

A Citizen's Guide to the Budget

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A CITIZEN'S GUIDE TO THE BUDGET

second, revised edition



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NOTE

The Institute of Public Finance first published “A Citizen’s Guide to the Budget” in 2000, its electronic edition having undergone several revisions since then. In front of you now is a completely new, revised edition. Over the past years, not only the data and statistical methodologies changed, but also the legislation and institutions dealing with the budget, as well as the interest of the media and the public in the budget and their knowledge about it. Therefore, while following the pattern of the previous one, this edition introduces numerous novelties and different approaches.

Given the changing nature of the budget, we tried to explain, as clearly as possible, the basic concepts and processes, without referring to particular laws, regulations or decrees, and without dwelling in greater detail on the current circumstances. All we wanted was to help you understand the essence of the budget and budgetary processes, so that you could use this Guide as an incentive to search for more details which you might be particularly interested in, and, of course, to get involved in the budgetary process.

As editor of the Guide, I would like to express my appreciation to all the co-authors: Mihaela Bronić, Vjekoslav Bratić and Danijela Medak Fell, and most of all to my colleague Anto Bajo, who has worked with me ever since the Institute embarked on its public-oriented activities. I also wish to thank my associate Ivica Urban, and Petar Sopek, a student, for their assistance in data processing, as well as Marijana Bađun, Marina Kesner-Škreb and Goran Vukšić, for their careful reading of the manuscript and very helpful suggestions. My cordial thanks also go to our “representative citizens”: Miljenko Bernfest, Ante Bronić, Marina Klepo, Nikolina Krtalić, Marija Ott Franolić, Draženka Polović, Hrvoje Puškarić, Miroslav Sambolek, Malina Sirotić and Pava Turudija, as well as to our colleagues from the Ministry of Finance: Ivana Jakir Bajo, Ivana Maletić and Andreja Milić, who reviewed the previous editions and gave us many useful comments in order to make this Guide more understandable and interesting to all citizens. I wish to thank Martina Fabris for editing the references and Marina Nekić for helping us develop our idea into a finished product.

The first Guide was published with the financial support of the Friedrich Ebert Foundation. As our co-operation continued and expanded over the years, the publishing of this Guide has been our shared effort. Therefore, I avail myself of the opportunity to once again express my thanks to the Friedrich Ebert Foundation and its Head Mirko Hempel, as well as to Tijana Defar, for their ongoing understanding, co-operation and support to our efforts to bring at least some of the numerous issues from the area of public sector economics closer to citizens.



A Citizen's Guide to the Budget is now in front of you. I hope you will read it with interest and use the acquired knowledge to improve the budget and budgetary process, if not at the national level then at least at the local one.

Katarina Ott



INTRODUCTION

The budget has always been an interesting and topical subject, and, given the accumulated problems in the Croatian public sector and the global recession that shook up even the richest countries' budgets, it is expected to remain in the very focus of public interest. New generations reading newspapers or watching TV increasingly wonder about the real meaning of the words budget, budget revision or extra-budgetary fund. Don't you also get confused sometimes by some article in a newspaper about the budgets of extra-budgetary funds being in part financed from the budget? Perhaps even you are not quite clear about the types of budgets and their actual purposes. You may also be unaware of the fact that the general government budget and the national budget are two different things, and do not know the real meaning of "consolidated general government budget".

The results of a survey conducted in county assemblies and city councils show that as many as 43% of council members, i.e. elected representatives of citizens, who decide upon the budgets, do not have a complete understanding of their local units' budgets (Bratić, 2008)? So, how can we expect more from "ordinary" citizens? This guide is supposed to help all those interested – members of parliament, the members of county assemblies and city and municipal councils, students and other citizens – understand the budget, budgetary process and main budget terms, while trying to act themselves and, perhaps, contribute to changes.

The text below consists of three parts. Part I introduces us to the national budget, central government budget and general government budget. Part II describes the main participants in and phases of the budgetary process. The third part should provide a basis for citizens to use the information from the previous two parts in an attempt to monitor the budget and contribute to its improvement. The Guide ends with a glossary and some useful references.



THE BUDGET

The first part of this Guide gradually introduces the reader to the basic information about the budget:

- ◆ First we provide a general definition of the budget and discuss the national budget, its users, functions, principles, structure, and revenue and expenditure account, expenditures according to different classifications, the measures of the national budget deficit/surplus, and the financing account.
- ◆ After discussing the national budget, we present the budgets of extra-budgetary users of the national budget, their users, revenues and expenditures. This will lead us to the consolidated central government budget.
- ◆ The presentation of the central government is followed by the budgets of local units, their users, revenues and expenditures.
- ◆ Then we discuss the consolidated general government budget, its deficit and the consequences of it, i.e. public debt and general government debt.
- ◆ Finally, we deal with the size of the state.

What is the budget?

To put it briefly and generally, the **budget** is the plan of revenue and expenditure in a given period of time

budget – a plan of revenue and expenditure for a given period of time.



The word *budget* derives from the French word *bougette*, denoting a little leather bag used by medieval French merchants for holding money. In English, it meant a leather bag in which the Chancellor of the Exchequer brought proposals for national revenues and expenditures for a certain period to parliament. The word survived and is used, for example in English, French, German (along with the terms *Haushalt* and *Etat*), Italian (along with *bilancio*) and Dutch (along with *begroting*).

A common example is the family budget. Each of us, as well as each family, has various needs and wishes. In order to satisfy them, we need money which is rarely sufficient, so that our needs and wishes should be in line with our financial capacities. It is reasonable for individuals and families, as well as for the state, to draw up a plan of income and expenditures at certain intervals and for a certain period of time. And this is what a personal, family or national budget actually is.



Let us assume that we want to draw up a budget for the next year. The size of this budget depends, on the one hand, on our estimated income in the next year, and on the other, on our needs and wishes. It is relatively easy to adjust the revenues and expenditures if our needs and wishes in the next year are not great, and if we intend to spend our earned income on food, clothing, utility fees, etc. However, if we plan to buy, for example, an apartment or a house next year, this can by no means be financed by the income earned in only one year. In such a case, even though we need an apartment, we can give it up and thus balance our spending with our income. Of course, we can buy an apartment by taking the money from our savings account or by borrowing it from our family, friends or from a bank. All this should be properly planned. On the other hand, if we intend to work hard and earn much, but spend less next year, our revenue will be greater than expenditure, and our only concern will be what to do with the surplus money – place it on a savings account, invest it in various funds, buy securities or simply sock it away. By doing so, we make provisions for future, less affluent times.

The same is true for the state. In accordance with its activities and wishes relating to the national development, the government plans its revenue and expenditure for the coming year. As the state is a complex system, the national budget is more sophisticated than the family budget. However, regardless of the complexity of structure or size, the essence of the budget is always the same: planning and adjustment of revenues to expenditures.

The responsibility for planning, drawing up and executing the family budget falls only on ourselves. However, the government is accountable to its citizens. Therefore, it has to present, accurately and on a regular basis, detailed information on collecting and spending the citizens' money. As a result, the budget and budgetary process, consisting of the planning, drawing up, adoption and execution of the budget, are formally regulated by the Budget Act.

In Croatia there are types of budget: the national budget, the budgets of extra-budgetary users of the national budget and the budgets of local and regional self-government units. Each of these budgets has its own revenue and expenditure. However, if we want to establish the total public revenue and spending we must add together all the three budget types to get a consolidated **general government** budget. This is comparable to a situation in which three members of a family: the father, mother and son earn and, of course, spend money. So, the raising and spending of the family funds is recorded in three budgets (that of the mother, of the father and of the son). Each of them has own revenues and expenditures, and, in order to calculate their total income and expenditures, we must add all the three budgets together and present them as a consolidated budget of the family.

general government – central government (budgetary and extra-budgetary users of the national budget) plus budgetary and extra-budgetary users of the county, city and municipality budgets consolidated general government budget.



How can we learn about the amount of revenue and expenditure of various budgets?

Information on the revenue and expenditure of the national budget, the budgets of **extra-budgetary users** of the national budget, and the budgets of local units are available at the website of the Ministry of Finance and in the *Narodne novine* (Official Gazette). The local units' budgets are published in the official journals of these units, and are also available at the special web pages of the Ministry of Finance.



Revenue and expenditure, receipts and expenses

For simplicity reasons, this guide will basically deal with revenue and expenditure. However, besides these two notions, the budget terminology also contains the terms *receipts* and *expenses*, where the terms *revenue* and *expenditure* are used in the revenue and expenditure account and relate to the purchase and sale of non-financial assets, and the terms *receipts* and *expenses* are used in the financing account and relate to financial assets, borrowing and loan repayments. Briefly, revenue and expenditure relate to non-financial, and receipts and expenses to financial transactions.

extra-budgetary users – extra-budgetary funds, enterprises and other legal persons in which the state or local units exercise a decisive influence on the management, and which enjoy considerable autonomy including independent decision-making on a part of their revenue and expenditure.



The national budget

state aid – state intervention used to grant an economic privilege granted to a certain enterprise, sector or region; it is selective and has adverse impacts on competition and trade; it is provided in the forms of subsidies, tax relief, equity participation, soft loans, tax deferrals or guarantees.

When we read, or hear in the media that the next year's budget envisages more money for **state aid** to shipyards and less for the procurement of military equipment, this most frequently relates to the national budget. The national budget is a document in which the state's revenues and expenditures for a one-year period are estimated, pursuant to law. In most countries, including Croatia, budgets are approved by the Parliament and the year to which the budget relates is called the fiscal year and it can, but not necessarily does, overlap with the calendar year.

What is the fiscal year?

The fiscal year is a twelve-month period for which the state plans revenue and expenditure. In Croatia, the fiscal year overlaps with the calendar year, i.e. it lasts from 1 January to 31 December. In some countries, however, the fiscal year does not overlap with the calendar year. In the United Kingdom, for example, the fiscal year lasts from 1 April to 31 March the following year.



Who are the national budget users?

tax – a kind of compulsory payment to the government without a direct counter-benefit.

To put it simply, the national budget users are institutions established by the state which are majority financed from the national budget, so that their budget revenues and expenditures constitute a part of the national budget. For example, they include the Government, Parliament, ministries, universities, courts, etc. A list of budget users is published in the Official Gazette each year before the preparation of the next year's budget.

social benefits – the benefits based on insurance rights (pensions, unemployment benefits, as well as sickness and maternity benefits), or provided in the form of assistance to the poor in difficult situations which are not covered by the basic social insurance (e.g. various allowances to families and disabled persons, transportation cost aid and public kitchens).

What are the functions of the national budget?

The national budget shows the *most important objectives of the Government*. By analysing the revenue and expenditure we can find out, for example, whether the Government intends to cut **taxes** in order to stimulate enterprise and economic growth, or increase them with a view to financing higher expenditures or, whether it gives priority to expenditures for **social benefits**, motorway construction or the salaries of members of parliament.



The national budget also serves as *an economic policy instrument* enabling the Government to exercise influence on the economic situation in the country, i.e. on economic growth, employment, income distribution, consumption, saving and inflation. The budget can also be used for achieving the main economic policy objectives, such as allocation, distribution and stabilisation.



How is the budget used to perform the economic policy functions?

The following economic policy functions can be performed through the budget: (1) *Stabilisation*: By intervening in taxes and public expenditure, the state tries to increase employment, ensure price stability, improve the balance of payments and ensure the most favourable economic growth rate; (2) *Allocation*: The Government can influence decisions on the public vs. private provision of goods and service (i.e. directly, through public offering of education or health services, for example, or indirectly, through taxes and state aid stimulating or discouraging certain activities); (3) *Distribution*: Depending on the public perception of equity and the efficiency of the public sector, the Government can influence the distribution of goods and services among members of the society, through progressive taxation and transfer systems. These functions frequently overlap. While this classification is sometimes considered as obsolete, it can still be used to study the functioning of the state.

The national budget provides for *control over the collection and spending of public money*. During the fiscal year, the control of the entire budget is exercised by the relevant directorates in the Ministry of Finance, but each ministry additionally supervises the parts of the budget for which it is responsible. The subsequent, final control of the budget execution is exercised by the State Audit Office. Of course, citizens, as providers of budget revenues and users of public goods and services financed from the budget, should also more actively participate in budget control. The purpose of this Guide is to support them in these efforts.

Budgetary principles

There are numerous **budgetary principles** to be adhered to when preparing the budget, but we will only explain some of the basic ones to be observed by all those involved in budgeting.

The principle of equilibrium briefly means that the amount of revenue must be equal to the amount of expenditure, i.e. the state is allowed to spend only as much as it can collect. Should expenditures increase, or revenues

budgetary principles
– the principles to be adhered to by all those dealing with the budget; they include the principles of equilibrium, annuality, unity and budget accuracy, universality, specification, transparency and sound financial management.



decrease during the budget year, for example, due to some contingencies, such as recession, the budget has to be balanced by reducing the estimated expenditure or finding new sources of revenue. Of course, the expenditure of the state in a given year frequently exceeds the revenue, and the difference is financed by borrowing. In such a case, the definition of equilibrium changes, and the sum of revenues and borrowed funds must be equal to the sum of expenditures and debt repayments. This means that as much can be spent as comes into the budget.

The principle of annuality means that the budget is drawn up for a one-year period and that revenue and expenditure are estimated for one year. However, these estimates must also include funds for the settlement of liabilities taken over from previous years (e.g. loan repayments).

The principles of unity and budget accuracy implies that all revenues and expenditures of all budget and extra-budgetary users have to be stated according to the gross principle, and all their expenditures have to be stated by function and programme to the amounts determined in the budget. Moreover, all proposals for laws, regulations and legal acts to be adopted by the Government and Parliament should contain an estimate of their impact on the budget.

The principle of universality means that total revenue must be used for total expenditure. However, there are some exceptions from this rule prescribed by law and government decisions. For example, all tax revenues are spent for all expenditures. By contrast, pension insurance contributions, for example, can only be used for pensions.

The principle of specification means that all revenues must be allocated according to the **economic classification**, and stated by source, and expenditures must be allocated according to the budgetary classifications and, of course, adjusted to revenues.

The principle of transparency implies that budgets and all documents pertaining to them must be publicly available, and therefore published in the Official Gazette or the official journals of local units.

economic classification

– the presentation of revenues and receipts by natural type (e.g. taxes, aid, receipts from assets), and of expenditures and expenses by economic purpose (e.g. compensation of employees, subsidies, social benefits).

Open Budget Index

The access to information on the fiscal activities of the Government does not only let citizens have a better understanding of political and economic decisions having a significant influence on their everyday lives, but also gives them an opportunity to participate in the decision-making process. Data about government activities facilitates civil control over policy-makers, which has a beneficial effect on the Government's accountability





to citizens. The availability of information is particularly important for combating corruption and improving the efficiency of public services. In view of this, the Centre on Budget and Policy Priorities, Washington has developed an Open Budget Index providing for an international comparison of budgetary process transparency. The index value ranges from 0 to 100. In the 2008 research cycle which referred to the fiscal year 2007 and included 85 countries, Croatia's score on the index was 59. Thus it ranked among the countries providing the public with "some, albeit incomplete information". This group also included Argentina, Bulgaria, India, Kenya, Russia, etc. The countries providing extensive information to the public on government finances included United Kingdom, South Africa, France, New Zealand and the USA. Unfortunately, as many as one half of observed countries provided the public with only minimal information on the state budget, enabling their governments to hide lavish spending and corruption. What the Ministry of Finance should do to improve the transparency of the Croatian national budget is discussed in an article by Ivica Urban and Marijana Bađun entitled "Open Budget Index 2008 – Small Advances Made in the Accessibility of Information about Croatian Public Finance" (2009), and the results for Croatia can be found at: [<http://openbudgetindex.org/files/IBPQuestionnaire2008Croatia.pdf>].



The principle of sound financial management requires that budgetary resources should be used in accordance with the principles of economy, efficiency and effectiveness.

In the following, we will try to answer the question of from where the money comes into the budget, where and how it is spent and how the Government monitors and records its borrowings and debt repayments.



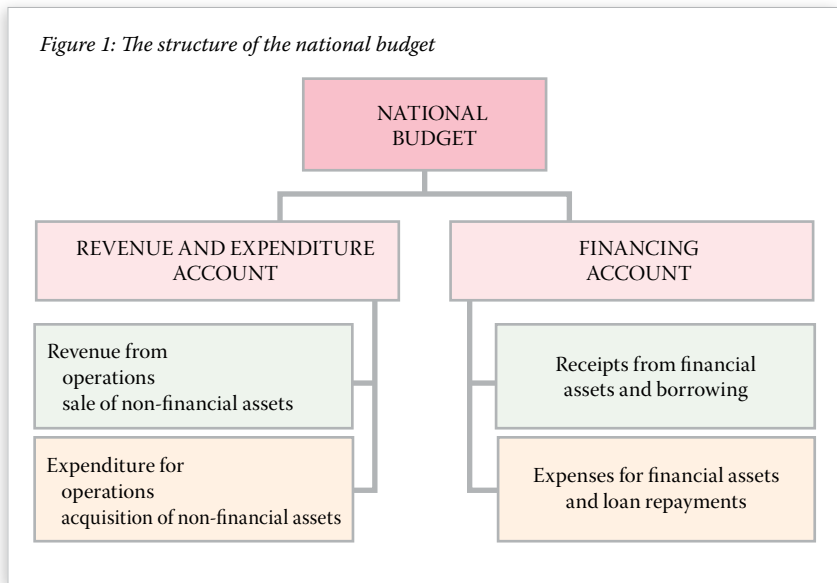
Where can one find the budgets?

Information on the national budget, the financial plans of extra-budgetary users, the consolidated central government budget, the budgets of local units, the consolidated general government budget and related documents can be found at the Ministry of Finance's website. However, sometimes, for example, in the case of proposals for such documents, one should visit the websites of the Government and Parliament.

The structure of the national budget

The national budget consists of a general and a specific section. The general section contains revenue and expenditure account and a financial account, whereas the specific section comprises the plans of expenditure of budget users allocated according to organisational and economic classifications, and according to current and development programmes.

Figure 1: The structure of the national budget



revenue and expenditure account – shows the revenue and expenditure of the state in a single year.

financing account – a part of the budget showing how budget deficit is financed and budget surplus spent.

Despite looking complicated, the structure shown is actually very simple. In the **revenue and expenditure account** the Government gives a clear classification of its annual income (revenue) and annual spending (expenditure). As the revenue rarely equals the expenditure, the Government keeps a special **financing account**, in which it records everything that it does with a possible surplus, when the revenue exceeds the expenditure, or of how it finances a possible deficit when expenditure outstrips the revenue.

Our household budgets are usually less complex, so they do not require such a clear and accurate structure. Moreover, unlike the Government which is obliged to keep records of its finances in a transparent manner, we do not have to account to anyone for the sources of our money and the things we spend it on. Nevertheless, just for illustration purposes, we would show our wages, fees, income from own business or income from interest on savings as revenue in the income and expenditure account. On the other hand, a new stove, a telephone bill or paid interest on a housing loan would be shown as expenditure in the same account. At the same time, loans



taken from and loans given to our relatives or friends would be recorded in the financing account.

These classifications may seem confusing and unnecessary at first glance, but they offer better insight into the numerous activities of the state. In addition, the structure of the Croatian national budget is harmonised with the International Monetary Fund's official methodology for the compilation of government finance statistics, which makes it possible to compare our national budgets with those of other countries.

How to find your way around the budget?

When you click on "budget" at the Ministry of Finance's website, you might first be intimidated by the very size of this document. However, you can count on the assistance of the budget compilers. You can inform yourself relatively easily and quickly about the revenue and expenditure according to the **economic classification**, as they are all divided into classes, groups, sub-groups and sections. To illustrate how this operates, we give the following examples of some basic revenue and expenditure items:

economic classification

– the presentation of revenues and receipts by natural type (e.g. taxes, aid, receipts from assets), and of expenditures and expenses by economic purpose (e.g. compensation of employees, subsidies, social benefits).

Class	Group	Subgroup	Section	Item
6				Operating revenues
	61			Tax revenue
		611		Personal income tax and surtax
			6111	Personal income tax and surtax on employment income
			6112	Personal income tax and surtax on income from self-employment, etc.
	62			Contributions
		621		Health insurance contributions
			6211	Health insurance contributions of employees, etc.
3				Operating expenditures
	31			Expenditures for employees
		311		Salaries
			3111	Salaries for regular and overtime work
			3112	Pay in kind, etc.
	32			Material expenditures
		321		Compensation of employees
			3211	Business trips
			3212	Travel allowance, field work and separation allowances, etc.





The revenue and expenditure account of the national budget

revenue – a term used in the revenue and expenditure account, for funds paid in that account on the basis of operations or the sale of non-financial assets.

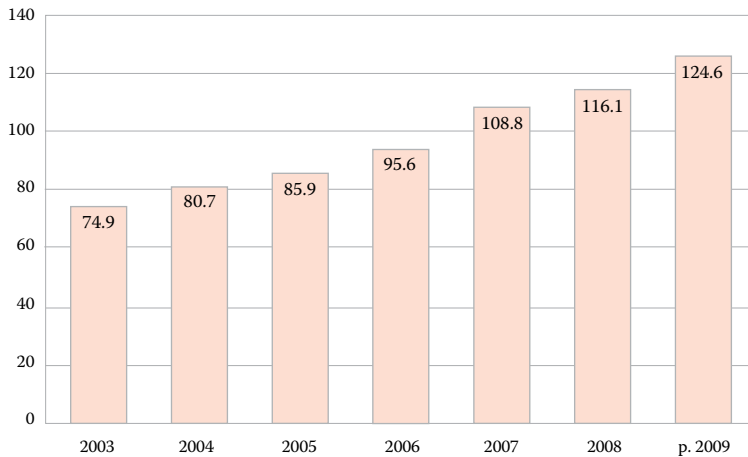
As shown by its name, the **revenue** and **expenditure** account shows the revenue and expenditure of the state in a given year. Let us first look at the revenue.

How large is the revenue of the national budget?

expenditure – a term used in the revenue and expenditure account, meaning funds disbursed from this account for government operations and the purchase of non-financial assets.

Graph 1 shows the growth of budget revenue in the period 2003-08. It can be seen that in 2003, total budget revenue stood at 75 billion kuna, whereas, according to the plan for 2009, it will reach almost 125 billion kuna. This means that the national budget revenue increases by 50 billion kuna, or by almost 70% in this period.

Graph 1: Total revenue of the national budget, 2003-09, in billion kuna



From what sources does the state draw its money?

The state derives operating revenues and revenues from the sale of non-financial assets. We will primarily focus on the operating revenues which accounts for over 99% of total national budget revenue.



