising line ministry. Generally, there is a trend to withdrawal by the line ministries from involvement in the companies' management. The central government budget includes subsidies to a number of enterprises in the transport, energy, agriculture, and communications sectors. The subsidies, which are authorized in specific laws, have been reduced in recent years in line with government policy. They are increasingly related to the actual costs of meeting specific community service obligations imposed by government. The audited annual reports of individual corporations are publicly available, but are not tabled in the National Assembly.

4. **Fiscal assistance provided to NFPCs is covered by the Law on State Aid.** An independent body, the Commission for the Protection of Competition, authorizes and

controls the granting of state aid of any kind (defined as assistance that distorts or threatens to distort free competition).² This includes fiscal assistance such as subsidies, tax deferrals, arrears to government, and debt write-offs. All central and local government bodies are required to submit details of aid granted or planned to the Minister of Finance, who in turn is required to publish a consolidated annual report. The latest State Aid Report, for 2003, was published in July 2004.

5. **There is no consolidated information on the extent of government equity holdings in private companies.** Many departments and ministries have equity holdings in private companies, although in many cases these are being sold. While information on ownership of individual companies is available through the Companies Office, there is no consolidated information publicly available on the overall extent of the government's equity holdings.

Government relations with nonfinancial public corporations (NFPCs) and the private sector

6. **Quasi-fiscal activities of NFPCs have been reduced, but some significant ones remain.** Government policy is to increase prices in sectors such as electricity for consumers hitherto charged concessional rates, in the process reducing cross-subsidies. Some cross-subsidies remain, however. General budget subsidies that have been used to compensate operational losses by NFPCs are being replaced with lower and targeted subsidies tailored to the delivery of specific noncommercial services. However, the reduction in subsidies to the transport (road and rail) sector is resulting in financial deficits due to the slow pace of reforms and the social functions they perform. For instance, Bulgaria Railways has been operating at a loss in respect to passenger transportation, for which it receives a subsidy. As a result, the Railways have considerable liabilities to other state-owned entities, including to a state company which owns the rail infrastructure.

7. **Arrangements regulating profit transfers from state enterprises to the budget are clear.** Current policy, established by the Council of Ministers, is for fifty percent of any profits of all central government public enterprises to be transferred to the budget each year, with the remainder being retained by the enterprise. This policy is set out in the Annual Budget Law, and the total expected revenues from state dividends in the next year are indicated in the Report on the State Budget Act.

8. **The legal framework for privatization has been made more transparent in recent years.** Large-scale privatization has taken place since 1992 in Bulgaria, and on current plans will be completed in 2008. Problems have been experienced with some large privatizations. The legal framework was revised in 2002 in the Privatization and Post-Privatization Control Act, which placed a greater emphasis on competitive and transparent sales processes. A key principle is that, with the exception of corporations listed in a

² State aid to agriculture, fisheries, and defense is excluded from coverage under the Act.

schedule to the Act, the government's interests in all commercial corporations are presumed to be available for privatization. The Act requires the Council of Ministers to present strategies for privatization of corporations specified in an Annex to the Privatization and Post-Privatization Control Act to the National Assembly for approval. Privatization is managed by the Privatization Agency, the supervisory board of which is elected by (and is removable by) the National Assembly. The Privatization Agency publishes an annual plan indicating its priorities and projected revenues and expenditures, and reports twice a year to the National Assembly.³ Privatization receipts are remitted to a special budget account, managed by the Minister of Finance. Ninety percent of receipts are transferred to the state budget, and ten percent to the Privatization Expense Recovery Fund. The privatization process is subject to audit by the National Audit Office (NAO), but concerns remain about the openness of the process particularly in respect to large-scale privatizations.⁴

9. **Government regulation of the nonfinancial private sector is complex, but efforts are being made to simplify business regulation.** Surveys of Bulgarian businesses suggest that lack of transparency and complexity in regulation of the private sector is a significant problem and a source of corruption.⁵ Legislation on business regulation has improved significantly. Thus in 2002 the government introduced a law aimed at simplifying central and municipal government regulation of business.⁶ Reviews and simplification of 160 regulatory regimes have now been completed. By law new regulations can only be introduced if they are specifically provided for in primary legislation, although there is no requirement for draft regulations to be published prior to enactment to allow public consultation. An independent national competition authority, the Commission for the Protection of Competition, has the role of enforcing antitrust laws. The implementation of the improved legislative framework of business regulation remains, however, a problem. Enforcement of the law by the courts is in general inadequate in Bulgaria, both because of the slowness of court proceedings and also because of corruption amongst judicial personnel, including judges. The quality of implementation of regulations by the nonjudicial public administration also continues to be

³ See the website of the Privatization Agency, at www.priv.government.bg.

⁴ Coalition 2000 observes ("Anti-corruption Reforms in Bulgaria," Coalition 2000, Center for Democracy, Sofia, 2005, available at www.anticorruption.bg) that implementation of the Privatization and Post-Privatization Control Act has been "controversial and full of changes and delays. The results of the involvement of the administrative prosecution and the courts in the privatization of the Bulgarian telecom operator and Bulgartabac Holding generated reasonable doubts as to the independence of the judiciary and the existence of strong political corruption pressure on the system." Coalition 2000 is a Bulgarian coalition that includes a range of NGOs, government institutions and the media. It has developed a Corruption Monitoring System, based on quarterly public surveys of the actual incidence of corruption since 1999.

⁵ "Corruption Assessment Report 2005," Coalition 2000, Center for Democracy, Sofia, 2003, available at www.anticorruption.bg.

⁶ *The Law for Reduction of Administrative Regulations and Administrative Control of Business Activity.*

perceived to be inadequate.⁷ Although there have been improvements in administrative practices and resources in some areas, further initiatives are required to improve the quality of regulation. There is, however, a perception that the level of “administrative” corruption⁸ affecting business has been falling.

10. Regulation of the banking sector meets international standards. The Bulgarian National Bank (BNB) is responsible for prudential regulation of the banking sector. External assessments of the quality of regulation have found that the Bulgarian banking sector is generally well supervised, and complies with the Basle core principles.⁹ Banks are required to contribute an annual fixed 0.5 percent of deposits to the Deposit Insurance Fund, and the level of the Fund’s reserves is being increased in line with EU standards. Regulation of the nonbank financial sector is conducted by an independent agency, the Financial Sector Commission. There is a need to strengthen regulation of the pensions and insurance industries.¹⁰

Government relations with the central bank and public financial sector

11. There is a clear separation between the monetary and fiscal authorities, and the BNB has a high degree of independence. The *Law on the Bulgarian National Bank* (LoBNB) prohibits the BNB from providing credit to government except against purchases of Special Drawing Rights from the IMF as part of a stabilization program supported by the Fund. The annual budget of the BNB is set by its Managing Board, and is then published in the government gazette and reported to the National Assembly. The LoBNB requires the Bank to report twice a year to the National Assembly on its activities. Expenditures are audited by the National Audit Office. The LoBNB stipulates that twenty percent of BNB profits go to a reserve fund, and the remainder is transferred to the government budget – after any amount deducted for special funds, which may be set up under a decision of the Managing Board. The amount of the annual transfer to the government budget is shown in the Report on the State Budget Act. The BNB law does not make fully clear the basis upon

⁷ These regulatory implementation problems were noted in a 2001 World Bank report (T. O’Brien and C. Filipo, *The Current Regulatory Framework Governing Business in Bulgaria*).

