

# Budgeting in Moldova: Strengthening public finance management

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This report examines public financial management in Moldova, with a particular focus on budget preparation, execution and reporting. Moldova has already implemented the foundations of modern budget arrangements, and has made good progress in aligning with the OECD Recommendation on Budgetary Governance. The most significant reforms have been the introduction of new budget legislation, greater transparency of budget arrangements, a medium-term budget framework, performance budgeting, reforms to capital expenditure management, and piloting spending reviews. This report focuses on ways to strengthen existing arrangements to improve the quality of the country's system of budgetary governance.

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**JEL codes:** H61

**Keywords:** budgetary discipline, fiscal discipline, budget deficit, public debt, parliament, financial management, budget preparation, budgeting, capital investment, local authorities, Moldova.

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This paper was approved for publication by the OECD Committee of Senior Budget Officials.

## Foreword

In 2023 the Ministry of Finance of Moldova asked the OECD to undertake a review of budgeting in Moldova. This report presents the findings of the review, which was conducted over 2023-24.

As a small ministry supporting a large-scale reform as part of Moldova's continued transition from a planned to a market-based economy, the Ministry of Finance is seeking ways to adopt best practices in budgeting. Related to this objective, in 2018 the Government of Moldova applied for accession to the European Union (EU).

This OECD budget review has taken account of both objectives by considering budget arrangements that would support EU accession, such as integrating climate change considerations in budget processes and establishing an independent fiscal council to advise on the fiscal sustainability of the government's budgets.

Two features of budgeting that are specific to Moldova are the interconnected budget arrangements between central government and local authorities, and extra-budgetary operations by subordinate institutions of central public authorities (CPAs). The scope of this OECD review did not extend to reforming these features, but it did consider ways to strengthen the existing arrangements.

The analysis undertaken in this review is based on the OECD's *Spending Better Framework* and the 2015 *Recommendation of the Council on Budgetary Governance*.

The report was approved by the Committee of Senior Budget Officials and prepared for publication by the Secretariat.

## Acknowledgements

The report was prepared by the OECD Directorate for Public Governance (GOV) under the leadership of Elsa Pilichowski, Director for Public Governance, and the direction of Jon Blondal, Head of GOV's Public Management and Budgeting Division. The report was prepared by Brian Finn, Senior Policy Analyst, Margaux Lelong, Policy Analyst and Patrick Ring, OECD expert in public finance management. Meral Gedik prepared the report for publication.

The authors would like to thank Andrew Blazey, Deputy Head of the OECD Public Management and Budgeting Division, for his insightful comments on the draft version of this report.

The OECD would like to express its sincere thanks to the Ministry of Finance and other bodies consulted in Chisinau for the excellent co-operation throughout the preparation of this review.

This review was supported by the Constituency Programme of the Netherlands Ministry of Finance.

## Abbreviations and acronyms

CCRM	Curtea de Conturi a Republicii <i>Moldova</i>
COFOG	Classification of the Functions of Government
CPA	Central Public Authority
EU	European Union
GDP	Gross Domestic Product
GFS	Government Finance Statistics
FMIS	Financial Management Information System
IFRS	International Financial Reporting Standards
ISSAI	International Standards of Supreme Audit Institutions
MoED	Ministry of Economic Development and Digitalization
MLD	Moldovan Leu
MoF	Mnistry of Finance
MTBF	Medium-Term Budget Framework
OBL	Organic Budget Law
OECD	Organisation of Economic Co-operation and Development
OMF	Order of the Ministry of Finance
PEFA	Public Expenditure and Financial Accountability
PFM	Public Finance Management
SOE	State Owned Enterprise
TSA	Treasury Single Account
SOE	State Owned Enterprise

## Executive summary

The Moldovan Ministry of Finance has already implemented the foundations of modern budget arrangements through budget legislation, a medium-term budget framework, the introduction of performance budgeting, reforms to capital expenditure management, and piloting spending reviews. The Ministry has also increased the transparency of its budget arrangements and is operating at a level of transparency that is comparable to OECD countries in the region. Based on these findings, the OECD's recommendations in this report focus on ways to strengthen the existing arrangements to improve the quality of budget information that is available to decision makers throughout the budget process.