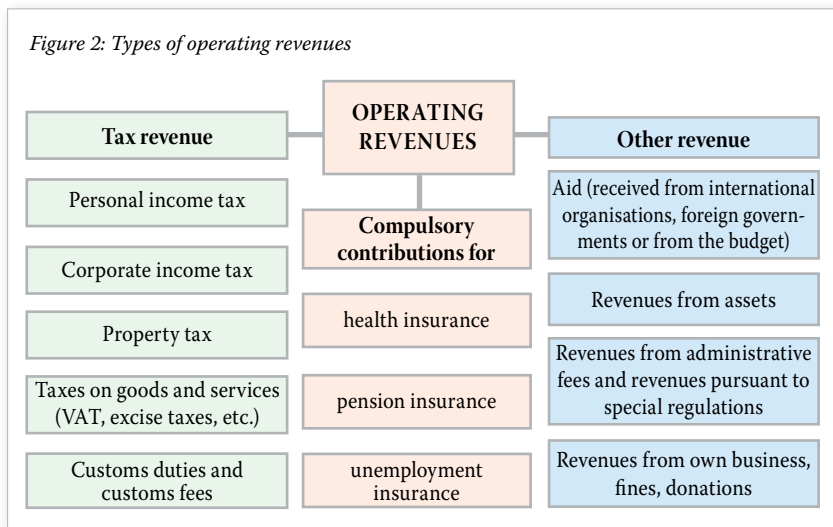
Operating revenues

The operating revenues constitute income from regular operations of the state, e.g. from **taxes** (on personal and corporate income or value added), **contributions** (for pension, health care and unemployment insurance) and other sources (assets, administrative fees and fines). Figure 2 and graph 2 show the types and the structure of this revenue. Taxation is the most significant regular activity of the state, as tax revenue participates with about 60% in total operating revenue, followed by compulsory insurance contributions, accounting for about 35% of the total and other revenue (5% of total operating revenues).

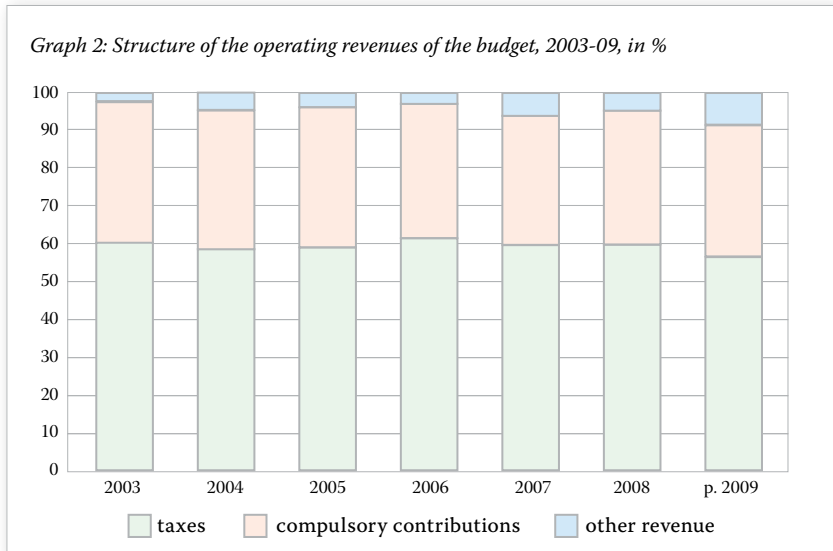
tax – a kind of compulsory payment to the government without a direct counter-benefit.

contributions – earmarked public revenues, paid for example for health and pension insurances. They are collected from employers and from employees. Unlike taxes which flow into the state treasury and can be used for any general public need, contributions are paid into special funds and can only be used for the purpose for which they are earmarked.

Figure 2: Types of operating revenues



Graph 2: Structure of the operating revenues of the budget, 2003-09, in %





Tax revenues

direct taxes – taxes imposed directly on taxpayers, i.e. the taxes to be paid by the taxpayer directly into the budget, e.g. corporate income tax and personal income tax, surtax on personal income tax, property tax and gift and inheritance tax.

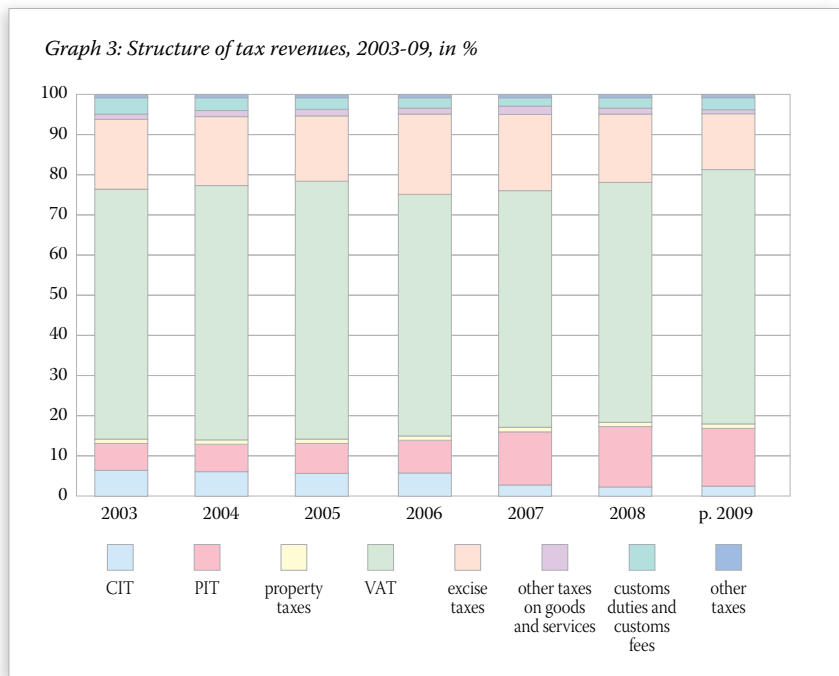
indirect taxes – taxes on goods and services collected indirectly through an intermediary, such as an importer, producer or seller (for example VAT, excise tax, and customs duty). They are included in prices, so that, despite being paid into the budget by intermediaries, they are indirectly borne by customers.

value added tax (VAT) – an indirect sales tax charged at every stage of production and distribution, i.e. for all final purchases of goods and services; it burdens the final consumer, but the actual taxpayer is the provider of goods and services.

excise taxes – special taxes, or excises, on the consumption of petroleum derivatives, tobacco products, coffee, beer, non-alcoholic beverages, spirits, personal cars and other motor vehicles, vessels, planes and luxu-

Tax revenues are the most important source of revenue for the national budget. They include revenues from personal income tax (PIT) and surtax, corporate income tax (CIT), property tax, tax on goods and services and tax on international trade and transactions. In this connection, we must differentiate between **direct taxes**, i.e. PIT and surtax on PIT, CIT and property tax, which are borne by taxpayers who pay a part of their income or property directly into the national budget, and **indirect taxes**, such as VAT or excise taxes, which are included in the price. Therefore, despite being paid into the budget by traders, these taxes are indirectly borne by consumers.¹

Graph 3: Structure of tax revenues, 2003-09, in %



As shown by graph 3, VAT and excise taxes represent the most affluent source of the national budget revenue, as, for many years, they have accounted for almost 80% of total tax revenue, or close to 50% of total operating revenues. So, in 2009, the state plans to collect about 70 billion kuna of tax revenue, of which over 44 billion from VAT and an additional 9.4 billion kuna from excise taxes.

¹ For more details about taxes, see Kesner-Škreb and Kuliš (2010).



Corporate and personal income taxes are not that significant, and their share in total tax revenue ranged from about 14% at the beginning of the reference period to 17% at the end of it. Moreover, since 2007, as the central government ceased to share the CIT revenue with local units, and increased the share of PIT allocated to local units, the share of PIT has decreased and the share of CIT went up (for more details about this, see the section about the structure of revenue of local units). So, why is the tax burden on labour in Croatia so often considered as very heavy, when the data on PIT suggest quite the opposite? The “mystery” will be solved in the next section about contributions.

ry products. They are justified by introducing tax progression (e.g. on luxury products), reducing pollution (e.g. on petroleum derivatives) and discouraging the consumption of certain products (e.g. tobacco and alcohol), hence: sin taxes.

Contributions

There has often been controversy about compulsory insurance contributions which account for about 35% of total operating revenues and represent the second most important source of the national budget revenue. Unlike the PIT and surtax on PIT, which are not too high in Croatia compared with other countries, the compulsory **contributions** represent a heavy burden on employees' salaries and count among the highest in the world.

Compulsory contributions

Despite a simplified division into pension, health and employment contributions, the compulsory contribution system is more complex. Specifically, there are compulsory contributions for (1) pension insurance under the pay-as-you-go scheme, (2) pension insurance based on individual capitalised saving, (3) health insurance, (4) unemployment insurance, and (5) employment incentives to disabled persons. Furthermore, the legislation on obligatory insurance determines more than seventy categories of contribution payers and lays down the base and rate for each category. However, the bulk of contribution payers can be classified into the following groups: (1) employees and their employers, (2) tradesmen and freelancers, (3) employees receiving salaries and some kind of additional income, and (4) pensioners.

We will discuss in more detail only the first (and largest) group which accounts for the bulk of revenues, i.e. employees and employers. The calculation base is the gross salary (GS) on which different contribution rates are applied. We distinguish between contributions from salary – paid by employees at a rate of 20% of GS for pension insurance, and contributions on salary – paid by employers at a rate of 1.7% of GS for unemployment insurance, 15% of GS for health insurance and 0.5% of GS for health protection at work.

The main difference between taxes and contributions is that tax revenue can be used for any budget expense, whereas contributions must only be used for the purposes for which they are earmarked.

contributions – earmarked public revenues, paid for example for health and pension insurances. They are collected from employers and from employees. Unlike taxes which flow into the state treasury and can be used for any general public need, contributions are paid into special funds and can only be used for the purpose for which they are earmarked.



Other operating revenues

Other operating revenues are less significant for the national budget, as, for many years, they have accounted for as little as 3% to 6% of total operating revenues. Included in this group are also various kinds of aid (from international organisations or foreign governments), revenue from assets (e.g. concessions for the use of the Croatian air space), charges and fees (e.g. revenue stamps for passport), etc.

public enterprise – an enterprise majority-owned and controlled by the state or a local unit which normally provides public or utility services; the definition is rather vague and the real status of some enterprises is not always clear.

extra-budgetary fund – a kind of extra-budgetary user established as a legal person for a special purpose and financed from earmarked revenues, from the budget or from other sources.



A Register of non-tax revenues

The Institute of Public Finance, in collaboration with the Ministry of Finance, has established a register of as many as 274 non-tax revenue items. These revenues are subject to special regulations related to particular administrative operations and economic functions of the Government. They are collected by central government authorities, **public enterprises**, **extra-budgetary funds**, local units, various organisations, chambers and associations (e.g. fire brigade associations or tourist boards), and are determined on the basis of various rates, rules and price lists.

Revenues from the sale of non-financial assets

These revenues account for less than one percent of total state revenue. The Government usually generates them by selling residential and business buildings, land, transportation facilities and strategic reserves.



Treasury Single Account

Did you know that most of the national budget revenue is paid into the Treasury Single Account (TSA) held by the Croatian National Bank? Actually, this is not a single account but a system of accounts in which all received revenues are deposited and from which all expenditures are paid to all budget users. It is supervised and controlled by the Ministry of Finance. Thanks to this account, the Ministry has full information about the balance of its funds at the end of each day and about how it is going to allocate them in accordance with set priorities.



Expenditure of the national budget

In order to establish who spends the collected revenue, as well as where and on what it is spent, expenditure of the national budget should be classified in several ways. The following classifications can be applied (but not always, not for all levels of budget, and often with a significant time lag): *economic classification*, i.e. according to the economic purpose of expenditure (e.g. compensation of employees, **subsidies** or social benefits); *functional classification* according to the purpose of expenditure (e.g. defence, health care or education); *programme classification*, according to specific programmes, activities and projects (e.g. environmental protection, informatisation or entrepreneurial support); *organisational classification*, according to organisational units (e.g. parliament, government, ministries, state administrations, etc.); *classification by source of finance*, showing the sources of revenue (e.g. taxes, contributions, **earmarked revenue** or **donations**); and *location classification*, i.e. by territorial unit (e.g. country, county, city, municipality or area of special state concern).

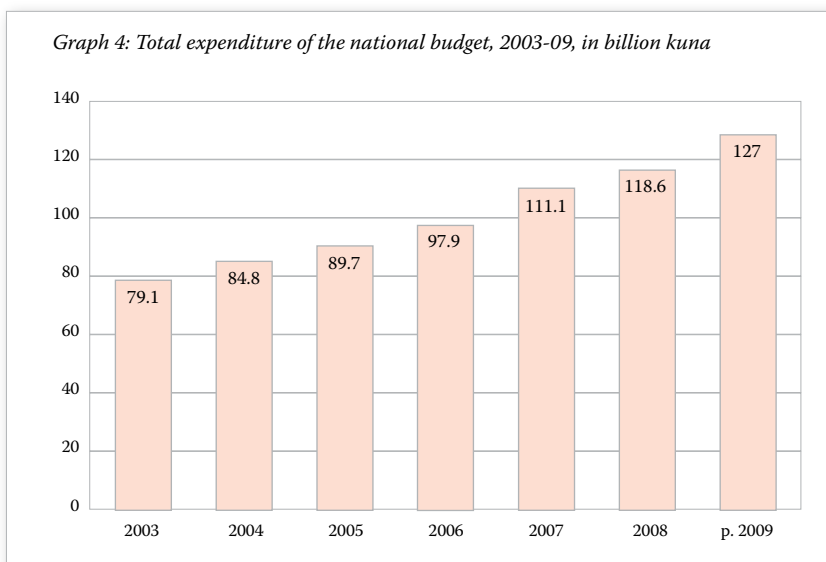
subsidies – non-repayable state aid to producers or consumers subject to a specific type of business or behaviour of the recipient.

earmarked revenue – the revenue whose purposes have been determined in advance; thus, for example, revenues from health insurance contributions must be used for health care.

donations – gifts in cash or in kind which can be given by the budget and budget users to non-profit organisations, households and citizens, or received from natural persons, non-profit organisations and companies.

What is the total amount of the national budget expenditure?

It is obvious that expenditure has grown from year to year. As shown by graph 4, they went up from about 79 billion kuna in 2003 to almost 127 billion kuna in 2009, which is an increase of about 62%.





fiscal consolidation – the policy aimed at reducing the national deficit and accumulated debts.

public sector – a part of the national economy comprising all levels of government, the social welfare, pension and health insurance systems and public enterprises.

There are many reasons for such a boost in expenditure: the consequences of war, adverse demographic situation, the unwillingness of both politicians and citizens to start effective structural reforms and **fiscal consolidation**, and above all, a too slow public administration reform, unsustainable pension and health care systems and lagging privatisation. All this resulted in high expenditures for **public sector** employees, high social benefits, and too generous subsidies to both private and public enterprises. As higher expenditure is to a large degree financed by borrowing, it is further increased by substantial amounts of interest.

What does the Government spend money on?

organisational classification – the presentation of expenditure according to organisational units, i.e. ministries, state offices, funds, institutes, agencies and other budget users (formerly known as administrative classification).

functional classification – a presentation of expenditure according to its purposes (e.g. defence, health care and education).

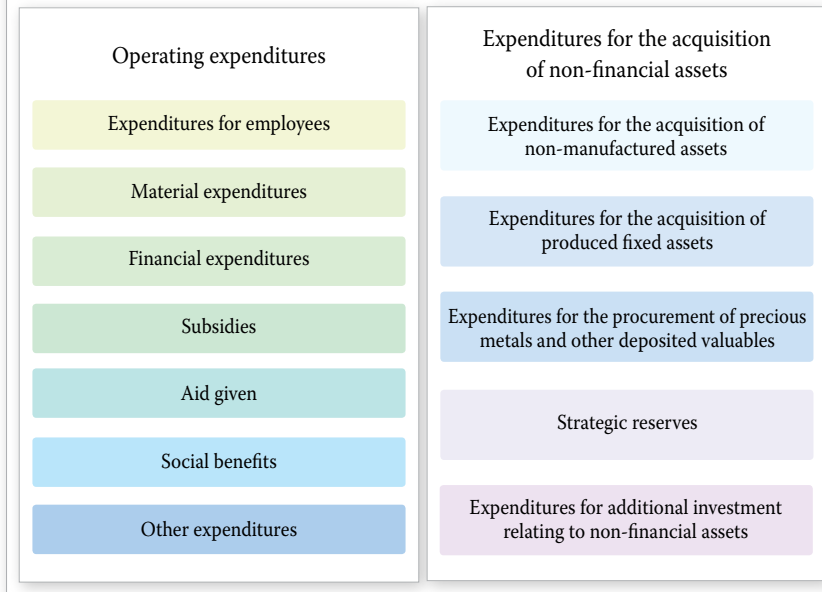
It is not always easy to find out on what the Government spends money. In order to establish this, we must consider state expenditure from various aspects. We already explained that there are various budget classifications. So, while the **organisational classification**, for example, shows the organisations which use budgetary resources, for example the Ministry of Health and Social Welfare or Ministry of Defence, the **functional classification** indicates the real amounts spent for defence or social welfare. But the fact that a certain amount of funds is allocated to a ministry does not necessarily mean that it is actually spent by this ministry for a specified purpose. The Ministry of Defence, for example, can give various social welfare benefits to ex-soldiers. In functional terms, these expenditures should be shown as welfare and not defence expenditures. Therefore, looking at the organisational budget classification alone can lead members of parliament astray in evaluating and deciding about the allocation of budgetary resources. It is therefore essential to show and analyse the budget according to different classifications. In the following part we will show expenditure according to the most common classifications: the economic, the functional, the organisational, classification by programme, and by source of financing.

Expenditure according to the economic classification

As we said before, expenditure is recorded in the revenue and expenditure account and it is divided into operating expenditures and expenditures for the acquisition of non-financial assets. For a number of years, operating expenditures have accounted for as much as 97-98% of total expenditure, whereas expenditures for non-financial assets accounted for the remaining 2%. A detailed division of operating expenditures and expenditures for non-financial assets is shown in figure 3.

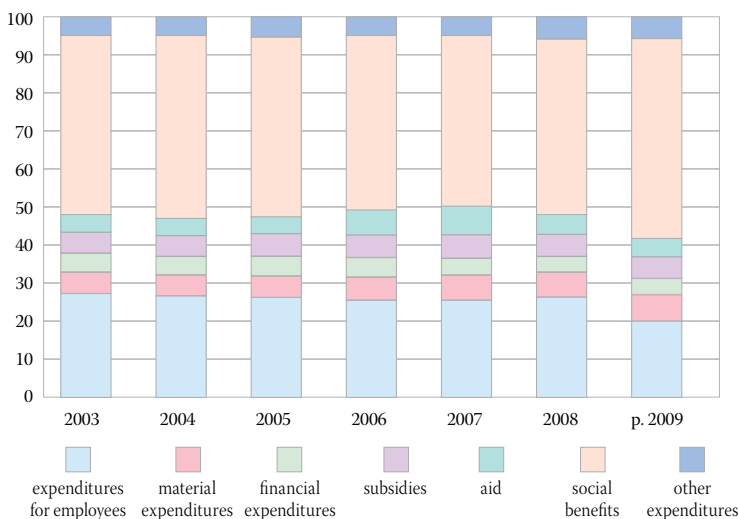


Figure 3: Types of expenditure of the national budget according to the economic classification



Particularly interesting is the structure of operating expenditures shown in graph 5. The most significant items are social benefits and expenditures for employees which jointly account for about 70% of total operating expenditures. Below we discuss the operating expenditures.

Graph 5: The structure of operating expenditures according to the economic classification, 2003-09, in %





Operating expenditures

As the name says, operating expenditures relate to the operations of the state. To be able to operate, the state must pay employees in its institutions. To enable these employees to work (make phone calls, send letters and stay in maintained business premises), the state must bear various material costs. As the state often lacks funds for its operation, it takes on loans and must therefore bear various financial costs (e.g. of interest payment); in order to provide incentive to various necessary activities, but also to “keep alive” loss-making businesses, it gives them subsidies; in order to enable underdeveloped **local units** to keep pace with more developed ones, the state provides them with various kinds of grants. And, of course, a welfare state must also provide social benefits (pensions, unemployment benefits, as well as sickness and maternity leave benefits). We will present here the usual operating expenditures categories by size, i.e. by their impact on the budget, from the largest (for social benefits) to the smallest (**financial expenditures**).

local units – municipalities and cities; the term sometimes also includes counties.

financial expenditures – the expenditures arising from financial operations, primarily due to borrowing (e.g. interest on issued securities, interest on loans and fees for banking services).

Social benefits

social benefits – the benefits based on insurance rights (pensions, unemployment benefits, as well as sickness and maternity benefits), or provided in the form of assistance to the poor in difficult situations which are not covered by the basic social insurance (e.g. various allowances to families and disabled persons, transportation cost aid and public kitchens).

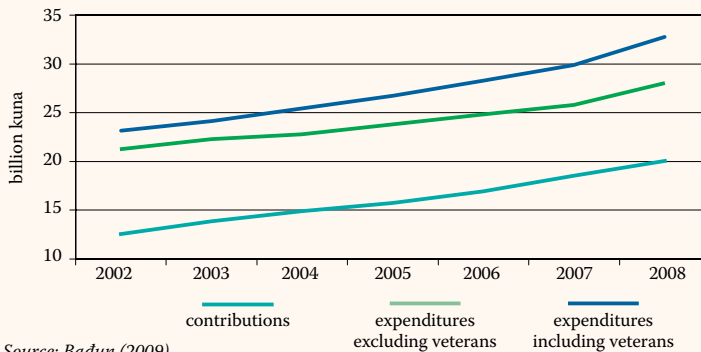
Social benefits are by far the most important group of the national budget expenditures. They include social security benefits (74%) and welfare benefits (26% of total social benefits). On top of these two kinds of benefits, there are also social benefits for civil servants, which are maintained as part of expenditures for employees.

- ◆ *Social security benefits* include pension, unemployment benefit, sickness and maternity leave benefits and child and family benefit, but also allowances for medical services, orthopaedic aids and appliances, pharmaceutical products and similar benefits provided by the state.
- ◆ *Welfare benefits* are intended for the poor in special situations which are not covered by the basic social insurance (e.g. various allowances to families and disabled persons, transportation co-financing and public kitchens). Of course, we would all like to live in a welfare state, but the problem is that social benefit expenditures jumped from 36 billion kuna in 2003 to almost 65 billion in 2009, their share in total expenditure increasing from 47% in 2003 to over 52% in 2009.



The growth of pensions

A dramatic increase in social benefits will be exemplified by pensions which account for more than a half of total social benefits and contribute strongly to overall social benefit growth. The graph shows their movements in the period 2002-08, and a gap between contributions collected (light blue curve) and benefits paid to pensioners (dark blue curve). This gap is due to several problems. First, the number of pension beneficiaries almost doubled (from about 650 thousand to 1.2 million) in the period 1990-2009, while the number of the actively insured, i.e. economically active population paying pension **contributions**, dropped from about 2 million to 1.6 million. While in 1990, three insured persons sustained one pensioner, today we have only 1.3 insured persons per pensioner. Second, more than 15% of beneficiaries have been granted pension under more favourable conditions, and their benefits accounted for 20% of total expenditures for pensions in 2008. Homeland war veterans' pensions account for the largest share in expenditures for "privileged pensions" (and almost 15% of total pension expenditures or about 5 billion kuna), and their number doubled in the last six years. Privileged pensioners receive higher benefits than "regular" pensioners, their required service periods are shorter; their retirement leads to erosion of contribution revenues and the loss of working-age population from the economically active population group. Besides causing inequality and inequity in the system, the differences between the "privileged" and "regular" pension beneficiaries increasingly burden the national budget.