⁸ The World Bank defines administrative corruption as “the intentional imposition of distortions in the prescribed *implementation* of existing laws, rules, and regulations to provide advantages to either state or nonstate actors as a result of the illicit and nontransparent provision of private gains to public officials. The classic example of administrative corruption is that of a hapless shop owner forced to pay bribes to a seemingly endless stream of official inspectors to overlook minor (or possibly major) infractions of existing regulations. Beyond such forms of extortion, administrative corruption also includes such familiar examples of ‘grease payments’ as bribes to gain licenses, to smooth customs procedures, to win public procurement contracts, or to be given priority in the provision of a variety of other government services.” (*Anticorruption in Transition: a Contribution to the Policy Debate*, 2000, xvii).

⁹ See the Financial Stability Assessment, July 12, 2002, and the FSAP Follow-Up, July 2004, available on the IMF website at www.imf.org.

¹⁰ See the Financial Stability Assessment, and the FSAP Follow-Up at www.imf.org.

which the amounts deducted from profits for special funds is determined. With the passage of amendments to the LoBNB (Art. 43, para. 1) in January 2005, the government is required to pay at market prices for all fiscal agency services provided to it by the BNB. As regards the functions related to servicing the primary and secondary government securities market, the requirement related to selling issues of government securities targeted at citizens and servicing external market debt has been applied since 1997, and the requirement related to state budget information servicing has been applied since 2000.¹¹ Under the currency board arrangement, the only monetary policy tool available to the BNB is the setting of reserve deposit requirements. The BNB does not pay interest to commercial banks on these deposits. The Bank does not provide quasi-fiscal assistance to public financial corporations. It is empowered to conduct a lender of last resort function, although this facility has not been utilized.

12. **There is very limited government ownership of financial institutions.** With the privatization of the State Savings Bank, there is only one remaining central government-owned bank, the Encouragement Bank.¹² This bank, which is small in the context of the Bulgarian banking sector, provides loans to small and medium enterprises. It is mainly financed through concessional foreign loans guaranteed by government. The BNB subjects it to the same prudential regulations that it applies to the rest of the banking sector in Bulgaria.

Fiscal management relations among the branches of government

13. **The fiscal roles of the executive, legislative, and judicial branches are clearly defined in law.** The 1991 Constitution of Bulgaria (Article 84) makes budget approval, taxation and state borrowings the prerogatives of the National Assembly. It also charges the Council of Ministers with responsibility both for presenting the budget to the National Assembly, and for executing the budget when it becomes law (Articles 86(1) and 106). The Organic Budget Law (*Law on the Structure of the State Budget*) defines the relevant processes, and the respective responsibilities of the executive and the parliament, in relation to the preparation and execution of the budget. It also provides arrangements (Article 26) for the carrying out of the fiscal activities of the state should the National Assembly delay the adoption of the budget until after the start of the fiscal year.

¹¹ The law had previously prohibited the BNB from charging government for fiscal agency services except for those relating to state debt servicing. Irrespective of this, based on the State Budget Law for the current year and pursuant to an agreement between the MoF and the BNB, the government used to recover BNB's costs related to state budget information servicing.

¹² There is also the Municipal Bank, majority owned by the municipality of Sofia.

Fiscal management relations among different levels of government

14. **The responsibilities of different levels of government are relatively clearly defined.** Significant fiscal decentralization reforms have been introduced over recent years, the principal legal instruments of which have been the *Local Self-Government and Local Administration Law*, the *Municipal Budgets Law*, and the *Local Taxes and Fees Law*. The assignment of expenditure responsibilities is specified in this legislation and in specific legislation covering relevant functional areas of government (for example, education, health, and culture). Tax assignment is also clearly specified in legislation, as are the forms of fiscal transfer from national government to municipalities and some of the principles which determine the allocation of these transfers. Other principles—including those governing fiscal equalization and the level of grants required to finance so-called state-delegated activities carried out by the municipalities – are subject by law to joint determination by the national government and representatives of the National Association of Municipalities. Intergovernmental working parties have been active in defining principles governing these matters, and these principles have been published. Municipalities at present face some within-year uncertainty in relation to transfers from the central government as a result of provisions under which the municipalities are guaranteed only 90 percent of the appropriated amount of national funding in respect to certain important grant categories, with the remaining 10 percent being conditional on the national government not exceeding the budget deficit approved in the State Budget Act. Municipalities may also apply for end-of-the-year supplementary funding from the central government which is potentially available on a discretionary basis if there is revenue overperformance in the central budget. The *Municipal Budgets Law* specifies the purposes for which municipalities may borrow, and requires the provision of information to the national government on borrowing. The *State Debt Law* (Article 11) empowers the national government to propose in the Annual Budget Law restrictions on municipal borrowing if the ratio of Bulgarian general government gross debt/projected GDP exceeds 60 percent.

The legal and administrative framework for budget management

15. **The legal framework for management of public funds is mostly clear and comprehensive.** Article 60 of the Bulgarian Constitution stipulates that citizens shall pay taxes and duties established by law proportionately to their income and property, and that any tax concession or surtax shall be established by law. The Constitution also requires that the National Assembly approve by law all international contracts which contain financial obligations for the state. Key principles for the management of the state budget¹³ of the

¹³ The state budget includes the republican budget (central budget and state authorities budgets, including that of the National Audit Office) and the budget of judicial authorities. The Supreme Judicial Council prepares a draft judicial budget which is presented to the Ministry of Finance in order to be included as part of the draft state budget. The draft State Budget Law is submitted by the CoM to the National Assembly together with the draft annual judicial budget proposed by the Supreme Judicial Council. The National Assembly adopts the judicial budget by judicial authorities as an independent part of the state budget.

Republic of Bulgaria are described in the Organic Budget Law. The *Municipal Budgets Law*, sets out similar arrangements for the municipal budgets. The procedure for issuance of government guarantees is based on clear rules that are specified in the *State Debt Law* and the *Municipal Budgets Law*. The debt law defines clearly the obligations of the Minister of Finance concerning public debt management, including concluding government loan agreements and issuing governments securities.¹⁴ The *Tax Procedure Code*, the *Law for Taxation of the Income of Physical Persons*, the *Corporate Income Levying Tax*, the *VAT law* and the *Excise Act* establishes tax rates and bases for domestic taxes. Customs duties are determined by the *Customs Act*. The *Local Taxes and Fees Act* defines the scope and coverage of all local revenues. The Ministry of Finance (MoF) plays a central role in fiscal management and oversees many of the reform processes currently underway to bring the fiscal aspects of the legislative framework in Bulgaria into line with the convergence requirements for EU accession.

16. **The organic budget law (Article 35(2)) endows the Minister of Finance with the authority to increase expenditure above the aggregate amount approved by the National Assembly if revenues are higher than expected and the budget deficit target will not be compromised.** Over recent years, revenue has exceeded expectations by a considerable margin,¹⁵ and this has given the executive arm of government the capacity to spend, on a discretionary basis, well above the level approved by the National Assembly.

17. **Mechanisms for the coordination and management of budgetary and extra-budgetary activities are well defined.** Chapter 7 of the Organic Budget Law provides that the procedures regulating extrabudgetary funds listed in Box 1 are in general the same as those that regulate the central government budget. In particular, the law provides that the draft state budget shall be accompanied by consolidated estimates and supplementary information on the financial position of the extrabudgetary funds, and that reports on state budget implementation shall be accompanied by reports on implementation of EBF budgets. The social security funds and the National Health Insurance Fund are financed by earmarked payroll contributions. The budgets of the Social Security Funds are adopted by the annual Law on the Budget of the State Social Security Fund, and the budget of the NHIF is adopted by the annual Law on the NHIF Budget. The National Assembly considers the draft annual budgets of the State Social Security Fund and the NHIF in parallel with the draft State Budget Law. The remaining extrabudgetary funds are approved by the Council of Ministers, but financial information about them is provided to the National Assembly in the annual Budget Report. Transfers from the central budget to the social security funds, the National Health Insurance Fund, the Agricultural Fund and the National Fund are approved by the National Assembly. The reorganization of the MoF carried out during 2003 led to the closer

¹⁴ See Articles 4–5, 12 and 16 of the *State Debt Law*.