In some instances, continuing to focus on the foundations of budgeting is still warranted. For example, adhering to the budget calendar would ensure that the Parliament receives the allocated time to consider, seek expert opinion, and adopt the draft budget. The timing of inputs in the budget calendar also merits further attention, as the government is incurring costs from preparing supplementary budgets that could be avoided by improving the sequence of budget inputs, specifically updates to fiscal forecasts.

As with other countries that have transitioned to a market-based economy, Moldova has a high demand for capital expenditure to upgrade infrastructure and support increased productivity. Existing reforms to budgeting capital expenditure appear well judged. Additional reforms that would complement the progress to date include strengthening the appraisal of capital proposals to ensure limited budget funds are allocated to the best possible proposals, adopting a multi-year approach to capital commitments, and introducing more effective ways to manage the budget implications from delays to the implementation of capital projects.

While this OECD review does not suggest reforms to the interconnected budget arrangements between central government and local authorities or to the extra-budgetary operations by subordinate institutions of central public authorities (CPAs), it does suggest ways to strengthen them. For instance, the Ministry of Finance should ensure it is well placed to monitor fiscal risks from local authorities, and extra-budgetary operations should be subject to the same monitoring and reporting obligations as any budgeted revenue or expenditure. The introduction of these measures is a first step to considering whether the operations should be brought within the budget.

The following table is a summary assessment of Moldova's performance against the *OECD Recommendation of the Council on Budgetary Governance* in terms of the budget principles covered in this report.

Table 1. Moldova and OECD Principles for Budgetary Governance

Budget principle	Assessment	Recommendations
<b>1. Manage budgets within clear, credible and predictable limits for fiscal policy</b>	Until 2023, public finances remained relatively stable despite the pressures posed by COVID-19, energy inflation and regional instability. There is a fiscal rule that the budget deficit may not exceed 2.5% of GDP. However, the ceiling was breached in 2022 and was expected to be breached for each year in the period 2023-2025. There is no specific requirement for mitigating action to correct breaches.	<ol style="list-style-type: none"> <li><b>Improve</b> macro-economic forecasting by building capacities in the Ministry of Finance (MoF) and/or the Central Bank to expand the expertise on the preparation of fiscal forecasts to support an informed basis for the budget.</li> <li><b>Introduce</b> a periodic and independent review of forecasting models and assumptions that contribute to the preparation of the budget.</li> <li><b>Strengthen</b> the operation of the existing fiscal rule by specifying in legislation for mitigating actions the government will take to correct any breaches of the budget deficit limit.</li> <li><b>Support</b> the government's credentials on budget discipline by introducing a fiscal rule to specify the government's objective on public debt to GDP.</li> </ol>
<b>2. Closely align budgets with the medium-term strategic priorities of government</b>	The Moldovan budget is formulated within a well-articulated legal framework and it contains OECD good practices for the preparation of a medium-term budget framework (MTBF). There is some alignment between policy objectives and the MTBF. However, the challenge is to ensure that these practices are implemented.	<ol style="list-style-type: none"> <li><b>Strengthen</b> the accuracy and reliability of the MTBF so that it can underpin medium-term strategic planning by the government and by central public authorities (CPAs).</li> <li><b>Align</b> budget programmes with the government's strategic objectives by streamlining and standardising budgetary classifications to better align them with the country's overall goals.</li> </ol>
<b>3. Capital budgeting framework</b>	The Government has introduced legislation to standardise project selection and appraisal, and to align proposals with strategic plans. Remaining areas to address include multi-annual funding arrangements for capital projects and carry-over arrangements when implementation differs from plan.	<ol style="list-style-type: none"> <li><b>Provide</b> stability and certainty to capital expenditure projects by committing budget allocations on a multi-annual basis.</li> <li><b>Strengthen</b> the standardised approach for project selection by developing a project assessment methodology and training for staff who prepare capital expenditure proposals.</li> </ol>
<b>4. Ensure that budget documents and data are open, transparent and accessible</b>	The budget documentation lacks detailed narrative statements regarding core public policy and budgetary allocations. Inadequate analysis, summary, and visualisation of budget data make it difficult for both the Parliament and the public to understand the budget's implications. However, a Citizens' Budget is published	<ol style="list-style-type: none"> <li><b>Enhance</b> budget transparency by: <ul style="list-style-type: none"> <li>producing information in accessible formats for users;</li> <li>providing detailed narrative statements in budget documentation; and</li> <li>improving the analysis and accessibility features of budget reports.</li> </ul> </li> </ol>
<b>5. Provide for an inclusive, participative and realistic debate on budgetary choices</b>	Parliament has just six weeks to consider and approve the annual budget even if the budget calendar is adhered to. The limited timetable inhibits analysis and the level of debate. It also limits the opportunity for public engagement by the Parliament on the draft budget.	<ol style="list-style-type: none"> <li><b>Ensure</b> that the milestones in the annual budget calendar are respected so that Parliament has the allocated time to debate the Budget.</li> <li><b>Consider</b> the establishment of a parliamentary budget office to support the resources available to parliamentarians on budgetary matters.</li> </ol>
<b>6. Present a comprehensive, accurate and reliable account of the public finances</b>	The legislative framework prescribes how financial information should be prepared and reported, including the use International of Financial Reporting Standards (IFRS). The Chart of Accounts is aligned with Government Finance Statistics (GFS) 2001. There are, however, significant extrabudgetary operations of subordinate institutions that are outside the national public budget and they are not monitored closely.	<ol style="list-style-type: none"> <li><b>Introduce</b> reporting obligations for subordinate institutions that maintain extrabudgetary operations.</li> </ol>

