Romania and the IMF

Press Release:
IMF Executive Board Completes First and Second Reviews Under the Stand-By Arrangement and Ex-Post Evaluation of Exceptional Access for Romania
March 26, 2014

Romania: Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding

March 5, 2014

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Romania: Letter of Intent

Bucharest, March 5, 2014

Mme. Christine Lagarde
Managing Director
International Monetary Fund
Washington, DC 20431
U.S.A.

Dear Mme. Lagarde:

The Romanian authorities reaffirm our commitment to our economic program supported by the International Monetary Fund (IMF), the European Union (EU), and the World Bank (WB). We met four out of five quantitative performance criteria and made good progress on structural reforms. In particular, we launched initial public offerings (IPOs) of shares in two state-owned energy companies, Romgaz and Nuclearelectrica, and the energy regulator implemented the next steps of the energy price liberalization roadmaps as planned. We accelerated our absorption of EU funds, which is particularly important since domestic demand has been weaker than expected. For 2014, we remain committed to gradually reduce the fiscal deficit but slightly moderate the adjustment path to facilitate greater absorption of EU funds with a view to enhancing the economy's growth potential.

1. Our performance on the quantitative targets and the structural reform agenda for the first and second reviews has been good (Tables 1 and 2).

- *Quantitative performance criteria and indicative targets*. Four of the five end-December 2013 quantitative performance criteria and four out of five indicative targets were observed. The performance criterion on the general government overall balance, set at the time of program approval, was missed by a small margin, largely due to higher spending on EU co-financing. We have adopted a budget for 2014 that provides for a continued gradual consolidation. The indicative target on outstanding payments past due of all central-government owned SOEs, however, was missed by a substantial margin. Corrective actions are being taken to achieve the arrears objective of the program, as described in the attached Memorandum of Economic and Financial Policies (MEFP). Inflation fell below the inner band of the inflation consultation mechanism and discussions were held with IMF staff, as required under the program.

- *Structural benchmarks*. We have made good progress on achieving the program's structural benchmarks. We successfully launched an IPO of 15 percent of the government's shares in Romgaz. We started to publish monthly arrears reports by the central and local governments, by administrative unit. We also prepared medium-term financial projections that properly identify the fiscal implications of EU-funded projects, including co-financing needs, financial corrections and non-eligible spending. We approved, by government memorandum, a list of significant priority projects, based on the prioritization criteria, to help prepare for the 2014 budget. The structural benchmark on appointing a professional board in Hidroelectrica in accordance with the provisions of Ordinance 109/2011 was met. We finalized the design and costing of our basic health care package, delineating the options for private sector involvement. The new commitment control system was made available to three pilot entities in January 2014; by end-April 2014, it is expected to cover all expenditures in those entities and produce the required reports. We propose to reset the structural benchmark accordingly. We have drafted a new covered bonds law and will submit it to parliament, later than originally expected, for consideration through the emergency procedure; we propose to reset the structural benchmark to end-March 2014. We have amended the accounting rules applied to the sale of NPLs to domestic debt management companies so that no tax liability is being created, in line with the outcome of the EC infringement case.

2. In the attached MEFP, we set out our plans to further advance towards meeting the objectives of our macroeconomic program. In view of our performance under the program supported by the IMF, the EU, and the World Bank and the corrective actions taken, the Government of Romania and the National Bank of Romania (NBR) request a waiver of nonobservance on the missed performance criterion and completion of the first and second reviews. We intend to continue to treat the arrangement as precautionary.

3. The program will continue to be monitored through quantitative performance criteria and indicative targets, structural benchmarks and consultation clauses, during quarterly reviews in 2014 and semi-annual reviews afterwards. We propose the establishment of quantitative performance criteria for March 31, 2014 and June 30, 2014 (MEFP, Table 1). We propose to modify the structural benchmark on launching an IPO for Hidroelectrica (end-June 2014) by increasing the amount from 10 to 15 percent of the government's shares, and dropping the reference to the planned capital increase. Additionally, we propose to modify the structural benchmark on the commitment control system for operation in all general government entities to facilitate monitoring. We also propose to modify the structural benchmark on the covered bond legislation so as to specify submission to

parliament as the required action. As detailed in the MEFP and TMU, we propose five new structural benchmarks, one prior action, and one new indicative target against which to measure progress under the program (MEFP, Table 2). The Technical Memorandum of Understanding (TMU) explains how program targets are measured. We request a rephasing of the availability dates for the purchase associated with this review and the following reviews. The third review of the program will take place on or after June 25, 2014, and the fourth review on or after September 28, 2014.

4. We believe that the policies set forth in the letter of September 12, 2013 and in this Letter are adequate to achieve the objectives of our economic program. We stand ready to take additional measures as appropriate to ensure achievement of these objectives. We will consult with the IMF and European Commission (EC) before modifying measures contained in this Letter and the attached MEFP or adopting new measures that would deviate from the goals of the program, and will provide the IMF and the EC with the necessary information for program monitoring.

5. We authorize the IMF and the EC to publish the Letter of Intent and its attachments, and the related staff report. This letter is being copied to Mr. Olli Rehn.

Sincerely,

/s/
Victor Ponta
Prime Minister

/s/
Mugur Isărescu
Governor of the
National Bank of Romania

Romania: Memorandum of Economic and Financial Policies

Recent Economic Developments and Outlook

1. Economic growth picked up in the first three quarters of 2013 with real GDP growing 2.7 percent, supported by strong export performance, while domestic demand remained subdued. Economic activity was driven mostly by robust industrial output and the abundant harvest. We expect annual growth of around 3.5 percent for 2013. Higher exports were mainly driven by sales of machinery and transportation equipment, against the background of greater external demand including from non-EU countries. At the same time, low domestic demand for energy including because of improved efficiency, contributed to a slowdown in imports. As a result, the current account deficit is expected to have narrowed significantly in 2013 to around 1–1¼ percent of GDP from 4.4 percent of GDP in 2012, mainly reflecting improvements in the trade and services balance. CPI inflation started to decline as expected in the second half of the year and dropped to 1.6 percent in December 2013 and further to 1.1 percent in January 2014, due to a good harvest, a favorable base effect, a reduction in VAT on flour and bakery products, as well as a persistent negative output gap and improved inflation expectations. Annual core inflation has also fallen from 2.9 percent in June to -0.1 percent in December and January of the current year. The unemployment rate reached 7.1 percent in December, down from 7.3 percent in July through November.

2. For 2014, real GDP is projected to advance by 2.2 to 2.5 percent. Better absorption of EU funds is set to support a pick-up in investment. At the same time, some firming in private consumption is expected on the back of a general improvement in confidence and an increase over time in real disposable income. CPI inflation is projected to decline further in the first half of 2014 before returning to the upper part of the central bank's target band in the second half of 2014, largely due to base effects and the impact of excise taxes. The current account deficit is expected to stay between 1 and 1½ percent of GDP in 2014. Risks to the economic outlook are broadly balanced: while final data on the agricultural and industrial output in 2013 could still surprise on the upside, credit growth appears constrained by both supply and demand factors, which could hinder the recovery in domestic demand. On the external side, Romania remains vulnerable to adverse developments in international financial markets and subdued growth in the euro area. Prudent policy implementation, which has contributed to a substantial narrowing of spreads, will be crucial in maintaining confidence and safeguarding policy buffers going forward. Standard & Poor's raised the outlook on its ratings of Romanian debt to positive from stable in November 2013.

Fiscal Policy

3. In 2013, the preliminary fiscal deficit was 2.5 percent of GDP (in cash terms), which implies a reduction in the ESA-based structural deficit by at least 0.4 percent of GDP in line with the EU's Stability and Growth Pact (SGP) rules. However, the cash deficit target under the program, set at the time of the program approval, was missed by a small margin, primarily due to higher EU cofinancing. At the same time, revenues underperformed reflecting lower personal income and goods and services taxes due to a less-tax rich recovery and weakened collections around mid-year following a

restructuring of the tax administration. Non-tax revenues also fell on lower dividend payments from public institutions. The revenue shortfalls were largely offset by lower than expected social transfers, spending on goods and services, and lower interest payments. While reimbursable spending on EU funded projects was below target, spending on national cofinancing exceeded projections. Arrears declined at both the central- and local- government level, meeting the program targets.

4. For 2014, we will continue the gradual adjustment process and have approved a budget consistent with a headline deficit target of 2.2 percent of GDP in cash terms. Given our recent success in accelerating the absorption of EU funds, the deficit ceiling is 0.2 percent of GDP higher compared to the deficit target envisaged in the September MEFP. This is to create room for more cofinancing of EU funds (in the form of an adjuster described in the TMU) and will support growth-enhancing investment while staying on track to reduce fiscal vulnerabilities. The budget envelope implies a minimum structural effort of 0.3 percent of GDP in 2014 (cumulative 0.7 percent of GDP in 2013–14, ESA based).

5. The budget envisages a RON 1.5 billion increase in the wage bill, less than projected nominal GDP growth. The minimum wage increased from RON 800/month to RON 850/month in January 2014, with a further increase to RON 900/month planned in July 2014. The cost of raising the minimum wage is embedded in the public sector wage bill. The Government will continue to adjust the size of the public sector, through attrition and by identifying redundancies to ensure a faster pace of implementation towards the wage grid. An additional allocation following a court ruling of 0.3 percent of GDP is included in the wage bill. Public pensions will be increased by 3.75 percent in line with the pension law. Final payments towards implementation of the Payments Directive are also budgeted. Starting January 1, 2014, the second step of the planned increase of the Guaranteed Minimum Income was implemented. To support growth-enhancing projects, we will increase the allocation for reimbursable funds.

6. To reach the deficit target, we implemented additional measures. Starting with 2014, we introduced a formula to index excise taxes to inflation. The base on property taxes for companies was expanded to include special structures. Royalties on mineral resources other than oil and gas were increased by 25 percent. The increase in the minimum wage will also generate additional revenues. To ensure that sufficient financial resources are available and hence minimize risks for arrears and deficits, we will align property taxes accruing to local governments with the increased devolution of spending assignments to the local governments currently being envisaged (see paragraph 14). As already provided for in the Fiscal Code, property tax rates for individuals can be increased by 20 percent at the discretion of local governments. To address local government arrears, the Fiscal Code already includes provisions.

7. On the expenditure side, to safeguard against revenue collection uncertainties, we have deferred the commitment of investment and subsidy spending of about 0.1 percent of GDP until the second half of the year. We will also not release the budget's 10 percent buffer, which applies to certain expenditure categories (about RON 2.3 billion, 0.3 percent of GDP) before the second budget rectification in 2014. Moreover, an unallocated amount of RON 220 million will be used to facilitate the reduction of state-owned railway company arrears.