¹⁵ Total revenues were 4 and 10 percent higher than estimated in the 2003 and 2004 budgets respectively.

integration of capital and current expenditure planning within the ministry. Program budgeting has also assisted in integrating current and capital budgeting more closely.¹⁶

The legal and administrative framework for tax policy and administration

18. **The legislative bases for some taxes have been harmonized with EU standards.** In recent years, the definitions and structures of the VAT, customs, and excise taxes have been progressively harmonized with EU standards. In general, tax legislation specifies the tax base, tax rates, and tax concessions for each tax. Numerous changes in tax policy in recent years have not always been accompanied by adequate explanatory materials for taxpayers, reducing predictability in a system based on self-assessment.

19. **Tax concessions have been reduced, but no estimates of their fiscal impact have been published.** The criteria for granting tax concessions are specified in legislation, and there is limited scope in the law for discretionary interpretation of the tax statutes by officials. Harmonization with EU standards has resulted in the removal of a number of tax concessions in recent years. Both tax concessions and effective tax rates are sector-neutral (with some exceptions, such as a lower VAT rate on the supply of tourist services). An estimate of the fiscal impact of tax exemptions was prepared for the EU, but no estimates have been published.

20. **Tax and customs administration are being strengthened, but the hidden economy remains large and the magnitude of corruption continues to be a major problem.** The *Tax Procedure Code* sets out in detail the arrangements for tax administration. There is a common taxpayer identification number (TIN) used for all tax administration purposes. In addition, a single identifier for all tax and social security contribution payments—the Bulstat number—has been introduced. Improvements have been made in compliance with the tax system. There is some evidence of a fall in the size of the hidden economy since 1998, but one estimate indicates that it remains around a quarter of the economy.¹⁷ Improvements have been made to the VAT refund process to speed up payment of refunds. Both the tax and customs administrations have introduced new procedures that aim to reduce corruption and improve operational efficiency by reducing the extent of face-to-face contact between officials and taxpayers. These include call centers, and integrated financial management information systems that improve the control and detection of irregularities and increasingly provide for electronic filing of documents. Procedures have also been put in place to reduce administrative discretion by improving the uniformity of interpretation of the tax and customs laws across different regional offices. Codes of Ethics for customs officials and tax officials were introduced in 2003 and 2004 respectively, supported by staff training. Surveys suggest, however, that corruption remains a major problem.¹⁸ Responsibility for tax administration is being progressively transferred to a

¹⁶ See Sigma Report, *Bulgaria: Public Expenditure Management System Assessment*, July 2004.

¹⁷ “Anti-corruption Reforms in Bulgaria,” Coalition 2000, Center for Democracy, Sofia, 2005.

¹⁸ Ibid.

National Revenue Agency (NRA), which is expected to unify collection of all taxes (other than customs duties) and social security contributions from January 2006.

21. **Taxpayers' legal rights are well defined.** The Tax Procedure Code sets out the main rights of taxpayers, including the right to information, clarification, confidentiality, and appeal. The tax and customs authorities provide substantial information to taxpayers via their websites. Taxpayers have access to administrative review. A tax assessment decision may be appealed, partially or fully, before a Regional Tax Director within fourteen days of its serving. The Regional Tax Director is required to issue a decision within forty-five days. Taxpayers may then appeal the decision before the Regional Court. Bulgarian tax law does not provide for the provision of advance tax rulings.

Public servants' code of behavior and anti-corruption activity

22. **Public servants are legally subject to a code of behavior and to other probity requirements** (such as obligations to report asset holdings and potential conflicts of interest). However, the relevant legislation is quite new, and implementation remains a challenge. For example, persuading all civil servants to comply with asset reporting requirements is made more difficult by the refusal of a significant group of parliamentarians to comply with similar reporting requirements for members of parliament.

B. Open Budget Preparation, Execution, and Reporting

The budget preparation process: clarity and consistency of process and presentation

23. **The annual budget process is mostly open but the presentation is not fully consistent with international standards.** The budget preparation process is clearly defined in the annual decision issued by the Council of Ministers with a set timetable for the preparation of the budget (see Box 2 below). The budget classification in the annual Budget Report presented to the National Assembly is based upon the "national methodology," under which the "Consolidated Fiscal Program" covers general government. The economic classification under the national methodology approximates that of GFS 1986, with the exception that defense and security expenditures are not decomposed but are, rather, presented as one functional total. It also reflects the process of migration to GFS 2001, as net lending to nonfinancial enterprises, acquisition of financial assets and equity, and privatization receipts are treated as financial assets and are shown "below the line." The functional classification is consistent with the Classification of the Functions of Government in GFS 1986. Expenditure is also classified administratively in the annual Budget Report, but at a high level of aggregation. Expenditure appropriations in the Annual Budget Law are made largely to ministries ("first level" spending agencies). The funding of "second level" agencies below ministries is subsumed within ministry appropriations, even when those second level agencies are significant and largely independent (e.g., the Tax Administration and the Customs Agency). With the progressive introduction of program budgeting, classification by objective is being developed.

Box 2. The Budget Preparation Process		
Due dates	Activities	Legal basis
The fiscal year is set on a calendar-year basis by the <i>Organic Budget Law</i> . The main steps in the process are as follows:		
End-January / early February	CoM issues a Decision which specifies a time schedule and also states the responsibilities of first-level spending units in respect to the preparation of the three-year budget forecast and the annual State Budget Law.	CoM issues annually a Decision on the budgetary procedure.
End-February	The Minister of Finance gives instructions to first-level spending units on the preparation of the three-year budget forecast, including unified models.	CoM Decision
Early April	First-level spending units update and submit their three-year forecasts to MoF.	CoM Decision
Early April	MoF develops: - a three-year tax policy proposal including an assessment of its impact on economic growth and budget; - a proposal on the national expenditure policy; - a proposal on debt policy as well as estimates for payments due.	CoM Decision
End-May	MoF develops and submits an updated three-year budget forecast to CoM.	CoM Decision
Mid-June	CoM discuss and approve the budget forecast.	CoM Decision
End-June	MoF prepares budgetary guidelines to first-level spending units on the preparation of their annual budgets.	CoM Decision
End-July	First-level spending units develop and submit their draft budgets for the following year to MoF.	CoM Decision
Mid-September	MoF and first-level spending units agree on their draft budgets.	CoM Decision
Mid-October	MoF submits the draft state budget to CoM for approval.	CoM Decision
End-October	CoM approves the draft budget.	Organic Budget Law / CoM Decision
End-October	Draft budget is submitted to National Assembly by CoM for discussion and approval.	Organic Budget Law
End-December	Budget is approved by National Assembly.	Organic Budget Law

The macroeconomic framework and policy basis for the budget

24. **The overall balance of general government is the main indicator of the fiscal position of the budget, and the general government balance is monitored during the year.** The primary focus of fiscal policy has been the balance of the Consolidated Fiscal Program, incorporating municipalities as well as central government.¹⁹

¹⁹ The broader public sector balance is not targeted, although this is not inappropriate given (i) the greatly reduced size of the public corporation sector after the large-scale privatization program of recent years; (ii) the

(continued...)

25. **Macroeconomic assumptions underlying the budget are presented in the annual Budget Report presented to the National Assembly, but there is no formal consultation process to agree on a consistent macroeconomic framework for the budget.** The budget is based on a medium-term macrofiscal framework that is compiled by MoF. A second level spending agency underneath MoF, the Agency for Economic Analysis and Forecasting (AEAF), prepares twice a year a macroeconomic framework as an input into the budget preparation procedures. It includes medium-term macroeconomic indicators together with a detailed breakdown of GDP by components and the balance of payments. The BNB also prepares macroeconomic forecasts and shares these forecasts with the MoF.