Budget principle	Assessment	Recommendations
<b>7. Actively plan, manage and monitor budget execution</b>	There is prudent control and monitoring of cash disbursements using a Treasury Single Account (TSA). There is clear assignment of responsibilities for managing the execution of the budget. However, extra-budgetary operations are a material proportion of total spending and are not monitored to the same extent as budget appropriations.	<p>13. <b>Introduce</b> expenditure monitoring for extra-budgetary operations that is consistent with the accountability arrangements for those operations.</p> <p>14. <b>Continue</b> to implement the existing programme of reforms to strengthen of internal controls on expenditure and the internal audit function in CPAs.</p> <p>15. <b>Enhance</b> monthly reports by including an analysis of the reasons for deviations from planned expenditure.</p> <p>16. <b>Reduce</b> the cost of the budget process by reducing the number of supplementary budgets that are prepared early in each fiscal year.</p>
<b>8. Ensure that performance, evaluation and value for money are integral to the budget process</b>	<p>The budget is prepared by programmes and sub-programmes according to national priorities and strategies. Each programme is linked to a CPA but not necessarily a government objective. The performance information developed during the budget process is not published systematically, so it does not inform allocations in the budget report. Spending reviews have been introduced on a pilot basis but have yet to be integrated into budget processes annually.</p> <p>Despite ambitious climate change policies, the MoF has yet to implement green budgeting.</p> <p>Efforts are ongoing to develop gender budgeting, although they are not yet integrated into the budgeting framework.</p>	<p>17. <b>Strengthen</b> engagement with CPAs on budget performance to improve performance indicators and the prioritisation of budget proposals.</p> <p>18. <b>Publish</b> budget performance information when the draft budget is submitted to Parliament to support informed debate and decision making.</p> <p>19. <b>Establish</b> a programme of spending reviews to ensure that all spending is subject to review over a specified number of years and that the recommendations from the reviews align with the budget calendar.</p> <p>20. <b>Integrate</b> green and gender budgeting into the annual budget cycle.</p> <ul style="list-style-type: none"> <li>– Green budgeting: Establish a green budget framework that links to the government’s strategic objectives on climate change.</li> <li>– Gender budgeting: Increase the MoF’s contribution on the design of gender budgeting to integrate gender-related considerations into the annual budget process, and to provide a legal basis for gender budgeting.</li> </ul>
<b>9. Identify, assess and manage prudently longer-term sustainability and other fiscal risks</b>	Practices generally align with OECD standards. The MoF prepares an annual report on Budgetary and Fiscal Risks. The report outlines and categorises fiscal risks by providing a thorough analysis of the identified risks. The MoF considers the impact of macroeconomic assumptions and conditional commitments on budgetary estimates. Closer monitoring of fiscal risks from state-owned enterprises (SOEs) and local authorities would help to strengthen the MoF’s fiscal risk management.	21. <b>Enhance</b> the monitoring of fiscal risks from SOEs and local authorities to strengthen fiscal risk management in the MoF.
<b>10. Conduct rigorous quality assurance including independent audit</b>	<p>The independence of the Court of Accounts is defined in legislation but the independence is not guaranteed under the Constitution. The Court carries out a high volume of audits but the effectiveness of audits is undermined by the low implementation rates of its recommendations.</p> <p>Moldova is considering establishing an independent fiscal institution to oversee and assess its fiscal policies, which would support EU accession and the information available to parliamentarians and the public generally.</p>	22. <b>Improve</b> the low implementation rate of the Court’s recommendations as a priority.