8. **Tax policy:** From September 2013, we reduced on a temporary basis the VAT on flour and bakery products to 9 percent and identified countervailing measures in excises to offset the budgetary impact. We initiated an analysis of the impact of this measure and will provide the requested data on VAT payments, including the number of registered VAT payers in this sector to evaluate the progress in compliance. During 2014, we will assess the efficiency of this measure and decide whether it will be applied on a permanent basis. We will prepare a strategy for reforming property taxes and the valuation system, which will introduce the principle of use but be based on owner as the primary taxpayer. An inter-ministerial working group is preparing a strategy for a new oil and gas taxation regime. We will establish a new regime that takes effect from 2015 through 2024, discussed with all stakeholders. Following recent IMF technical assistance, we have requested additional support to help us develop an action plan for the implementation of these taxes. In this context, we will ensure that the mineral agency (ANMR) provides all necessary resource data to relevant parties consistent with national security concerns. We will seek amendments, including lowering the threshold, to the draft lump sum tax law before Parliament takes a vote on the law.

9. The Ministry of Public Finance and the Ministry of Labor, Family, and Social Protection will undertake a comprehensive analysis to assess the performance of the second pillar of the pension system and its implications for the sustainability and adequacy of the pension system and on the development of the Romanian capital market. We are also assessing options to reduce the tax burden in a budget neutral way.

10. In order to stimulate the business environment and reduce the labor tax wedge, a main goal of the Government is a reduction in the social security contribution rate. To this effect, we will seek to implement in the second half of 2014 a significant reduction in the rate. Any such rate reduction will be conducted in a budget neutral manner, with an emphasis on base broadening measures. The reduction will safeguard the stability of the social security system, the soundness of public finances, and promote program objectives. Towards this goal, we will conduct a feasibility study that will be discussed with all stakeholders. The conclusions of the study will be agreed with the EC, IMF, and World Bank.

11. We will implement measures for the 2015 budget based on the tax expenditure report, which is currently being drafted. We will consult with the IMF and EC staff before undertaking any further changes of the tax system.

12. In order to lock in the benefits of the previous fiscal adjustment efforts, we will undertake efforts to strengthen fiscal institutions. Key areas of reforms will include:

13. **Fiscal Compact and medium-term budget:** In compliance with the EU fiscal governance requirements, we have amended the Fiscal Responsibility Law to integrate structural fiscal targets and corrective actions in case of deviations. We will seek to target an average structural effort of ½ percent of GDP until a medium-term budgetary objective (MTO) of 1 percent of GDP deficit is reached. Under this path, we expect to reach the MTO by 2015. We will also seek to shift to a medium-term budgetary framework.

14. **Fiscal decentralization:** We plan to implement a public administration reform that will decentralize some of the tasks from the central government to the local governments, ensuring the financial resources needed for these tasks in a budget neutral way and safeguarding the integrity of payments and controls. Before enacting any legal changes, we will present the new decentralization law, in accordance with the decision of the Constitutional Court, accompanied by a substantiation note in which we will clarify the responsibilities of the local governments, the costs related to these responsibilities, the financial resources needed, and the timetable for implementation. The draft legislation will be presented and discussed with relevant stakeholders. Clear guidelines on assigning wages will be prepared. Resources will be allocated commensurate with these responsibilities. The draft legislation will thus identify local government financing mechanisms to cover the costs of the increased responsibilities. These measures are necessary to safeguard public finances against higher deficits or arrears in the future. We will also monitor closely that local governments adhere to the deficit and debt limits set in legislation and we will apply the insolvency procedures if needed, as spelled out in Emergency Ordinance 46 (2013).

15. **Public financial management:** We will seek to advance the reforms currently underway with the goal of improving the commitment control and fiscal reporting systems, preventing arrears, and better managing fiscal risks.

- To help bring arrears under control, especially at the local government level, we have started publishing, on a monthly basis from end-September 2013, arrears reports, by territorial administrative unit. We will maintain arrears for the central and local governments at a low level consistent with the targets under the program. The Court of Accounts conducted audits of the disputed invoices presented to the local governments (360 million lei) in early 2013 and prepared a report based on the audits findings. The report noted that the arrears in dispute resulted from contracting for and receiving goods and services without proper budget authority and the under-reporting of the related invoices. The disputed amounts are therefore the obligation of the contracting local officials, which are contesting the findings of the Court of Accounts. We made central government transfers to local government units to cover the unpaid bills that represent valid liabilities of the government as verified by the Treasury, which in turn were used to cover the suppliers' payable taxes. We will ask the local governments to provide an update of the amount of local-government arrears in dispute by end-March 2014. The central government will ensure stricter control of the local government unit's total spending, consistent with Emergency Ordinance 46 (2013).

- We have made progress in the implementation of the commitment control system. We have approved a government emergency ordinance to provide standard definitions of commitments in September 2013. We developed a commitment control application, which supplements a new data warehouse and the existing treasury application to form the commitment control system. By end-January 2014, all users in the identified three pilot entities (Ministry of Public Finance, Ministry of Communication, and District 6 of the City of Bucharest) were connected and are starting to use the new commitment control system. By end-April 2014, the system will produce for all pilot institutions reports showing, at the minimum, approved budget, committed amounts, and paid amounts (reset structural benchmark). We intend to make the system available for operation (connected, tested, trained, and all functionalities in place) in all general government entities, as a pilot, by end-June 2014 (structural benchmark). In preparation of this transition, we started pilot testing on several public units in early December 2013.

- We continue working on the consolidated fiscal reporting system; capacity constraints hamper achieving rapid progress. The Government plans to request additional technical assistance from the IFIs on this project. We will define the standard reporting forms, including financial statements and reports of key fiscal aggregates (derived from the cash balance), and roll out the new system to all government entities by June 2014 (i.e., sending the trial balance using the system) (structural benchmark). We will run in parallel with the existing system until the end of 2014. Consolidated general government accrual based financial statements and ESA95 based reports will be prepared from the system and published from June 2015 (the first sets of reports will be for the year ended December 31, 2014), be reconciled with each other and with cash-based budget execution reports (structural benchmark).

- To improve fiscal transparency and ensure more consistency with ESA, we have requested that the IMF undertake a fiscal transparency assessment. A mission related to the assessment will take place in February 2014.

- The budget report contains a discussion on fiscal risks. This commenced with the 2014 budget. Future reports will be more comprehensive and extend the discussion on risks to include all legal requirements and will elaborate further on and quantify risks related to forecast expenditure and revenue, contingent liabilities, the debt composition, the banking system, all PPPs, all state-owned enterprises (SOEs), and natural disasters.

16. **EU funds absorption and public investment planning:** A key priority of the Government is to improve budgetary planning and project prioritization. This will also help to increase absorption of EU funds with a view to creating fiscal space and supporting economic growth. We have already made good progress in the agricultural, structural, and cohesion funds absorption as the cumulative absorption rate reached 33.5 percent for structural and cohesion funds and 67 percent for agricultural funds at end-2013 (from an average of 20.2 percent at end-2012). Further efforts are required to reduce decommitment risk in 2015, as the EUR 2.8 billion of funding subject to decommitment risk in 2014 is less than anticipated expenditures in 2014.

- We will better prioritize capital projects. We have staffed the Public Investment Evaluation and Monitoring Unit at the Ministry of Finance. This office will help strengthen quality control in the preparation, prioritization, appraisal and management of new significant public investment projects financed by the central government. In September 2013, we approved a government emergency ordinance defining a prioritization criteria framework for significant public investment projects. We will adopt norms to guide the application of the framework by end-March 2014, including comprehensive reporting requirements. In October

2013, we approved, by government memorandum, a list of prioritized projects, based on the prioritization criteria, to help prepare for the 2014 budget (structural benchmark). All new significant public investment projects financed by the central government will be subject to the prioritization criteria and vetting by the Public Investment Evaluation and Monitoring Unit.

- We will reappraise the significant projects according to the approved investment prioritization norms. Based on this exercise, we will identify a list of projects to be cancelled in time for preparation of the 2015 budget. The list of the local government projects that will no longer be cofinanced by the central government in 2014 will also be approved and published. We will introduce a process of consultation with local governments to review and prioritize local government projects with a view to cancelling the non-performing projects. These are necessary steps to ensure sufficient resources for the Government's high priority projects.

- We will seek to maximize the EU funding for projects that need cofinancing of local governments. To this end, the Ministry of Regional Development will update and improve the database of prioritized local government investment projects and publish the list of projects included in the budget on the website together with their rolling three year budgetary projections by end-March 2014.

- We established an inter-ministerial committee to make an initial assessment about pursuing potential PPPs earlier in the project life cycle. We will strengthen MOPF capacity to (1) provide inputs to the PM/Line ministries unit to develop a methodology for identifying and evaluating fiscal commitment to PPPs; (2) assess the affordability of PPP fiscal commitment as an input to approval of any initiative; and (3) develop guidelines for incorporating PPP projects in decision-making at the level of MOPF at various stages of the PPP project life cycle (identification, preparation, bidding, implementation).

- We consider the Comarnic-Brasov highway project a priority project of the Government. We are committed to carry it out at least cost and in a fiscally affordable way. We have made a budgetary allocation to cover the potential risks to the budget from this project. For 2014 and 2015, this will amount to RON 400 million and RON 1,200 million respectively. If we reach financial closure of the PPP and Eurostat does not decide in 2014 that this is an off-budget project, the allocation will be used to reduce the cash deficit. This is provided for in the budget law. We understand that multilateral financiers, such as EIB, IFC and EBRD, will get involved in the project only if the structure of the concession agreement and the proposed project implementation arrangements meet their requirements. This will enable the multilateral financiers to engage, with the sponsors and the awarding authority, in a due diligence process with the view to seeking approvals from their respective governing bodies. The due diligence will aim to confirm that the project is economically, technically, environmentally, financially and procurement-wise sound and viable and that it meets the standards of the multilateral financiers and the provisions of all relevant EU Directives.

- We will prepare by end-March 2014 an implementation mechanism for EU funding as part of our medium-term budget planning, in compliance with our sectoral strategies. This does not replace the already established mechanism for assessing the eligibility under the EU co-funded programs. In addition, capital projects financed from EU funds are already closely monitored to ensure the achievement of monthly payment targets.

- We are committed to submit a new partnership agreement by end-April 2014. We have prepared medium-term financial projections that properly identify the fiscal implications of EU funded projects (structural benchmark) and allow proper monitoring of the spending on EU funded projects by the managing authorities. We will identify by end-March 2014 the implications for the budget due to the amounts related to the 2007–13 programming period at risk of not being operational at end 2015. We will seek to expedite the adoption of the transport master plan and the administrative reform strategy, documents critical for the programming and implementation of EU funds in the 2014-20 programming period.

- To allow greater flexibility in financing of EU funded projects given lags in reimbursement, net lending of EU projects will be provided within a ceiling on net lending of RON4 billion for 2014 (set as an indicative target).

- In 2014, we will ensure that non-eligible spending for EU co-financed projects is limited to RON1 billion.

17. **Unified Wage Law:** We will ensure the sustainability of the public wage bill and will establish a more efficient and equitable public sector. Towards this objective, we will seek to implement the Unified Public Wage Law within the available budgetary envelope. We commit not to introduce a stimulente regime in any government agency and we will amend the government ordinance to remove the stimulente in ANAF. The MOPF will develop staffing plans based on ongoing modernization efforts in the Treasury and ANAF. A methodology for determining staffing levels in subnational governments will be developed while balancing local responsibilities with fiscal prudence. This will be done in accordance with decentralized responsibilities and after cost standards are developed by the responsible line ministries. In the meantime, the Government will continue to adjust the size of the public sector, through attrition and by identifying redundancies to ensure a faster pace of implementation towards the wage grid. We will consult with the IFIs before making changes in the public employment policy and the Unified Wage Law.