Medium-term planning and analysis of fiscal risks

26. **A statement on medium-term fiscal policy objectives is included in the Budget Report presented to the National Assembly with the budget bill.** At present, these involve targets for the budget balance, as well as objectives in respect to the primary balance and the debt/GDP ratio.

27. **The government has also set out a medium-term tax strategy.** The Report on the State Budget Act for 2003 outlines the government's tax policy objectives, which are to reduce the tax burden; maintain a stable tax system; align legislation with EU requirements; determine exactly the rights and obligations of taxpayers and the tax administration; and achieve sectoral neutrality and equal treatment of taxpayers.

28. **Fiscal sustainability issues are not presented in the Budget Report.** With respect to future social security obligations, while long-term projections of such expenditures, as well as estimates of the net present value of the liabilities of the accident insurance scheme, are produced by the National Social Security Institute (NSSI), they are not publicly available.

29. **Fiscal rules are used in the budget process.** Article 10 of the *State Debt Law* imposes a sixty percent ceiling on the ratio of gross general government (consolidated fiscal program) debt to projected GDP. Since 2003, the debt/GDP ratio has been below this level.

30. **Estimates of the fiscal impact of new initiatives and ongoing costs of government expenditure policies are not distinguished in the budget documents presented to the National Assembly.** In the budget process within the executive government, there is a requirement in the guidelines for the preparation of the medium-term budget forecasts, issued by the MoF, that each first level spending unit has to cost all new policy initiatives. However, this information is used only within the executive government.

31. **The assessment of the sensitivity of budget estimates to changes in economic variables is limited, as is the discussion on fiscal risks to the budget.** The annual Budget Report identifies the main external and domestic macroeconomic factors that could threaten

reduction in quasi-fiscal activities by public corporations; and (iii) the comprehensive reporting of state aid to public corporations.

fiscal targets. However, no sensitivity analysis has been reported or discussed in the budget documents apart from analysis of the impact of possible variations in international interest rates on interest expenditures. No broader analysis of fiscal risks—for example, relating to contingent and other hidden liabilities—is presented.

Clarity of control of budget execution

32. **Accounting and internal control procedures are gradually improving.** Most budgetary and extrabudgetary payments and receipts of central government (including social security funds) are handled through a treasury single account (TSA). The TSA is under MoF's supervision and management. A significant number of central government's suspense accounts are part of the TSA, and the automated payment system (SEBRA) handles all payments of state budget entities, except those of EU resources in the National Fund and those of the judiciary (although it is expected that these judiciary payments will be brought within SEBRA by the end of September 2005). The accounts of the municipalities are not included in TSA. Data on state budget payment arrears is available on a quarterly basis on MoF's website. Although payment arrears were problematic in the past, the stock of arrears of central government agencies has been reduced substantially in the last few years. However, arrears still exist at the municipal level. Data on tax payments due are available with the tax authorities. Tax arrears data are available in a separate information system of the tax and social security administrations, which is not based on double entry recording. A new information system with double entry modified accrual recording for taxes and social security contributions is under development by the NRA.

33. **The coordination of financial management practices has been improving.** The linkage between cash and debt management has been improving with the creation of a fully operational debt management unit in MoF tasked to compile the government's domestic and external debt management strategy.

34. **Internal audit is not fully effective and is currently undergoing major reform.** As recommended in the earlier ROSC, modern internal control practices are gradually being introduced in Bulgaria. Ex ante financial control is the responsibility of spending agencies. As described in the *Public Internal Financial Control Law*, the Public Internal Financial Control Agency (PIFCA) is responsible for two separate areas of control, namely internal audit and financial inspection.²⁰ In May 2004 a separate unit (the Central Harmonization Unit) was established in MoF to facilitate reforms and harmonization of functions. Both the European Commission and the OECD SIGMA closely monitor progress in reforms and have recommended that internal audit should be decentralized to enable the development of a stronger sense of managerial responsibility and accountability at the level of the spending agencies.²¹ A new draft *Law on Public Internal Financial Control* was introduced in

²⁰ See PIFC's website, at www.advfk.minfin.bg/en/za_agenciata.php.

²¹ The NAO has recommended in their reports that an independent body, separate from PIFCA and MoF be established with specific powers to enforce sanctions for noncompliance.

September 2004, but this will now need to be redrafted as it does not embody the EU recommendation on decentralization. Further training is crucial for these proposed reforms to succeed.

35. **Procurement rules have been improved by recent legislative changes, but problems in their implementation remain.** The *Public Procurement Law of 2004* is in compliance with most EU directives. According to this Law, the rules and conditions for awarding public contracts are mandatory for the awarding of public procurement contracts where their value is above thresholds stipulated in Article 14 of the Law (which are lower than EU thresholds). Procurement procedures and documentation are mainly monitored by the Public Procurement Agency. However, this agency has limited enforcement powers and can only monitor the procurement process. It has no power to impose sanctions in cases of proven violations. The Procurement Law allows for an appeal process in the civil courts, which as noted above (para. 9) are perceived to be slow and open to corruption. The NAO also audits procurement procedures.²²

36. **Civil service employment procedures are relatively clear, but the relevant legislation will take some time to fully implement.** New civil service legislation in 2003 contains many sound elements, including compulsory competitive appointment and promotion procedures, and clearly defined grading and associated salary ranges, as well as probity principles referred to in paragraph 21. The extent to which these requirements have been implemented or well-understood is unclear at this stage. Moreover, the new legislation does not apply to the administrative staff supporting the judiciary.

Clarity of internal control and independence of tax administration

37. **The independence of the tax administration is set out in law, but there is provision for ministerial instruction.** Article 7 of the Tax Procedure Code specifies that the tax administration and the public enforcement authority shall perform their functions independently and solely on the basis of the law; and that no matters regarding taxation may be resolved by other administrative authorities. However, a 2003 amendment to the Tax Procedure Code (SG No. 42/2003) empowers the MoF to issue binding instructions to the tax authorities on the uniform application of tax legislation (Article 232(2)2 of the Code). The Tax Administration and Customs Agency are second level spending units within the MoF. Neither produces annual reports for parliament or the public, although reports are made to the Minister of Finance and Minister for the Civil Service.

Accounting and reporting on budget execution

38. **The accounting system is capable of producing accurate in-year reports on the general government budget outturn.** Monthly Budget Execution Reports of general

²² During their audits of public procurement, the NAO has found irregularities in approximately one-third of all cases.

government are prepared on a cash basis with a lag of approximately one month. Interim quarterly reports of general government are prepared 60 days after the end of the quarter. This also includes data on payment arrears which is available on a quarterly basis on the MoF's website. According to the legal requirement in the Organic Budget Law, MoF compiles the consolidated general government final annual accounts three months after the end of the financial year (January to December) and completes the report on its execution by the end of May each year.²³ In June the Minister of Finance submits these reports for discussion to the Council of Ministers, and after that the government presents it for adoption by the National Assembly. Annual fiscal data provided by the Council of Ministers to the National Assembly are disseminated by the MoF six months after the end of the budget year. This annual fiscal data is on a cash basis as required by the Unified Budget Classification. After some initial delays, the MoF is currently pilot testing the implementation of a fully-developed integrated financial management information system (FMIS). If successful, it will be rolled out to all other line ministries during 2006.