## 1.1. Budget planning

The Moldovan budget is formulated within a well-articulated legal framework and it contains OECD good practices for the preparation of a MTBF. However, the challenge is to ensure that these practices are implemented. The key challenges to be addressed are:

- Ensuring that the milestones of the annual budget calendar are adhered to
- Improving the operation of the fiscal rule by including in the OBL the actions that are required to correct breaches of the budget deficit limit
- Introducing a rule to limit the public debt to GDP ratio
- Improving economic forecasting so that the fiscal forecasts on which budget appropriations are based are robust and do not vary significantly from actual expenditure
- Strengthening the accuracy and reliability of the MTBF so that it can underpin medium-term strategic planning by the government and by CPAs
- Building capacities in the MoF and/or the Central Bank to develop a wider source of expertise for macroeconomic forecasting.

### 1.1.1. Budget context

Moldova has a relatively small economy of 2.6 million people that is based largely on services and agriculture. Following the dissolution of the Soviet Union in 1991, Moldova's rapid transition from a planned economy to a market economy has not always been smooth, as evidenced by high rates of unemployment. The challenges have been compounded by a large current account deficit and inadequate savings. The country is also highly vulnerable to energy insecurity and climate change.

In 2022, economic activity contracted by 5.9% under the impact of regional destabilisation, which aggravated an energy crisis following the hike in gas prices at the end of 2021. Against this backdrop and prior to COVID-19, the economy enjoyed successive years of economic growth, backstopped by a sizeable inward flow of remittances.

In terms of budget management, Moldova has a good record of budget and fiscal discipline. For example, the budget deficit was 1.9% and 3.3% in 2021 and 2022 respectively. The public debt ratio at the end of 2022 was relatively low at 34.7% of GDP. However, the Government remains dependent on international donors to cover its financing needs.

Moldova applied to join the European Union (EU) in July of 2018, and the process of EU accession has been unfolding since. The accession process is a way for non-member countries to establish a closer relationship with EU institutions. For Moldova, this process is expected to bring greater levels of economic integration and investment, as well as the possibility of increased security and stability. It also means the country would gain access to the EU's wide range of resources, such as financing, technical assistance, and policy guidance, which could help achieve further economic and social progress.

Of course, EU accession presents considerable economic and social challenges for a candidate country across all chapters of the *Acquis Communautaire*. In this regard, Moldova's record of fiscal discipline in the face of difficult budgetary pressures arising from the COVID-19 pandemic, higher energy prices and regional instability owing to Russia's war of aggression against Ukraine, is evidence of a determination to place the country in the best fiscal position to cope with these pressures and to maintain the confidence of international donors.

### **1.1.2. Institutional and legislative framework**

The Constitution provides that the Parliament approves the state budget and the national public budget and that the Government submits both to the Parliament. The budgetary responsibilities of the Government and the Parliament are prescribed in the Law on Public Finances and Budgetary Fiscal Responsibility No. 181/2014 (Organic Budget Law, OBL) and are consistent with good practice.

The most important organic laws are the OBL and the Law on Local Public Finances No. 397/2003 (LLPF). The OBL defines the national public budget as the state budget, the state social insurance budget, the mandatory medical assistance insurance funds and local authority budgets. The OBL underpins overall fiscal discipline and governs the budget process, both for central and local authority governments. The LLPF prescribes the local authority budget process in greater detail and is consistent with the OBL.