18. **Tax administration:** With a view to raising revenue collection and efficiency, and address recent revenue underperformance, we will, with immediate effect, intensify our efforts to monitor all aspects of tax collection while continuing with our comprehensive reforms of the tax administration (ANAF):

- We set up a high-level task force in October 2013 to better understand the low revenue collection in the third and fourth quarters of 2013. We found that it was to a limited extent reflecting the ongoing reorganization of ANAF. We are allocating additional resources to monitor more closely new business registrations, filing activity—especially for large tax payers—payments, stock and flow of arrears, number of audits conducted, and number and value of installment agreements signed. The task force will also be responsible for ensuring that on-going revenue collection activities will not be affected by the restructuring. We also set up regional task forces charged with meeting revenue collection targets.

- To facilitate monitoring and public communication of the efforts underway, starting end-December 2013, we provided an initial quarterly progress report on the number of completed audits in the large taxpayers unit and high net wealth individuals unit, and number of installment agreements signed for large taxpayers and medium-size taxpayers to clear tax arrears as well as collection targets based on these actions. Based on the agreed targets for 2014, we will provide subsequent progress reports commencing with the report as of end-March 2014 (structural benchmark). No government guarantees will be used for the tax installment agreements.

- As part of ANAF restructuring and modernization, we created eight regional directorates in September 2013 and will set up 47 local offices by 2015. We reallocated around 1,700 staff to prevention and control activities, and we will increase resources in the Bucharest Region to combat fraud. The positions in the ANAF's new anti-fraud department will be filled following strict selection procedures. We will provide additional professional training to all staff involved in combating tax evasion.

- We are committed to accelerate progress on our High Net-Wealth Individual (HNWI) taxpayers initiative. The Fiscal Verification Unit (FVU) will continue the initial phase of its first application of indirect audit techniques; from the 30 pre-verifications started in 2013, 24 were completed by end-December 2013 and the remaining will be completed by end-March 2014. The FVU will commerce phase two by initiating verifications on individuals resulting from the original grouping that meet the un-sourced income requirements designated in the Fiscal Tax Code within 60 days of such determination.

- Voluntary compliance, i.e. the ratio of return submitted on time to expected return, is improving. We have improved the quality of our personal income tax audits more generally. We will strengthen our auditing further using the indirect proofs method, expanding the definition of un-sourced income and clarifying the taxability of dividend payments, which are currently often disguised as non-taxable loan repayments to businesses. To help us achieve these goals, we have undertaken training programs with the assistance of partner-country tax administration specialists and IMF technical assistance.

- We will conduct a pilot structural compliance project targeted at undocumented labor and tax evasion, in line with the EU version of the Compliance Risk Management Model. The design of the project will be finalized by end-February 2014. The process will be launched with a press release explaining the project to the public by end-May 2014 (structural benchmark). Audits, jointly organized with the Labor Inspectorate, will be conducted during the second half of 2014. This pilot program is expected to increase voluntary compliance and reduce tax evasion for labor and raise awareness nationwide on the related issues.

- We also aim to develop taxpayer services, for example, offered through ANAF's portal by end-June 2014 and by ensuring that the interpretation of the tax law is unambiguous. To this end we will issue a common procedure with the MOFP and set up a single channel dealing with all enquiries on tax law interpretation by end-December 2014. Moreover, we will streamline the VAT reimbursement procedures based on a risk analysis, in order to significantly diminish the burden on tax audit in this field and for decreasing the time needed for solving refund cases by June 2014. We will set up a central database that will allow us to manage and assess together with local authorities data regarding taxes and contributions owed to the general consolidated budget as well as information on properties. This will be an important source of information for taxpayers and should also raise compliance by end-December 2014. Finally, we will make all efforts to ensure SMEs in distress are granted payments terms in installments to clear tax arrears.

19. **Health care:** We are preparing a comprehensive reform of the healthcare system, which should contribute to make the system financially sustainable, raise the efficiency of healthcare spending and improve health outcomes. The reforms consist of four pillars: (i) a minimum health package, (ii) a basic health package, (iii) revision to the list of reimbursable medicines, and (iv) revision to existing and introduction of new national health programs. The new minimum health package aims at providing prevention services (assessment of health risks) and treatments to the uninsured population, in addition to emergency services that they are currently entitled to. The basic health package, for the insured population, is based on streamlining hospital services by reducing the redundant capacity for inpatient services in line with the national health strategy and shifting the delivery of health services away from hospitals to primary health care providers and medical ambulatory services; developing institutional capacity in Health Technology Assessments and evidence-based protocols (Agency for Evaluation and Quality in Health); and allocating more resources towards primary and secondary preventive care. Moreover, under the new basic package, some services are excluded from the current benefits of the insured population (which might be covered by private insurance companies), while more critical services are added.

20. The new services to be started in 2014 under the health care reforms will be limited to the available budget allocation. The design and costing of the basic package was completed in January 2014 within the existing budget envelope, delineating the options for private sector involvement (structural benchmark from end-September 2013). The process involved discussions with various stakeholders, including public consultation on the website of the Ministry of Health. The modalities of private sector financing will be defined by end-September 2014. The updated package of the National Health Programs will be implemented by August 2014 within existing budget allocation, while the implementation of the minimum health package will begin in January 2015. The additional cost of the new list of reimbursable medicines will be financed through a revised claw-back tax on pharmaceutical expenditures and achieved savings from revised pharmaceutical policies as well as an update of the list, for instance in line with the NICE study. Quarterly audits will be conducted regarding the prescription of expensive medicines to prevent over-prescription and ensure the sustainability of the claw back tax system. The new claw-back system has already been discussed with the stakeholders in the pharmaceutical industry. The revised claw-back tax will

provide a lower tax rate for generics and will be budget-neutral compared to the current tax. The Government will adopt the reforms by May 2014, including the revised services to be started in 2014.

21. As part of the comprehensive health strategy, we will implement the following measures to address health sector financial imbalances and modernize its operations:

- To increase the share of spending on primary and ambulatory services in total health spending, we revised in December 2013 the list of services, which can be contracted with primary care providers as part of the 2014 health care framework agreement. We will ensure that expenditures on continuous admissions to hospitals will be reduced and the risk of future arrears eliminated.

- We will establish an adequate institutional framework and allocate necessary resources to properly run the central acquisition system. The system is already operational, covering currently four out of ten main groups of medicines, medical devices and medical supplies. The Ministry will seek to expand coverage to all ten groups. The Ministry of Health will prepare an action plan with a view to reaching government level agreement on defining an expedited timeline on the centralized procurement process. The related savings per unit cost are expected to be higher than the savings obtained by running the local tender procedure while decreasing the variability through standardization will impact the quality of care. By end-February 2014, the NHIH paid off any remaining outstanding payments to the pharmaceutical sector, thereby completing the implementation of the EU Late Payment Directive.

- We will continue to monitor public hospital budgets to ensure that they are consistent with the expenditure programmed in the general government budget and continue to publish online up-to-date financial statements of all public hospitals. We will collect and analyze the cost of service provision across hospitals with the aim of developing benchmarks in the future.

- The National Printing Office produced 4½ million patient cards by end-2013 and will produce the remainder (10½ million) for the eligible population by September 2014.We will accelerate the distribution of these cards. To promote awareness and encourage the increased use of generic drugs, we will print from March 2014 the patient's co-payment required to receive the benchmark priced medicinal product (zero or lowest co-payment) and the patient rights with respect to pharmacists' obligation to provide full information on available drugs on the printed prescription.

- We will continue to implement the hospital rationalization strategy, including through streamlining hospital services, shifting the delivery of health services to outpatient services, building physical and functional integrated referral networks (including regional hospitals) and the referral system that surrounds them from the primary health care to post-hospital care as well as patient pathways in the health system in order to consolidate and reduce redundant capacity. For this we will seek financial support from the EC and World Bank over the period 2014–2020.

22. **Debt management:** In line with our debt management strategy, we will continue to work towards improving our risk management, in particular towards lengthening the average remaining maturity of our debt. For example, we issued 30-year U.S. dollar denominated Eurobonds for the first time ever, at favorable financing conditions in January 2014. We will update our Debt Management Strategy for 2014-16 consistently with the annual Borrowing Plan published at the end of 2013. We have consolidated the fiscal buffers, to achieve our objective of covering four months of gross financing needs to protect against unforeseen external shocks. The net interest paid on these buffers represents a necessary cost for insurance against shocks. We will expand the share of issuances on the domestic market in order to develop the domestic bond market. At the same time, we intend to smooth volatility in the treasury account by issuing shorter maturity treasury bills. We are making good progress on electronic trading platform. We are continuing our efforts to create the necessary framework for liability management operations as well as widen the investor base and improve outreach efforts. We are receiving technical assistance financed with EU funds and implemented with support of the World Bank to strengthen the debt management department. We will ensure that increases in guarantees issued remain prudent.

Monetary and Exchange Rate Policy

23. Annual headline inflation decelerated sharply since July 2013. At 1.9 percent in September, it fell within our medium-term target band of 2.5±1 percentage point and declined further to 1.6 percent in December and 1.1 percent in January 2014. The deceleration was mainly on account of the reversal of base effects for food prices, the abundant harvest in 2013, and the cut in the VAT rate for flour and bakery products, as well as the improvement in inflation expectations against the background of slack in the economy. We currently project annual headline inflation to decline temporarily to levels below the target band, then gradually return into the band, and move into its upper part in the second half of 2014. We also continue to closely monitor annual core inflation, which has been below zero since October and is expected to remain around similar levels through mid-2014.

24. We further lowered the policy rate during September 2013-January 2014 by a cumulative 100 basis points to 3.50 percent as headline inflation was seen to continue its declining trend, in the context of persistent negative output gaps. Reflecting these cuts, average interest rates on new loans reached historical lows in December at 7.6 percent; a less pronounced development took place in deposit yields. In addition, in January we reduced the high minimum reserve requirements (MRRs) by three and two percentage points for leu- and foreign exchange denominated liabilities, respectively, with a view to gradually bring the MRRs closer to levels practiced by the ECB and prevailing in most other EU countries. We discussed the policy outlook with IMF and EC staff as part of the inflation consultation mechanism. We agreed that anchoring inflation expectations and dealing with volatile international capital flows continues to require a prudent monetary policy stance supported by the consistent implementation of the macroeconomic policy mix. There is little

room left for further monetary easing including interest rate cuts. We will closely monitor inflation developments following the recent easing steps to ascertain that inflation expectations remain firmly anchored, and market conditions remain favorable.

25. Base money creation has increasingly reflected treasury operations related to growing disbursements of EU funds. The resulting buildup of excess liquidity, which in the meantime has been mopped up, explained the divergence between interbank rates and the policy rate, which has complicated monetary operations. We will ensure adequate liquidity conditions in the banking system, while underpinning the good functioning of money markets and reducing the divergence between interbank rates and the policy rate in order to strengthen the transmission of monetary policy signals. To this end, we are considering a further narrowing of the interest rate corridor and a gradual reintroduction of liquidity absorbing operations. Going forward, the NBR will preserve the wedge between minimum reserve requirement ratios for foreign and domestic currency liabilities in order to discourage foreign-currency lending. Moreover, any further changes with respect to minimum reserve requirements would be implemented gradually, after evaluating the effect of previous steps, and taking into account the impact on inflation expectations.