Source: *Badun* (2009)

contributions – earmarked public revenues, paid for example for health and pension insurances. They are collected from employers and from employees. Unlike taxes which flow into the state treasury and can be used for any general public need, contributions are paid into special funds and can only be used for the purpose for which they are earmarked.

expenditures for employees – the salaries of employed civil servants, contributions for their compulsory health and pension insurance and various benefits in kind.

Expenditures for employees

As shown by graph 5, **expenditures for employees**, the second largest category of operating expenditures, account for an annual average of about 26% of the total. It is planned to spend about 25 billion kuna for employees in 2009. This category contains the salaries of **public sector** employees and contributions paid by the Government for their compulsory health and pension insurance. As a matter of fact, the Government pays the contributions to itself, because, as we have seen, social contributions are recorded as state revenue. However, although they do not represent an actual cost for the Government, they still have to be recorded.

public sector – a part of the national economy comprising all levels of government, the social welfare, pension and health insurance systems and public enterprises.



Material expenditures

Material expenditures include the total value of goods and services purchased by the state from the private sector on the market for the performance of its operations. Also recorded are expenditures for business trips, professional improvement, office supplies, power, telephone, utility services, information, etc. About a half of these expenditures relate to telephone, postal and transportation services, regular and investment maintenance, etc. Despite being the third largest operating expenditures, material expenditures still represent a less significant expenditures category. Their share has grown continuously, from about 5.4% of total operating expenditures at the beginning of the period, to 6.8% at its end. In 2009, they are planned to amount to 8.4 billion kuna.

Subsidies

subsidies – non-repayable state aid to producers or consumers subject to a specific type of business or behaviour of the recipient.

Subsidies are current non-repayable funds provided by the Government to enterprises in order to stimulate their production, make up for their losses, maintain lower prices of certain goods, etc. We are talking here about the implementation of certain economic and social policy measures of the Government for which almost 7 billion kuna were earmarked in 2009. It should be noted that, during the reference period, subsidies to private enterprises (mainly agricultural businesses) outstripped markedly the subsidies to public enterprises, and that the share of subsidies in total operating expenditures is constant (about 6%).

Grants

grants – non-returnable transfers of funds to international organisations, foreign governments, budgets, extra-budgetary users, banks, financial institutions and enterprises. Aid is often given by the national budget to local budgets, but they can also be given among local units of the same level, e.g. counties. They are divided into current grants (for current expenses) and capital grants (for the purchase of fixed assets), as well as into special-purpose and general-purpose grants.

Grants account for about 5.4% of total expenditure and include current and capital transfers to international organisations, foreign governments, budgets, extra-budgetary funds, banks and other financial institutions, but also to enterprises.

Financial expenditures

These expenditures arise from financial operations, primarily from the foreign borrowing of the state. They include, for example, interest arising from securities issued, interest arising from loans received from other levels of government, foreign governments, international organisations, banks and other financial organisations, fees for banking and payment services, default interest, etc. About a half of financial expenditures relate to interest on government bonds issued. Financial expenditures account for an annual average of 4.6% of total operating expenditures, are projected at about 5.3 billion kuna in 2009.

Expenditures for the acquisition of non-financial assets

Unlike the above described operating expenditures which relate to the current or regular operation of the state, expenditures for the acquisition of non-financial assets relate to fixed assets. They involve the acquisition of non-manu-



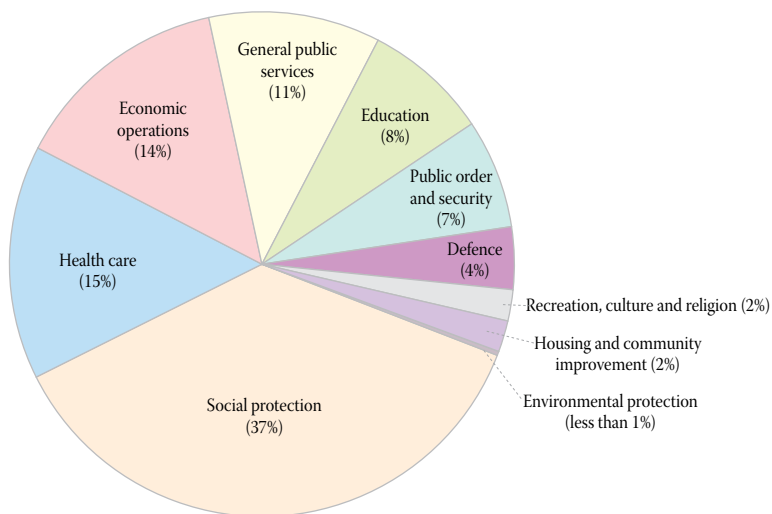
factured assets (e.g. land), manufactured assets (such as buildings), precious metals, strategic reserves, etc. The bulk of these expenditures usually relate to the procurement of buildings. Despite being relatively small, the share of expenditures for the acquisition of non-financial assets in total expenditure increased from 2 billion kuna in 2003 to almost 3.6 billion planned for 2009.

Expenditure according to the functional classification

As said before, there are numerous classification methods, and not all of them are used for each level of government. Moreover, the necessary data are often delivered with a time lag. Therefore, we present the structure of total expenditure of the national budget according to the **functional classification** for 2007. As this structure is not subject to significant change from year to year, it will provide us with an insight into how the Government spends money.

functional classification
– a presentation of expenditure according to its purposes (e.g. defence, health care and education).

Graph 6: Structure of total expenditure according to the functional classification, 2007



Source: Ministry of Finance (2007: 56-58)

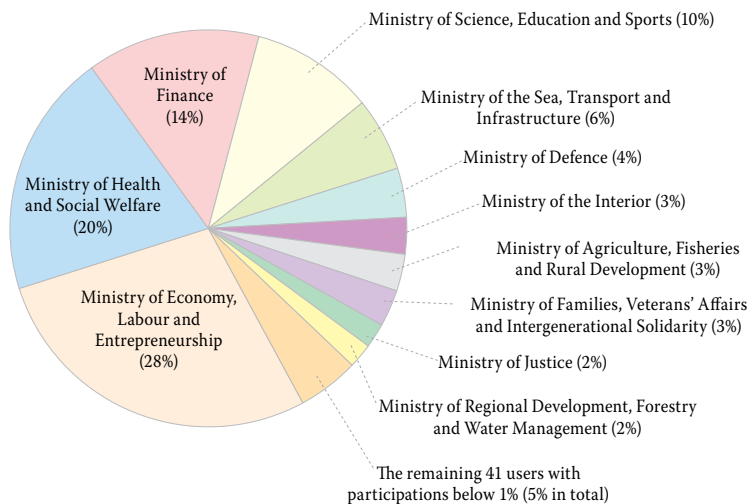
As suggested, most funds (more than a third or 37%) are spent on social protection. Together with health care (15%) these expenses account for more than a half (52%) of expenditure. This could be as sign of a social consensus reached on the need to improve the social and health conditions of the nation, but also of lavish spending in the sectors which have not been reformed or restructured. The third largest item of expenditures – economic operations (14% of total expenditure) shows that the role of the state in the economy is too strong, primarily as concerns subsidies to non-efficient sectors like the railways, agriculture or shipbuilding.

Expenditure according to the organisational classification

organisational classification – the presentation of expenditure according to organisational units, i.e. ministries, state offices, funds, institutes, agencies and other budget users (formerly known as administrative classification).

The **organisational classification** ensures up-to-date records of expenditures, so that table 1 shows us the amount of budgetary funds used by each organisational unit in 2008. This relates to ministries, state administrations, funds, institutes, agencies and other budget users. Although there were as many as fifty such users, only eleven of them spent more than 1%, and only five accounted for more than 6% of total budgetary resources. As few as five users, i.e. the Ministry of Economy, Labour and Entrepreneurship, the Ministry of Science, Education and Sports, and the Ministry of the Sea, Transport and Infrastructure, spent almost 80% of total budgetary resources. What can we conclude from this? The fact that the Ministry of Economy, Labour and Entrepreneurship is the largest beneficiary could lead us to the idea that the bulk of resources are used in the economy. However, this is not true. Of the total funds allocated to this Ministry, 93% goes to the Croatian Pension Insurance Institute and 3.3% to the Croatian Employment Service. It follows that 96% of the Ministry of Economy's resources is allocated for social purposes. If the funds used by this Ministry (28% of total budget expenditure) are added to the resources allocated to the Ministry of Health and Social Welfare (20% of the total), we see that more than a half of total budgetary resources is spent on various social benefits. After all, a similar picture is presented by the functional classification. It is obvious then that these sectors need to be reformed and restructured in order to cut down the huge budget expenditure.

Graph 7: Structure of budget users according to the organisational classification; the 2008 budget execution



Source: Ministry of Finance (2007: 56-58)



Table 1: The 2008 national budget execution according to the organisational classification

Budget user	Execution	
	in million kuna	in %
Total	126,923.4	100.00
050 Ministry of Economy, Labour and Entrepreneurship	35,965.9	28.34
100 Ministry of Health and Social Welfare	24,754.5	19.50
025 Ministry of Finance	18,019.1	14.20
080 Ministry of Science, Education and Sports	12,061.7	9.50
065 Ministry of the Sea, Transport and Infrastructure	7,812.2	6.16
030 Ministry of Defence	5,218.6	4.11
040 Ministry of the Interior	4,415.9	3.48
060 Ministry of Agriculture, Fisheries and Rural Development	4,047.1	3.19
046 Ministry of Families, Veterans' Affairs and Intergenerational Solidarity	4,010.6	3.16
110 Ministry of Justice	2,574.5	2.03
062 Ministry of Regional Development, Forestry and Water Management	2,275.2	1.79
055 Ministry of Culture	1,250.5	0.99
075 Ministry of Environmental Protection, Physical Planning and Construction	670.9	0.53
048 Ministry of Foreign Affairs and European Integration	635.7	0.50
021 Central State Administrative Office for Public Administration	480.6	0.38
027 Security and Intelligence Agency	317.5	0.25
180 State Geodetic Directorate	286.2	0.23
020 Government	258.4	0.20
220 Croatian Mine Action Centre	257.2	0.20
115 Development and Employment Fund	248.8	0.20
090 Ministry of Tourism	218.7	0.17
010 Croatian Parliament	163.5	0.13
225 State Inspectorate	148.8	0.12
116 Regional Development Fund	130.4	0.10
140 Meteorological and Hydrological Service	108.5	0.09
160 Central Bureau of Statistics	86.4	0.07
106 Croatian Academy of Sciences and Arts	63.5	0.05
015 President of the Republic of Croatia	52.8	0.04
185 State Audit Office	51.5	0.04
022 Central State Administrative Office for E-Croatia	46.0	0.04
024 Central State Administrative Office for State Property Management	40.6	0.03
023 Central Office for Development Strategy and Coordination of EU Funds	31.7	0.02
150 State Office for Metrology	28.7	0.02
017 Constitutional Court of the Republic of Croatia	27.9	0.02
156 State Intellectual Property Office	19.7	0.02
241 Operational and Tech. Centre for the Supervision of Telecommunications	17.8	0.01
175 Croatian Hydrographic Institute	16.4	0.01
018 Croatian Competition Agency	15.0	0.01
151 Croatian Standards Institute	14.6	0.01
240 Office of the National Security Council	14.2	0.01
260 National Nuclear Safety Office	9.2	0.01
242 Information System Security Bureau	9.0	0.01
152 Croatian Accreditation Agency	8.1	0.01
250 Croatian Personal Data Protection Agency	6.9	0.01
196 State Commission for Supervision of Public Procurement Procedure	6.6	0.01
120 Office of the Ombudsman	6.3	0.00
235 Croatian Information and Documentation Referral Agency	5.6	0.00
121 Ombudsman for Children	5.3	0.00
255 State Office for Radiation Protection	4.4	0.00
122 Croatian Gender Equality Ombudsperson	2.5	0.00
123 Ombudsman for Disabled Persons	1.1	0.00
230 Committee for Relations with Religious Communities	0.6	0.00

Source: Croatian Parliament (2009: 28-31)



Numeration in the organisational classification

Table 1 shows budget users according to their respective shares in total expenditure. However, as we can see, each organisation is assigned a certain numerical code, representing the section. The organisational classification includes sections from 010 Croatian Parliament, 015 President of the Republic, 017 Constitutional Court to 250 Personal Data Protection Agency, 255 State Office for Radiation Protection, and 260 National Nuclear Safety Office. Individual organisations, e.g. the Ministry of Economy, Labour and Entrepreneurship, are further divided into chapters, so we have chapter 05005 Economy and Entrepreneurship, chapter 05010 Commodity Reserves Directorate, etc.

Expenditure by programme

programme classification – the statement of expenditure by programme, activity and project (e.g. environmental protection, informatisation or entrepreneurial support).

programme – a set of independent and closely connected activities and projects aimed at achieving a common goal.

activity – a part of a programme of no pre-defined duration, but with planned expenses for the achievement of goals set by the programme.

project – a part of a programme of a pre-defined duration, with planned expenses for the achievement of the goals set by a programme.

Expenditure is also classified according to the programmes for achieving the budget users' goals. The idea of the **programme classification** is to determine, as accurately as possible, the purpose of expenditures and to improve the efficiency control of spending. The fact is that, based on its strategy, the Government adopts a four-year general **programme** in which its financial priorities are specified. The general programme is a set of programmes with the same goal, to be implemented by individual ministries. A special part of the budget contains all expenditures classified by user and programme. Each programme has its target group of users, a determined budget, the necessary staff and resources as well as defined goals and estimated results.

The classification by programme will be shown on the example of the Ministry of Defence. The code 030 denotes a section, and 03005 stands for a chapter in the national budget. The defence programme is identified by four digits (1552). Programmes are usually divided into sub programmes with codes beginning with letters A (**activity**), K (capital project) or T (current **project**). Each of the letters is followed by a six-digit number. The Ministry of Defence has twelve activities, one capital project and one current project.

Budget classification by programme

030	Ministry of Defence
03005	Ministry of Defence
1552	Defence programme
A545008	International co-operation
A545019	Armed forces functioning
A545023	Education and professional development
A545025	Equipment and modernisation, etc.
K545040	Fire fighting aircrafts
T545041	Establishment of the company Aviation Technical Centre, Ltd.



Each activity is further divided by type of expenditure, so that we can see how much was spent within A545025 for business trips, professional improvement, etc. Each of these types of expenditures within an activity is denoted by a four-digit number.

Budget by activity	
A545025	Equipment and modernisation
3211	Business trips
3213	Professional improvement
3221	Office supplies and other material expenditures, etc.

The classification by programme should provide for measuring the results of each programme, activity and project within a programme, and for measuring the costs of particular services financed from the budget. This should provide for budget execution control and the appropriateness of the use of government resources.

Expenditure by source of financing

Thanks to the Treasury Single Account it is also possible to monitor the expenditure by source of financing. The sources of financing are all revenues used for financing the expenditures of a particular type and for a particular purpose. Each source of financing is assigned a one-digit code representing the section (e.g. 1 – general revenues and receipts; 2 – compulsory insurance contributions; 3 – own revenue; 4 – special-purpose revenue; 5 – **Grants**, etc.), and a two-digit code indicating the group.

As an example we take the activity “A618184 Early detection, treatment and rehabilitation of drug addiction”, in the national budget section “100 Ministry of Health and Social Welfare”. The sources of financing for this activity are: 11 General revenues and receipts, 41 Revenues from games of chance, and 51 EU grants.

To conclude the chapter on classifications, we should note that all classifications must be interconnected, and that it should be possible to monitor each expenditure according to several criteria. Expenditures by institution must also be divided by programme, economic type and source of financing. Moreover, thanks to the numeration system, data on expenditures should also be classified according to individual government functions. The purpose of combining classifications is to provide a better insight into the purposes, types and effects of the national budget expenditure.

grants – non-returnable transfers of funds to international organisations, foreign governments, budgets, extra-budgetary users, banks, financial institutions and enterprises. Aid is often given by the national budget to local budgets, but they can also be given among local units of the same level, e.g. counties. They are divided into current grants (for current expenses) and capital grants (for the purchase of fixed assets), as well as into special-purpose and general-purpose grants.



Measures of the national budget deficit/surplus

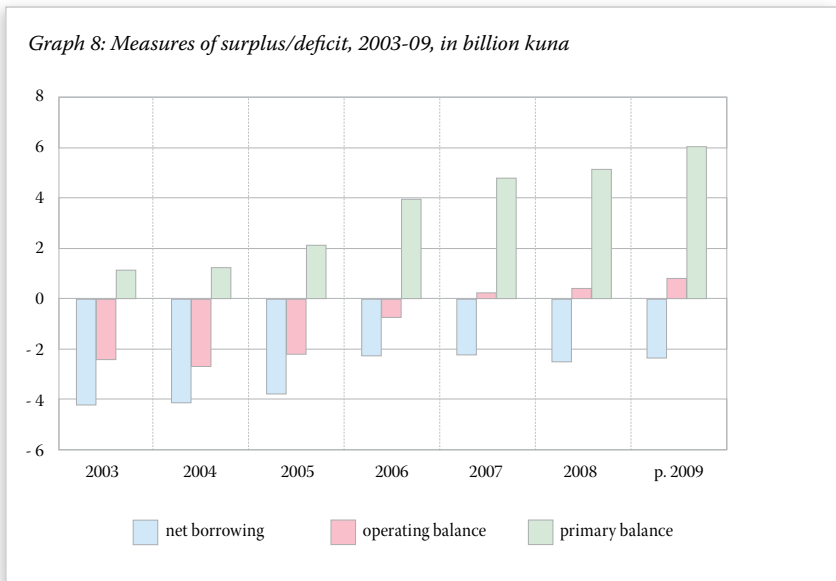
budgetary principles – the principles to be adhered to by all those dealing with the budget; they include the principles of equilibrium, annuality, unity and budget accuracy, universality, specification, transparency and sound financial management.

As the balance between budget revenue and expenditure constitutes one of the basic **budgetary principles**, whenever there is imbalance between revenue and expenditure, and this is practically always the case, the Government has to show the gap in various ways.

One of the basic categories to be shown is the difference between total revenue and total expenditure. When revenue is higher than expenditure we talk about net lending, and when expenditure exceeds revenue we have *net borrowing*.

Another indicator to be shown is the *operating balance*, representing the ratio between regular operating revenues and operating expenditures excluding changes in non-financial fixed assets.

There is also the *primary operating balance* showing the difference between operating revenues and operating expenditures net of interest expenses.



Graph 8 shows the measures of the national budget surplus/deficit in the period 2003-09. As we can see, the overall deficit declines gradually over time, and the Government tries to maintain positive operating and primary balances, thus reducing total net borrowing.

deficit – excess of expenditure over revenue in a given period.

It is worth mentioning that the public is rarely informed about all of these measures, but only about the *national budget deficit*. According to the



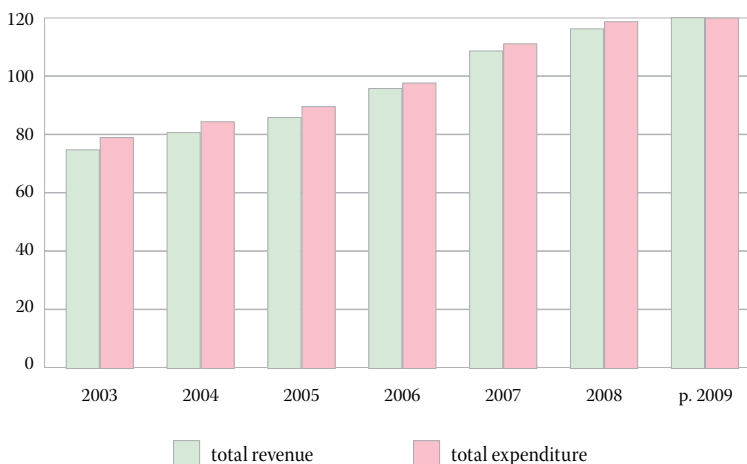
International Monetary Fund's methodology, the national budget deficit should equal net borrowing. However, to make things more complicated, as usual, the deficit calculations are still made by partly using the old methodology according to which expenditure includes some categories of expenditures for non-financial assets. As a result, instead of being equal to net borrowing, the Croatian budget deficit is usually slightly higher. As these differences are really insignificant, they will not be further discussed in this Guide.

The financing account

So far we have explained how the Government collects money and how it spends it. Graphs 8 and 9 show that, in all the reference years, the Government spent more than it collected. As we said in the introduction, if we want to spend more than we have, we must borrow funds in order to cover the excess spending. We can take out a bank loan, borrow money from friends or the family, draw money from our own savings account or use a combination of all these options. If we want to maintain our finances very carefully, we must record such transactions in a special account within our budget, called the **financing account**. This account gives us an insight into how we financed our increased spending, or what we invested our increased income in.

financing account – a part of the budget showing how budget deficit is financed and budget surplus spent.

Graph 9: Total revenue and expenditure of the national budget, 2003-09, in billion kuna



Where are the privatisation receipts recorded?

Privatisation receipts are one-off receipts used for the financing of the national budget deficits, and are recorded in the financing account as receipts from financial assets. They used to be substantial in the years of major privatisations (e.g. of banks and telecommunications), but they fell to a relatively low level over the last few years. In future, all sales of state assets, including sales of shares in **public enterprises**, will be recorded as the national budget's one-off receipts from the sale of financial assets, and will be used for the repayment of debt from previous periods. A larger share of privatisation receipts in total receipts (also including the receipts from borrowing) is usually due to the poor fiscal position of the national budget, forcing the Government to sell valuable assets.

public enterprise – an enterprise majority-owned and controlled by the state or a local unit which normally provides public or utility services; the definition is rather vague and the real status of some enterprises is not always clear.

The same behaviour is required from the Government. Figure 4 shows what the state's financing account looks like.

Figure 4: The national budget's financing account



The states' receipts include various monetary inflows arising from domestic and foreign deposits and loans, as well as receipts from other financial assets like securities. The records of expenses include the outflows of funds according to the same categories. The difference between these receipts and expenses constitutes the *net financing*, i.e. the amount that should equal the deficit/surplus from the revenue and expenditures account, or the net lending/borrowing of the state.

What is a budget revision?

A budget revision is a change in the budget amounts, i.e. their decrease or increase relative to the budget plan adopted at the beginning of the calendar year. A revision occurs if it is established during the fiscal year that budget revenues have been estimated inaccurately, or if unforeseen expenditures occur. A budget revision can be necessitated by contingencies in the domestic or world economies, such as the global recession, but it can also be the consequence of the Government's inability to make realistic estimates of its revenue and expenditure.