The OBL contains provisions that are consistent with a sound budget framework. For instance, OBL prescribes that the MoF is responsible for ensuring “the management of the financial means of the component budgets of the national public budget”. (Ministry of Finance of Moldova, 2014<sup>[1]</sup>) This provision is to ensure that budgets beyond the state budget are subject to scrutiny by the MoF. In 2017, the government’s decision (No. 696) to re-organise the MoF, and its subordinate institutions, established the basis for the MoF to fulfil that role.

In addition, the OBL prescribes the roles of central public authorities (CPA), which includes line ministries, the institutions responsible for the two insurance funds, local authorities and subordinate CPAs. The law assigns each body with the responsibility to manage its expenditures and report to the MoF on the execution of the budget and on the performance of budget programmes. By providing that these institutions work closely with the MoF to manage their budgets, the law contains provisions that support budgetary discipline.

The OBL also provides for the medium-term budget framework, the management of public debt, capital investments, a 2.5% of GDP ceiling on the annual budget deficit, the budget calendar and the procedures for formulating, executing and reporting on the budget. The provisions of the OBL are supported by Government decisions and Orders of the Ministry of Finance, including Order of the Ministry of Finance No. 209 of 2015 on the methodology for development, approval, and modification of the budget and Government Decision No. 684 of 2022 on the regulation of capital investments.

While the legislative framework provides a sound basis for public finance management (PFM), there are several weaknesses in the implementation. The budget calendar is regularly not adhered to. There are significant extra-budgetary operations outside the national public budget, with 160 CPAs having such operations. The budget deficit ceiling was exceeded in 2022 and is projected to be exceeded again in each of the years for the medium-term period 2023-2025, which is contrary to the government's track record on budget discipline and undermines the credibility of the framework. The only requirement for mitigating action to correct breaches of the deficit ceiling is a general requirement for the Government to report to the Parliament every six months regarding measures to bring the deficit below the threshold.

### **1.1.3. Macroeconomic and fiscal forecasting**

The macroeconomic forecasts on which the MTBF is based are those supplied by the Ministry of Economic Development and Digitalization (MoED). The Central Bank provides the inflation forecast. The MoED provides forecasts to the MoF in January (preliminary) and February (revised) for the MTBF, which means that the MoF has a basis for estimating a preliminary resources envelope, within which it requires CPAs to make their initial medium-term requests. The MoED updates its forecasts in July for the preparation of the State Budget Law. Those forecasts are further updated in October in light of new data emerging and from forecast data prepared by the IMF in October as part of the IMF programme. The MoF uses the updated forecast when drafting the State Budget Law.



It is uncommon in OECD countries for the MoED to be the sole public institution with capacity for producing macroeconomic forecasts. Even with those capacities sitting in a single institution in Moldova, an established practice in OECD countries is to independently review the macro-economic forecasting model and its assumptions on a periodic basis. Between 2012 and 2018 the number of OECD countries publishing the results of independent reviews of economic and/or fiscal forecasting grew from 16 to 25 countries, which illustrates the extent of the practice. Accordingly, it could be useful if the MoED were to commission and publish an independent review of its forecasting methodology to identify where improvements could be made to reduce forecasting errors and to verify the underlying assumptions of its forecasting model.

Forecasting accuracy also could improve by establishing a macroeconomic forecasting unit in either the MoF or the Central Bank to help inform and cross-check the MoED's forecasts. The value of a second opinion is also one of the arguments in favour of establishing an independent fiscal council in Moldova.

The budget documentation contains revenue estimates for the budget year and the following two years with a breakdown by individual revenue types. Revenue forecasts are the MoF's responsibility. The MoF produces tax forecasts using the MoED macroeconomic forecasts, taking account of the trends of the current year and past two years, and after consulting the Tax Administration. Estimates for revenue from other areas such as health insurance and social insurance are developed between the MoF and the respective authorities.

Expenditure by service category (e.g. health and education) is presented in the documents by recurrent and capital aggregates for the budget year and the following two years. Debt and financing requirements are also included. The changes in total revenue, expenditure and the budget balance are shown in nominal terms and as a share of GDP.

Owing to the COVID-19 pandemic and the impact of Russia's invasion of Ukraine, including an influx of refugees, it is difficult to assess the reliability of forecasts. While both actual expenditure and revenue has varied significantly from the MTBF and budget estimates in recent years, the incidence of extreme events and variations underscores the merit of a periodic and independent review of the forecasting model and assumptions.