Financial Sector

26. The Romanian banking sector maintains appropriate capital buffers, enhanced liquidity, and provisioning, but is still faced with pressures on asset quality, and from foreign bank deleveraging, while also remaining vulnerable to external shocks. Annual credit growth in real terms to both corporates and households remains negative year-on-year with -6.5 and -2.7 percent, respectively, at end-2013. Non-performing loans (NPLs) closed the year at 21.9 percent of total loans, the same level as in November, (compared to 18.2 percent at end-2012), reflecting the difficult economic environment, stagnant credit growth, and slow removal of fully provisioned NPLs from bank balance sheets. Total provisions for NPLs (IFRS plus the total prudential filter) cover 89.8 percent of NPLs while the IFRS provisioning ratio (without prudential filters) increased to 67.6 percent at end-2013 (61 percent at end-2012). In line with EU regulatory requirements, the prudential filter started its scheduled phase-out period at end-January 2014. It was reduced by one fifth, and will be gradually eliminated until 2018. This measure will have a positive impact over the level of own funds that are taken into account for determining the level of the capital adequacy ratio due to the gradual decrease of the amount of prudential filters previously used as deductions from own funds; the phase-out will lead to a gradual transition of the total provisioning for NPLs towards its IFRS value. In accounting terms capital will not be affected and it is expected that it will facilitate the resumption of credit growth over time. The provisioning requirements along with slow lending activity and relatively high cost base led banks to obtain a positive financial result in 2013 (RON 498 million or 0.1 percent ROA based on preliminary data).

27. The capitalization of the banking sector remained strong at 15 percent at end-December 2013 albeit with some differences between banks. The level of system-wide provisions significantly increased in the second half of 2013 mainly as a consequence of the interim audit of the banks June financial statements followed by the on-site inspections performed by NBR to the first 20 large

banks on IT adequacy and loans restructuring practices. A new NBR-mandated collateral audit in the last quarter of 2013 led to identify a system-wide provisioning gap of RON 800 million, which was closed by year-end. While the liquidity position has been less restrictive than in previous years for the banking system as a whole, funding conditions are still uneven among some banks. The pace of foreign-owned bank deleveraging has accelerated in line with the rest of the region but remains orderly, with a parent funding decline of 30 percent since end-2011 (19 percent in 2013 alone up to December). As a result, reliance on local funding has increased, especially deposits, prompting a significant fall of the system-wide loan-to-deposit ratio to 105 percent at end-2013, from 117 percent the previous year. The risks from continuing parent funding retrenchment remain significant, especially if credit demand recovers, though they are mitigated by the lower prudential filter and minimum reserve requirements.

28. The NBR will continue to closely monitor and supervise the banking system and take any necessary measures to ensure that banks maintain sufficient capital and liquidity, in light of the uncertain economic environment which could pose further challenges with respect to asset quality, profitability and parent funding retrenchment for most banks. In that regard and in close coordination with the IMF and EC, the NBR will continue to regularly conduct top-down and bottom-up solvency stress tests as well as liquidity stress tests of the banking industry. A recent top-down stress test performed by the NBR for the 2013 Financial Stability Report illustrated that under an adverse scenario with a prolonged recession and 20 percent depreciation, the aggregate solvency ratio would decline by 4 percentage points to 10.8 percent (above the prudential NBR threshold), on the basis of the June 2013 CAR, with the overall banking system remaining resilient but also revealing that a few non-systemic credit institutions would need to raise additional capital.

29. The NBR and Deposit Guarantee Fund (DGF) will continue to coordinate the implementation of operational preparedness plans and the arrangements for the acquired bank resolution powers according to their competencies. An amendment to the Government Emergency Ordinance no. 99/2006 has provided the NBR with more flexibility and powers to stabilize the financial system to protect depositors and maintain public confidence in the banking sector. The bank resolution directive will be transposed ahead of the implementation deadline as a law adopted by the end of September 2014. The law will also clarify the role of DGF in financing bank resolution measures in line with the principles envisaged by the incoming EU Directive for deposit guarantee schemes. Based on the amended legal framework, the NBR will also amend the internal procedures for bridge-banks by end-September 2014. The details of the updated NBR contingency planning framework will be agreed with the IMF and EC staff. The NBR is preparing detailed contingency plans on an ongoing basis.

30. To avoid any perceived conflict of interest of its senior management, the DGF corporate governance principles will adhere to good international practices.

31. Consistent with ESRB and IMF recommendations, a macroprudential policy committee is being established, in which the NBR's leading role is reflected in the committee's voting structure.

32. The NBR will continue to closely oversee bank practices to avoid evergreening so as to ensure that IFRS loan-loss provisioning and collateral valuations, as well as the assessment of credit risk of restructured loans remain prudent and in line with good international practices and are properly supported by IT systems. The on-site inspections of banks' IT adequacy and loan restructuring practices for a sample of 20 banks finalized at end-2013 will be followed up by a similar inspection for the rest of banking institutions. The asset quality report will be updated with any new information coming from such assessment. In consultation with the IMF and EC, an NPL resolution action plan will be prepared by end-May 2014 (structural benchmark) and implemented by end-June 2014. The plan will establish the role of the NBR in the process, set out the responsibilities of supervised entities, and foresee changes to prudential regulations so as to avoid moral hazard and provide appropriate incentives for a timely balance sheet clean-up from unrecoverable loans.

33. The NBR will collect periodic and detailed supervisory data on restructured loans, including to SOEs, on a quarterly frequency. To ensure transparency, the NBR will publish aggregate data.

34. To foster the development of a viable distressed debt market, we have amended the accounting rules applied to the sale of NPLs to domestic debt management companies in such a way that a tax liability has ceased to be created; this treatment is in line with the outcome of the EC infringement case (structural benchmark met by end-December 2013).

35. To enable much needed longer-term bank funding instruments, we will approve the covered bond legislation by end-March 2014 as a law presented to Parliament for consideration through the emergency procedure (structural benchmark). Outstanding differences on the covered bond legislation with the Banking Association will be addressed so as to ensure a proper registration of the property claims. The MOPF recently passed an order on the new guarantee scheme for bank lending to SMEs that is more effective and operational as well as contributing to the de-euroization of banks' portfolios. It replaces the existing scheme.

36. The FSA should swiftly complete the integration of the former three supervisory authorities. Based on the assessment of the selected independent consultancy company on staff levels and the staff *per se*, an action plan will be elaborated within two months (from the date of the assessment made by the consultancy company) in order to rationalize the FSA. Following the assessment of the consultant, the FSA will perform a business optimization exercise. In addition, the FSA will also enhance transparency and public disclosure of all fees and commissions charged to the supervised entities. The FSA is performing a comprehensive fee structure comparison with other European countries, after which the very high fee structure, in certain areas, will be brought in line with best international practices.

37. Because preserving credit discipline among debtors contributes significantly towards enhancing financial stability, we will take all efforts to avoid the adoption of legislative initiatives dealing with personal insolvency that create a moral hazard and are open to widespread abuse by debtors as this would undermine credit discipline. Furthermore, in order to avoid threats to financial stability from the new provisions on abusive clauses in the law for the application of the civil

procedure code (that took effect October 1, 2013), we will ensure that the new specialized court is swiftly set-up (including the necessary budget allocations for the headquarters and the supplementary personnel: judges and clerks) and will take all necessary measures to ensure a harmonized application of these provisions, such as training of judges. If the new institutional arrangement of this specialized court does not succeed in avoiding financial stability threats, we will consult extensively with all relevant stakeholders as well as with the IMF and EC to come up with alternative solutions. Given the substantial NPL overhang, the authorities will remove, where possible, impediments to corporate and household out-of-court debt restructuring and NPL resolution.

Energy and Transportation Sector Reforms

38. Reforms that foster investment and better service delivery in the energy and transportation sectors are central to our efforts to stimulate growth in Romania. To this end, we are implementing a three-pronged approach to decisively improve the financial position, operating efficiency, and overall transparency of SOEs and the pricing framework in the energy and transportation sectors.

39. Measures to reduce existing arrears and prevent the accumulation of new arrears in state-owned enterprises comprise the first prong of the approach. We missed the December indicative target on the cumulative arrears of all central-government owned enterprises (SOE arrears). As a corrective measure, the Government will take a number of actions to reduce arrears in the first quarter of 2014 by more than the reduction implied by the original target path in order to meet the target for end-March. Three electricity service companies with arrears have already entered into voluntary liquidation procedures and payments from the budget will be made to partially clear arrears of state-owned railway companies to electricity suppliers as well as the arrears of the National Road Company. We will provide a report to the IMF that specifies the actions we took to significantly reduce the SOE arrears and achieve the end-March 2014 indicative target (prior action). We will also provide this report to the European Commission. Also, all line ministries with oversight of state-owned enterprises with arrears will submit to the MOPF action plans by end-March in order to reduce arrears in those companies by end-December 2014. In addition, we will strengthen the monitoring of the arrears situation inter alia through regular status reports to the MOPF and to the cabinet, improve the oversight function of the SOE monitoring unit (with World Bank support), and move to monthly data collection. Moreover, we will review and update the plans later in 2014 with the aim of reducing arrears to a de minimis level by September 2015. The plans will consider a wide range of options for arrears reduction, including placement of companies into insolvency or liquidation process. The MOPF will ensure that the ministries' plans are consistent with the overall arrears reduction path established under the program and prepare a summary report that clearly identifies the companies and the actions that will be taken to adhere to the overall path. This summary report will be provided to the IMF by end-April 2014 (structural benchmark).

40. Steps to improve the governance, transparency, and monitoring of SOEs form the second part of our approach. We have appointed the board of the state-owned hydroelectric power producer (Hidroelectrica by end-November 2013 in accordance with Government Emergency

Ordinance 109/2011 on SOE corporate governance (end-November 2013 structural benchmark). We are also working with the World Bank to hire an independent consultant to conduct an assessment of the implementation of the Government Emergency Ordinance (109/2011). When completed, the assessment will be published, and we intend to use the findings to improve emergency ordinance 109, by, among others, improving the SOE oversight function of the Ministry of Public Finance. Following the assessment, we will develop guidelines for its implementation across all ministries. Moreover, with a view to improve the management and performance of SOEs we will clarify and improve, with World Bank support, the roles and responsibilities of the various agencies that act as owners of SOEs on behalf of the state (e.g., line ministries, the MOPF, and other state agencies). In contrast, the SOE corporate governance law was not passed by the Parliament by end-September 2013. We now plan to wait for the conclusion of the independent assessment before obtaining the Parliamentary approval of the law. Among other provisions, the law would tighten the professional criteria of Board and management appointees and give legal responsibility to the MOPF to supervise its proper implementation.

