



# **Report on the main budgetary lines for 2015 of the Autonomous Region of the Balearic Islands**

**In the two years 2014-2015, the Autonomous Region of the Balearic Islands must make a fiscal effort equivalent to 0.5% of its expected regional GDP for 2015.** At year-end 2013, the Region's net borrowing was €324m, which is 1.2% of its regional GDP. Using the year-end as a starting point, in order to meet its stability target in 2015 it has to reduce its deficit by €129m. This is 0.5% of the regional GDP forecast for 2015.

**There are risks that in 2015 the Autonomous Region of the Balearic Islands might not reach its deficit target for the year, which has been set at 0.7% of its regional GDP.** On the basis of the information available in the main budgetary lines questionnaire submitted by the Region, facilitated by the General Government Financial Information Centre (Ministry of Finance & Public Administration, MINHAP), and in the draft Budget published by this region for 2015, there are implementation risks that jeopardise compliance with the stability target for this year. These risks are based on:

The mission of AIReF, the Independent Authority for Fiscal Responsibility, is to ensure strict compliance with the principles of budgetary stability and financial sustainability contained in article 135 of the Spanish Constitution.

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- **High risk of non-compliance with the target set for 2014, driven by the fiscal tension observed, especially in the expenditure scenario, along with uncertainty concerning the receipt of State funds from a highways construction agreement signed in 2004.** In the fiscal scenario foreseen by the Region for the year-end, the forecasts are very tight, taking into account the implementation to date. Moreover, there is a specific risk of deviation in the forecasted revenues to be received from the State under a 2004 roads construction and financing agreement. Should it materialise, it would mean that the region would have to make additional retrenchment not initially envisaged in the plans.
- **Deviation risk observed in the draft budget for 2015.** The greatest deviation risks detected in the draft budget for 2015 are driven by capital transfers and the uncertainty surrounding the implementation of some of the expected public accounting adjustments in national accounts terms.

**The Region's 2014 deficit could stand at around 1.3% of regional GDP.** Taking into account the performance of revenues and expenditure to date, compliance with the year-end figures envisaged in the 2014 fiscal scenario forecast by the Region in the main budgetary lines questionnaire for 2015 is highly stressed. There seems to be no buffer for absorbing or correcting deviations that may occur towards the end of the year. In these circumstances, the high level of uncertainty around the materialisation of the revenues expected from the State under the 2004 roads construction and financing agreement could lead to a greater deficit than targeted.

**In application of article 20 of Royal Decree 215/2014, 28th March, approving the Organic Charter of the Independent Authority for Fiscal Responsibility, an independent section is included in this report on the deviation risk detected in 2014.**

## **Analysis of the possible deviation from the 2014 budget stability target**

The Autonomous Region of the Balearic Islands expects to achieve its 2014 stability target with a 2.2% increase in revenues and a 0.9% reduction in expenditure in public-sector accounting terms. On the basis of the information available in the main budgetary lines questionnaire submitted by the Region to the Ministry of Finance & Public Administration (MINHAP), by year-end 2014 the Region expects to achieve the stability target set for the year at -1% of its regional GDP. This outcome would be obtained by a 2.2% increase in non-financial revenues, driven by an increase in capital revenues; and a 0.9% increase in non-financial expenditure, mainly driven by current expenses, especially transfers. Additionally, adjustments in national accounts terms are expected that would correct the budget outcome and bring down the deficit by €63m.

**The primary deficit expected by the Region is 0.4% of the regional GDP in public-sector accounting terms.** Expected non-financial interest expenditure (chapter 3 of the expenditure budget) for year-end 2014 accounts for 0.8% of the regional GDP.

**Revenues from the funding system paid out by the State to the Region in 2014 fell by 3.2% against 2013.** The largest items recorded as non-financial revenues are the revenues from the funding system payable with interim instalments and final settlement. These were down 3.2% against those received in 2013. The average reduction for all the Autonomous Regions under the common regime is 3.3%.

**The Region has not quantified the measures adopted for this year.** The Region has not reported on the measures adopted for 2014 for income and expenditure in the main budgetary lines questionnaire.