39. **Fiscal reporting covers all of general government.** Fiscal reporting occurs both on a "national methodology" basis and on a GFS basis. The national methodology reports information for the Consolidated Fiscal Program, as well as for central government, for local government and for the social security funds and the National Health Insurance Fund. GFS data covers consolidated general government. Data is comprehensive.

40. **The legislature does not undertake a mid-year budget review.** Although monthly and quarterly reports are disseminated to the public on a timely basis by means of publication on MoF's website, no formal procedure exists whereby these reports are presented to the National Assembly. In-year changes to the approved budget or supplementary expenditures, which do not change targets for the budget balance, have not been subject to approval by the legislature in recent years.

41. **The audited final accounts are presented to the National Assembly within nine months of the end of the fiscal year, but have not always been promptly made public.** A Budget Execution Report is submitted to the National Assembly after the conclusion of each financial year, containing the final accounts of the Consolidated Fiscal Program. The policy of the government has been to make these reports public only after they are approved by the National Assembly. However, the National Assembly did not approve the 2003 report, which as a result was not made public. The withholding of these annual Budget Execution Report from public release pending National Assembly approval is an administrative decision which is not required by any law. Since the mission visit, the 2003 Budget Executive Report has been placed on the MoF website.

²³ The preliminary annual fiscal data are disseminated three months after the reference period.

Results-oriented budgeting and reporting

42. **The objectives and expected results from government activities are at this stage discussed in the budget documents only in respect to a selected number of ministries which are piloting the introduction of program budgeting.** The budget documents presented to the National Assembly in recent years have included a program budgeting appendix in respect to each of a number of ministries piloting the introduction of program budgeting. These appendices contain information on the program objectives and performance indicators. At present, program budgeting is not fully integrated into the budget process. However, the aim is to place the whole budget on a program basis by 2007, and to adjust appropriation and other procedures accordingly.

C. Public Availability of Information

The coverage and quality of budget documents

43. **The budget documents provide comprehensive data on general government.** A “Budget Report” is presented to the legislature in conjunction with the appropriations legislation. This document provides information on expenditure, revenue, and the budget balance for the consolidated general government sector (including municipal governments and, with limited exceptions discussed elsewhere, extrabudgetary funds).

44. **Defense and security expenditures are not transparently reported in the budget.** Military and security expenditures are included in the expenditure aggregates reported in the budget. However, military and security expenditures are not decomposed in the economic classification information.

Past and forecast fiscal data in the budget

45. The budget document discloses the main general government fiscal aggregates for two years prior to the budget year and provides some information in respect of the two years beyond the budget year. The annual Budget Report presents expenditure, revenues and the budget balance for consolidated general government for the two years prior to the current budget year. With respect to forecast data, the Budget Report presents in diagrammatic form data on the projected general government budget balance and primary balance as a percentage of GDP for the two years beyond the budget year, without reporting the projected values. No information on projected expenditure, revenue or financing is presented. A medium-term budgeting document (“Budget Forecast”) presented to the Council of Ministers during the budget process and subsequently made available to the budget committee of the National Assembly contains information on projected expenditures and revenues for general government for the two years following the budget year. It does not, however, project the budget balance or financing. This document is not made public.

Budget treatment of off-budget fiscal activity

46. **Some information is published on contingent liabilities, but there is no information published on QFAs or tax expenditures.** The MoF maintains a complete official register of government guaranteed debt and the aggregate amount of such guarantees for each of central government and the municipalities as a whole is published in annual and monthly debt reports.²⁴ Other contingent liabilities of government are not centrally recorded²⁵—although an amendment to the *Law for the Concessions* in 2004 requires maintenance of a publicly available National Concession Register, including details of the type and size of the liability for nonfulfillment of obligations under the contract. No estimates of QFAs or of tax expenditures are published.

Publication of data on debt and financial assets

47. **Comprehensive information on gross public debt is published.** Comprehensive monthly and annual reports²⁶ of general government gross debt are made available on the MoF's website. Debt is reported by source (external or domestic), with external debt broken down by type of instrument and domestic debt by creditor. A breakdown by currency, interest-rate structure, maturity and other characteristics is also presented. The BNB also publishes information on government debt in its quarterly Government Securities Market bulletin.

48. **Partial information on government financial assets is published.** The authorities advise that, as part of a gradual move to GFSM 2001, a partial balance sheet identifying government financial assets has been developed. This is not, however, made available publicly at the present time. The National Statistical Institute anticipates publishing in the near future a set of national financial accounts which will include estimates of government financial asset holdings. The government publishes monthly reports on the total balance in the Fiscal Reserve Account, which comprises all central government budgetary and extrabudgetary bank accounts.

Commitment to timely publication of fiscal data

49. **Commitments for the regular publication of fiscal data have not been enshrined in law.** Timelines for the preparation and presentation to the National Assembly of the annual report on budget execution are set by the MoF in consultation with the NAO. Monthly and

²⁴ For instance, the total of domestic government guaranteed debt, and total external guaranteed debt broken down by World Bank, EIB, EBRD, and other.

²⁵ Examples include a government-guaranteed minimum rate of return on compulsory private pension contributions; guarantees entailed in public infrastructure concession contracts; and legal action against the state.

²⁶ These are the annual Government Debt Review and the monthly Government Debt Management report.

quarterly Budget Execution Reports are prepared and made available publicly on a timetable established by the Council of Minister by regulation pursuant to the Annual Budget Law. The procedure for preparation and submission of the Budget Execution Report to the National Assembly is defined in Art. 41 of the Organic Budget Law, which is administered by the Minister of Finance. There is an administratively-defined timetable for the publication of GFS 1986 data. Bulgaria has committed itself to the publication of extensive fiscal data through its participation from 2003 in the Special Data Dissemination Standard.

D. Assurances of Integrity

Integrity of data processes

50. **Budget estimates are not a reliable indicator of the actual budget outcome.** The ability of the Minister of Finance to authorize additional expenditure in the second half of the year if revenue over-performance makes this possible without compromising the target for the budget balance has led, over recent years, to actual expenditure significantly exceeding the level expressly authorized by the Annual Budget Law. This is because, in both 2003 and 2004, actual outturns of aggregate revenues were much higher than budgeted. The tendency for actual expenditure to exceed budgeted expenditure is reinforced by the underbudgeting of certain expenditures, such as customary end-of-year staff and pension bonuses. The variation between the estimate and outturn for aggregate expenditure is disclosed in monthly reports published on the MoF's website—so that highly aggregated information on the annual fiscal outcome is publicly available—but the nonpublication of the 2003 Budget Execution Report makes the position less transparent than it need be. In 2004, the legislature requested, and was provided with, an explanation of the revenue overperformance. In respect to the composition of the budget, the Organic Budget Law (Article 34) allows the Minister of Finance to change budget appropriations from one line ministry to another or within the budget of a spending agency, provided that the targeted budget balance is maintained, so that the actual allocation of the budget may vary significantly from the allocation in the Annual Budget Law. These potential amendments have led to three or more changes in the budget allocations per year during recent years.

51. **Statements on accounting policy are not included in the budget and final accounts documents for government as a whole (the Consolidated Fiscal Program).** Budget transactions are essentially recorded on a cash basis. All general government entities apply partial accrual accounting (excluding depreciation), based on the methodology as set out in the “Unified Chart of Accounts for Budget Entities,”²⁷ as adopted in 2001. The MoF is responsible for setting accounting policies and standards, and for enforcing compliance with established accounting standards.

52. **The process of accounts reconciliation is mostly effective.** Most treasury transactions are now executed through the TSA. This allows for timely reconciliation of

²⁷ See MoF's website at www.minfin.bg.

information on treasury transactions with banking system. The BNB also undertakes a detailed reconciliation of the monetary survey and budget execution data on a monthly basis.