41. We remain committed to enhancing the transparency of SOE operations to help ensure that all SOE transactions are consistent with creating value for the benefit of all Romanians. In particular, all new bilateral contracts of electricity producers will continue to be made transparently and non-discriminatorily at market prices through the OPCOM power exchange. We made significant progress in 2013 and the share of trading at OPCOM in Romania's electricity supply increased from 35 percent in 2012 to 73 percent in 2013. Annual reports on SOE performance will be published in accordance with provisions of the SOE corporate governance Government Emergency Ordinance. We will also make best efforts to address audit qualifications on the SOE's annual financial statements. While the 2014 budgets of SOEs were to be submitted to the MOPF one month after the approval of the state budget, there were some delays, particularly with the budgets of CFR S.A. and CFR Calatori S.A. We will have these budgets approved by mid-March 2014, the latest.

42. The third prong includes measures to improve the pricing framework and efficiency of the energy and transportation sectors. We will continue to implement the electricity and gas price road maps and the pass-through mechanism for electricity and gas purchases by the supply companies will continue to be applied. For electricity, complete deregulation of electricity prices for non-residential consumers was achieved by January 1, 2014, and for households it will be achieved by December 31, 2017. For natural gas, we increased regulated prices in October and January as called for in the gas price liberalization road map. We intend to implement the remainder of the road map to deregulate gas prices as planned to achieve complete price deregulation for non-residential consumers at the latest by December 31, 2015, and for residential consumers by December 31, 2018. We are considering completing deregulation of gas prices for non-residential consumers earlier than scheduled based on a risk assessment study. If necessary, such deregulation would be accompanied by a requirement for producers to sell a certain percentage of their gas production available for the competitive market and for wholesale suppliers to trade a certain percentage of their estimated sales by using the centralized gas trading platforms licensed by ANRE. ANRE will conduct a risk analysis, based on which it will decide on the early deregulation for wholesale suppliers. We will also continue to take steps to strengthen OPCOM as an electricity and gas trading platform, including

through ownership diversification. Moreover, the Government will prepare a new energy strategy to help ensure Romania's energy security and the realization of potential of the energy sector as an engine of economic growth through investment and exports.

43. We have made significant progress in implementing our privatization agenda. Through initial public offerings (IPOs), we sold 10 percent of the shares in the nuclear energy company (Nuclearelectrica) prior to October 2013 and 15 percent of the shares in the state-controlled natural gas producer (Romgaz) in November. Both IPOs were oversubscribed and generated about €450 million in gross proceeds. Of particular note, the Romgaz transaction was completed at the upper end of the price range. Also, the Romgaz IPO was the first time we issued Global Depository Receipts (GDRs) in conjunction with a public offering on the Bucharest stock exchange. We will apply the experience gained through the Nuclearelectrica and Romgaz transactions to the preparation of IPOs in other energy companies. In particular, we intend to issue GDRs or undertake a dual listing in conjunction with the IPOs of state-owned electricity supply and distribution company (Electrica) and Hidroelectrica. Except as provided for in the reorganization plan of Hidroelectrica as well as below for Electrica and Oltenia, we will not break up and/or merge the companies or the assets of the companies slated for IPOs. Other steps taken or to be taken to prepare for the upcoming IPOs, all of which are structural benchmarks under the program, include:

- **Electrica:** We hired a transaction advisor for the IPO in mid-September 2013. Work is currently underway to separate through liquidation three loss making regional service companies from Electrica and to take out Electrica's minority shareholdings in already privatized distribution companies prior to the IPO. We have also hired an international legal advisor to promote the offer abroad. Moreover, we will address the issue of nonpayment by CFR Infrastructura for its electricity purchases from Electrica ahead of the IPO.

- **Hidroelectrica:** We secured the repeal of our appeal of the ruling against the initial government decision to sell shares in Hidroelectrica before September 30. In December, we issued a new government decision for the sale of 15 percent of Hidroelectrica's shares and have selected a transaction advisor. In February, an Appeals Court placed Hidroelectrica back into insolvency until the legal claims of energy traders against the company are resolved. We remain committed to launch an IPO of Hidroelectrica, in line with the existing structural benchmark, as soon as possible after it exits insolvency.

- **Oltenia:** The transaction advisor has completed its financial, legal, and environmental due diligence work. We have initiated the selection procedure for hiring a consultant to conduct a coal reserve assessment. However, a significant number of material qualifications from the 2012 financial audit of the company need to be addressed. We will strongly encourage Oltenia's management to work closely with the transaction advisor to overcome these obstacles and prepare the company for the IPO, including the possible measures of restructuring or divesting the mine of Berbești, in order to diminish the company's arrears and make it more attractive to potential buyers.

44. Despite our efforts, the majority privatization of the state-owned freight railway company (Marfa) was not concluded before the expiration of the deadline set in the government decision approving the transaction. While the privatization was not concluded, the Romanian Competition Council has confirmed that a debt-equity swap conducted to lower arrears will not be considered state aid as long as there is a credible intention to privatize Marfa. In 2013, Marfa incurred an operating loss, which was within the overall operating balance target. To ensure the viability of Marfa, we intend to aggressively restructure the company and continue the privatization process. We approved Marfa's 2014 budget which is based on a list of specific restructuring measures, including a reduction in personnel costs, the sale of obsolete freight cars for scrap, and halting delivery to customers with arrears to Marfa, that will generate an operating surplus in 2014 and a positive cash flow. Marfa's management has already taken steps in this direction by recently securing new freight service contracts and starting discussions with the labor union on reducing personnel cost as provided for in the budget to start taking effect from end-March 2014. The Ministry of Transportation commits to fully support Marfa management as it implements these measures. Marfa's operating performance will continue to be monitored through the existing quarterly indicative target on the operating performance of the three main railway companies. We have also established a new quarterly indicative target on the accumulation of Marfa's arrears. The target is set at zero, excluding interest and penalties on arrears, for the remainder of the program and will provide an early indication of the success of the restructuring. The restructuring of Marfa is critical and reaching the indicative targets is a priority under the program. In the event that the restructuring does not yield the desired results, which will be reflected in missing the arrears target on Marfa, we will consider other options for moving the restructuring process forward including those noted in paragraph 39. In December we approved a government decision to continue with Marfa's privatization through a strategic investor, which is expected to occur in May 2015.

45. We met the December indicative target on the aggregate operating balance of the three largest railway companies and their subsidiaries. We will continue to work closely with the World Bank and European Bank for Reconstruction and Development (EBRD) to reform the rail sector with the goal of improving the financial and operational performance of railway SOEs and the quality of rail service. A key element of the reform process will be stopping the accumulation of arrears from Marfa and the state-owned passenger rail company (Calatori) to the state-owned railway infrastructure company (CFR Infrastructura) and the accumulation of arrears by the three railway companies with the central government and electricity providers. Based on 2014 budget subsidies we will approve budgets for CFR S.A. and CFR Calatori S.A. consistent with our commitments under the program. The budgets will provide for full financing of the above obligations. In addition, the 2014 subsidy payments, which will be made on a monthly basis, will be applied first to cover access and electricity charges and obligations to the central government with the remainder available for other expenses. This will likely require further restructuring of Calatori and Infrastructura. Measures to improve the operating and financial performance of these companies could include:

- **CFR Infrastructura:** We have agreed with the EBRD on a roadmap to address deficiencies in meeting the covenants and other terms of the EBRD loan agreement signed in 2012 and secure the disbursement of the second tranche of the loan based on progress in implementing the roadmap. We will also work with the EBRD on terms of reference to hire a consultant to develop a restructuring action plan. Moreover, we will approve a government decision to lease or close over 700 km of rail line. We intend to follow this measure with leasing or closure of another 900 km of rail line during the course of 2014. We estimate that these steps will generate annual savings of RON 70 million. We will continue to fill management and board positions in Infrastructura following the letter and spirit of the procedures specified in the SOE Corporate Governance ordinance (109/2011).

- **CFR Calatori:** Calatori's management has taken a number of steps to improve the company's operations including raising ticket prices by up to 10 percent in September and putting in place better controls over ticket revenue, reducing fuel consumption by 20 percent and the wage bill by 5 percent through attrition and reduction in working days, and stopping services on five unprofitable rail sections. By mid-March 2014 we will further amend the formula for calculation of the PSO to give more weight to passenger-train kilometers travelled.

46. We will continue the regulatory reform of the railway sector as well. Performance schemes related to delays have been elaborated and discussed among the relevant parties. The rail operators and infrastructure manager are planning to introduce them in their respective access contracts for 2014. A system of incentives for the infrastructure manager to reduce unit costs and charges has been elaborated in cooperation with the World Bank. We will introduce it in the 2014 addendum to the activity contract of CFR Infrastructura.

Labor Markets

47. The Labor Code continued to improve the functioning of the labor market, as the share of fixed term contracts picked up slightly from 8.2 percent of total active contracts in 2012 to 8.4 percent in 2013. We will continue to monitor the implementation of the Social Dialogue Law and ensure that any amendment will be undertaken in consultation with all stakeholders through the normal legislative process. Proposals on possible amendments from social partners received last December, if considered appropriate, will be submitted for discussion in Parliament. We will continue our cooperation with the International Labor Organization (ILO) to ensure that the current legislation respects core ILO Conventions.

48. In view of the high youth unemployment in Romania, we are implementing the National Job Plan adopted in April 2013 and developing indicators to monitor progress by April 2014. In addition, we plan to introduce further measures to improve the transition of young Romanians to the labor market. The Youth Guarantee Implementation Plan 2014-2015, approved by the Government in December 2013, which includes measures that qualify for support under the Youth Employment Initiative, was submitted for review to the European Commission. Pilot projects started under this initiative are expected to provide better information on career development and training to a targeted group of youth nationwide. The secondary legislation for the Apprenticeship Law that introduces a dual apprenticeship model and a law facilitating professional training stages for higher education graduates were adopted last December. The new work-based professional school and

vocational training scheme, now in its second year, is expected to attract a growing number of students and partner companies following the changes to the National Education Law introduced in December, which extended its duration by one year.

Legislative Initiatives

49. The Romanian constitutional court found the manner of promulgation of the insolvency code as an emergency ordinance and part of its contents to be unconstitutional. Therefore a new adoption procedure has started, whereby the insolvency code was approved as draft law by the Government and has been submitted to Parliament for adoption. We will continue our consultation with all relevant stakeholders in order to propose to Parliament, on occasion of the debates of the draft code, amendments aimed at better supporting the early rescue of viable firms and speedy exit of non-viable ones. These proposals will be prepared in consultation with IMF staff, at a minimum on: pre-insolvency procedures, creditor voting, priority financing, automatic stay, ranking of claims, notice requirements, means for preventing associates/administrators abuses which may lead to failure of the reorganization plan, increased transparency of the insolvency procedure, including ensuring public access to information related to associates/significant shareholders and administrators of insolvent company (through the Trade Register) (structural benchmark end-April 2014).

50. We will seek amendments to the draft Holding Laws, currently in the Parliament, in line with good international practices.