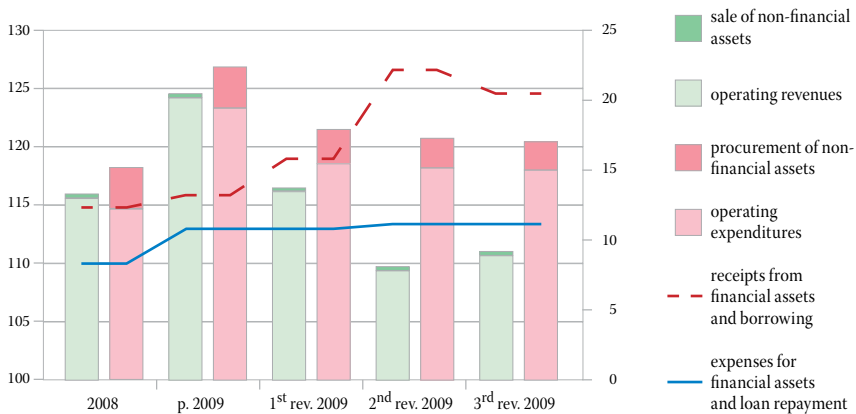


Table 2 and graph 10 provide a simple presentation of the 2009 budget plan made at end-2008, and as many as three revisions that followed – the first one in April, and the second and the third in July 2009.

Table 2: Total revenue, expenditure and financing of the national budget, in billion kuna

	2008 Execution	2009 Plan	Revisions in 2009		
			I	II	III
Revenue and expenditure account					
Operating revenue	115,756	124,242	116,222	109,485	110,872
Revenue from the sale of non-financial assets	303	395	381	339	339
Operating expenditures	115,060	123,397	118,599	118,211	118,041
Expenditures for the acquisition of non-financial assets	3,292	3,594	2,979	2,587	2,496
Surplus/deficit	-2,291	-2,355	-4,975	-10,975	-9,327
Financing account					
Receipts from financial assets and borrowing	12,308	13,183	15,763	22,129	20,471
Expenses for financial assets and loan repayment	8,360	10,828	10,788	11,155	11,144
Change in deposit balance	1,441	0	0	0	0
Net financing	2,508	2,355	4,975	10,975	9,327

Graph 10: Total revenue and expenditure (left-hand scale) and financing of the national budget (right-hand scale), in billion kuna



Source: Ministry of Finance (2009a)

Specifically, even though it was obvious, as early as the beginning of autumn 2008 that the world economy had got into a recession which Cro-



atia would not be able to avoid, the Government late in 2008 planned its 2009 budget too optimistically.

At that time, the Government was already aware that public spending was unsustainably high and that the public debt of almost 11 billion kuna would fall due in 2009 (as represented by the solid blue curve on the graph, right-hand scale). The Government was supposed to know that further borrowing was irresponsible towards (declining) future generations which will have to repay this debt, and that excess government borrowing would hamper private sector development, as a result of both funding difficulties and an inevitable increase in the tax burden. However, under the pressure of various interest groups, the 2009 budget plan was as optimistic as in the times of strongest economic growth. Such a budget plan soon proved to be unsustainable. Therefore, despite the introduction of new taxes and a VAT rate increase, in the budget revisions that followed the Government had to plan significant cuts in revenues, because, due to recession, the revenues were simply not flowing in.

Alas, the Government was not strong enough to make any significant spending cuts, but rather decided to sharply increase borrowing (see the dashed red curve on the graph, right-hand scale). As a consequence of such irresponsible fiscal behaviour of both the previous governments in the period of the average 5-percent annual growth of GDP (2002-07) and of the present government in planning and revising the 2009 budget, the national budget deficit of 2.4 billion kuna, projected at end-2008, grew to 9.3 billion kuna projected in August 2009 (see the vertical space between the solid blue and dashed red curves, right-hand scale).

We must keep in mind, however, that the growth of the dashed red curve (borrowing) in a given year will definitely lead to the growth of the solid blue curve (debt repayments and, of course, the interest making this debt significantly heavier) in the coming years.



The budgets of extra-budgetary funds

A major part of the funds collected and spent in the state are recorded in the national budget, and a smaller part in the budgets of extra-budgetary users of the national budget and in the budgets of local units. In the previous section we explained the main concepts related to the national budget, and now we will discuss the **extra-budgetary users** of the national budget.

Who are the extra-budgetary users?

The extra-budgetary users of the national budget are **extra-budgetary funds**, companies and other legal entities in which the Government exerts a decisive influence on the management, but which also enjoy a high level of autonomy, including independent decision-making on a part of their own revenue and expenditure. Each extra-budgetary user of the national budget has a separate budget, which is why, in many countries, the revenue and expenditure of such users are not included in the national budget. In Croatia, however, in order to make the management of the money of major extra-budgetary users (the pension and health insurance institutes and employment service) more efficient, their revenue and expenditure have been included in the national budget since 2007. As shown by table 3, the status and number of extra-budgetary users are subject to frequent changes, which hamper the monitoring of their revenue and expenditure.

extra-budgetary users

– extra-budgetary funds, enterprises and other legal persons in which the state or local units exercise a decisive influence on the management, and which enjoy considerable autonomy including independent decision-making on a part of their revenue and expenditure.

extra-budgetary fund

– a kind of extra-budgetary user established as a legal person for a special purpose and financed from earmarked revenues, from the budget or from other sources.

Table 3: Extra-budgetary users of the national budget, 1999-2008

	1999- 2000	2002	2003	2004- 2006	2007	2008
Croatian Pension Insurance Institute	+	+	+	+	-	-
Croatian Health Insurance Institute	+	+	+	+	-	-
Croatian Employment Service	+	+	+	+	-	-
Child Benefit Fund	+	-	-	-	-	-
Croatian Waters	+	+	+	+	+	+
Croatian Motorways	-	+	+	+	+	-
Croatian Roads	-	+	+	+	+	+
State Agency for Deposit Insurance and Bank Rehabilitation	-	+	+	+	+	+
Croatian Privatisation Fund	-	+	+	+	+	+
Development and Employment Fund	-	+	-	-	-	-
Regional Development Fund	-	+	-	-	-	-
Environmental Protection Fund	-	-	-	+	+	+



financial plan – a document drafted by a budgetary or extra-budgetary user showing its revenue and expenditure.

revenue – a term used in the revenue and expenditure account, for funds paid in that account on the basis of operations or the sale of non-financial assets.

Hence, the main characteristic of the extra-budgetary users is that they are independent legal entities which use their budgets, also called **financial plans**, to finance certain public needs like road construction or water supply. The most common reason for their establishment is to ensure a source of financing for a particular purpose and thus prevent a situation where, due to the pressures from certain interest groups, there would not be enough revenues for that purpose. Therefore, the Croatian Pension Insurance Institute has long had status as an extra-budgetary user, as it was considered that the funds for pensions had to be provided at all times, regardless of the pressures coming, for example, from shipbuilding or construction lobbies during parliamentary budget debates.

The extra-budgetary users are financed from earmarked **revenues**, but also from budgetary resources. The special-purpose revenue means the revenue whose purpose has been determined in advance (for example, revenues from health insurance contributions must be spent on health care).

Besides the extra-budgetary users of the national budget, there are also extra-budgetary users of local units' budgets which will be discussed in the section on local units.

Table 4: Extra-budgetary users of the national budget and their sources of revenue

Extra-budgetary user of the national budget	Sources of revenue
Croatian Pension Insurance Institute	Contributions from wages, and the shortfall covered from the national budget (until 2007)
Croatian Health Insurance Institute	Contributions on wages, and the shortfall covered from the national budget (until 2007)
Croatian Employment Service	Various types of contributions, and the shortfall covered from the national budget (until 2007)
Croatian Privatisation Fund	Receipts from the sale of the Fund's shares or stakes in companies, dividends, transfers from the national budget and other revenue
Croatian Waters	Revenue from rates (e.g. water utilisation rates) and transfers (grants) from the national budget and other revenue
Croatian Motorways	Transfers (grants) from the national budget, road tolls, various charges (motorway tolls) and other revenue (until 2008)
Croatian Roads	Transfers (grants) from the national budget, various fees (e.g. motor fuel fee) and other sources
State Agency for Deposit Insurance and Bank Rehabilitation	Insurance premiums paid by banks and savings banks for savings deposit insurance, revenue raised through the Agency's operations (various fees and charges) and transfers from the national budget
Environmental Protection Fund	Fees (e.g. environmental pollution fee), transfers from the national budget, and other sources

**Bolded are current extra-budgetary funds.*



The extra-budgetary users' own revenue (e.g. the Croatian Roads' motor fuel fee) is most frequently insufficient to cover their expenditure. The largest shortfalls in own revenue have been reported, for example, by Croatian Roads and Croatian Motorways (at the time when they had status as extra-budgetary users), because they finance new capital transportation projects. A part of the shortfall is tried to be covered by the national budget transfers, whereas the remainder is financed through borrowing. Specifically, the Government takes out loans and issues bonds to be sold on the international capital markets. These debt instruments have been very popular for the financing of new motorway sections. This could be compared with a situation of, for example, a husband having insufficient own income to buy a car. A part of the shortfall is covered by transferring funds from the wife's budget and the rest is financed by taking out a bank loan.

How are the financial plans of extra-budgetary users of the national budget adopted?

Just as the state draws up its budget, extra-budgetary users prepare their financial plans. The extra-budgetary users of the national budget draw up their financial plans at the same time as the national budget is being made. Each user makes its own financial plan proposal for the following year and submits it to the relevant ministry, which delivers it, together with its own financial plan, to the Ministry of Finance. The summaries of the extra-budgetary users' financial plans are appended to the proposal for the national budget and submitted to Parliament. After a debate, the Parliament will approve them together with the national budget for the following year. The adoption procedure for the financial plans of extra-budgetary users of the national budget is explained in detail in the Budget Act, and financial plans are published in the Official Gazette on the date of publishing the national budget and the national budget execution act.



general government – central government (budgetary and extra-budgetary users of the national budget) plus budgetary and extra-budgetary users of the county, city and municipality budgets consolidated general government budget.

The revenue and expenditure of extra-budgetary users

As shown by graph 11, the revenue and expenditure of extra-budgetary users grew continuously over the period 2005-07, with the expenditure constantly exceeding the revenue. The situation changed in the following years, as the Health Insurance Institute, Pension Insurance Institute and Employment Service lost their status as extra-budgetary users and were included in the national budget, and as Croatian Motorways were excluded from the **general government** to be maintained as **public enterprise**. Of course, such changes hamper the monitoring of the budgetary and extra-budgetary users' operations and prevent comparisons across years.

public enterprise – an enterprise majority-owned and controlled by the state or a local unit which normally provides public or utility services; the definition is rather vague and the real status of some enterprises is not always clear.

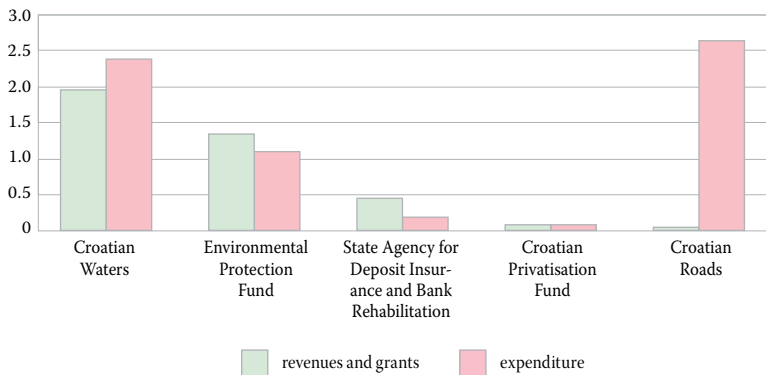


Graph 11: Total revenue and expenditure of extra-budgetary users, 2005-09, in billion kuna



Source: Ministry of Finance (2009b; 2009c)

Graph 12: The revenue and expenditure plan of extra-budgetary users for 2009, in billion kuna



Source: Ministry of Finance (2009c)

deficit – excess of expenditure over revenue in a given period.

Almost 80% (5.1 billion kuna) of the extra-budgetary users' expenditure is allocated to Croatian Roads and Croatian Waters which account for the total **deficit** of extra-budgetary users amounting to 2.5 billion kuna. It should be noted that the 2009 deficit of Croatian Roads (2.6 billion kuna) exceeds the overall deficit of all extra-budgetary users (2.5 billion kuna), which shows the need for more rational spending of the funds earmarked for roads and for considering the possibility to privatise a part of this sector. This would, at least in the long run, narrow the huge gap between revenue and expenditure of the Croatian Roads company (71 million kuna vs. 2.7 billion kuna)

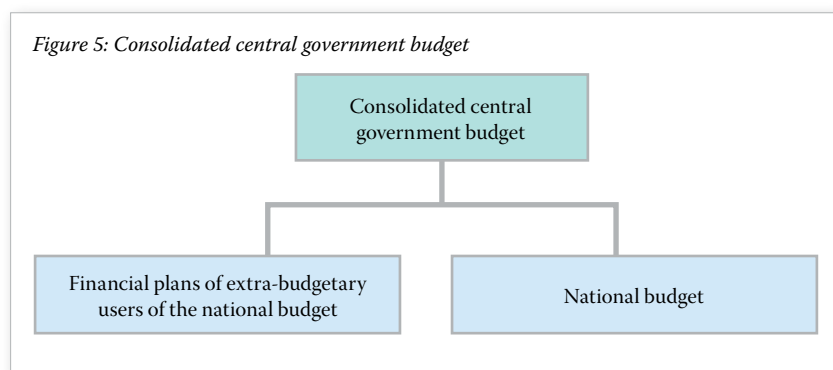


The consolidated central government budget

We will try to explain the consolidated **central government** budget on the example of a family in which only the husband and wife are employed. We assume that each of them earns 5,000 kuna per month. In a given month, the husband spends 4,000 kuna and gives 1,000 kuna to his wife for overhead expenses. The wife spends 5,500 kuna. Consolidation means procedure in which the data for several units are presented as data for one unit. The consolidated budget of the family then represents the sum of their income and expenditures in a given month. The consolidated income of the family amounts to 10,000 kuna (5,000 + 5,000), and consolidated expenditures 9,500 kuna (4,000 + 5,500). The remaining 500 kuna are set aside as savings. For consolidation purposes, mutual transactions, i.e. money transfers between the husband and wife, are eliminated. Essentially, the consolidation means that, although the husband has paid 1,000 kuna to the wife for overhead costs, this amount is not considered to be the wife's extra income, because it represents a simple transfer within the family.

central government – the national budget users (e.g. ministries, state agencies) and extra-budgetary users (e.g. Croatian Waters and Croatian Roads).

Similarly, the consolidated central government budget, also called the consolidated national budget, is nothing but the sum of revenue and expenditure of the two budget components: the national budget and the financial plans of extra-budgetary users of the national budget. In the consolidation process, it is important that transactions between the national budget and the extra-budgetary users, if any, should be omitted.



Then why at all is the central government budget drawn up? Only to find out how much money has been jointly collected and spent by the national budget and the extra-budgetary users of the national budget. In order to arrive at the consolidated central government budget, we go through the following two phases:



- 1) consolidation within the extra-budgetary users of the national budget which implies the cancelling out of transfers among the extra-budgetary users (e.g. the funds paid by the Croatian Waters to the Environmental Protection Fund and vice versa); and
- 2) consolidation of transfers from the national budget to the extra-budgetary users of the national budget and vice versa.

Table 5: Consolidated central government budget (national budget and financial plans of extra-budgetary users) for 2009, in million kuna

	2009 plan
TOTAL REVENUE AND GRANTS	128,697
National budget	124,636
Extra-budgetary funds	4,061
Croatian Waters	1,983
Environmental Protection Fund	1,385
Croatian Roads	71
State Agency for Deposit Insurance and Bank Rehabilitation	507
Croatian Privatisation Fund	115
TOTAL EXPENDITURE	131,512
National budget	124,954
Extra-budgetary funds	6,558
Croatian Waters	2,418
Environmental Protection Fund	1,130
Croatian Roads	2,663
State Agency for Deposit Insurance and Bank Rehabilitation	236
Croatian Privatisation Fund	111
TOTAL DEFICIT/SURPLUS	-2,815
Percentage of GDP	-0.88
National budget	-318
Extra-budgetary funds	-2,497
Croatian Waters	-436
Environmental Protection Fund	-255
Croatian Roads	-2,592
State Agency for Deposit Insurance and Bank Rehabilitation	271
Croatian Privatisation Fund	4

Source: Ministry of Finance (2009c)

The consolidated central government revenue amounts to 128.7 billion kuna. When we put this against the consolidated expenditure of 131.5 billion kuna, we get the consolidated central budget deficit of 2.8 billion kuna.

Extra-budgetary users account for 2.5 billion kuna or almost 90% of this deficit, whereas the national budget participates with as little as 0.3 billion kuna. The total deficit of the consolidated central government budget has to be financed by borrowing.



The local units' budgets

Citizens have a constitutional right to local and regional self-government which includes the right to participate in deciding on local and regional needs and interests. Therefore the country is divided into cities and municipalities (the **units of local self-government**) and counties (the **units of regional self-government**). Some cities (e.g. Zagreb) also have city districts.

So far, we have got acquainted with the national budget and extra-budgetary users of the national budget. In the following part we will explain the third administrative level, the one keeping records of the collection and spending of the public money, i.e. local units which include municipalities, cities and counties.

units of local self-government – municipalities and cities.

units of regional self-government – counties.



Laws regulating the territorial organisation and budgetary issues of local units

Currently (2009), Croatia has 20 counties (and the City of Zagreb), 429 municipalities and 126 cities. The division of responsibilities, the territorial organisation and the matters related to the local unit budgets are regulated by numerous legislation, e.g. the Budget Act, the Act on the Financing of Units of Local and Regional Self-governments, the Local and Regional Self-government Act, the County, Municipality and City Areas Act, the City of Zagreb Act, the Act on the Areas of Special State Concern, the Hill and Mountain Areas Act, and the Islands Act. The budgets of all the counties, municipalities and cities from 2001 on can be found at the Ministry of Finance's website.

Each **local unit** has its own **local budget** or plan of revenue and expenditure. Concurrently, all the budgets of local units are managed at the national level as a single local units' budget. Therefore, instead of analysing the budget of each and every local unit, it is sufficient to know that the budget of a local unit shows the revenues pertaining to this unit and expenditures for carrying out the activities within its competence.

local units – municipalities and cities; the term sometimes also includes counties.

local budget – a document in which a local unit plans its revenue and estimates expenditure for a single year, and which is passed by the local unit's representative body.



How are the local budgets adopted?

Based on the guidelines from the Government, the Ministry of Finance compiles instructions for drawing up local budgets and submits them to the local units by end-June. In accordance with these instructions, the local units' financial administration bodies draw up guidelines and submit them to the budgetary and extra-budgetary users within their competence. The budgetary and extra-budgetary users make their financial



plan proposals and submit them to the financial administration body no later than 15 September. The administration body examines the proposals, reconciles the financial plans with revenue estimates, makes a draft budget for the following year and projections for the next two years, and submits them to the executive body (a head of municipality mayor/county prefect) no later than 15 October. The executive body approves the budget proposal and the projections and submits them to the representative body no later than 15 November. The representative body adopts the budget for the following year and projections for the next two years by the end of the current year and within the time limits enabling the implementation of the budget as of 1 January. The head of municipality mayor/county prefect submits the budget to the Ministry of Finance within fifteen days from its entering into force.

Who are the local budget users?

The local budget users are institutions established by a local unit, which are majority financed from the local budget, their budget revenue and expenditure being constituent parts of the local budget. They include, for example, primary and secondary schools and kindergartens. When we say, for example, that the budget of the city of Karlovac for 2008 amounts to 202 million kuna this means that it includes the revenues and expenditures of all users of the Karlovac city budget.

Besides the local budget users, there are also the extra-budgetary users of local budgets. These are legal persons in which the local units exert a decisive influence on the management, and which are financed in part from the budget and partly by the revenues from own operations. An important fact about the extra-budgetary users of local budgets is that they maintain their own budgets, also called the financial plans. Their revenues and expenditures are not constituent parts of local budgets, but are only included in the local units' consolidated budget. This means that the revenues and expenditures of the extra-budgetary users of, for example, the Karlovac city budget are not shown in the 2008 budget of the city of Karlovac amounting to 202 million kuna.

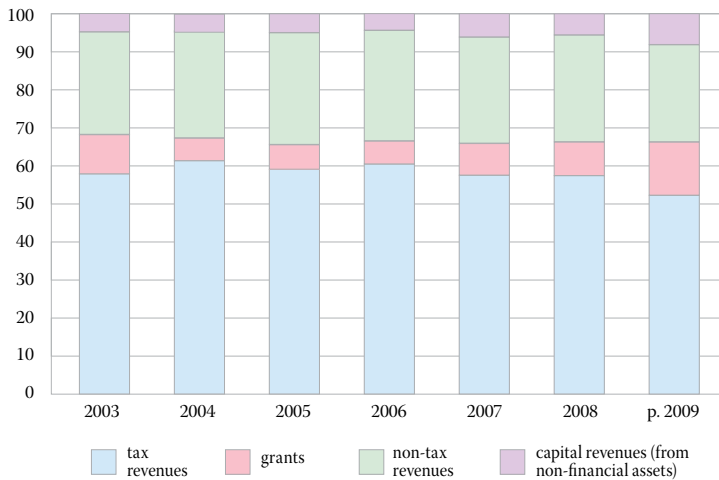
Detailed explanations and the lists of local budget users and the extra-budgetary users of local budgets are published annually, in May or June of the current year for the following year.



The local units' revenues

The local units' budget revenues are recorded in the same way as the national budget revenue, and are divided into tax revenues, non-tax revenues, **grants** and revenues from non-financial assets.

Graph 13: Structure of local units' revenues, 2003-09, in %



The structure of local units' revenues has recently undergone considerable changes. Taxes have constantly been the main item of the local units' budgets. However, while they accounted for an average of 60% of total revenue in the period 2003-06, their share dropped to 52% of the total, according to the 2009 plan. The second largest revenue item (about 27%) is the non-tax revenue, e.g. revenues from the sale of goods and services, from fines, etc., followed by grants, whose share has grown rapidly over recent years (from about 6% in 2006 to almost 14.5% planned for 2009), and capital revenues whose share has almost doubled, from 4.8% in 2006 to 8.8% of total revenue planned for 2009. Consequently, the last few years saw a decline in the share of tax revenues and a rise in the share of grants and capital revenues. Primary reason of this trend is a large number of economically underdeveloped local units.

What are the grants?