Independent oversight

53. **External audit is independent of the executive branch, and its mandate covers almost all public sector activities.** The NAO starts auditing the cash report on the execution of the budget in February–March of each year. The report of the NAO is usually submitted to the National Assembly three months later. After adoption by the National Assembly a summary of the auditing report is published on the website of the NAO. The NAO does not have the right to audit public corporations (unless the parliament takes a special decision requiring it to do so). This means that it is unable to initiate an audit of companies performing general government activities (such as the newly-established Public Infrastructure Projects company). The NAO has a separate independent budget, which is approved by the National Assembly, after which it becomes an integral part of the State Budget of the Republic of Bulgaria. Although capacity to carry out financial audits is adequate, as the NAO moves increasingly into more specialized areas of audits, such as performance audits, more staff training will be needed.

54. **The legislature does not have processes for systematically following up on audit findings.** The legislature is notified of reports of the NAO, but these reports are not automatically presented to the National Assembly. There is no legal impediment limiting any person or committee of the National Assembly from requesting and considering these reports, however there is no specialized group (“Public Accounts Committee”) tasked with following up audit reports. There is little awareness of these matters and of the availability of the NAO’s reports amongst the public in Bulgaria.²⁸

55. **External scrutiny of macroeconomic models and assumptions is not generally encouraged.** Only some general data of the macroeconomic forecasts are now published, but the AEAF indicates that is willing to provide information on request to outside experts. The Agency provides its forecasts and the assumptions underpinning them to the MoF, which publishes this information in the budget documentation. No description of the model itself is, however, published.

56. **The National Statistical Institute has a substantial degree of independence by law.** The Director and Deputy Directors are appointed for terms of seven years, and the NSI does not fall within the control of any individual minister. It has, rather, autonomous status under the Council of Ministers. The NSI has a direct reporting relationship with Eurostat, arising from data notification requirements of the European Union.

²⁸ See Sigma Report: *Bulgaria: External Audit Assessment*, July 2004.

III. IMF STAFF COMMENTARY

57. **Bulgaria has made considerable progress in improving fiscal transparency since the time of the 2000 fiscal transparency ROSC and the 2001 and 2002 updates, and now meets the requirements of the fiscal transparency code in a number of areas.** Important areas where Bulgaria meets the code include the consistent use of the consolidated general government as the basis for fiscal policy and reporting; clear articulation of fiscal targets and rules; independent external audits, and clear definition of the fiscal roles of the branches of government. Areas where the Bulgarian practices approach best practice include the reporting of public debt, the timeliness of within-year fiscal reporting and reporting of the general government outturn, the stipulation of an advance release date calendar for fiscal reporting, government/central bank relations, reporting of state aid to corporations, and financial sector regulation.

58. **There are a number of other areas where Bulgaria has made recent progress toward meeting the requirements of the code.** Expenditure arrears data are now also published. In respect to public corporations, progress has been made in placing community service obligations on a more transparent basis, with explicit government funding. A medium-term budgeting perspective has been introduced, encompassing the preparation of forward expenditure estimates and greater consideration of macroeconomic parameters as part of the budget formulation process. Progress has been made toward the development of a program budgeting system which should over time help focus greater attention on the results achieved by public expenditure, and make these results clearer to the public. In the field of taxation and customs, progress has been made in developing better systems for internal control and the assurance of compliance and integrity, although there is a long way to go in the implementation of these systems to rid these areas of administration of corruption.

59. **In a number of fields relevant to the fiscal transparency code, there has been significant recent legislative action, much of it linked to European Union accession requirements.** Some of this legislation is quite strong, while other legislation could be better described as representing a useful step forward. But what will be crucial in all cases is not only what is written in the new laws, but the extent to which these laws are implemented, especially given Bulgaria's long-standing corruption problems. It remains to be seen, for example, how effectively the proposed asset register for civil servants will be implemented when a similar register requirement for members of the National Assembly and some public officials introduced some years ago has been met with only partial compliance. Similarly, in the problematic field of government procurement much will depend upon the capacity of the new procurement agency to deal with the many strategies adopted by agencies to circumvent the procedural requirements laid down in recent legislation.

60. **Bulgaria made significant progress following the 2000 ROSC in relation to extra-budgetary funds.** Most of these funds were closed down, and those that remained were in general brought within the consolidated general government reporting framework. The recent establishment of Public Infrastructure Projects company, however, has raised this issue again. Because of the source of its funding and nature of the expenditure it is envisaged

to undertake, the company should be regarded as an extrabudgetary fund and its general government expenditure should be counted as part of the expenditure of the CFP. This is not, however, the treatment which the PIP has been accorded in the 2005 state budget.

61. **The capacity of the Minister of Finance (in practice the Council of Ministers), under the terms of the current organic budget law, to authorize additional discretionary spending at the end of the year in the event of revenue over-performance, is problematic because it reduces fiscal transparency and also accountability to the parliament.** Moreover, it encourages a surge of unprogrammed agency spending some of which will be less productive than if it could be properly pre-planned (an “end-of-the-year spend-up”).

62. **The recommendations below cover not only steps which would bring Bulgaria fully into compliance with the fiscal transparency code, but also other measures, including some that would take Bulgaria further toward international best practice.** These are presented broadly in order of priority. Some recommendations are also made in respect to revisions to the Organic Budget Law.

Highest priority recommendations for improving fiscal transparency

63. Provisions permitting executive government to spend revenue in excess of that forecast in the budget without prior parliamentary approval should be eliminated from the Organic Budget Law, thus limiting aggregate expenditure to an amount expressly appropriated in advance by the National Assembly. Provision for customary year-end salary and pension bonuses should be made in the Annual Budget Law. Unanticipated changes in spending should be managed through the use of supplementary budgets (in conjunction with limited contingency allowances and appropriate virement provisions).

64. The audited annual report on budget execution should be routinely published at the time it is presented to the National Assembly, without any requirement that it first be accepted by the National Assembly. Unpublished reports pertaining to previous financial years should be immediately published.

65. The economic classification of expenditure should be aligned further with international standards, through the allocation of defense and security expenditure by economic item.

66. The use of company structures, such as the Public Infrastructure Projects company, to carry out predominantly government fiscal activities should be discontinued.

High priority recommendations for improving fiscal transparency

67. In addition to prior year information, the annual budget documents should report projections of the main fiscal aggregates (including aggregate expenditure, aggregate revenue, the budget balance, debt and financing) for at least the two years subsequent to the budget year.

68. Procurement procedures should be improved by strengthening the independence and role of the Public Procurement Agency beyond the monitoring of the procurement process.
69. The independence of the tax administration, in respect to the enforcement of tax legislation, should be strengthened by reversing the 2003 amendment that empowers the Minister of Finance to issue binding instructions to the tax authorities on the uniform application of tax legislation (Article 232(2)2 of the *Tax Procedure Code*).
70. In addition to reporting government debt guarantees, a statement of central government contingent liabilities should be presented in documents accompanying the annual central government budget, and in the annual Budget Execution Report.²⁹
71. Data on the level and composition of financial asset holdings of general government should be regularly published.
72. Steps should be taken to significantly improve fiscal risk analysis to cover variations in the full range of key relevant macroeconomic and other variables, and include it in the budget documents.
73. Steps should be taken to improve the accuracy of revenue forecasting, including by further enhancements to macroeconomic forecasting and coordination of forecasting agencies. The budget report and annual execution report should also include discussion on the outcomes of revenues compared to forecasts done at the time of budget and the reasons for deviations.
74. Monthly and quarterly GFS data should be presented on a disaggregated basis, reporting types of revenue and decomposing expenditure by both economic and functional category.
75. The Annual Budget Law should provide separate appropriations to significant second level spending units, such as the National Revenue Agency and the Customs Agency, which need to operate with a clear budget of their own.
76. A mid-year report on budget execution should be prepared for presentation to the National Assembly. This report should present revised fiscal forecasts, and propose any corrective action which changed circumstances might require to meet fiscal policy objectives. These reports should be made public at the time of presentation to the National Assembly.