Table 1. Romania: Quantitative Program Targets

	2012	2013					2014					
	Dec	June	Sept	Sept	Dec		March		June		Sept	Dec
	Actual	Actual	Prog.	Actual	Prog.	Actual	Indicative	Prog.	Indicative	Prog.	Indicative	Indicative
I. Quantitative Performance Criteria												
1. Floor on the change in net international reserves (mln euros) 1/ 2/	16,344	3,922	3,922	6,326	4,622	7,343	250	-500	0	0	200	500
2. Floor on the general government overall balance (mln lei) 3/	-17,430	-6,629	-9,340	-8,143	-15,300	-15,771	-4,000	-4,539	-6,200	-8,230	-7,209	-14,712
3. Ceiling on the stock of central government and social security arrears (bn lei)	0.027	0.04	0.020	0.018	0.02	0.01995	0.02	0.02	0.02	0.02	0.0175	0.015
4. Ceiling on general government guarantees issued since end-2008 (face value, bn lei)	9.8	10.9	16.0	11.45	16.0	12.1	18.0	18.0	18.0	18.0	18.0	18.0
II. Continuous Performance Criterion												
5. Nonaccumulation of external debt arrears	0	0	0	0	0	0	0	0	0	0	0	0
III. Inflation Consultation												
6. 12-month rate of inflation in consumer prices												
Outer band (upper limit)	...	...	5.1	...	5.3	...	4.6	3.0	5.0	3.6	5.0	5.5
Inner band (upper limit)	...	...	4.1	...	4.3	...	3.6	2.0	4.0	2.6	4.0	4.5
Actual/Center point	5.0	5.4	3.1	1.9	3.3	1.6	2.6	1.0	3.0	1.6	3.0	3.5
Inner band (lower limit)	...	...	2.1	...	2.3	...	1.6	0.0	2.0	0.6	2.0	2.5
Outer band (lower limit)	...	...	1.1	...	1.3	...	0.6	-1.0	1.0	-0.4	1.0	1.5
IV. Indicative Target												
7. Ceiling on general government current primary spending (excl. EU funds and social assistance, mln lei) 3/	134,330	70,412	106,300	105,570	147,509	144,560	36,700	36,500	74,400	73,000	109,000	150,500
8. Floor on operating balance (earnings before interest and tax, net of subsidies and one-off adjustments to income due to financial or accounting operations) of key SOEs (as defined in paragraph 22 of the TMU (bn. lei)) 3/	-3.1	-1.0	-1.6	-1.3	-2.3	-2.2	-0.5	-0.7	-0.8	-0.9	-1.2	-2.1
9. Ceiling on outstanding payments past due of all central-government owned enterprises (as defined in TMU, bn lei) 4/	12.7	8.3	7.5	7.0	5.6	7.2	4.7	5.4	3.7	4.6	3.9	3.4
10. Ceiling on stock of local government arrears (bn lei)	0.84	0.14	0.30	0.24	0.30	0.20	0.30	0.30	0.30	0.25	0.20	0.20
11. Ceiling on stock of net Treasury loans for EU-funded projects (mln lei) 3/	...	1,546	3,000	2,004	3,000	1,852	3,000	4,000	3,000	4,000	4,000	4,000
12. Ceiling on outstanding payments past due of CFR Marfa (as defined in TMU, mln lei)	...	...	...	...	...		...	99.2	...	99.2	99.2	99.2
Memorandum items:												
Central government hospital arrears (bn lei)	...	...	...	0.011	...	0.014	...	...	...	...	...	...
Local government hospital arrears (bn lei)	...	...	...	0.045	...	0.053	...	...	...	...	...	...

1/ The end-December 2012 figure is a stock. Reported at program exchange rates and gold price.

2/ The December 2013 target is adjusted upward by EUR 700 million to reflect the higher than projected program financing due to the drawings under the World Bank DPL-DDO.

3/ Cumulative figure during calendar year (e.g. September 2013 figure is cumulative from January 1, 2013). The September 2013 target is adjusted downward by RON 159 million for higher than programmed spending on national cofinancing of EU funded projects. The December 2013 target is adjusted downward by RON 600 million for higher than programmed spending on national cofinancing of EU funded projects.

4/ Starting end-March 2014, outstanding payments past due accumulated and reported by companies while they are under insolvency procedures are excluded from the target. These past due payments amounted to RON 438 million for end-December 2013.

Table 2. Romania: Performance for First and Second Reviews

	Measure	Target Date	Comments
Prior action			
1.	Provide a report to the IMF on the completion of the actions specified in Section L of the TMU to significantly reduce SOE arrears		
Quantitative performance criteria			
1.	Floor on net international reserves	December 31, 2013	Met
2.	Floor on general government overall balance	December 31, 2013	Not met
3.	Ceiling on central government and social security domestic arrears	December 31, 2013	Met
4.	Ceiling on general government guarantees	December 31, 2013	Met
5.	Non-accumulation of external debt arrears	December 31, 2013	Met
Quantitative Indicative Target			
1.	Ceiling on general government current primary spending	December 31, 2013	Met
2.	Floor on operating balance of key SOEs	December 31, 2013	Met
3.	Ceiling on outstanding payments past due of all central-government owned SOEs	December 31, 2013	Not met
4.	Ceiling on stock of local government arrears	December 31, 2013	Met
5.	Ceiling on stock of net Treasury loans for EU-funded projects	December 31, 2013	Met
Inflation consultation band			
	Inner band	December 31, 2013	Crossed
	Outer band	December 31, 2013	Met
Structural benchmarks			
1.	Start publishing monthly arrears reports and corrective measures being taken by the central and local governments, by unit, on a quarterly basis.	End-September 2013	Met
2.	Prepare the basic health package within the existing spending envelope which will also define the scope of the private sector in the health care system in the future.	End-September 2013	Met with delay
3.	Prepare medium-term financial projections that properly identify the fiscal implications of EU-funded projects, including co-financing needs, financial corrections and non-eligible spending.	Mid-October 2013	Met
4.	Approve, by government memorandum, a list of significant priority projects, based on the prioritization criteria, to help prepare for the 2014 budget.	Mid-October 2013	Met
5.	Launch an initial public offering of 15 percent of the government's shares in Romgaz.	Mid-November 2013	Met
6.	Appoint a professional board in Hidroelectrica in accordance with the provisions of Ordinance 109/2011.	End-November 2013	Met
7.	Approve Covered Bond legislation. 1/	End-December 2013	Not met; propose to reset to end-March
8.	Fully operationalize the commitment control system, supported by necessary legal and procedural changes and cover expenditures of the MoPF and at least one additional unit at both the central and local government levels.	End-January 2014	Not met; propose to reset to end-April
9.	Launch an initial public offering of a majority of the government's shares in Electrica, after the planned capital increase.	End-May 2014	
10.	Make the commitment control system available for operation in all general government entities as a pilot. 2/	End-June 2014	
11.	Launch an initial public offering of 15 percent of the government's shares in Oltenia, prior to the planned capital increase.	End-June 2014	
12.	Launch an initial public offering of 15 percent of shares in Hidroelectrica. 3/	End-June 2014	
13.	Roll out the consolidated fiscal reporting system to all government entities.	End-June 2014	
14.	Resolve possible discrepancies in the fiscal code and IFRS accounting rules on the treatment of NPLs sold to domestic debt management companies in line with the outcome of the pending EC infringement case.	End-December 2014	Met
15.	Prepare and publish consolidated general government accrual based financial statements and ESA95 based reports from the system (the first sets of reports will be for the year ending 2014), and reconcile with each other and with cash-based budget execution reports.	End-June 2015	
New structural benchmarks			
1.	Provide quarterly progress reports on the number of completed audits in the large taxpayers unit and high net wealth individuals unit, and number of installment agreements signed for large taxpayers and medium-size taxpayers to clear tax arrears as well as collection targets based on these actions (see TMU, paragraph 28).	End-March 2014	
2.	Submit to parliament an insolvency code aimed at better supporting early rescue of viable firms and speedy exit of non-viable firms, prepared in consultation with IMF staff, at a minimum on: pre-insolvency procedures, creditor voting, priority financing, automatic stay, ranking of claims, and notice requirements.	End-April 2014	
3.	Prepare a strategy for the reduction of fully provisioned uncollectible NPLs on commercial banks' balance sheets	End-May 2014	
4.	Prepare a plan that clearly identifies the companies and the actions that will be taken to adhere to the overall path of arrears reduction established under the program.	End-April 2014	
5.	Issue a press release announcing the pilot structural compliance project targeted at undocumented labor and tax evasion.	End-May 2014	

1/ A modification of this benchmark is proposed to specify that the required action is submission of draft legislation to parliament.
2/ A modification of this benchmark is proposed to facilitate monitoring by specifying the required actions.
3/ The content of this benchmark has been modified: the size of the IPO was increased from 10 to 15 percent and the reference to the planned capital increase dropped.

Attachment II. Romania: Technical Memorandum of Understanding

1. This Technical Memorandum of Understanding (TMU) defines the variables included in the quantitative performance criteria and indicative targets set out in the Memorandum of Economic and Financial Policies (MEFP), the key assumptions, the methods to be applied in assessing program performance, and the reporting requirements to ensure adequate monitoring of economic and financial developments. The quantitative performance criteria and indicative targets, and structural benchmarks for 2013 and 2014 are listed in Tables 1 and 2 of the MEFP, respectively.

2. For the purposes of the program, *the exchange rates* of the Romanian Leu (RON) to the euro is set at RON 4.4588 = €1, to the U.S. dollar at RON 3.4151 = $1, to the Japanese yen at RON 3.4480 = ¥100, and to the pound sterling at RON 5.2077 = £1, and *the gold price* is set at RON 132.1562 per gram as shown on the National Bank of Romania's (NBR's) website as of June 30, 2013. The exchange rates to other currencies, where applicable, will also be the ones shown on the NBR's website as of June 30, 2013.

3. For the purposes of the program, the *general government* includes the entities *as defined in the 2013 and 2014 budgets*. These are: the central government (state budget, self-financed state entities included in the budget, etc.), local governments, social security funds (pension, health, and unemployment), and the road fund company. This definition of general government also includes any new funds, or other special budgetary and extra budgetary programs that may be created during the program period to carry out operation of a fiscal nature as defined in the IMF's *Manual on Government Finance Statistics 2001*. The authorities will inform the IMF staff of the creation of any such new funds or programs immediately.

QUANTITATIVE PERFORMANCE CRITERIA, INDICATIVE TARGETS, INFLATION CONSULTATION BAND, AND CONTINUOUS PERFORMANCE CRITERIA

A. Floor on the Change in Net International Reserves

4. For program purposes, Net International Reserves (NIR) are defined as the NIR of the NBR minus Treasury liabilities to the International Monetary Fund.

5. NIR of the NBR are defined as the euro value of gross foreign assets of the NBR minus gross foreign liabilities of the NBR; and will be measured on the basis of the NBR's operational rather than accounting definitions. Non-euro denominated foreign assets and liabilities will be converted into euro at the program exchange rates and gold price.

6. Gross foreign assets of the NBR are defined to include the NBR's holdings of monetary gold, SDRs, the country's reserve position at the IMF, holdings of cash, securities and deposits abroad in convertible foreign currencies. Excluded from reserve assets are: (i) precious metals other than monetary gold; (ii) assets in nonconvertible currencies; (iii) illiquid assets; (iv) any assets that are pledged, collateralized, or otherwise encumbered, unless there is also a gross foreign liability associated with it; (v) claims on residents; and (vi) claims in foreign exchange arising from derivatives in foreign currencies vis-à-vis domestic currency (such as futures, forwards, swaps, and options).