Despite being only the third largest revenue item in the local units' budgets, grants are relatively important. They constitute the funds received by one government unit from another government unit or from an international institution, which do not have to be repaid or compensated for. Grants are comparable to a situation where, for example, in a given month, your income cannot cover your expenditures, so that your par-

grants – non-returnable transfers of funds to international organisations, foreign governments, budgets, extra-budgetary users, banks, financial institutions and enterprises. Aid is often given by the national budget to local budgets, but they can also be given among local units of the same level, e.g. counties. They are divided into current grants (for current expenses) and capital grants (for the purchase of fixed assets), as well as into special-purpose and general-purpose grants.



ents give you 1,000 kuna as a gift which you are neither supposed to repay, nor do your parents expect anything in return. Most frequently, the higher-level units of government give grants to the lower-level units. For example, the central government gives a grant to a county, or a county gives a grant to a municipality. Grants can also be provided between local units of the same level, e.g. between two counties or two cities.

We distinguish between current and capital grants. Current grants must be used for current expenditure, and there are currently six types of current grants to counties, cities and municipalities: equalisation grants for **decentralised public services**, the Ministry of Finance's grants to municipalities and cities in the areas of special state concern (groups I and II), the Ministry of Finance's grants to counties, grants from other ministries and central government institutions, budgetary reserve and compensation for damage caused by natural disasters, and replacement of CIT revenue. Capital grants are intended for the procurement of fixed assets.²

decentralised public services – responsibilities for a part of public services (education, health care, social welfare and fire fighting), which the state delegates to a certain number of local units (counties, cities and municipalities), providing them, in return, with access to additional forms of financing.

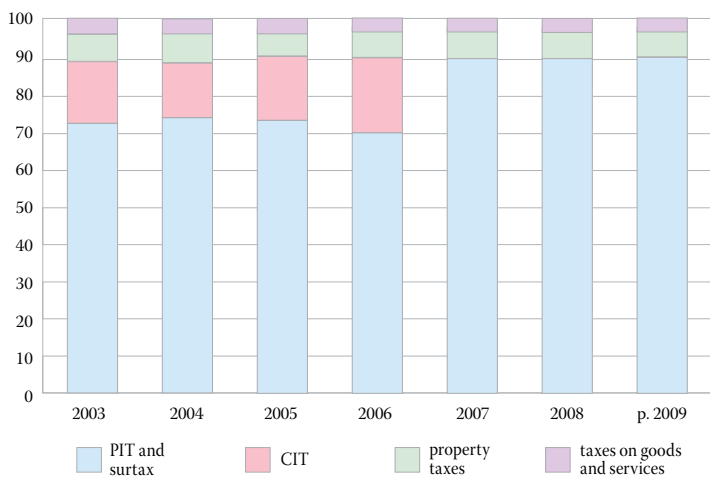
personal income tax – a direct tax levied on a natural person's income.

So then, the key sources of financing for local units are taxes, primarily the personal income tax and surtax on **personal income tax**.

What is the surtax on personal income tax?

The surtax on PIT is an extra tax that can be levied by municipalities and cities, and is payable on top of the PIT. The surtax base is the PIT itself, and the surtax rates are determined by local units independently. Municipalities and cities can introduce surtax on PIT at limited rates, i.e. the municipality surtax rate can be up to 10%; cities with less than 30,000 inhabitants can have a rate up to 12%; cities with more than 30,000 inhabitants up to 15% and the City of Zagreb up to 30%. The surtax PIT constitutes the revenue of the local unit in which a taxpayer has a domicile or habitual abode.

Graph 14: Structure of local units' tax revenues, 2003-09, in %



² For more details about grants, see Bronić and Bajo (2007) and Bronić (2008).



As shown by graph 14, PIT and surtax on PIT are the local units' most important tax revenues. For many years, these taxes accounted for about 70% of total tax revenue of local units, whereas CIT accounted for 16-20%, property taxes for about 7%, and taxes on goods and services for about 4% of the total. The situation changed abruptly in early 2007, when the Government stopped sharing the CIT revenue with local units, making them the exclusive revenue of the national budget. In return for the loss of CIT revenue, the state ceded a larger share in PIT to local units. Therefore, since 2007, the revenue from PIT and surtax on PIT have accounted for almost 90% of the local units' total revenue.

When talking about tax sharing, we should explain tax sharing and **shared taxes**. As already shown, taxes are the basic source of financing for local units and the sharing of common taxes between the central government and local units is legally defined. Shared taxation includes PIT and real property transfer tax and implies the division of these taxes among the central government, county, city and municipality. Table 6 shows how it actually looks like.

corporate income tax – a direct tax levied on the profits of legal and natural persons pursuing a business activity independently and on a permanent basis with a view to deriving profits.

shared taxation – division of taxes between the central government and local units (counties, cities and municipalities). By changing tax rates and percentages of divided taxes, e.g. income tax, the government influences the amount of tax revenue remaining with the local units.

Decentralised public services

Within the fiscal decentralisation process, the central government enabled local units, as of 2001, to assume responsibility for the financing of education, health care, social welfare and fire fighting. This represented the transfer of powers over a part of expenditures (material expenditures and expenditures for the acquisition of non-financial assets) to those local units which assumed responsibility for the financing of health care and education, and over the full expenditures, including salaries, to those local units which assumed responsibility for the financing of social welfare (the payment of benefits, and services such as nursing home and child protection services) and fire fighting. All the counties, 32 cities and the City of Zagreb agreed to assume part of public services, i.e. expenditures, for education, health care and social welfare, whereas 126 municipalities/cities took over the regular fire fighting activities. Those local units which took over the decentralised public services were allocated an additional share in PIT (further increased from 2007) for each public service.





areas of special state concern (ASSC) – the areas devastated by war (groups I and II) or areas lagging behind due to poor economic development, structural problems, demographic or other reasons (group III). All the three groups cover up to 15% of the total country population. The government provides them with special grants and cedes them the total amount of income tax collected; the difference between the ASSCs and hill and mountain areas (HMA) is sometimes not clear cut.

hill and mountain areas (HMA) – areas defined by a special law, in which the state stimulates demographic renewal, economic growth and sustainable development, and creates prerequisites for improved social circumstances and higher standards of living for citizens. Depending on the cause of their lagging behind other parts of the country, these areas are classified into two groups: Group I, with negative natural population growth, higher unemployment rate, etc.; and Group II, with unfavourable climate and other natural characteristics.

equalisation fund – a portion of the collected personal income tax from which central government gives transfers to local units which are unable to adequately finance their decentralised functions.

Table 6: Tax sharing, in %

Type of tax	Central government	County (basic share)	Municipality or city (basic share)	Fire brigades (decent. function)*	Other decent. functions**	Equalis. fund for decent. functions***	Share for joint capital project financing
PIT – standard sharing	–	15.5	55	1.3	10.7	17.5	–
PIT – Zagreb	–	–	70.5	1.3	10.7	17.5	–
PIT – ASSC, HMA	–	10	90	–	–	–	–
PIT – islands with special financial status	–	15	52	1.3	10.7	–	21
real property transfer tax	40		60				

* Goes to the municipality/city that has established and that finances the regular operations of public fire brigades; otherwise, it goes to the central government.

** Goes to the municipality/city/county that finances its decentralised public services; otherwise it goes to the central government.

*** Funds from the central government from which transfers are made to those local units which are unable to finance their own decentralised public services up to the minimum standard from an additional share in PIT.

Source: Based on the Act on the Financing of Units of Local and Regional Self-government

Let us now explain table 6:

- ◆ In the case of the *real property transfer tax*, the situation is very simple. Of each kuna collected as tax, 40 lipa belong to the central government and 60 lipa to a municipality or city.
- ◆ The distribution of the *PIT* is much more complex and depends on the area in which the municipality or city of a given taxpayer is. So, there are *four ways of PIT sharing*:
 - ordinary or standard;
 - that applied in the City of Zagreb;
 - that applied in the **areas of special state concern (ASSC)** and **hill and mountain areas (HMA)**; and
 - that applied on the islands having a special financial status.

Thus, in the *ordinary or standard tax sharing*, of 1 kuna collected as PIT, a county receives 15.5 lipa, and a municipality or city 55 lipa; 17.5 lipa go to the **equalisation fund** and 12 lipa (10.7+1.3) to the level of government which took over decentralised public services.

So then, of 1 kuna collected as PIT in its territory, the county receives 15.5 lipa for the performance of its basic public services, whereas a municipality or city receives 55 lipa. Where a local unit assumes an obligation to finance certain decentralised public services, the central government allocates an additional amount of 10.7 lipa to this unit in order to ensure that it has at least the minimum funds necessary to finance the activities taken over. In the case of assuming the obligation to finance fire brigades, it receives 1.3



lipa more. The more decentralised public services a local unit takes over, the larger its share in the PIT revenue.

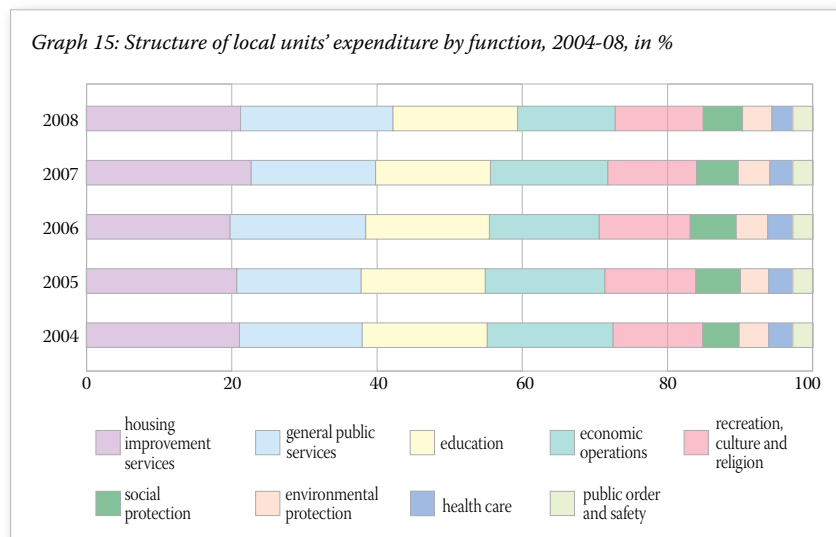
Local units which took over some or all of the decentralised public services, and which do not raise enough funds from the additional share in PIT to meet the minimum financial standard prescribed by the competent ministry, are allocated grants from the equalisation fund by the central government. This is the fund in which 17.5 lipa of each kuna collected as PIT is paid.

Table 6 explains the PIT sharing for each of the four special cases in which you may be particularly interested.³

The local units' expenditures

We will show the local unit's expenditures according to the **functional classification** on graph 15, indicating the purposes for which the local units' funds were used in the period 2004-08. The bulk of funds (20%) were spent on housing improvement services (e.g. water and gas supply), followed by expenditures for general services, i.e. the financing of executive and legislative bodies (19%), and expenditures for education (17%), economic operations (16%) and recreation, culture and religion (12%). These expenditures accounted for over 80% of total local spending, whereas the rest related to social protection, environmental protection, health care and public order and safety.

functional classification – a presentation of expenditure according to its purposes (e.g. defence, health care and education).



³ For more details about the PIT sharing, see Bronić (2007).

The consolidated general government budget

In contrast to the *central government budget* which comprises all the revenue and expenditure of the national budget and the budgets of extra-budgetary users of the national budget, the *general government budget* includes the central government budget plus the budgets of local units.

general government
– central government (budgetary and extra-budgetary users of the national budget) plus budgetary and extra-budgetary users of the county, city and municipality budgets consolidated general government budget.

This means that the **general government** comprises all institutions collecting revenues on behalf of the state and incurring expenditures, i.e. all institutions financed from the national budget, the extra-budgetary users and budgets of local units. *The consolidated general government budget* is obtained by putting together all the three levels of budget and eliminating all transfers among the national government budget, extra-budgetary users and local units. It is only the consolidated general government budget that gives us the exact information on the amounts of public funds collected and spent in the entire country.

We compared the consolidated central government budget to a family in which only the husband and the wife were employed. We can now compare the consolidated general government budget to a family in which the husband, the wife and the son are employed. The consolidated budget of such a family would be the sum of their income and expenditures, excluding money transfers between the husband and the wife, between the son and the mother and between the son and the father. For example, if the father gives 7,000 kuna to the son for buying a computer, this amount cannot be considered as the son's extra income, but simply as a transfer of funds between family members.

Figure 6: Consolidated general government budget

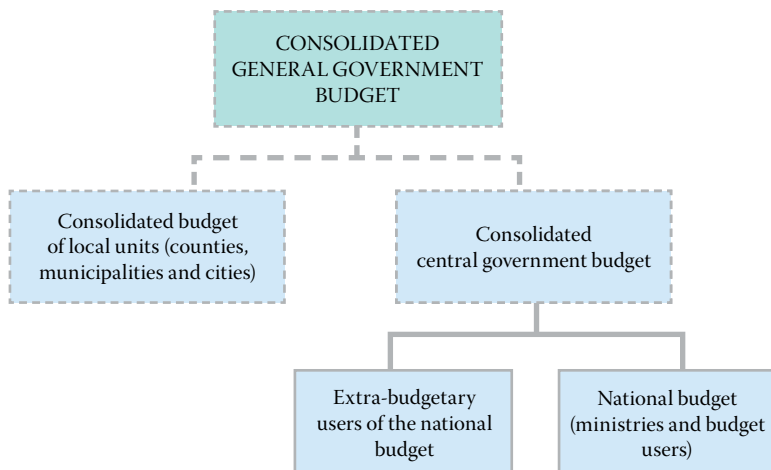




Table 7: Consolidated general government budget by level of authority, 2005-08, in million kuna

	2005	2006	2007	2008
TOTAL REVENUE PLUS GRANTS	103,966	113,561	128,020	136,270
National budget	85,928	95,587	108,796	116,070
Extra-budgetary funds	7,039	5,534	5,109	4,405
Croatian Pension Insurance Institute	41	310		
Croatian Health Insurance Institute	864	850		
Croatian Employment Service	19	19		
Croatian Waters	1,228	1,529	1,996	2,060
Environmental Protection Fund	215	660	1,103	1,221
Croatian Motorways	2,547	1,571	1,392	
Croatian Roads	1,478	66	121	82
State Agency for Deposit Insurance and Bank Rehabilitation	368	410	412	844
Croatian Privatisation Fund	279	120	85	199
Local budgets	10,998	12,441	14,116	15,795
TOTAL EXPENDITURE	110,435	118,072	131,090	139,135
National budget	87,069	92,434	103,980	114,591
Extra-budgetary funds	10,752	11,655	11,350	6,730
Croatian Pension Insurance Institute	405	612		
Croatian Health Insurance Institute	953	962		
Croatian Employment Service	151	163		
Croatian Waters	1,720	1,999	2,405	2,561
Environmental Protection Fund	125	709	1,068	1,068
Croatian Motorways	5,028	4,522	4,896	
Croatian Roads	1,989	2,579	2,841	2,732
State Agency for Deposit Insurance and Bank Rehabilitation	197	28	49	280
Croatian Privatisation Fund	184	81	92	90
Local budgets	12,614	13,983	15,760	17,814
TOTAL DEFICIT/SURPLUS	-6,470	-4,511	-3,069	-2,865
Percentage of GDP	-2.45	-1.58	-0.98	-0.84
National budget	-1,141	3,153	4,815	1,479
Extra-budgetary funds	-3,713	-6,121	-6,241	-2,324
Croatian Pension Insurance Institute	-363	-302		
Croatian Health Insurance Institute	-89	-112		
Croatian Employment Service	-132	-144		
Croatian Waters	-492	-470	-410	-501
Environmental Protection Fund	89	-49	35	153
Croatian Motorways	-2,481	-2,951	-3,503	
Croatian Roads	-511	-2,513	-2,720	-2,650
State Agency for Deposit Insurance and Bank Rehabilitation	170	382	363	564
Croatian Privatisation Fund	95	39	-6	109
Local budgets	-1,616	-1,543	-1,644	-2,019

Given the consolidated general government revenue of 136.2 billion kuna, and consolidated expenditure of 139.1 billion kuna in 2008, the consolidated general government deficit reached 2.9 billion kuna.

Total deficit of extra-budgetary users amounts to 2.3 billion kuna and the local budgets' deficit is 2 billion kuna. A part of these deficits are covered from the national budget surplus of 1.4 billion kuna, whereas the remaining deficit of the consolidated general government budget of 2.9 billion kuna must be financed by borrowing.

Sources: Ministry of Finance (2009b; 2009d: 31); CBS (2009a; 2009b: 79)

Notes:

Since 2007, the Croatian Pension Insurance Institute, Croatian Health Insurance Institute and Croatian Employment Service have been included in the scope of the national budget.

Since 2008, the Croatian Motorways have been excluded from the scope of the general government and classified as public enterprise.



Even though we already explained the essence of consolidation on the example of the central government, given its extreme complexity, we will also exemplify the consolidation of the general government budget. So, the consolidated general government budget is obtained in the following four phases:

- 1) consolidation within the extra-budgetary users of the national budget, i.e. the cancelling out (omission) of payments between individual users (e.g. funds paid by the Croatian Waters to the Environmental Protection Fund and vice versa);
- 2) consolidation of transfers from the national budget to the extra-budgetary users of the national budget and vice versa;
- 3) consolidation of payments between local units and their budgetary and extra-budgetary users, which leads us to the consolidated budget of local units or the local government budget; and
- 4) consolidation of payments between the central government budget and the budgets of local units, which leads us to the consolidated general government budget.



What is the structure of the general government budget?

As already said, the general government budget consists of the national budget, the budgets of extra-budgetary funds and local budgets. In the structure of revenue and expenditure, the largest share is that of the national budget, which accounts for about 85% of revenue and about 82% of expenditure. This structure also shows marked growth of both the national budget revenue and expenditure over the reference period. As some of the extra-budgetary users moved to the national budget over time, the structure of the general government budget shows a decline in the revenue of extra-budgetary users, from 6.8% at the beginning, to about 3.2% at the end of the period, and a fall in expenditure from 9.7% to 4.8% of the total general government budget expenditure. The share of local budgets rose slightly, standing at an average of about 11% and 12% of expenditure respectively.

Graph 16: Structure of general government revenue, 2004-08, in %



Source: Ministry of Finance (2009b, 2009d: 31)

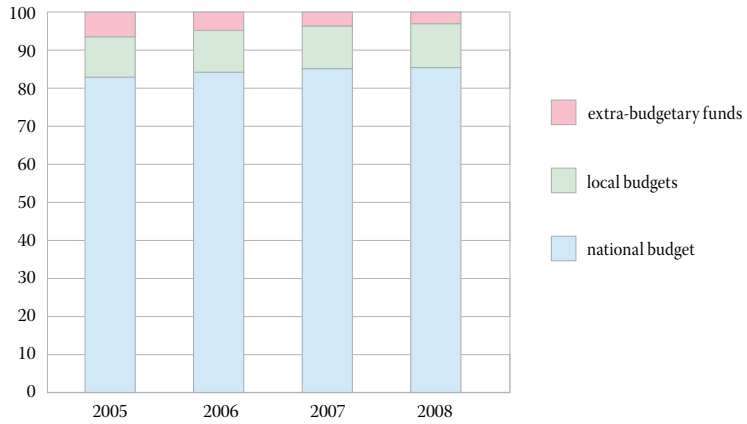
Notes:

Since 2007, the Croatian Pension Insurance Institute, Croatian Health Insurance Institute and Croatian Employment Service have been included in the scope of the national budget.

Since 2008, the Croatian Motorways have been excluded from the scope of the general government and classified as public enterprise.



Graph 17: Structure of general government expenditure, 2004-08, in %



Source: Ministry of Finance (2009b, 2009d: 31)

Notes:

Since 2007, the Croatian Pension Insurance Institute, Croatian Health Insurance Institute and Croatian Employment Service have been included in the scope of the national budget.

Since 2008, the Croatian Motorways have been excluded from the scope of the general government and classified as public enterprise.



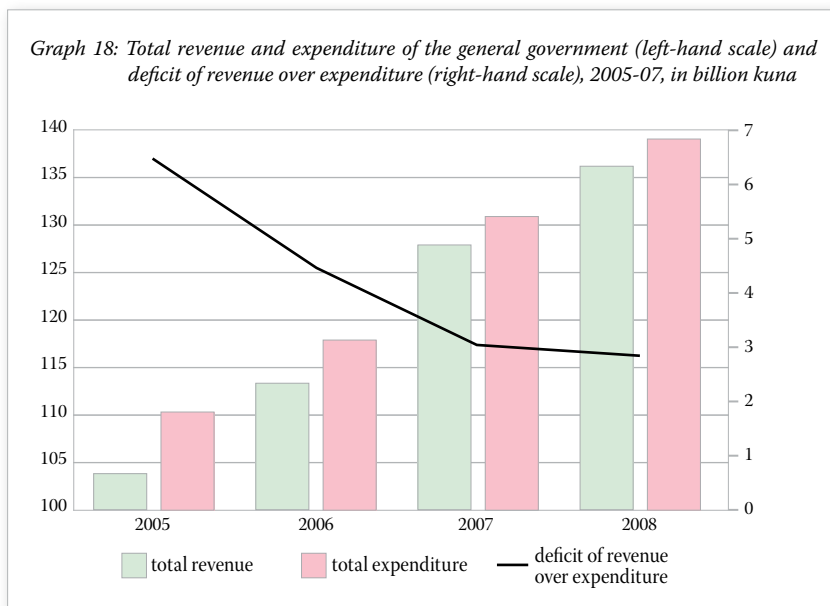
Deficit of the consolidated general government budget

As shown by table 7 and graph 18, the revenue and expenditure of the consolidated general government budget grew in the period 2005-08, and the budget ran a deficit in each year. However, the **deficit** declined continuously, from 6.5 billion kuna in 2005 to 2.9 billion kuna in 2008. While the national budget showed a **surplus** in most of the reference years, from year to year the deficit was mostly due to the deficits of extra-budgetary funds. They ran a deficit even after some of them, e.g. Pension Insurance Institute, Health Insurance Institute and Employment Service, moved to the national budget and Croatian Motorways became public enterprise. Local budgets also showed deficits in all the observed years, their deficits increasing constantly, from 1.6 billion kuna in 2005 to 2 billion kuna in 2008.

deficit – excess of expenditure over revenue in a given period.

surplus – excess of revenue over expenditure in a given period.

Graph 18: Total revenue and expenditure of the general government (left-hand scale) and deficit of revenue over expenditure (right-hand scale), 2005-07, in billion kuna



It is obvious that the public sector needs to be reformed, as concerns its parts covered by both former and current extra-budgetary funds (e.g. pensions, health care, road management, etc.) and that the unsustainably large number of local units needs to be reduced. This particularly relates to municipalities whose independent financial operation is seriously hampered.

And how does the Government finance this deficit? Mainly through **borrowing**. All the debts arising from financing the general government deficits constitute the general government debt or *public debt*.

borrowing – taking credit and taking out loans or issuing securities.



Public debt

The public debt represents the accumulated budget deficits financed by the Government through borrowing. These are simply the funds that the Government has borrowed but not yet repaid, and that are claimed by creditors at a given time.

national debt – accumulated central government deficits financed by borrowing.

government guarantee – an instrument by which the government guarantees the settlement of liabilities for which the guarantee is issued.