²⁹ To fully meet the Code's requirement for reporting the nature and fiscal significance of contingent liabilities, these statements should provide details on the stock of contingent liabilities (gross exposure by individual category [i.e., by category such as loan guarantees, warranties, indemnities, uncalled capital, and legal action against the state]), where feasible an estimate of likely cost in the next period, any calls on guarantees in the previous period, and an explanation of expected/actual changes in the stock of contingent liabilities. It is recognized that not all of this information will be able to be provided in the short term.

77. The modernization process of internal control operations in line ministries and other government agencies should be completed by first separating the functions of inspection and audit in PIFCA and making PIFCA responsible only for inspection; and secondly by decentralization of the responsibility of internal control to departmental managers to enhance their managerial accountability.

Other recommendations for improving fiscal transparency

78. Data on the equity holdings of government should be consolidated and regularly published.

79. A statement of tax expenditures should accompany the annual budget, starting with a list of all tax expenditures and any existing estimates of their fiscal impacts. (To move toward international best practice, the statement should be progressively expanded over time to include the public policy purpose, duration, intended beneficiaries and fiscal impact of each tax expenditure.)

80. All reports of the National Audit Office should be formally tabled in the National Assembly.

81. All central government general government ministries and other agencies and public corporations should present annual reports to the National Assembly. These annual reports should contain both annual financial statements and a report on nonfinancial performance.

82. The judiciary should be encouraged to adopt budgetary and other practices consistent with sound financial management and probity. The same anticorruption measures should be adopted in the judicial administration as have been legislated for the state civil service.

83. The scope of the audit mandate of the National Audit Office should be extended to cover not only agencies within the scope of the republican budget, but also any central government public corporations insofar as they are recipients of general government funding.

84. All central government transfers to the municipalities should be based on rules and principles which are clearly defined and publicly known. To this end, the practice of discretionary end-of-the year supplementary grants to municipalities in years when national revenues are strong should be discontinued.

85. The coordination of agencies tasked with the setting of the macroeconomic framework for the budget should be improved. This should include the formalization of the consultation process between the MoF, Agency for Economic Analysis and Forecasting, and the Central Bank by the creation of a Macroeconomic Forecast Committee which would meet regularly to discuss macroeconomic forecasts pertaining to the budget.

86. Make the macroeconomic model used to provide the framework for the budget available to outside experts.

87. The annual Budget Execution Report, and the annual financial statements of agencies, should be accompanied by statements of accounting policy.

Moving toward international best practice

88. The National Assembly should give consideration to the establishment of a public accounts committee or sub-committee with the mandate of following up reports of the NAO—that is, to receive the reports, to consider the adequacy of agencies' responses to their recommendations, to determine which NAO reports raise other issues of importance which should be pursued further at a parliamentary level, and to hold hearings and carry out other investigations into these matters.

89. To improve the ability to assess fiscal sustainability, the National Social Security Institute should regularly publish long-term projections of future social security expenditures, as well as estimates of the net present value of the workers compensation scheme.³⁰

90. A statement on concessions (public private partnerships) should be presented annually to the National Assembly.³¹ The *Law for the Concessions* should be amended to require that concessions can only be awarded after a competitive process.

91. The annual government budget documents should contain an expanded discussion of the public policy purpose of each subsidy to corporations, together with performance indicators each recipient is expected to meet in supplying the services.

92. Public nonfinancial corporations should disclose in their annual reports the financial impact of any quasi-fiscal activities that they conduct (e.g., community service obligations beyond that for which they receive government subsidies; cross-subsidies between different categories of consumers).

93. Consideration should be given to withdrawing serving civil servants from the Supervisory Boards of public nonfinancial corporations.

94. Consideration should be given by the BNB to paying interest on the compulsory reserve deposits of banks, to be introduced when macroeconomic conditions are appropriate.

³⁰ Such projections and actuarial estimates are presently available within the NSSI.

³¹ This should provide, for each concession, a description of the arrangement, significant terms of the arrangement, and details of the annual long-term stream of future government payment obligations to service operators, future government revenues and contingent revenues, and contingent liabilities assumed by government (e.g., guaranteed minimum service levels).

Revisions to the Organic Budget Law

95. Many of the recommendations above require amendments to the present Organic Budget Law. Moreover, the current budget law needs to be updated in line with other developments currently underway.

96. The Organic Budget Law should be revised in order to incorporate, amongst other things:

- Fiscal reporting provisions identified above, including the obligation to publish the annual Budget Execution Report on presentation to parliament; the obligation to present to the National Assembly and make public a mid-year Budget Execution Report; the required content of the budget documents (e.g., fiscal risk analysis; the identification and costing of all new budget expenditure and revenue initiatives; medium-term estimates; and information on financial assets, contingent liabilities, concessions, and tax expenditures); and the timing of reporting.
- Budget management provisions identified above, including in particular the requirement that expenditure be limited to an aggregate total explicitly approved in advance by the National Assembly, limits on transferring funds between budget appropriations and that spending from own-revenues be authorized by parliament.
- The provision of separate appropriations for significant current second-level spending units important enough to require their own distinct budget.
- Changes to appropriation and budget information required by the introduction of program budgeting – including the role of program appropriation, and requirements for information on program goals and program performance information.

Summary Tables

Table 1. A Summary Assessment of Practices

Code Reference	Summary Assessment	Comment
Overall summary		
Clarity of roles and responsibilities		
1.1.1	General government is largely defined consistently with Government Finance Statistics (GFS) principles, and is well covered in the budget process.	
1.1.2	The fiscal roles of the executive, legislative and judicial branches are clearly defined in law. The responsibilities of different levels of government are relatively clearly defined.	Recent progress has been made.
1.1.3	Mechanisms for the coordination and management of budgetary and extrabudgetary activities are well defined.	Need to ensure that extrabudgetary funds continue to be transparently reported and subject to appropriate procedures.
1.1.4	There is a clear separation between the monetary and fiscal authorities, and the BNB has a high degree of independence. Relationships between government and nonfinancial public corporations are being progressively clarified.	Progress made recently in relation to nonfinancial corporations, with further steps required.
1.1.5	Government regulation of the nonfinancial private sector is complex, but efforts are being made to simplify business regulation. The legal framework for privatization has been made more transparent in recent years.	Progress made recently. High priority should be given to better legal and administrative enforcement of legislation on business regulation.
1.2.1	The legal framework for management of public funds is mostly clear and comprehensive.	
1.2.2	Tax and customs administration are being strengthened, but the hidden economy remains large and the magnitude of corruption continues to be a major problem. The legislative bases for some taxes have been harmonized with EU standards. Taxpayers' legal rights are well defined.	Progress has been made recently. High priority should be attached to the implementation of reforms to improve tax and customs administration.
1.2.3	Public servants are legally subject to a code of behavior and to other probity requirements.	Progress has been made recently. Priority should be attached to the effective implementation of the code of behavior and other new probity requirements.
Public availability of information		
2.1.1	Fiscal reporting covers all of general government. Defense and security expenditures are not transparently reported in the budget.	High priority should be attached to allocating defense and security expenditure by economic item in accordance with GFS principles.
2.1.2	The budget document discloses the main general government fiscal aggregates for two years prior to the budget year and provides some information in respect of the two years beyond the budget year.	Recent progress made. Priority should be given to completing the coverage of key medium-term fiscal projections.