7. Gross foreign liabilities of the NBR are defined as all foreign exchange liabilities to residents and nonresidents, including commitments to sell foreign exchange arising from derivatives (such as futures, forwards, swaps, and options), banks' foreign currency deposits against reserve requirements, and all credit outstanding from the IMF, but excluding government foreign currency deposits at the NBR.

Floor on Cumulative Change in NIR from the Beginning of 2013 and 2014 (in million euros)[1]

	2012	2013	2013			2014			
	Dec. stock	June stock	June actual	Sept. actual	Dec. actual	March PC	June PC	Sept. ind.	Dec. ind.
Cumulative change in NIR	16,344	20,266	3,922	6,326	7,343	-500	0	200	500
Memorandum Item: Gross Foreign Assets	34,152	35,381	1,229	2,226	2,003	-1,911	-2,932	-3,625	-3,970

[1]PC = performance criterion; data for end-month. Flows are cumulative from the beginning of the same calendar year (e.g., June 2013 figure is cumulative from January 1, 2013). Current year stocks are obtained by adding the flows to the previous end-year stock.

8. The NIR targets will be adjusted (i) upward (downward) by the surplus (shortfall) in program disbursements relative to the baseline projection (Program disbursements are defined as external disbursements from official creditors (WB and the EC) that are usable for the financing of the overall central government budget); and (ii) downward by the full amount of the shortfall relative to the baseline of external bond placement by the MOPF.

External Program and MOPF Disbursements—Baseline Projections (in million euros)[1]

	2013			2014			
	June actual	Sept.	Dec.	March	June	Sept.	Dec.
Cumulative change under external program	0	0	0	0	500	500	800
Cumulative change in external MOPF bond placement	1,122	1,122	2,322	1,532	2,532	2,532	2,532

[1]Flows are cumulative from the beginning of the same calendar year (e.g., June 2013 figure is cumulative from January 1, 2013).

B. Consultation Mechanism on the 12-Month Rate of Inflation

9. The quarterly consultation bands around the 12-month projected rate of inflation in consumer prices (as measured by the headline consumer price index (CPI) published by the Romanian Statistical Institute), are specified below. Should the observed year-on-year rate of CPI inflation fall outside the outer bands specified below, the authorities will complete a consultation with the IMF on their proposed policy response before requesting further purchases under the program. In addition, the NBR will conduct discussions with IMF staff should the observed year-on-year rate of CPI inflation fall outside the inner bands specified for the end of each quarter in the table below.

Inflation Consultation Band

	2013			2014			
	June actual	Sept. actual	Dec. actual	March target	June target	Sept. ind.	Dec. ind.
Outer band (upper limit)				3.0	3.6	5.0	5.5
Inner band (upper limit)				2.0	2.6	4.0	4.5
Actual / *Center point*	5.4	1.9	1.6	*1.0*	*1.6*	*3.0*	*3.5*
Inner band (lower limit)				0	0.6	2.0	2.5
Outer band (lower limit)				-1.0	-0.4	1.0	1.5

C. Performance Criterion on General Government Balance

10. The budget deficit for 2013 and 2014 will be monitored through the cash balance of the general government in GFS 1986 classification. Consistent with the national methodology,

revenues and spending for EU funds will be treated on an accrual basis. Any privatization receipts will be treated as a below the line item. The authorities will consult with IMF staff on corrective measures in the event of shortfalls in government revenue and financing.

Cumulative Floor on General Government Balance[1]

	(In millions of lei)
End-June 2013 (actual)	-6,621
End-September 2013 (actual)	-8,143
End-December 2013 (actual)	-15,711
End-March 2014 (performance criterion)	-4,539
End-June 2014 (performance criterion)	-8,230
End-September 2014 (indicative)	-7,209
End-December 2014 (indicative)	-14,712

[1] Cumulative figure during calendar year (e.g., June 2013 figure is cumulative from January 1, 2013).

11. The cumulative floor on the general government balance will be adjusted upward by the shortfall in spending on national cofinancing of EU funded projects (excluding cofinancing from the top-up funds). For end-March 2014, the general government balance will be adjusted upward by the shortfall in quarterly spending on national cofinancing of EU funded projects (excluding cofinancing from the top-up funds) relative to a baseline of 3,223 million RON, up to a limit of 650 million RON. For end-June 2014, the general government balance will be adjusted upward by the shortfall in quarterly spending on national cofinancing of EU funded projects (excluding cofinancing from the top-up funds) relative to a baseline of 3,223 million RON, up to a limit of 650 million RON.

12. The Ministry of Public Finance (MOPF) will also provide monthly data to measure the deficit from below the line. The balance of the general government measured from below the line will include:

+ (i) net external financing, excluding valuation gains and losses;
+ (ii) change in net domestic credit from the financial system, excluding valuation gains and losses from deposits denominated in foreign currency and including adjustments for;
    + (a) received EU funds not yet spent (advance payments);
    + (b) claims of the government on EU funds;
    + (c) property fund obligations not yet paid;
+ (iii) change in the stock of issued government securities, net of valuation changes;
+ (iv) net changes in other financing;
    of which: (a) temporary financing for EU projects, out of which temporary financing for structural and cohesion fund projects;
    (b) reimbursement payments from EU for the EU projects, out of which reimbursement payments for structural and cohesion fund projects

The data on the beginning and ending balance of the Treasury account will also be provided.

13. If the difference between the general government deficit measured from above the line and from below the line is larger than lei 200 million each quarter during 2014, the MOPF will consult with IMF staff. The first quarter deficit target includes a treasury loan to Calatori to provide for arrears clearance which at the first budget revision will be recorded as budget expenditure. The overall deficit for the year includes RON 220 million for this purpose.

D. Indicative Target on the Stock of Net Treasury Loans for EU-Funded Projects

14. The Ministry of Public Finance may provide net loans from the Treasury for EU funded projects, defined as the temporary financing for EU structural and cohesion fund projects minus the reimbursements from EU for the EU structural and cohesion fund projects. The net stock outstanding at end-March and end-June 2014 cannot exceed 4 billion RON (indicative targets).

E. Performance Criterion Limiting the Issuance of Government Guarantees to the Non-Financial Private Sector and Public Enterprises

15. The issuance of general government guarantees to the nonfinancial private sector and public enterprises will be limited during the program period. The ceilings are specified in the table below.

Ceiling on New General Government Guarantees Issued from end 2008 Until:	(In billions of lei)
End-June 2013 (actual)	10.9
End-September 2013 (actual)	11.45
End-December 2013 (actual)	12.1
End-March 2014 (performance criterion)	18
End-June 2014 (performance criterion)	18
End-September 2014 (indicative)	18
End-December 2014 (indicative)	18

F. Performance Criterion on the Stock of Domestic Arrears by the Central Government and Social Security System

16. The performance criterion established on the stock in domestic payments arrears of the central government and social security sector (as defined in ¶3 above) contemplates their elimination during the program period. The stock will be measured net of intergovernmental arrears, but both gross and net arrears will be reported by the government. In case of need, the government will take corrective measures to prevent the accumulation of new spending arrears. For the purpose of the program, arrears mean accounts payable past due date by 90 days (in line with ESA95 definitions for expenditures). The authorities will consult with IMF staff if new arrears are disputed following an audit by the Central Harmonization Unit for Financial Management and Control Systems. As a memorandum item, arrears of central government hospitals will be reported separately.

Stock of Central Government and Social Security Arrears	(In billions of lei)
End-June 2013 (actual)	.035
End-September 2013 (actual)	.018
End-December 2013 (actual)	.01995
End-March 2014 (performance criterion)	.02
End-June 2014 (performance criterion)	.02
End-September 2014 (indicative)	.0175
End-December 2014 (indicative)	.015

G. Continuous Performance Criteria on Non-Accumulation of External Payments Arrears by the General Government

17. The general government will not accumulate external payment arrears during the program period. For the purposes of this performance criterion, an external payment arrear will be defined as a payment by the general government that has not been made within seven days of falling due. The performance criterion will apply on a continuous basis.

H. Indicative Target on General Government Current Primary Spending

18. The indicative target on current primary expenditure of the general government is defined as spending on personnel, goods and services excluding EU funds (specified under external grant category), subsidies, transfers to public entities, pensions (social security budget in social assistance category), state aid and other spending in other transfers category, Reserve Fund, and other expenditure as classified in the monthly reporting tables. Actual data (to which the target will be compared) should include payments related to arrears reduction plans and spending funded through the clawback tax.

Cumulative Change in General Government Current Primary Expenditures[1]	(In millions of lei)
End-June 2013 (actual)	70,412
End-September 2013 (actual)	105,570
End-December 2013 (actual)	144,560
End-March 2014 (target)	36,500
End-June 2014 (target)	73,000
End-September 2014 (indicative)	109,000
End-December 2014 (indicative)	150,500

[1] Cumulative figure during calendar year (e.g., June 2013 figure is cumulative from January 1, 2013).

I. Indicative Target on Local Government Arrears

19. The indicative target on the stock of domestic payments arrears of local governments contemplates no accumulation of new arrears and their reduction during the program period. In case of need, the government will take corrective measures to prevent the accumulation of new spending arrears. For the purpose of the program, arrears mean accounts payable past the due date by 90 days (in line with ESA95 definitions for expenditures). As a memorandum item, arrears of local government hospitals will be reported separately on a quarterly basis.

Stock in Local Government Arrears	(In billions of lei)
End-June 2013 (actual)	.143
End-September 2013 (actual)	.238
End-December 2013 (actual)	.196
End-March 2014 (target)	.300
End-June 2014 (target)	.250
End-September 2014 (indicative)	.200
End-December 2014 (indicative)	.200

J. Absorption of EU Funds

20. The EU funds contribution mentioned in the MoU conditionality is to be measured taking into account the eligible expenditure from both the structural and cohesion funds (SCF) and the European Agricultural Fund for Rural Development (EAFRD).

K. Monitoring of Public Enterprises

21. Public enterprises are defined as all companies including research institutes, incorporated under Law 31/1990 (as amended) and *regii autonome,* organized under Law 15/1990 (as amended), with a cumulative public capital share of 50 percent or more, held directly or indirectly by the central or local governments.

22. Quarterly indicative targets for the first and second quarters of 2014 are set on the aggregate operating balance net of subsidies and the effects of one-off financial or accounting operations, accumulated per calendar year, of the following public enterprises: C.N. Căi Ferate CFR S.A. and five of its subsidiaries (S.C. Interventii Feroviare S.A., Informaticã Feroviarã S.A., S.C. Sere şi Pepiniere S.A., S.C. Electrificare CFR S.A., and S.C. Întreţinere Mecanizata S.A.) S.N. de Transport Feroviar de Marfă "CFR Marfă" S.A. and its subsidiary (S.C. Întreţinere şi Reparaţii Locomotive şi Utilaje S.A.), and S.N. Transport Feroviar de Călători "CFR Călători" S.A. and its subsidiary (S.C. de reparaţii locomotive C.F.R. SCRL Braşov S.A.). The data shall be reported with operating results by firm. The targets will be as follows:

Floor on Cumulative Operating Balance[1]	(In billions of lei)
End-December 2012 (actual)	-3.1
End-June 2013 (actual)	-1.0
End-September 2013 (preliminary)	-1.3
End-December 2013 (preliminary)	-2.2
End-March 2014 (target)	-0.7
End-June 2014 (target)	-0.9
End-September 2014 (indicative)	-1.2
End-December 2014 (indicative)	-2.1

[1] Cumulative figure during calendar year (e.g., June 2013 figure is cumulative from January 1, 2013).