**The main risks of deviation from the 2014 stability target are driven by the expected year-end figure for capital transfers:**

1. A risk of non-compliance can be observed in the **revenue** scenario given by the Region for 2014 in its estimates of

**capital transfers**, 172% up against the previous year. On the basis of the information provided by the Region, this item includes State funds under the 2004 roads construction and financing agreement. The State has not recognised this obligation to date, thus creating uncertainty as to whether these funds will be received or not.

2. Additionally, the buffer seems very meagre in the **expenditure** scenario expected by the Region for 2014, mainly with respect to **current transfers**. Once the expected effect of account 409/413 has been factored out, the year-end increase is expected to be 3% against last year, which falls below the figure recorded for the year to September. Nonetheless, according to the additional information submitted by the Region, this performance is affected by the differences in the rate at which certain expenses are recognised. Moreover, implementation in the last quarter is affected by the Closure of Accounts Order of 24th November and the non-availability of expenditure established since 30<sup>th</sup> November, which the Region expects to extend and turn into a ruling on non-availability of funds to finance concrete budget appropriations. With this additional information the expected scenario could be achieved. However, meeting these estimates demands strict application of the Region's cost curtailment plans.

## **Analysis of possible deviation in the 2015 forecasts**

The Autonomous Region of the Balearic Islands expects to achieve its 2015 stability target with a 6.2% increase in revenues and a 6.9% increase in expenditure, in public-sector accounting terms. For 2015, the budgetary stability target is -0.7% of regional GDP. According to the information available, this outcome would be obtained with a 6.2% positive year-on-year change in non-financial revenues and a 6.9% year-on-year increase in non-financial expenditure. Additionally, in public-sector accounting terms the deficit would be reduced with positive adjustments in national accounts terms, estimated at €177m, which would bring its net borrowing into line with the stability target.

**The primary deficit expected by the Region is 0.7% of the regional GDP in public-sector accounting terms.** Expected non-financial interest expenditures (chapter 3 of the expenditure budget) for year-end 2015 accounts for 0.7% of the regional GDP.

**Revenues from the funding system that the State is expected to pay out to the Region increase 6.7% against 2014.** The largest items recorded as non-financial revenues are from the funding system payable with interim instalments and final settlement. The 2015 General State Budget envisages a 6.7% increase in these revenues compared against 2014. The average increase for all the Autonomous Regions under the common regime is 2.8%.

**The Region has not quantified the measures adopted or planned for this year.** The Region has not submitted information on the income and expenditure measures adopted or planned for 2015 in the main budgetary lines questionnaire. Its draft budget legislation for 2015 refers to a series of unquantified tax measures, aimed basically at reducing rates, lowering tax rates and raising the tax threshold. With respect to personnel expenditure, the bill states that there will be no increase against 2014 in like-for-like terms. It also regulates the partial claw-back of the extra pay

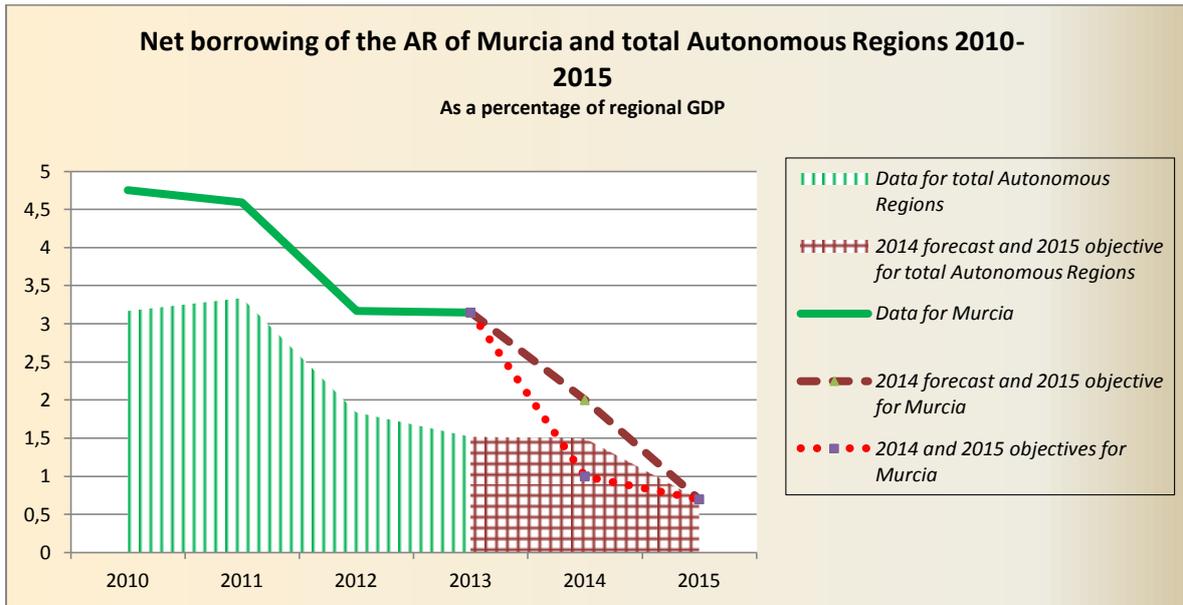
packet for public employees not paid in 2012 and it suspends certain social contributions and benefits.