Code Reference	Summary Assessment	Comment
2.1.3	Some information is published on contingent liabilities, but there is no information published on QFAs or tax expenditures.	High priority should be given to reporting of contingent liabilities other than debt guarantees (which are already reported).
2.1.4	Comprehensive information on gross public debt is published. Information on government financial assets is not published.	Priority should be given to reporting of financial assets.
2.1.5	Fiscal data is published on a basis which covers all general government including relevant local government activities.	
2.2.1	Commitments for the regular publication of fiscal data have not been enshrined in law.	Priority should be attached to including reporting requirements in the Organic Budget Law.
2.2.2	Monthly and quarterly Budget Execution Reports are prepared and made available publicly on a timetable established by the Council of Minister by regulation pursuant to the Annual Budget Law. There is an administratively-defined timetable for the publication of GFS 1986.	
Open budget preparation, execution, and reporting		
3.1.1	A statement on medium-term fiscal policy objectives is included in the Budget Report presented to the National Assembly with the budget bill.	
3.1.2	Fiscal rules are used in the budget process.	
3.1.3	Macroeconomic assumptions underlying the budget are presented in the annual Budget Report presented to the National Assembly, but there is no formal consultation process to agree on a consistent macroeconomic framework for the budget.	More systematic internal consultation on the macroeconomic framework will be of benefit.
3.1.4	Estimates of the fiscal impact of new initiatives and ongoing costs of government expenditure policies are not distinguished in the budget documents presented to the National Assembly.	
3.1.5	The assessment of the sensitivity of budget estimates to changes in economic variables is limited, as is the discussion on fiscal risks to the budget.	Further development of fiscal risk analysis is required.
3.2.1	The annual budget process is mostly open but the presentation is not fully consistent with international standards.	High priority should be given to the allocation of defense and security expenditure by economic item.
3.2.2	The objectives and expected results from government activities are at this stage discussed in the budget documents only in respect to a selected number of ministries which are piloting the introduction of program budgeting.	The further development of the program budgeting system will address this need.
3.2.3	The overall balance of general government is the main indicator of the fiscal position of the budget, and the general government balance is monitored during the year.	
3.2.4	The broader public sector balance is not targeted, although this is not inappropriate given (i) the greatly reduced size of the public corporation sector after the large-scale privatization program of recent years; (ii) the reduction in quasi-fiscal activities by public corporations and (iii) the comprehensive reporting of state aid to public corporations.	

Code Reference	Summary Assessment	Comment
3.3.1	The accounting system is capable of producing accurate in-year reports on the general government budget outcome.	
3.3.2	Procurement rules have been improved by recent legislative changes, but problems in their implementation remain. Civil service employment procedures are relatively clear, but the relevant legislation will take some time to fully implement.	There is a need for considerable attention to the implementation of these new legislation and rules in both the procurement and civil service areas.
3.3.3	Internal audit is not fully effective and is currently undergoing major reform.	Reforms currently underway need to be pursued.
3.3.4	The independence of the tax administration is set out in law, but there is provision for Ministerial instruction.	Provisions allowing the minister of finance to issue instructions on the application of tax law should be removed.
3.4.1	The legislature does not undertake a mid-year budget review.	Such reviews should be instituted.
3.4.2	The audited final accounts are presented to the National Assembly within nine months of the end of the fiscal year, but have not always been promptly made public.	The Budget Execution Report, including the final accounts, should be made public promptly at the time it is presented to the National Assembly.
3.4.3	The budget documents presented to the National Assembly in recent years have included a program budgeting appendix in respect to each of a number of ministries piloting the introduction of program budgeting. These appendices contain information on the program objectives and performance indicators.	
Assurances of integrity		
4.1.1	Budget estimates are not a reliable indicator of the actual budget outcome.	Provisions permitting spending of revenue in excess of forecast need to be removed.
4.1.2	Statements on accounting policy are not included in the budget and final accounts documents for government as a whole (the Consolidated Fiscal Program).	Such statements should be included.
4.1.3	The process of accounts reconciliation is mostly effective.	
4.2.1	External audit is independent of the executive branch, and its mandate covers almost all public sector activities. The legislature does not have processes for systematically following up on audit findings.	National Audit Office reports should be tabled in the National Assembly, and followed up by a Public Accounts Committee.
4.2.2	External scrutiny of macroeconomic models and assumptions is not generally encouraged.	The model should be made available to outside experts.
4.2.3	The National Statistical Institute has a substantial degree of independence by law.	

Table 2. Public Availability of Information—A Summary

	Budget and Fiscal Report Element	Included in Budget/Report Documents	Available to the Public	Para. Ref.	Code Ref.
1.	Central government (CG) budget estimates	Yes, mostly for GG.	Published/press/internet	22-23, 38-39, 42	2.1.1
2.	CG Defense Expenditures	Yes, But, it is not decomposed in the economic classification presented in the budget execution reports.	Yes, but in aggregated format.	43	2.1.1
3.	CG EBFs (including special development funds, social security funds, resource revenue funds)	Yes. Consolidated in state budget data and published in annual budget documents.	Yes. The OBL specifies that financial information of EBFs should accompany reports on the state budget.	16	2.1.1
4.	CG Budget outturns	Yes. Annual Budget Reports contain expenditure, revenues and the budget balance for consolidated general government for the two years prior to the current budget year.	Yes, but last 2 years not presented to the legislature.	44	2.1.2
5.	CG Budget forecasts	Some. Annual Budget Reports contain in diagrammatic form data on the projected general government budget balance and primary balance as a percentage of GDP for the two years beyond the budget year, without reporting the projected values. No forward forecasts of revenue and expenditure are reported.	No, it is not made public.	44	2.1.2
6.	CG Contingent liabilities	Some. Information on government guaranteed debt is published but not provided for in the budget. Some limited information available from National Concessions Register.	Yes, information on loan guarantees is published on MoF's website.	45	2.1.3
7.	CG Tax Expenditures	No. Some estimates on tax expenditure have been attempted but no listing has been published.	No, not published.	45	2.1.3
8.	CG QFAs	No information on QFAs are available.	No, not published.	45	2.1.3

	Budget and Fiscal Report Element	Included in Budget/Report Documents	Available to the Public	Para. Ref.	Code Ref.
9.	Macroeconomic assumptions	Yes, medium-term macroeconomic assumptions are presented to legislature.	Yes, with annual draft budget to legislature. Also on website..	24	3.1.3
10.	Analysis of fiscal risks/sensitivity analysis	Yes, fiscal risks identified but limited analysis on fiscal sustainability. Covers mainly GG.	No, not normally published.	25, 28	3.1.5
11.	CG Debt	Yes. Information on state debt is available on a monthly and annual basis. The MoF periodically presents to the government, parliament, and public a statement of public debt, with composition of public and publicly guaranteed debt.	Yes	46	2.1.4
12.	CG Financial Assets	No.	No.	47	2.1.4
13.	Sustainability Analysis	No.	No.	25	3.1.1
14.	General government budget estimates	Yes, medium-term estimates are available in budget reports. Mainly on an aggregated basis. Includes EBFs and loan guarantees of central and municipal governments.	Yes.	23	2.1.5
15.	CG Monthly/quarterly reports on fiscal outturn	GG data is available on a quarterly basis (with one quarter lag). Reconciliation with monetary data. No mid-term review document is prepared.	Yes. Website.	42	3.4.1
16.	General government Monthly/quarterly reports on fiscal outturn	Yes. Monthly budget execution reports (in more aggregated format) are available.	Yes. Website.	38	3.4.1
17.	Consolidated general government Final Accounts	Yes. Audited final accounts are usually presented to legislature 9 months after year-end.	Yes, but last two years not made public—awaiting approval of National Assembly.	40	3.4.2