Confusion may sometimes arise from the fact that the term public debt is often used along with the term **national debt**. *Public debt* should relate to the financing of the public sector deficit or, in our case, the general government deficit, whereas *national debt* should relate to the financing of the central government deficit. However, we should also differentiate between *public debt* as a sum of debts of the national budget, extra-budgetary users and local units including **government guarantees** given, and the *national debt* as a sum of debts of the national budget, extra-budgetary users and local units, but excluding government guarantees given. Therefore, the explanations and definitions in each text and each table relating to public or national debt must be read very carefully.

Depending on whether the state owes money to domestic or foreign creditors, we can distinguish between *domestic or internal debt* and *foreign or external debt*.

There is also *the potential public debt* comprising the Government guarantees given and the debt of the Croatian Bank for Reconstruction and Development.

The Croatian Bank for Reconstruction and Development (HBOR)


The HBOR, established and owned by the state, is responsible for the financing of the reconstruction and development of the economy and infrastructure, promoting exports, providing support to small and medium-sized enterprises and environmental protection, as well as insuring the goods and services exports against non-market risks. The bank's capital is provided from the budget and the bank extends credit to its clients, directly or via commercial banks (e.g. for the financing of export, agriculture and tourism), issues guarantees and provides support in EU funds utilisation.

The Budget Execution Act lays down the ceilings for borrowing and the total amount of guarantees for each year. A decision to this effect is taken by the Parliament at the proposal of the Government. The Ministry of Finance maintains a list of debts and guarantees issued. Decisions on debt and guarantees are published in the Official Gazette.

What are the main problems facing the state as a result of a huge public debt?

- 1) Because of repayments of the public debt principal and interest, the country has less money for the financing of public needs (e.g. the construction of roads, hospitals or kindergartens).



- 
- 2) The public debt repayment requires higher taxes which pose a burden not only on the present but also future generations of taxpayers.
 - 3) As a result of government borrowing, the amount of domestic money that could be lent to the private sector is limited. This is particularly important in the case of restricted access to foreign borrowing.
 - 4) Excessive public debt may boost inflation, raise interest rates on household and corporate loans and thus destabilise the economy and reduce the growth capacity of **gross domestic product**.

gross domestic product (GDP) – an indicator of the total value of goods and services produced in a country within a year.

General government debt

Table 8 and graph 19 show the general government debt in the period 2002-08. First we must note that the monitoring of public finance is subject to frequent changes. As already mentioned, the status of extra-budgetary users changes very often, and international institutions and organisations, such as the International Monetary Fund and European Union, change their statistical monitoring methodologies, so that Croatian statistical monitoring systems have to be adjusted. For all this, one should be very careful about the figures we are offered and closely read explanations.

Briefly, in the period 2002-08, the domestic debt of the general government more than doubled (from 32.2 to 68.8 billion kuna), whereas the external debt of the general government dropped (from 40.2 to 30.5 billion kuna). The Croatian public debt, both domestic and foreign, thus went up from 72.5 to 99.3 billion kuna. The central government debt accounts for over 90% of this debt, and the remainder relates to extra-budgetary users and local units. Unfortunately, potential debt also went up by more than twofold (from 19.9 to 44.1 billion kuna). Over three-thirds of this amount relate to domestic and foreign guarantees of the Republic of Croatia (mostly foreign ones), and the rest represents the debt of the Croatian Bank for Reconstruction and Development.

Taken together, total public and potential debts rose, in absolute terms, from 92.4 billion kuna in 2002 to 143.5 billion kuna in 2008. If these total public and potential debts are divided by population number, each living man, woman and new-born child owe 33.000 kuna. If we exclude the potential debt, the situation is “more favourable”, i.e. each of us owes 24.000 kuna.

However, thanks to GDP corrections necessary for the adjustment of the statistics to EU requirements, GDP is now higher than before, so that the share of debt in GDP decreases. Consequently, in 2008, public debt stood at 29% of GDP and public and potential debts totalled 42% of GDP.



Graph 19: Domestic, foreign and potential debt (in billion kuna, left-hand scale) and public debt (in % of GDP, right-hand scale), 2002-08

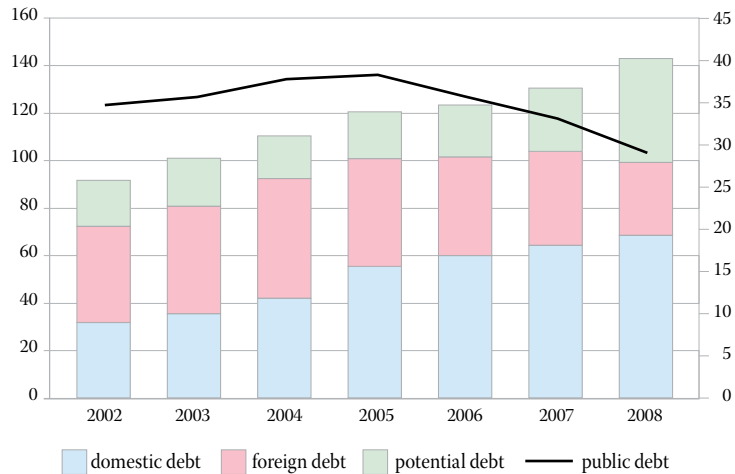


Table 8: General government debt, 2002-08, in billion kuna, end-of-period

GENERAL GOVERNMENT DEBT, in billion kuna	2002	2003	2004	2005	2006	2007	2008
1) General government internal debt	32.21	35.55	42.55	55.82	60.55	64.41	68.83
Central government internal debt	23.32	28.16	37.22	50.56	54.22	56.51	63.96
Internal debt of extra-budgetary funds	7.66	6.25	3.91	3.94	5.17	6.33	3.00
Local government internal debt	1.23	1.14	1.42	1.33	1.16	1.57	1.86
2) General government external debt	40.24	45.68	50.24	45.36	41.66	39.66	30.50
Central government external debt	37.43	41.04	42.23	36.41	32.56	29.42	28.65
External debt of extra-budgetary funds	2.59	4.29	7.75	8.75	8.94	10.19	1.83
Local government external debt	0.22	0.35	0.26	0.20	0.17	0.05	0.03
3) Public debt (1+2)	72.45	81.22	92.80	101.19	102.21	104.07	99.33
Total central government debt	60.75	69.20	79.45	86.97	86.77	85.93	92.61
Total debt of extra-budgetary funds	10.24	10.53	11.66	12.68	14.11	16.52	4.83
Local government total debt	1.46	1.49	1.68	1.53	1.33	1.62	1.89
4) RC guarantees issued	16.08	15.42	12.26	12.46	14.19	17.40	33.31
Domestic	7.42	6.80	4.55	5.27	7.25	7.87	12.39
Foreign	8.66	8.62	7.71	7.19	6.94	9.53	20.92
5) Total debt of the HBOR	3.82	4.93	5.84	7.14	7.69	9.66	10.81
Domestic debt	0.44	0.33	0.38	0.53	0.35	0.19	0.84
Foreign debt	3.38	4.60	5.46	6.61	7.34	9.47	9.97
6) Total potential debt (4+5)	19.90	20.34	18.10	19.59	21.87	27.06	44.12
7) Public and potential debt, total (3+6)	92.35	101.56	110.90	120.78	124.08	131.13	143.45
DEBT INDICATORS (% of GDP)							
Public debt	34.80	35.78	37.79	38.27	35.70	33.12	29.03
Public and potential debt, total	44.36	44.74	45.16	45.69	43.33	41.73	41.93
Internal debt	15.47	15.66	17.33	21.12	21.15	20.50	20.12
External debt	19.33	20.12	20.46	17.16	14.55	12.62	8.92
Potential debt	9.56	8.96	7.37	7.41	7.64	8.61	12.89

Source: Ministry of Finance (2009e)



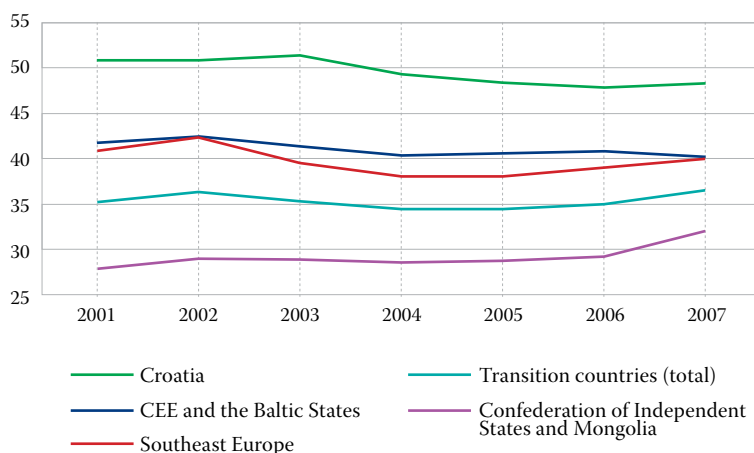
How big is our state?

The size of the state in terms of public finance is the share of **general government** expenditure in GDP.

A state that is too large, i.e. too large a share of government spending in GDP, can be an indicator of a significant welfare role of the state (as is the case, for example, in Scandinavian countries), but also of uneconomical spending of public resources. As we can see from graph 20, our state is really big. For a number of years now, general government expenditure has accounted for over 48% of Croatian GDP, which is much above the average for all transition countries (35%) and the averages for other groups of transition countries ranging from below 30% (Confederation of Independent States and Mongolia) to around 40% (Central and Eastern Europe, the Baltic States and Southeast Europe).

general government
– central government (budgetary and extra-budgetary users of the national budget) plus budgetary and extra-budgetary users of the county, city and municipality budgets consolidated general government budget.

Graph 20: General government spending, 2001-07, as a % of GDP



Source: EBRD (2008)

The share of the Croatian general government's expenditure in GDP is about 48%, meaning that about a half of our GDP is spent on the state and expenditures financed by the state. This suggests that we must keep an attentive eye on how all those funds are spent, and reduce the irrational spending of taxpayers' money. In other words, these funds have to be redistributed in the way to ensure the financing of national priorities that will contribute to long-



social benefits – the benefits based on insurance rights (pensions, unemployment benefits, as well as sickness and maternity benefits), or provided in the form of assistance to the poor in difficult situations which are not covered by the basic social insurance (e.g. various allowances to families and disabled persons, transportation cost aid and public kitchens).

term economic growth. Indeed, almost 70% of public resources are spent on the salaries of civil servants and various **social benefits** (pensions, health care and social welfare). The benefits on account of population aging will inevitably continue to grow, hampering the efforts to curb public spending. However, it is encouraging that other transition countries, showing similar demographic trends as observed in Croatia, succeeded in significantly restructuring their public spending.

Decisions about the allocation of budgetary resources, reduction of certain expenditures, etc. are adopted within the budgetary process in which all taxpayers should have an important role. This is another reason to become even better acquainted with all budgetary activities. Therefore, it is worth getting to know the budgetary process and its key participants.



THE BUDGETARY PROCESS

The budgetary process includes the preparation, proposal, acceptance, execution and control of the **budget**. It is determined and influenced by a number of formal and informal rules. The **budgetary process** is very important because, during its various phases, decisions are made on the manner of collecting and spending public money. But before getting acquainted with the budgetary process and its phases, let us learn something about the main participants in this process and their roles.

budget – a plan of revenue and expenditure for a given period of time.

budgetary process – a process consisting of the planning, preparation, adoption, execution, supervision and audit of the budget.

Who are the main participants in the budgetary process?

Among numerous participants in the various phases of the budgetary process, the most important are: the Government, Parliament, Ministry of Finance and other budget users, and citizens. We will say a little more about each of them.

Parliament

To put it very briefly, the Parliament (Sabor) represents the citizens, adopts laws and keeps oversight of the Government. The current, sixth assembly of Parliament has a hundred and fifty-three members who are in session twice a year: from 15 January to 15 July and from 15 September to 15 December. Special sessions are convened as necessary. The Parliament has 29 committees, the most important of them for the budgetary process being the Legislation Committee and the Finance and Central Budget Committee.

The Finance and Central Budget Committee establishes and monitors the system to finance public needs, financial and credit relations with foreign countries, the foreign exchange, tax and customs systems, the banking, currency and monetary systems, the state treasury, the Croatian National Bank, the insurance system for property and persons and other issues relating to the budget and finances, as well as and the structure, authority and operating methods of the State Audit Office and the Financial Agency (FINA). The Committee also examines, discusses and adopts the national budget, annual financial statements of the national budget and the reports of the State Audit Office on completed audits. The Committee has its chairperson coming from the ruling party and the vice-chairperson from the opposition parties, as well as eleven mem-





bers who are MPs. Participating in the Committee's activities are also the so-called appointed members who are the representatives of trade unions, associations, chambers and academic community, and professional organisations.

The Legislation Committee considers all legislative issues and documents enacted by Parliament, oversees the unity of the legal system and provides opinions on matters of principle pertaining to the development of the legal system or the uniform application of laws, establishes and issues consolidated texts of laws and other regulations enacted by Parliament when authorised to do so by said legislation, or when such regulations have been amended at least three times, and considers proposals for providing authoritative interpretations of laws and other regulations enacted by Parliament. Besides a chairperson and a vice-chairperson, the Committee includes eleven MPs and the so-called appointed members, i.e. the representatives of trade unions, associations, chambers, academic community and professional organisations, as well as prominent legal experts.

In its budgetary debates, the Parliament analyses the programmes and fiscal policies proposed by the Government, but it should also protect the interests of citizens. The budget is formally considered as adopted only after the Parliament has approved the revenue and expenditure proposed by the Government. Therefore, it is justified to say that it is in Parliament that some of the most important activities of the budgetary process are carried out.

The Government

The Government is the executive authority, carrying out the policy determined by Parliament. The Government proposes fiscal policy, formulates the national budget strategies within the context of defined economic, social and political objectives, prepares all the measures necessary for revenue collection, makes proposals for earmarking budgetary resources for planned purposes and priorities, and sets guidelines for and supervises the work of government administration. In other words, the Government is responsible for the entire economic and social development of the country.

The budget is a fiscal policy instrument reflecting the strategic goals of the Government. So, for example, in the budget for the period ending in 2011, the Government plans to support economic growth at high and sustainable long-term rates, to create new jobs and reduce unemployment, cut the overall general government deficit and public debt, which would result in a balanced budget and stable public debt. The goal is to additionally improve living standards, promote public welfare and enhance competitiveness of the economy. However, plans do not always come to fruition, because they depend on economic and political circumstances both in the country and abroad.



The central role in the Government is played by the ruling party (or the ruling coalition of parties), where the members of the Government usually come from. The work of the Government is constantly under a watchful eye of the broadest public and is the subject of its interest. It is also exposed to constant pressures from various interest groups. In the parliamentary elections, voters evaluate how successfully the Government has done its job. A negative rating of the Government's performance also means a negative rating of its members, as well as of the political party to which they belong.

As a rule, the Government is confirmed by Parliament to which it is accountable for its work and decisions. At the Parliament's request, the Government is obliged to submit a report on its work and the policies it implements.

The Ministry of Finance

The Ministry of Finance is the executive body of the Government and a beneficiary of the national budget. It is responsible for the Government's fiscal policy implementation and the accomplishment of the defined budgetary goals. In the first phase of the budgetary process, the Ministry of Finance makes analyses and forecasts of macroeconomic developments which provide a basis for fiscal policy and budget formulation; draws up the Government's **programme** strategy as a framework for developing **economic and fiscal policy guidelines** and drawing up a budget by programme. It also issues and delivers to budget users instructions for drafting a national budget proposal, draws up and checks the budget, devises the revenue collection methods, monitors the execution of expenditure and provides, on behalf of the Government, all services relating to the collection and spending of budgetary resources. Briefly said, the Ministry of Finance creates a basis for the financing of all public needs of both budgetary and extra-budgetary users, as well as of local and regional units.

programme – a set of independent and closely connected activities and projects aimed at achieving a common goal.

economic and fiscal policy guidelines – a document in which the government annually adopts the course of its fiscal policy for the following three-year period; it defines macroeconomic and fiscal assumptions for budget preparation.

Budget users

The users of the national budget are government bodies (the ministries and state agencies), institutions, minority self-government councils, **budgetary funds** and **territorial self-government** units whose expenses for employees and/or material expenses are financed from the national budget. Consequently, this also includes: Parliament, the President of the Republic, the Government and the Ministry of Finance. The budget users must use budgetary resources for the purposes and objectives for which they have been founded (for example, the Ministry of Science, Education and Sports – for education and university education programmes, for the development of science and promotion of scientific and research activities, as well as sports). The checking, supervision and audit of the use of budgetary resources allo-

budgetary fund – a kind of a budget user financed from earmarked revenues or from the budget.

territorial self-government – municipal office branches, city areas and city districts which can be established within the units of local self-government.

State Audit Office – an independent and autonomous institution accountable to Parliament, which is responsible for the audit of all the budgets, extra-budgetary users, state and public enterprises, ownership transformation and privatisation, and the audit of enterprises fully or partly financed from the budget.

cated to individual budget users is carried out by the Ministry of Finance and the **State Audit Office** (external audit), but also by each budget user for itself (internal supervision).

Citizens

Citizens elect their representatives who decide on their behalf about all matters of national importance, including the national budget. Large amounts of money flow into the budget, but are spent as well. The way of collecting and, particularly, spending this money is not just the concern of our representatives in the Government, Parliament, the Ministry of Finance and other ministries. The budget is too important to be left to individual politicians and various interest groups and lobbies. Citizens and various governmental and non-governmental institutions and organisations should be actively involved in the budgetary process.



What can every citizen do?

Members of parliament and other agents wanting to move a law or amendments to a particular law can refer to petitions and proposals from citizens, which they are entitled to submit pursuant to the Constitution (Article 130 of the Standing Orders of the Croatian Parliament). Each citizen has the right to file petitions and complaints, or make proposals to the national and other public authorities, and to receive replies from them. Where a citizen's petition or proposal is submitted to Parliament, the Speaker of Parliament will forward it to the chairperson of the relevant working body which is bound, no later than within three months, to make a report on the outcome of the petition or proposal (Article 46 of the Constitution).

The representatives elected by citizens can set priorities for the financing of public needs and projects that do not necessarily reflect the citizens' desires. However, through the media, through scientific institutions, non-government organisations and interest groups, the public can and even ought to be involved in the debate about the budget adoption and budgetary resources allocation. Interest groups like trade unions or employers do try, and very often manage, to push through their own interests. Apart from them, the budget can be influenced by citizens' associations, various chambers (the chambers of industry or commerce, bar associations, and medical chambers), churches and religious communities, as well as individuals. The influence of particular agents depends on their power and level of organisation. Once you get to know the budgetary process, you can also try to contribute to the more efficient management of the taxpayers' money flowing into the budget.



Main phases of the budgetary process

A budget is the outcome of the budgetary process which represents a whole lot of relationships among the main participants providing a basis for parliamentary debates on the budget and its adoption. It is therefore necessary to understand the entire procedures for the preparation, adoption, execution and control of the budget, so that we ourselves can have some influence on budgetary resources allocation.

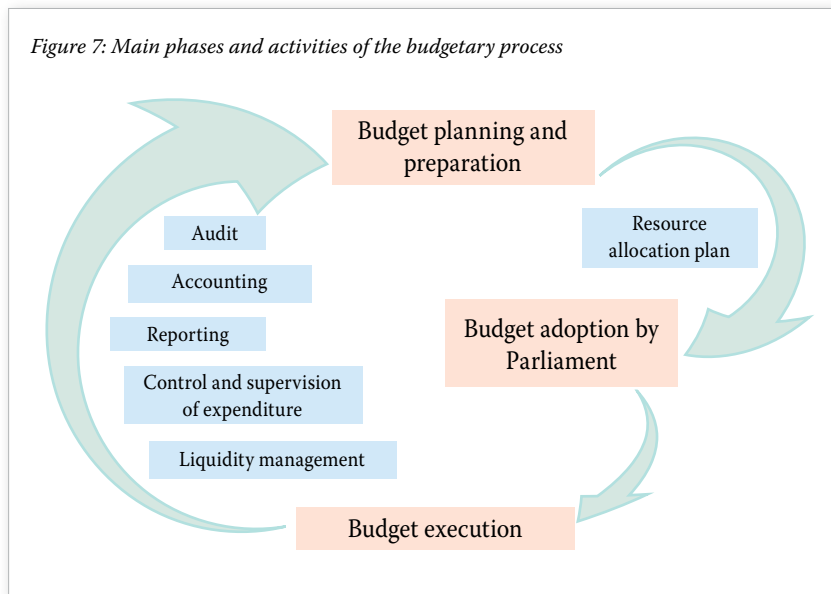


Figure 7 provides a simple presentation of the budgetary process, omitting numerous activities and relationships among all the participants in the process. Let us now look at the phases of the budgetary process.

- 1) *The preparation of a budget proposal*, which includes the drafting and adoption of a Government's programme strategy, the economic and fiscal policy guidelines for the following years and instructions for drafting a national budget proposal and of **financial plans** of budgetary and extra-budgetary users. Then follows the planning of revenue and expenditure and explanation of the proposed financial plans of budgetary and extra-budgetary users. The first phase lasts for about eight months, from March to November.
- 2) *Proposal, debate on and approval of the budget*, which takes place in Parliament during November and December, and lasts for one and a half months, except where a decision on the temporary financing is taken, as was the case in 2008.

financial plan – a document drafted by a budgetary or extra-budgetary user showing its revenue and expenditure.



3) *Execution of the budget* which includes the collection of planned revenue and its spending on planned purposes. This phase lasts exactly one year, from 1 January to 31 December.

Upon expiry of a budget year, the annual account of the budget is drawn up. That means that the Ministry of Finance collects reports from all budget users and draws up a draft proposal for a consolidated national budget account and submits it to the Government. The Government approves the annual budget execution report no later than 1 June and submits it to Parliament. The budgetary process officially ends after adopting the annual account of the budget by Parliament. So, for example, the budgetary process for 2007 ended formally with the adoption of the annual account of the 2007 budget by Parliament on 26 September 2008. However, during all the phases of the budgetary process internal and external supervision of the budget is carried out, together with the audit of the spending of budget resources. Moreover, the State Audit Office carries out annual controls and submits reports to Parliament and the public on irregularities and abuses.

So then, the lifetime of the budget is up to two and a half years. For example, the lifetime of the 2009 budget is from April 2008 to end-September 2010.



In what way does the budget plan differ from budget execution?

The budget plan is the amount of revenue and expenditure that the Government intends to collect and spend in the next year, and the execution is the realisation of the planned amounts of resources. In reality, there will be differences between the plan and the execution, because, for a number of economic, political and social reasons, it is impossible to foresee exactly the revenue and expenditure. In order to account for the difference between the plan and execution, at the end of the year, the Government submits to Parliament a Report on the Execution of the Budget for the past year, with an explanation of major departures.