**The main risks of deviation from the 2015 stability target are driven by the amount of expected revenues from capital transfers.** The revenue scenario forecast by the Region for 2015 reflects a slight increase in revenues from capital transfers. This scenario includes the annual amount the Region receives from the State under the aforementioned road agreement. The risk of these expected revenues not materialising in 2014 can be extrapolated to the 2015 scenario.

## **Report on the application of the corrective mechanisms established in Organic Law 2/20152, of 27th April, on Budgetary Stability & Financial Sustainability (article 21 of Organic Law 6/2013 on the establishment of an Independent Authority for Fiscal Responsibility and article 20 of the AIReF Statute)**

The fiscal adjustment achieved by the Autonomous Region of the Balearic Islands between 2010 and 2013 was €825m. This is equivalent to almost 3.1% of its 2013 regional GDP. The graph below shows that this adjustment is far greater than that of the Autonomous Regions as a whole (vertical green bars), which was almost 1.8% of GDP.

The graph also shows the expected fiscal adjustment for 2014 and 2015 in line with the targets established (dotted red line) and the amount needed to reach the 2015 target if the risks of not meeting the target for 2014 materialise (dotted brown line).



The Autonomous Region of the Balearic Islands is deemed to have a high risk of non-compliance with the stability target, set at -1% of regional GDP for 2014, due to the meagre buffer it has to absorb possible deviations in its implementation of the budget to date, together with uncertainty around the receipt of the transfers from the State under the 2014 road-building agreement. According to the available information for the issuing of the individualised Report on the main lines of the Autonomous Regions’ budgets for 2015 (information from the questionnaire submitted by the Ministry of Finance & Public Administration and draft budgets presented by the Autonomous Regions) and taking into account the data on the Region’s execution of non-financial transactions to 30th September<sup>1</sup>, in national accounting terms, certain specific circumstances can be observed in the Autonomous Region of the Balearic Islands that, along with the tension observed in budget implementation —above all in expenditure— could mean a deviation in its compliance with the targets set for 2014. These situations arise specifically from the uncertainty regarding the receipt of the funds that the Region

<sup>1</sup> According to the latest data published by the IGAE (Government Comptroller's Office), **the Region's net borrowing to September 2014 was €166m**. This is 0.6% of its GDP, 0.45% higher than the figure recorded on the same date of 2013.

<http://www.igae.pap.minhap.gob.es/sitios/igae/es-ES/ContabilidadNacional/infadmPublicas/infadmcomunidadesautonomas/Paginas/imnofinancierasCA.aspx>

expects from the State pursuant to the 2004 road-building agreement this year, in the terms indicated in the section *Analysis of the possible deviation from the 2014 budgetary stability target*.

**In compliance with article 20.1, section b) of the AIReF Organic Statute, this possible deviation is explicitly stated in this report, in an independent section, for the effects established in Organic Law 6/2013, of 14<sup>th</sup> November.**

**Consequently, this report is submitted to the Ministry of Finance & Public Administration as it is deemed advisable to activate the measures established in article 19 of Organic Law 2/2012, of 27th April, on Budgetary Stability & Financial Stability.**