23. In case one of these enterprises is placed into insolvency or liquidation procedures, which occurs when it is recorded in the trade registry that the enterprise was placed into insolvency or liquidation procedures, or its majority share is privatized, which occurs when payment is received from an entity, in which the government does not have a controlling interest, in exchange for the majority shares of the enterprise, the aggregate target listed above will not be adjusted by the original operating balance target for this firm. If any of the companies listed above is split into a new company, both companies will remain under monitoring. If some of the above companies are merged, the newly created companies will remain under monitoring.

24. Quarterly indicative targets for the first and second quarters of 2014 are set on the stock of outstanding payments of public enterprises owned by the central government that were not made by the due date. The stock excludes outstanding payments past due of those public enterprises owned by the central government that are already under insolvency or liquidation procedures. The beginning date for measuring the stock is December 31, 2012. The data shall be reported at the firm level. The targets will be as follows:

Ceiling on Outstanding Payments Past Due[1]	(In billions of lei)
End-December 2012 (actual)	12.7
End-June 2013 (actual)	8.3
End-September 2013 (preliminary)	7.0
End-December 2013 (preliminary)	7.2
End-March 2014 (target)	5.4
End-June 2014 (target)	4.6
End-September 2014 (indicative)	3.9
End-December 2014 (indicative)	3.4

[1] Starting end-March 2014, outstanding payments past due accumulated and reported by companies while they are under insolvency procedures are excluded from the target.

In case one of these enterprises is placed into insolvency or liquidation procedures, which occurs when it is recorded in the trade registry that the enterprise was placed into insolvency or liquidation procedures, or its majority share is privatized, which occurs when payment is received from an entity, in which the government does not have a controlling interest, in exchange for the majority shares of the enterprise, the aggregate target listed above will not be adjusted by the outstanding payments past due for this firm. If any of the companies listed above is split into a new company, both companies will remain under monitoring. If some of the above companies are merged, the newly created companies will remain under monitoring.

25. Quarterly indicative targets for the first and second quarters of 2014 are set on the stock of outstanding past due principal payments of S.N. de Transport Feroviar de Marfă "CFR Marfă" S.A. and its subsidiary (S.C. Întreţinere şi Reparaţii Locomotive şi Utilaje S.A.). The beginning date for measuring the principal stock is December 31, 2013. The target excludes existing and future interest and penalties incurred on the stock of outstanding past due payments as of December 31, 2013. The targets will be as follows:

Ceiling on Outstanding Payments Past Due	(In millions of lei)
End-December 2013 (preliminary)	99.2
End-March 2014 (target)	99.2
End-June 2014 (target)	99.2
End-September 2014 (indicative)	99.2
End-December 2014 (indicative)	99.2

L. Reporting Requirements for the Prior Action

26. Completion of the prior action related to the reporting of actions taken to reduce SOE arrears requires receipt by the IMF of:

- for the three public enterprises SC Interventii Feroviare S.A., SC Servicii Energetice Oltenia SA Filiala Electrica, and "S.C. Tipografica Filaret S.A." placed into insolvency or liquidation procedures – the general shareholders meetings' decisions on placing the enterprises into insolvency or liquidation procedures;

- for the payment from the budget in the amount of at least RON 220 million to partially clear arrears of state-owned railway companies for electricity supplies – government emergency ordinance and approved withdrawal request;

- for the payment from the budget to clear the arrears of the National Road Company as of December 31, 2013 - the credit opening document;

- for the lease or closure of over 700 km of rail line - an approved government decision, published in the Official Gazette.

M. Reporting Requirements on Tax Administration

27. ANAF will provide quarterly data (within 25 days) on the performance of audit and installment agreements relative to the targets as specified in the following table:

Romania: Audit and Installment Agreements

	2011	2012	2013	2014				
			Total	Total	Q1	Q2	Q3	Q4
Audits								
Large Taxpayers								
No. of closed audits	282	243	242	305	58	95	82	70
Supplementary amounts discovered (mill. lei)	2445.5	944	2,559.10	1447.2	275.2	450.8	389.1	332.2
Fiscal Verifications								
High Net Wealth Unit								
Closed preliminary verifications	-	-	24	6	6	-	-	-
Fiscal verifications	-	-	-	10	-	-	-	10
Income tax amounts declared by HNWI group population (mill lei) 1/	238.3	252.2	267.3	283.4	-	-	-	-
Installment Arrangements to Clear Tax Arrears 2/								
Large taxpayers								
Number of installments granted	15	42	57	87	74	80	83	87
Value of installments granted ('000 lei)	379	553	939.24	1479	1184	1280	1245	1479
Medium-sized taxpayers								
Number of installments granted	232	550	775	1154	933	1018	1096	1154
Value of installments granted ('000 lei)	174	396	395.21	669.3	606.5	692.2	602.8	669.3

1/ The income tax declared during the current year refers to the income received during the previous year.

2/ Refers to the evolution of the stock (new entries minus payments done or cancelations) of installment agreements and the corresponding amounts.

N. Reporting Requirements

28. Performance under the program will be monitored from data supplied to the IMF and EC by the NBR and the MOPF as outlined in the table below. The authorities will transmit promptly to IMF and EC staff any data revisions as well as other information necessary to monitor the arrangement with the IMF and EC.

Romania: Data Provision to the IMF and EC

Item	Periodicity
To be provided by the Ministry of Public Finance	
Preliminary monthly data on general government accounts, including on GFSM 2001 basis	Monthly, on the 25th day of the following month
Quarterly final data on net lending from the Treasury for EU funded projects	Quarterly, on the 5th day past the test date
Preliminary monthly data providing a breakdown of general government expenditures on post-accession EU projects (co-financing, non-eligible spending, corrections, reimbursable funds, and EU top-ups)	Monthly, on the 25th day of the following month
Preliminary monthly data on EU funds with breakdown on each operation program, including inflows.	Monthly, on the last day of the following month
Quarterly final data on general government accounts, including public enterprises as defined by ESA95 and breakdown of general government spending on EU projects	Quarterly cash data, on the 35th day past the test date; Quarterly accrual data, on the 55th day past test date
The budget deficit of the general government using ESA95 definition	Quarterly, with a lag of three months
Preliminary data on below-the-line financing for the general government	Monthly, with a lag of no more than 35 days past the test date
Final quarterly data on below-the-line financing for the general government, including details of the domestic and external issuances and repayments (by currency)	Quarterly, no later than 45 days past the test date
Total accounts payable and arrears of the general government, including local governments and central and local government hospitals	Preliminary monthly, within the next month. Quarterly, within 55 days

Progress report on the status of the audit of the stock of the disputed local arrears.	Quarterly, no later than 45 days past the end of each quarter
Data on payment delays and arears with respect to drug reimbursement by the National Health Insurance House (pharmacies and wholesale), with a particular view on the implementation of directive 7	Monthly, at the end of each month
Stock of the central government external arrears	Daily, with a lag of not more than seven days
Public debt and new guarantees issued by the general government	Monthly, within one month
Preliminary monthly data on general government primary spending, net of EU disbursements	Preliminary monthly data within 25 days
Final quarterly data on general government primary spending, net of EU disbursements	Quarterly, within 35 days from the test date
Time lines showing the expected completion dates for key steps leading to the launching of the initial public offerings of the energy state-owned companies	Quarterly, within 10 days of the end of each quarter
Preliminary data on the operating balance, profits, stock of outstanding payments past due, and personnel expenditures for each key public enterprise as defined in ¶22	Monthly, within 25 days
Final data on the operating balance, profits, stock of outstanding payments past due, and personnel expenditures for each key public enterprise as defined in ¶22	Quarterly, end-May for the previous year and end-August for first half of the current year
Preliminary data on the stock of outstanding principal payments past due for the public enterprises identified in ¶26. The data will show separately the principal, interest, and penalty amounts of the outstanding payments past due.	Monthly, within 25 days

Preliminary data on the stock of outstanding payments past due for each public enterprise as defined in ¶21	Quarterly, within 35 days
Final data on the stock of outstanding payments past due for each public enterprise as defined in ¶21	Quarterly, end-May for the previous year and end-August for first half of the current year
Data on EU project grants (reimbursements and advances), capital expenditures and subsidies covered by EU advances or eligible for EU reimbursement on EU supported projects specifically agreed with the EU	Monthly, within three weeks of the end of each month
The balance of the TSA in RON	Monthly, within two weeks of the end of each month
The balance of the two foreign currency accounts used for budget financing and public debt redemption purposes (average, and end-of-period)	Monthly, within two weeks of the end of each month
The balance of the privatization receipts registered in the account of the State Treasury, details on any claims on these receipts and projected net outflows.	Monthly, within two weeks of the end of each month
Reporting of progress in the implementation of the Romanian public administration's functional review	Quarterly, to be sent two weeks before each mission for each of the 12 ministries
Data on subsidies by ministries	Quarterly, one month after the end of the quarter. Additional reporting one week before review mission
Data on public employment and status of ordinance 77/2013 implementation, in particular numbers of staff reductions at central government ministries and staff increases at local governments	Monthly, at the end of each month

To be provided by the National Bank of Romania	
NIR data, by components, in both program and actual exchange rates	Weekly, each Monday succeeding the reporting week and with a 3 working day lag in the case of end-quarter data
Monetary survey data in the format agreed with IMF and EC staff	Monthly, within 30 days of the end of the month
The schedule of contractual external payments of the *banking sector* falling due in the next four quarters, interest and amortization (for medium and long-term loans)	Monthly, 45 days after the end of each month
The schedule of contractual external payments of the *corporate sector* falling due in the next four quarters interest and amortization (for medium and long-term loans)	Monthly, 45 days after the end of each month
The stock of short-term external debt of banks and corporate	Monthly, 45 days after the end of each month
Balance of payments in the IMF format currently used to report	Monthly, 45 days after the end of each month
Exposure (deposits, loans, subordinated loans) of (i) foreign parent banks to their subsidiaries in Romania; (ii) IFI and (iii) other creditors to banks in Romania (by national and foreign currency).	Monthly, 20 days after the end of each month
Detailed bank-by-bank data on restructured loans to households and corporates including SOEs	Quarterly, 45 days after the end of each quarter
Financial soundness indicators[1]	Monthly, 45 days after the end of each month
Foreign currency reserves including	Bi-weekly

[1] Data on solvency should be provided on quarterly basis.

information on FX market interventions and swaps by the NBR	
The IMF and the EC shall be immediately informed in case of sudden loss of reserves exceeding EUR 600 million	Immediately, upon occurrence