Now, let us see how the budgetary process looks like from the beginning to the end of the lifetime of a budget.

Table 9: Phases and duration of a budget

Deadline	Action
PHASE 1	THE PREPARATION OF A NATIONAL BUDGET PROPOSAL
Step 1	The Government's programme strategy for a three-year period
by mid-March 2010	The Ministry of Finance, in co-operation with the Central Office for Development Strategy, draws up instructions for drafting strategic plans for a three-year period and submits them to the ministries and other government bodies.
by mid-April 2010	Based on the instructions, the ministries and other government bodies prepare strategic plans for a three-year period and submit them to the Ministry of Finance.
by end-April 2010	Based on the strategic plans, the Ministry of Finance and the Central Office for Development Strategy formulate a strategy for a three-year period and propose it to the Government.
by mid-May 2010	The Government adopts a three-year strategy.



Deadline	Action
Step 2	Economic and fiscal policy guidelines for a three-year period
by end-May 2010	Based on the strategy, the Ministry of Finance draws up economic and fiscal policy guidelines and proposes them to the Government.
by mid-June 2010	The Government adopts the guidelines.
Step 3	Instructions for drafting a national budget proposal
by end-June 2010	Based on the guidelines, the Ministry of Finance delivers instructions for drafting a national budget proposal to the ministries and other government bodies at the sectional level (organisational classification).
Step 4	Drafting proposals for the financial plans of budgetary and extra-budgetary users
by 15 July 2010	Based on the instructions, budgetary and extra-budgetary users draft proposals for their financial plans and submit them to the ministries and other government bodies at the sectional level (organisational classification).
by end-July 2010	The relevant ministries and other government bodies submit the adjusted financial plan proposals of budgetary and extra-budgetary users to the Ministry of Finance.
Step 5	The Ministry of Finance prepares a draft national budget and submits it to the Government
by 15 October 2010	The Ministry of Finance considers the proposals and adjusts the financial plans to its revenue estimates. It also prepares a budget for the next year and projections for the following two years, and submits them to the Government.
by 15 November 2010	The Government approves the budget proposal for the next year and projections for the following two years, and submits them to Parliament together with the financial plans of extra-budgetary users.
PHASE 2	THE BUDGET ADOPTION PROCEDURE
Step 6	Debate on the budget proposal and its adoption in Parliament
by end-2010	Parliament adopts the next year's budget at the level of subgroups (economic classification) and projections for the next two year, and gives its approval to the financial plans of extra-budgetary users, all within the time limits enabling the implementation of these documents as of 1 January 2011.
PHASE 3	THE EXECUTION OF THE NATIONAL BUDGET
Step 7	The execution of the national budget
by 15 January 2011	Based on the amounts planned in the national budget, budgetary users draft their monthly financial plans for the entire year which are subject to approval by the Ministry of Finance.
1 January - 31 Dec. 2011	The budget is executed in accordance with the available resources and due liabilities.
Step 8	Reporting on the semi-annual execution of the national budget and financial plans of extra-budgetary users
by 30 July 2011	Extra-budgetary users draft semi-annual reports on the execution of their financial plans for the past period and submit them to the Ministry of Finance together with explanations.
by 5 September 2011	The Ministry of Finance submits a report to the Government on the semi-annual execution of the national budget and of the financial plans of extra-budgetary users.
by 15 September 2011	The Government submits the report on the semi-annual execution of the national budget and financial plans of extra-budgetary users to Parliament.
Step 9	Reporting on the annual execution of the national budget and financial plans of extra-budgetary users
by 31 March 2012	Extra-budgetary users draft annual reports on the execution of their financial plans for the past period and submit them to the Ministry of Finance together with explanations.
by 1 May 2012	The Ministry of Finance drafts an annual report on the execution of the budgets and financial plans of extra-budgetary users and submits it to the Government.
by 1 June 2012	The Government submits to Parliament the annual report on the execution of the budgets and financial plans of extra-budgetary users for 2011.
Step 10	Budget supervision and internal audit



budget revision – a change in budgetary amounts, i.e. their reduction and/or increase relative to the budget plan adopted at the beginning of the calendar year. It occurs during the budget year, when budget revenue estimates are unrealistic, or where unexpected expenditures arise. Budget revisions can be due to unforeseen circumstances in the domestic or world economy, but they can also be the consequence of the government's inability to make realistic revenue and expenditure plans.

Given a number of recent changes that impacted on the budgetary process (e.g. amendments to the budget act, several **revisions** of the 2009 budget, temporary financing in 2008), table 9 shows the phases and their duration on the example of a 2011 budget. We hope that everything will be as anticipated, because the new budget act fully satisfies the EU requirements and should be applied by all the participants in the budgetary process.

To sum up, the entire budgetary process comprises three phases and ten steps which will be explained further in the text.

I. Phase 1: Preparation of the budget proposal

Phase 1 of the budgetary process includes five steps. First, the Government formulates its strategy based on which the Ministry of Finance draws up economic and fiscal policy guidelines for a three-year period which are subject to approval by the Government. After that, based on these guidelines, the Ministry of Finance compiles instructions for the preparation of financial plans and submits them to budgetary and extra-budgetary users. They use these guidelines for drawing up their financial plans, on the basis of which the Ministry of Finance prepares a detailed proposal for a national budget and a consolidated plan of the **central government** budget.

1. Step 1: The Government's programme strategy for a three-year period

central government – the national budget users (e.g. ministries, state agencies) and extra-budgetary users (e.g. Croatian Waters and Croatian Roads).

The Ministry of Finance and the Central Office for Development Strategy compile instructions for drafting strategic plans for a three-year period and submit them to the ministries and other government bodies. The ministries and other bodies draw up their strategic plans and submit them to the Ministry of Finance and the Central Office for Development Strategy which jointly formulate a strategy for a three-year period. The Government is obliged to adopt such strategy by mid-May.

2. Step 2: Economic and fiscal policy guidelines

Based on the strategy, the Ministry of Finance draws up economic and fiscal policy guidelines which are subject to approval by the Government by mid-June. These guidelines help budgetary and extra-budgetary users prepare their own financial plans and budgets. In this way, the strategy and the guidelines provide a basis for all the remaining steps in the budgetary process.



The guidelines comprise the following:

- ◆ strategic goals of economic and fiscal policies;
- ◆ basic macroeconomic and fiscal indicators;
- ◆ revenue and expenditure estimates for all the levels of general government;
- ◆ a proposal for the financial plan amounts by section (organisational classification) which includes the amount of the financial plans for the previous and current budget years, and the proposed amount of the financial plan for the next budget year, as well as for the following two years; and
- ◆ anticipated changes in public debt and the public debt management strategy.



Step 3: Instructions for drafting a budget proposal

3.

Based on the adopted guidelines, the Ministry of Finance compiles instructions for drafting a national budget proposal and submits them to all budgetary and extra-budgetary users by end-June. The purpose of the instructions is to inform the users on the basic economic and fiscal indicators, as well as on the methods and time limits for the national budget preparation. The users are encouraged to independently formulate and explain their financial plans and applications for the necessary budget resources, taking account of the available revenue and time restrictions.

Step 4: Drafting proposals for the financial plans of budgetary and extra-budgetary users

4.

Based on the instructions, the budgetary and extra-budgetary users draft proposals for their financial plans and submit them by mid-July. After having adjusted and adopted the financial plans of their budgetary users, the relevant ministries and other government bodies at the sectional level of the **organisational classification** are obliged to submit them to the Ministry of Finance by end-July.

A financial plan proposal includes the following:

- ◆ revenue by type;
- ◆ expenditure estimates for a three-year period classified according to the budgetary classifications; and
- ◆ explanation of the financial plan proposal.



organisational classification – the presentation of expenditure according to organisational units, i.e. ministries, state offices, funds, institutes, agencies and other budget users (formerly known as administrative classification).



Extra-budgetary users also prepare their financial plan proposals and submit them to the relevant ministries for examination and submission to the Ministry of Finance.

5.

Step 5: The Ministry of Finance prepares a draft budget and submits it to the Government

extra-budgetary users – extra-budgetary funds, enterprises and other legal persons in which the state or local units exercise a decisive influence on the management, and which enjoy considerable autonomy including independent decision-making on a part of their revenue and expenditure.

After the users have prepared and submitted their financial plans, the Ministry of Finance, from July to October, considers them and adjusts them to the estimated revenue. After the adjustment of applications for resources, the Ministry of Finance prepares a draft national budget and projection for the following two years and submits then, together with the financial plans of extra-budgetary users, to the Government by 15 October.



Where, during a debate on the proposed national budget, there is disagreement between some budgetary users or relevant ministers and the minister of finance, the latter notifies this to the prime minister who will take the final decision.

At its sessions, the Government debates about the submitted draft documents and submits a national budget proposal, a proposal for a budget execution act, projection for the following two years and financial plans of extra-budgetary users to the Parliament Speaker by 15 November. This marks the end of Step 5, Phase II of the budgetary process.

II.

Phase 2: The budget adoption procedure

6.


Step 6: Debate on the budget proposal and its adoption in Parliament

amendments – proposals for changes and additions to the budget proposal, usually representing requests for increased or reduced amounts of funds for certain budget users.

In the second half of November, the Parliament Speaker delivers the budget proposal to the committees and MPs. All the MPs must receive the budget proposal in time to be able to study it closely. Each MP or parliamentary working body and the Government can submit to the Speaker their proposals for changes and additions to the budget proposal. Such proposals are called the **amendments** and, before the session, they are forwarded to all the MPs and the Government. Any amendments to the proposed budget, adopted by Parliament, must be in line with the determined amount of the permitted consolidated budget deficit. Due to the principle of equilibrium, the



amendments aimed at increasing the budget expenditure above the amount specified in the budget proposal can only be accepted if accompanied by proposals to reduce other expenses. However, these proposals must not burden budgetary reserves or result in further borrowing.




In practice to date, a considerable number of MPs (of various professions and educational backgrounds) have found it difficult to cope with the numerous tables and copious paperwork to be studied before the sessions on the budget. Very frequently, the members receive the proposals only some ten days before the session. Many of them find this period of time inadequate to closely study all the figures and to define their own attitude towards the budget which they are supposed to present at the parliamentary session.

The final debate on the national budget proposal is held at a parliamentary session in December. Budget users usually complain about insufficient resources allocated to them, so that the MPs and deputy clubs lobby for more funds to be allocated to certain ministries and **local units**. Members of Parliament are the elected representatives of citizens coming from various parties. Therefore, the adoption of the budget is also a political affair which depends on the balance of forces in Parliament.

local units – municipalities and cities; the term sometimes also includes counties.

Through its committees and budgetary debates, Parliament analyses the programmes and fiscal policy proposed by the Government. The Finance and Central Budget Committee and Legislation Committee are supposed to give their opinions to the Parliament Speaker on the submitted budgetary documents. These committees also receive any possible amendments, so that they can give their opinions on the proposed budgetary changes.



In case that the proposed budget and the budget execution act have not been drawn up with due professional expertise, the Speaker can, at the recommendation of the Finance and Central Budget Committee and Legislation Committee, return the proposal and the act to the Government and Ministry of Finance. For this reason, the two committees should have well-qualified and professional staff to be able to detect, in good time, any shortcomings in the documents they consider.

The debate on the budget has its timetable. First of all, there is a general discussion on the budget, followed by a debate on the amount of funds allocated to individual ministries and other budgetary users. At the end, there is voting. After the budget and Budget Execution Act have been voted, the execution of the budget becomes obligatory for all the participants in and users of the budget. In order to start applying the national budget as of 1 January next year, Parliament is obliged to adopt the budget and pass the Budget Execution Act on 31 December at the latest. In accordance with the principle of transparency, both the budget and Budget Act must be published in the Official Gazette. Except in the cases of **temporary financing**,

temporary financing – the financing of budgetary and extra-budgetary users in the cases where Parliament or a representative body fails to adopt the budget before the beginning of the budget year; this facility can be used for no longer than the first three months of a budget year.



extra-budgetary fund – a kind of extra-budgetary user established as a legal person for a special purpose and financed from earmarked revenues, from the budget or from other sources.

State Treasury – a system, organised and IT-supported in such a way that it provides for the preparation and execution of the budget, state accounting, cash management and public debt management.

the procedures of budget adoption and giving consent to the financial plans of **extra-budgetary funds** are usually completed in December. The execution of the budget starts from 1 January next year.



Decision on temporary financing

During 2007, it was clear that the elections would be held too late to constitute a Parliament which would be able to adopt the 2008 budget on time. Therefore, a decision on temporary financing was adopted. As early as 3 August, the Ministry of Finance submitted instructions for drafting proposals for the financial plans of the national budget users for the first three months of 2008, and approved a draft decision on temporary financing for budgetary and extra-budgetary users of the national budget. On 23 August, the Government laid down limits on drawing up the three-month financial plans. From 27 to 31 August, ministries and other government administration bodies included the financial plan proposals in the **State Treasury** system and submitted them to the Ministry of Finance which prepared a draft decision on the temporary financing of the national budget for the first three months of 2008 and submitted it to the Government. Before the end of 2007, Parliament adopted this decision pursuant to which the activities, functions and programmes of the national budget users continued to be financed to the amounts necessary for their functioning. The funds thus provided were proportional to the revenue raised in the first three months of 2007, up to one fourth of total revenue minus receipts raised in 2007. During the period of temporary financing, funds were provided only for those programmes, activities and functions that had been performed in 2007, and the users were not allowed to increase the number of employees or assume new financial obligations. After the expiry of the temporary financing period, the revenues and expenditures realised in that period were included in the budget for 2008, adopted by the new assembly of Parliament on 5, March 2008.

III.

Phase 3: Budget execution

fiscal year – a period of twelve months for which government plans revenue and expenditure and adopts the budget. In many countries, including Croatia, it corresponds with the calendar year and lasts from 1 January to 31 December. By contrast, in the UK, for example, it lasts from 1 April to 31 March.

7.

Step 7: Budget execution

After the budget is voted in by Parliament, the Ministry of Finance notifies the ministries and other users of the funds they have been allocated. On 1 January, the **fiscal year** officially begins, the budget is implemented, i.e. revenue is collected and spent, and these operations are supervised and checked. The budget is executed on the basis of monthly budgetary disbursements and in accordance with the available resources and assumed liabilities, up to the amounts specified in annual financial plans.



Who is responsible for the execution of the budget? The top officials in all the budgetary and extra-budgetary users are responsible for the lawful and accurate planning and execution of their respective parts of the budget. The Ministry of Finance is responsible for the orderly execution of the national budget and for the coordination of the budget users' activities. The minister of finance prescribes the procedure and conditions to be complied with and the measures to be taken in the case of irregularities. Of course, the responsibility also rests with the Government, and other national budget users. However, a special role in the execution of the budget and the control of its resources is played by the State Treasury of the Ministry of Finance.

What is the State Treasury?

The State Treasury is nothing like a vault or safe, but a complex system of budgetary and financial public money management, aimed at rationalising public spending, reducing the need for government borrowing and improving liquidity in the economy. The State Treasury prepares, consolidates and executes the budget, keeps the state's accounts, carries out cash and public debt management, as well as the management of EU aid funds. The Treasury conducts transactions with government funds, maintains accounts and drafts reports on budget implementation, receives funds, informs major spending units of available resources and makes payments within the limits of granted budgetary authorisations. The Treasury consists of organisational units which are supposed, subject to a well-developed financial information system of the Government, to ensure full oversight and control of the use of budget resources. For example, it includes organisational units responsible for budget preparation and local unit financing, for the national budget execution, for public debt management, etc.



Step 8: A semi-annual report on budget execution and the financial plans of extra-budgetary users

8.

By end-July each budget year, budgetary users draft semi-annual reports on the implementation of their financial plans. After that, in order to establish the balances of budgetary resources, the Ministry of Finance is obliged, by 5 September, to draw up a report on the semi-annual execution of the national budget and of the financial plans of extra-budgetary users and to submit it to the Government. After a debate, but no later than 15 September each budget year, the Government must submit the report to Parliament.



9. Step 9: Drawing up the annual accounts for the past year

The fiscal year closes on 31 December. During the fiscal year, a number of payments into and from the budget are made through the State Treasury. In the next year, the Ministry of Finance must undertake a number of actions in order to draw up the *final (annual) report on the use of budgetary resources and the execution of financial plans of extra-budgetary users for the past year*. First of all, all budgetary users submit to the relevant ministries and other government bodies at the level of sections, the accounts of their financial plans for the past year. These accounts are then examined, adjusted and consolidated, and finally submitted to the Ministry of Finance. Extra-budgetary users draft such reports independently and submit them directly to the Ministry of Finance by end-March.

After that, the Ministry of Finance consolidates the reports of the ministries and extra-budgetary users and, by 1 May, submits to the Government a consolidated annual report on the execution of the budgets and financial plans of extra-budgetary users for the past year.

The Government adopts and submits to Parliament no later than 1 June, the report on the execution of the budgets and financial plans of extra-budgetary users for the past year.



For example, the Government submitted a proposal for the Annual Accounts for 2007 to the Parliament Speaker on 29 May 2008, and the Speaker forwarded it to the Finance and Central Budget Committee. At its meeting held on 12 June 2008, the Committee discussed the proposal, adopted it and submitted it for voting in the parliamentary chamber. The debate in the parliamentary chamber was closed on 24 September 2008, and the Annual Accounts were accepted on 26 September 2008 (with 74 votes in favour, 26 votes against and 2 abstentions). Apart from the Finance and Central Budget Committee, opinions on this agenda item were also given by the Agriculture, Fishing and Rural Development Committee, Health and Social Welfare Committee, Committee on Croats outside the Republic of Croatia, and Development and Reconstruction Committee.



Step 10: Budget supervision, internal and external audit

10.

The supervision and audit of the spending of budgetary resources is carried out through all the phases and steps of the budgetary process. The Ministry of Finance is responsible for the external supervision of budgetary spending for designated purposes, and for the financial plans of all the users. In addition to this, all budgetary and extra-budgetary users have their own internal audit departments. Their purpose is to supervise the legality, purposefulness and timeliness of the use of budgetary resources, to eliminate the established irregularities and abuses and take measures to improve the situation.

Due to the overall complexity and importance of the budget, the way of spending budgetary resources is of exceptional interest to the public. The State Audit Office assesses the degree to which the spending of budgetary resources is in line with planned and approved amounts, and verifies the credibility of reports and other documents. By the end of the year, the State Audit Office submits to Parliament a report on its work and completed audits for the previous year. After the parliamentary debate, the report becomes a public document and is published on the website of the State Audit Office.

The State Audit Office is an autonomous and independent institution and is accountable exclusively to Parliament. It is responsible for the audit of all the Government revenues and expenditures, state and **public enterprises**, ownership transformation and privatisation, the audit of legal persons fully or partly financed from the budget, and of the use of EU and international organisations' funds for the financing of public needs. Through its recommendations, orders and suggestions, the Office should contribute to the proper application of regulations and to the lawful, cost-effective, efficient and appropriate use of budgetary resources.



public enterprise – an enterprise majority-owned and controlled by the state or a local unit which normally provides public or utility services; the definition is rather vague and the real status of some enterprises is not always clear.

The entire budgetary process and budget execution are finished when Parliament accepts the annual accounts of the national budget.



NOW, WHAT DO YOU DO WITH ALL THIS INFORMATION?

Now, what do you do with all this information about the national budget, functional classification, consolidated general government budget, revision, economic policy guidelines, or the role of the State Audit Office? For starters, you may be happy, for now you can better understand some newspaper articles or TV news. However, they may start annoying you now, even more than before. You may want to change something, because, let us remember, it is you who elect your delegates in executive and representative bodies to make decisions on your behalf. And, as you saw in the part of this Guide dealing with the size of our state, these decisions involve really large amounts of money, so large that deciding on them must not be left only to the elected representatives in the central, regional and local executive and representative authorities, or to various politicians and interest groups represented by them.

The participation of citizens is also necessary. Our goal should be to have sound, efficient and equitable public finances, in accordance with our possibilities and needs. And it is the budget that shows the condition of public finances, as all public funds flow through the budget. To achieve this goal we need sound public policies based on the accountability of all levels of government. The main prerequisite for government accountability is transparency. And then, who if not us, the citizens, will require transparency?

Civil monitoring or citizens' budget watch

In many countries, citizens are actively involved in budgetary affairs; they make demands on and supervise the budgets. A relatively new activity coined **budget watch** is spreading around the globe. It relates neither to internal supervision carried out by budgetary users, nor to external audit conducted by the State Audit Office. What we have here is the supervision carried out by citizens themselves. These can be individuals but also non-profit, non-government organisations aimed at promoting transparency, openness and accountability of government, and the participation of citizens in the budgetary process. Budget watchers emphasize that the budget is too important a document, containing data on public revenue

budget watch – the monitoring of the budget by citizens, individually or through non-profit and non-governmental organisations with a view to promoting transparency, openness and accountability of government, and participation of citizens in the budgetary process.



and expenditure, to be left to government officials and elected representatives. As taxpayers, citizens contribute to the budget and should therefore be included in the decision making on the distribution of its resources. For this reason, budget watchers insist on providing the citizens with an insight into the collection of revenues and distribution of expenditures, and they particularly deal with the issues of equity, fairness and efficiency. In order to carry out budgetary supervision in practice, budgetary documents and procedures must be transparent and citizens must be given an opportunity to participate in these procedures. The final goal is to improve government accountability to the public.

The watchers cannot be satisfied only with the reports from state audit offices, so they analyse the budget independently, disseminate the results of the analyses in the form of short popular articles, such as the Institute of Public Finance' press releases or citizen's guides to the budget, like the one you have in front of you. The budget watchers can concern themselves generally with the transparency of the budgetary process, accountability of the government and citizens' participation, but they can also monitor some specific areas such as, for example, the influence of the budget on poverty, education, health care, environment, women or children. Moreover, the watchers can focus on the national budget, but also on local budgets, because many problems directly affecting citizens, like education or social welfare, fall within the local authorities' competence.

Budget monitoring is particularly efficient in the USA, where it is exercised by numerous organisations at the federal, state and county levels. The most committed among them is the International Budget Partnership (IBP). Many other countries also have very efficient budget monitoring organisations. In Croatia, it is the Institute of Public Finance that tries to bring budget supervision closer to common citizens.

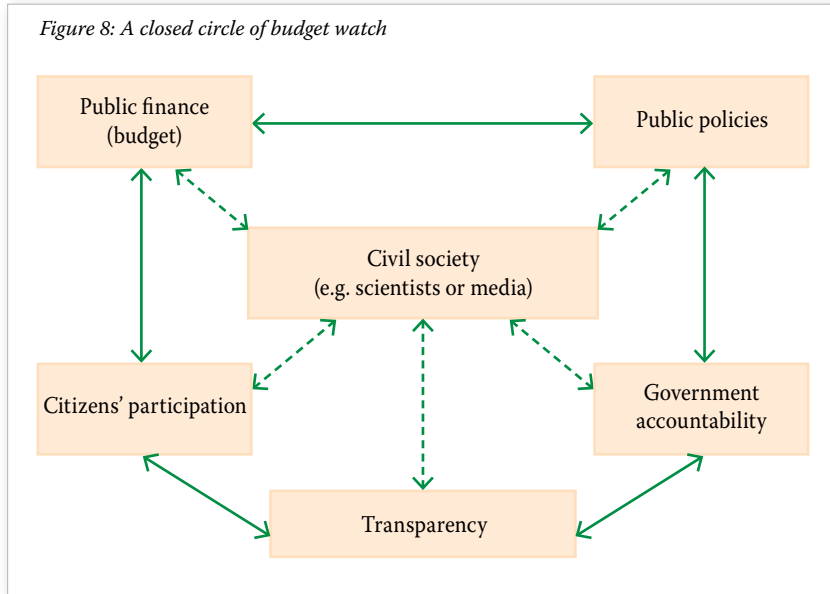
What should the civil monitoring of the budget look like?

Figure 8 shows the opportunities offered by budget watch. Let us start with citizens who should demand that the budget be transparent. If they are successful in their demands they should make the authorities publish understandable and reliable information in a timely manner. More transparent budgets provide for a better oversight of the work of authorities, so they would make efforts to be more accountable to better informed citizens. More accountable authorities would administer more effective public policies, which would in turn lead to sounder, more efficient and more equitable public finance, i.e. a more stable and balanced budget in accordance with the possibilities and needs of the society. The left/right arrows describe full circles in both directions, because all the factors within boxes



influence one another. As the authorities can hardly be expected to become more accountable of their own accord, there is nothing else we can do but be more active as individuals, through non-profit and non-government organisations or through representatives in civil society organisations, academic community and the media.

Figure 8: A closed circle of budget watch



What does the Institute of Public Finance do to promote the budget watch?

The Institute of Public Finance, an academic and research institution established in 1970, started to participate in stimulating the civil supervision of the budget as late as the end of the 1990s. After the breakdown of the old, and establishment of the new state, during the transition from socialism to market economy, due to the war and its political and institutional, as well as economic and social consequences, the Croatian public finances were in a rather bad shape, with practically no public awareness of the need for transparency in the public sector, government accountability and citizens' participation.

Our goal has been to offer professional and independent analyses capable of attracting public attention and to emphasize the need for a better access to information and for well-argued budgetary debates. We focused on



budget expenditure, the necessity to provide access to reliable data, and to make and publish classifications of these data, as well as on transparency in general. We also concentrated on tax revenues, i.e. their appropriateness and structure, tax rates and tax burden.

Budget expenditure is, of course, a more interesting issue, particularly for non-governmental organisations, dealing with some specific subjects like the rights of the poor or the disabled, etc. However, the budget consists of two parts, revenue and expenditure, and they must be balanced. This is why we constantly analyse both revenue and expenditure, trying to inform the public of the most topical issues.

It is hard to make the budget interesting. It is a complex and fairly boring issue, and to deal with it is a rather thankless task. Publishing texts about budgetary problems brings more enemies than friends to their authors, because every topic they tackle and every change they suggest will be to somebody's detriment. Everyone who embarks on a budget analysis and demands changes must be aware of this.

How do we choose our topics? This is very simple: sometimes we comment on the decisions of Parliament, the Government or the Ministry of Finance, and sometimes motivation for an analysis comes from the media. Exporters, farmers or fishermen demand additional incentives, the minister of education requires free textbooks for all pupils, or patients demand repealing of co-payments... Each such requirement must be financed from budget revenue. So, either some users of public goods and services receive less goods and services, or some taxes have to go up, or the Government resorts to additional borrowing. In such situations we examine the problem, analyse figures and, taking account of the social justice and economic efficiency, we try to offer some solutions. It is not always easy to offer solutions that are satisfactory to everyone, particularly in difficult economic circumstances. However, making the problem more understandable is already considered a huge step forward.



Publications of the Institute of Public Finance that might be of help to those interested in the civil budget monitoring:

- ◆ Press Releases [<http://www.ijf.hr/eng/index.php?ime=141>]
- ◆ Newsletters [<http://www.ijf.hr/eng/index.php?ime=28>]
- ◆ Public Finance Glossary [<http://www.ijf.hr/eng/index.php?ime=159>]
- ◆ The Citizen's Guide to Taxation [<http://www.ijf.hr/eng/index.php?ime=160>]
- ◆ The Croatian Tax System [<http://www.ijf.hr/eng/taxguide/taxtable.pdf>]
- ◆ Javne financije u Hrvatskoj (Public Finance in Croatia): [<http://www.ijf.hr/index.php?ime=102>]
- ◆ Making Public Finance Public: [http://lgi.osi.hu/publications/2006/338/Making_Public_Finance_Public_2.pdf]



What can you do yourself?

None of us, either as an individual, or a member of an organisation, can at once influence the size of the Croatian public debt, or the total amounts of funds allocated for pensions of the public employees' salaries. What each of us can easily do is to find their local budget at the website of their respective municipality of city. As this budget is neither so big nor so complex as the national budget, with the help of this Guide you can "master" it with ease.

If you, for example, live in Karlovac, or if you are particularly interested in that city, you can easily find the budgets for 2007, 2008, and 2009, and even the revised 2009 budget at: <http://www.karlovac.hr>. After reading it, you will certainly have a lot of questions. You may, for example, wish to know the reason for a 6.4 billion kuna increase in capital grants from other entities within general government, stated in the revised budget, which led to a rise in this item from the initially planned 8.8 million kuna to 15.2 million kuna, despite the general cost-cutting trend.

However, if you are interested in Komiža, you can only find the budgets for 2007 and 2008 at: <http://www.komiza.hr>, but not the 2009 budget or its revision. But of course, you can always visit the Ministry of Finance's website, where you can find, although not so easily, the budget of the city of Komiža (up to the plan for 2009) (→ Proračun → Lokalni proračun 2008 → Lokalni proračun – Arhiva → Lokalni proračun 2002. – Plan 2009. → Splitsko-dalmatinska županija → Komiža). So, to start with, you can require from the city authorities to publish up-to-date information. When this is done, you can analyse it and ask specific questions.

So, then, your task is clear:

- ◆ participate actively, communicate and ask questions;
- ◆ require from local authorities to publish timely information on the budget, to organise a public hearing prior to adopting any crucial decisions, and to provide persons to publish the information and respond to inquiries from the public, because you are entitled to information;
- ◆ improve your knowledge and understanding of your local budget and compare the budget of your municipality or city with those of other municipalities or cities; submit specific suggestions to your local authorities.

If you want to learn more about the possibilities of citizens to participate in budget monitoring, read a very informative and interesting article by Ivana Maletić entitled "Subnational Budget Watch in Croatia: Is Anybody There?" (2006).





Participate actively in all the phases of the budgetary process:

- ◆ In the budget preparation phase, get involved in decision-making about the programmes. This will help you better understand the work and goals of your local government and perhaps influence the quality of local public services.
- ◆ Monitor the execution of the budget and inquire about its performance. This might help you in preventing the inefficient use of public resources, frauds and irregularities, and in providing your co-citizens with reports on budget execution.
- ◆ In the financial reporting phase, make comments, demand simple reports and compare the financial performance of your municipality or city with that of other municipalities and cities. In doing so you will be able to better understand your local community situation, and, perhaps, to suggest some improvements.

Be aware of your rights and possibilities to monitor the budget, but also of your obligations toward the state and the treasury. And, yes, be very, very patient, because it takes a lot of time to make changes in an area that is so complex and uninteresting for most people, as the budget.



GLOSSARY

activity – a part of a programme of no pre-defined duration, but with planned expenses for the achievement of goals set by the programme.

administrative classification → organisational classification

aid – receipts without any counter-obligation, non-repayable, non-obliging receipts from domestic and foreign units of government or international institutions.

allocation function of the budget – government action to influence the decision about goods and services to be considered as public and those to be considered as private (directly, through the public offering of, for example, education or health care, or indirectly, through taxes and grants aimed at stimulating or discouraging certain activities).

amendments – proposals for changes and additions to the budget proposal, usually representing requests for increased or reduced amounts of funds for certain budget users.

areas of special state concern (ASSC) – the areas devastated by war (groups I and II) or areas lagging behind due to poor economic development, structural problems, demographic or other reasons (group III). All the three groups cover up to 15% of the total country population. The government provides them with special grants and cedes them the total amount of income tax collected; the difference between the ASSCs and hill and mountain areas (HMA) is sometimes not clear cut.

borrowing – taking credit and taking out loans or issuing securities.

budget – a plan of revenue and expenditure for a given period of time.

budget classifications → budgetary classifications

budget projections → budgetary projections

budget revision – a change in budgetary amounts, i.e. their reduction and/or increase relative to the budget plan adopted at the beginning of the calendar year. It occurs during the budget year, when budget revenue estimates are unrealistic, or where unexpected expenditures arise. Budget revisions can be due to unforeseen circumstances in the domestic or world economy, but they can also be the consequence of the government's inability to make realistic revenue and expenditure plans.

budget watch – the monitoring of the budget by citizens, individually or through non-profit and non-governmental organisations with a view to promoting transparency, openness and accountability of government, and participation of citizens in the budgetary process.

budget – a plan of revenue and expenditure for a given period of time.

budgetary classifications – the systems of revenue and expenditure presentation according to certain criteria (e.g. by user, goal, purpose, type, location and source of finance). → economic c. → functional c. → location c. → organisational c. → programme c.

budgetary fund – a kind of a budget user financed from earmarked revenues or from the budget.

budgetary principles – the principles to be adhered to by all those dealing with the budget; they include the principles of equilibrium, annuality, unity and budget accuracy, universality, specification, transparency and sound financial management.

budgetary process – a process consisting of the planning, preparation, adoption, execution, supervision and audit of the budget.

budgetary projections – the estimates of revenue and expenditure for a several-year period, adopted by parliament or the representative bodies of local units.

budgetary users – government bodies, institutions, minority self-government coun-



cils, funds and territorial self-government, whose expenses for employees and/or material expenses are financed from the budget.

central government – the national budget users (e.g. ministries, state agencies) and extra-budgetary users (e.g. Croatian Waters and Croatian Roads).

consolidated central government budget – the budget obtained as a result of consolidation within individual extra-budgetary users and between extra-budgetary users and the national budget.

consolidated general government budget – the budget obtained as a result of consolidation among extra-budgetary users, between extra-budgetary users and the national budget, between local units and their extra-budgetary users and between local units and the central government budget.

consolidated local government budget – the budget obtained as a result of consolidation between local units and their budgetary and extra-budgetary users.

consolidation – the cancellation (omission) of payments among individual budget users in order to obtain a consolidated budget of several budget users, i.e. of a certain level of government.

contributions – earmarked public revenues, paid for example for health and pension insurances. They are collected from employers and from employees. Unlike taxes which flow into the state treasury and can be used for any general public need, contributions are paid into special funds and can only be used for the purpose for which they are earmarked.

corporate income tax (CIT) – a direct tax levied on the profits of legal and natural persons pursuing a business activity independently and on a permanent basis with a view to deriving profits.

Croatian Bank for Reconstruction and Development (HBOR) – a state-owned bank responsible for financing the reconstruction and development of the economy and infrastructure, providing incentives to export, supporting SMEs, promoting environmental protection and protecting the

goods and services export from non-market risks.

debt → domestic or internal debt, foreign or external debt, public debt

decentralised public services – responsibilities for a part of public services (education, health care, social welfare and fire fighting), which the state delegates to a certain number of local units (counties, cities and municipalities), providing them, in return, with access to additional forms of financing.

deficit – excess of expenditure over revenue in a given period.

direct taxes – taxes imposed directly on taxpayers, i.e. the taxes to be paid by the taxpayer directly into the budget, e.g. corporate income tax and personal income tax, surtax on personal income tax, property tax and gift and inheritance tax.

distribution function of the budget – government action to influence the distribution of produced goods and services among members of society, either through progressive taxation policy or through the system of transfers, depending on whether the society gives priority to equity or efficiency.

domestic or internal debt – accumulated budget deficit financed by borrowing within the country.

donations – gifts in cash or in kind which can be given by the budget and budget users to non-profit organisations, households and citizens, or received from natural persons, non-profit organisations and companies.

earmarked revenue – the revenue whose purposes have been determined in advance; thus, for example, revenues from health insurance contributions must be used for health care.

economic and fiscal policy guidelines – a document in which the government annually adopts the course of its fiscal policy for the following three-year period; it defines macroeconomic and fiscal assumptions for budget preparation.

economic classification – the presentation of revenues and receipts by natural type



(e.g. taxes, aid, receipts from assets), and of expenditures and expenses by economic purpose (e.g. compensation of employees, subsidies, social benefits).

equalisation fund – a portion of the collected personal income tax from which central government gives transfers to local units which are unable to adequately finance their decentralised functions.

excise taxes – special taxes, or excises, on the consumption of petroleum derivatives, tobacco products, coffee, beer, non-alcoholic beverages, spirits, personal cars and other motor vehicles, vessels, planes and luxury products. They are justified by introducing tax progression (e.g. on luxury products), reducing pollution (e.g. on petroleum derivatives) and discouraging the consumption of certain products (e.g. tobacco and alcohol), hence: sin taxes.

expenditure – a term used in the revenue and expenditure account, meaning funds disbursed from this account for government operations and the purchase of non-financial assets.

expenditures for employees – the salaries of employed civil servants, contributions for their compulsory health and pension insurance and various benefits in kind.

expenses – the term used in the financing account meaning the funds paid from this account for the procurement of financial assets, borrowing and loan repayment.

external debt → foreign debt

extra-budgetary fund – a kind of extra-budgetary user established as a legal person for a special purpose and financed from earmarked revenues, from the budget or from other sources.

extra-budgetary users – extra-budgetary funds, enterprises and other legal persons in which the state or local units exercise a decisive influence on the management, and which enjoy considerable autonomy including independent decision-making on a part of their revenue and expenditure.

financial expenditures – the expenditures arising from financial operations, primarily due to borrowing (e.g. interest on issued se-

curities, interest on loans and fees for banking services).

financial plan – a document drafted by a budgetary or extra-budgetary user showing its revenue and expenditure.

financing account – a part of the budget showing how budget deficit is financed and budget surplus spent.

fiscal capacity – the ability of local units to finance their budget expenditure with their own budget revenue.

fiscal consolidation – the policy aimed at reducing the national deficit and accumulated debts.

fiscal year – a period of twelve months for which government plans revenue and expenditure and adopts the budget. In many countries, including Croatia, it corresponds with the calendar year and lasts from 1 January to 31 December. By contrast, in the UK, for example, it lasts from 1 April to 31 March.

foreign or external debt – the accumulated budget deficits financed through foreign borrowing.

functional classification – a presentation of expenditure according to its purposes (e.g. defence, health care and education).

functions of the budget – besides the collection and spending of funds, the budget also reflects the main objectives of the state, and serves as an economic policy instrument and an instrument for the collection and spending of public money.

GDP → gross domestic product

general government – central government (budgetary and extra-budgetary users of the national budget) plus budgetary and extra-budgetary users of the county, city and municipality budgets consolidated general government budget.

government guarantee – an instrument by which the government guarantees the settlement of liabilities for which the guarantee is issued.

grants – non-returnable transfers of funds to international organisations, foreign gov-



ernments, budgets, extra-budgetary users, banks, financial institutions and enterprises. Aid is often given by the national budget to local budgets, but they can also be given among local units of the same level, e.g. counties. They are divided into current grants (for current expenses) and capital grants (for the purchase of fixed assets), as well as into special-purpose and general-purpose grants.

gross domestic product (GDP) – an indicator of the total value of goods and services produced in a country within a year.

guarantee → state guarantee

hill and mountain areas (HMA) – areas defined by a special law, in which the state stimulates demographic renewal, economic growth and sustainable development, and creates prerequisites for improved social circumstances and higher standards of living for citizens. Depending on the cause of their lagging behind other parts of the country, these areas are classified into two groups: Group I, with negative natural population growth, higher unemployment rate, etc., and Group II, with unfavourable climate and other natural characteristics.

income tax → corporate income tax, personal income tax

indirect taxes – taxes on goods and services collected indirectly through an intermediary, such as an importer, producer or seller (for example VAT, excise tax, and customs duty). They are included in prices, so that, despite being paid into the budget by intermediaries, they are indirectly borne by customers.

internal debt → domestic debt

local budget – a document in which a local unit plans its revenue and estimates expenditure for a single year, and which is passed by the local unit's representative body.

local government – the budgetary users in local units (counties, cities and municipalities).

local self-government – the legal framework within which cities and municipalities are responsible for certain functions (e.g. primary education, social welfare, housing

and utility services) and are entitled to own revenue and own representative and executive authorities; the government cannot interfere in their powers and is obliged to provide aid to economically less developed units of local self-government.

local units – municipalities and cities; the term sometimes also includes counties.

location classification – expenditure shown according to territorial units (e.g. country, county, city, municipality, or area of special state concern).

material expenditures – the value of goods and services purchased by the state from the private sector on the open market for the performance of its operations (e.g. telephone, postal and transportation services or regular and investment maintenance services).

national budget – a document in which the government plans its revenue and estimates expenditure for a single year in accordance with law, and which is passed by parliament.

national debt – accumulated central government deficits financed by borrowing.

net borrowing – an indicator of surplus of expenditure over revenue in the financing account.

net financing – the amount that should equal the deficit/surplus from the revenue and expenditures account, or the net lending/borrowing of the state.

net lending – an indicator of surplus of revenue over expenditure in the financing account.

operating balance – a difference between operating revenues and operating expenses excluding changes in non-financial fixed assets.

operating revenues – the revenues from regular operations, e.g. from taxes (personal and corporate income taxes and VAT), contributions (for pension, health and unemployment insurance) and other revenues (from property, administrative fees or fines).



organisational classification – the presentation of expenditure according to organisational units, i.e. ministries, state offices, funds, institutes, agencies and other budget users (formerly known as administrative classification).

personal income tax (PIT) – a direct tax levied on a natural person's income.

potential public debt – public debt increased by given state guarantees and the debt of the Croatian Bank for Reconstruction and Development.

primary operating balance – a difference between operating revenues and operating expenses net of interest expenses.

profit tax → corporate income tax

programme classification – the statement of expenditure by programme, activity and project (e.g. environmental protection, informatisation or entrepreneurial support).

programme – a set of independent and closely connected activities and projects aimed at achieving a common goal.

project – a part of a programme of a pre-defined duration, with planned expenses for the achievement of the goals set by a programme.

property tax – a tax on ownership (e.g. of houses, apartments or land), or on net property (total movable and immovable property reduced by liabilities arising from it).

public debt – accumulated general government deficits financed by borrowing.

public debt instruments – credit, loans, bonds, treasury bills and other securities that the government can use to finance its deficit.

public enterprise – an enterprise majority-owned and controlled by the state or a local unit which normally provides public or utility services; the definition is rather vague and the real status of some enterprises is not always clear.

public finances – an economic area dealing with the analysis of the public revenue and expenditure policy.

public sector – a part of the national economy comprising all levels of government, the social welfare, pension and health insurance systems and public enterprises.

receipts – a term used in the financing account, for funds flowing into this account from the sale of financial assets, and from debt and loan repayments.

regional self-government – a legal framework within which counties and the City of Zagreb are responsible for certain functions (e.g. primary and secondary education, health care, social security and welfare) and are entitled to have own revenue and own representative and executive authorities; the government cannot interfere in their powers and is obliged to provide aid to economically less developed counties.

revenue – a term used in the revenue and expenditure account, for funds paid in that account on the basis of operations or the sale of non-financial assets.

revenue and expenditure account – shows the revenue and expenditure of the state in a single year.

revenues according to special regulations – the revenue raised by extra-budgetary users, e.g. the Croatian Waters' revenues from water regulation charge, water contribution, water protection charge, and water use charge.

revenues from non-financial assets – the revenue derived from the sale of residential or business buildings, land, transportation facilities or strategic reserves.

shared taxation – division of taxes between the central government and local units (counties, cities and municipalities). By changing tax rates and percentages of divided taxes, e.g. income tax, the government influences the amount of tax revenue remaining with the local units.

size of government – the share of the general government expenditure in gross domestic product.

social benefits – the benefits based on insurance rights (pensions, unemployment benefits, as well as sickness and maternity benefits), or provided in the form of as-



sistance to the poor in difficult situations which are not covered by the basic social insurance (e.g. various allowances to families and disabled persons, transportation cost aid and public kitchens).

social security contributions → contributions

stabilisation function of the budget – government action in taxation and public expenditure aimed at increasing employment, ensuring price stability, improving the balance of payments and achieving most favourable economic growth rates.

state aid – state intervention used to grant an economic privilege granted to a certain enterprise, sector or region; it is selective and has adverse impacts on competition and trade; it is provided in the forms of subsidies, tax relief, equity participation, soft loans, tax deferrals or guarantees.

State Audit Office – an independent and autonomous institution accountable to Parliament, which is responsible for the audit of all the budgets, extra-budgetary users, state and public enterprises, ownership transformation and privatisation, and the audit of enterprises fully or partly financed from the budget.

State Treasury – a system, organised and IT-supported in such a way that it provides for the preparation and execution of the budget, state accounting, cash management and public debt management.

subsidies – non-repayable state aid to producers or consumers subject to a specific type of business or behaviour of the recipient.

surplus – excess of revenue over expenditure in a given period.

surtax – an extra-tax on personal income tax levied by municipalities and cities. The surtax base is the personal income tax, and the rate is set by local units which collect the surtax as their revenue.

tax – a kind of compulsory payment to the government without a direct counter-benefit.

tax base – an amount to which a tax rate is applied, e.g. a company's profits, a natural person's income or the value of real estate; it represents the final amount net of all deductions, losses and personal allowances.

tax rate – a percentage or a fixed amount of income, profits, or of the value of goods and services, paid to the government; it is applied to the tax base and it can be progressive, proportional or regressive.

tax sharing → shared taxation

taxpayer – a person who bears the tax burden for any given status, business activity or transaction.

temporary financing – the financing of budgetary and extra-budgetary users in the cases where parliament or a representative body fails to adopt the budget before the beginning of the budget year; this facility can be used for no longer than the first three months of a budget year.

territorial self-government – municipal office branches, city areas and city districts which can be established within the units of local self-government.

Treasury → State Treasury

Treasury Single Account (TSA) – a system of accounts across which all payments of all budget users are made; it is maintained by the Croatian National Bank and supervised by the Ministry of Finance.

units of local and regional self-government – municipalities, cities and counties.

units of local self-government – municipalities and cities.

units or regional self-government – counties.

value added tax (VAT) – an indirect sales tax charged at every stage of production and distribution, i.e. for all final purchases of goods and services; it burdens the final consumer, but the actual taxpayer is the provider of goods and services.



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- Annual reports [<http://www.revizija.hr/hr/izvjesce/>]
- Survey Results on the Transparency of Local Self-government Units by City/Municipality** [<http://www.gong.hr/survey/default.aspx>]



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