#### **1.1.4. Medium-term budget framework**

In February each year, the MoF issues the MTBF Circular, which contains the preliminary medium-term expenditure ceilings as well as the sector policy objectives as set by the State Chancellery for each budget organisation. The lead ministries from the budget organisations establish working groups, that include a representative from the MoF, to assess how policy proposals can be accommodated within the expenditure ceilings.

If the proposals exceed the available resources, the MoF applies proportional reductions or identifies certain programmes/items for potential reductions and informs the relevant spending authority. The spending authority can accept the changes or propose alternatives. The expenditure ceilings, and any variations to them from the working group process, are then compiled in the draft MTBF. Although the centralised position of the MoF places it in a strong position for budget negotiations, expenditure ceilings are also determined through political processes. The Cabinet agrees the finalised revenue and expenditure ceilings in the MTBF by 1 June each year and includes a contingency provision for unforeseen expenditure, which is referred to as a 'general action'.

Several expenditures are linked to inflation and the forecast for inflation is updated in March each year. This leads to changes in expenditure on certain activities (e.g. social support benefits and health insurance benefits) which in turn leads to the need for a supplementary budget in the summer (usually July). The difference in timing between setting expenditure ceilings and preparing the inflation forecast undermines the ceilings for the current year and the forthcoming budget. It further lessens the benefit of the MTBF as a framework for annual and medium-term budget planning. There is a risk that the reliance on a mid-year

supplementary budget undermines fiscal discipline in the absence of requiring savings from CPAs to offset at least some of the additional expenditure.

Sectoral top-down ceilings are set in the MTBF which provide a hard ceiling for the coming year's budget but are indicative for the following two years. The ceilings are not allocated to each CPA and so there may be a difference between the ceilings in the MTBF and the allocations to administrative units in the annual budget. After the MTBF is approved, however, the sectoral ceilings provide the basis for budget negotiations, which take place at the institutional and sub-programme levels. The ceiling agreed for each CPA does not include a contingency. If a CPA needs to draw on the contingency reserve, it must first make a case for this and receive approval from the MoF before the request can be approved by the Cabinet.

In relation to forecasting the expenditure baseline, the MoF uses the current year's budget, supplemented by the commitments in the MTBF, as well as taking into account of technical factors, such as macroeconomic parameters and demographic developments. Sectoral forecasts are composed in consultation with line ministries and other relevant bodies (e.g. Health Insurance Fund). Local authorities are not involved in developing the MTBF even though in Moldova local authorities and regional bodies are responsible for disbursing large amounts of public moneys and collecting some taxes. Their responsibilities mean they have knowledge that could be useful in formulating the MTBF.

The MTBF operates on a rolling basis and ceilings are set in nominal terms with a contingency margin for unforeseen events. However, there is no standard methodology for calculating the contingency. Even with the provision of contingencies, there are no incentives for CPAs to respect the ceilings and manage resources within the framework. However, it is clearly understood that CPAs are responsible for managing resources within the framework and to maintain the multi-annual expenditure baseline in accordance with the provisions of Order of the Ministry of Finance (OMF) No. 209 of 2015 on the methodology for development, approval and modification of the budget.

Variations between the ceiling and actual expenditure are analysed by the MoF but not published. In the years prior to 2023, there have been significant deviations between planned and actual expenditure. The accountability held by CPAs would be stronger if the MoF published its analysis to show where ceilings were breached.

### **1.1.5. Fiscal risk management**

In accordance with the OBL (Article 48.5(d)), the MoF produces an annual Budgetary and Fiscal Risk Report. The report describes and ranks various fiscal risks, and it contains an analysis of those risks. It includes an assessment of the sensitivity of budgetary estimates to macroeconomic assumptions and conditional commitments. The analysis of fiscal budget risks includes:

- possible variations in macroeconomic and budgetary assumptions (e.g. changes to growth inflation or exchange rate);
- risks associated with the management of the public debt; and
- an analysis of implicit risks such as those related to local budgets, state owned enterprises (SOEs), loan guarantees, public private partnerships, and natural disasters.

The Report contains a section on the consolidated fiscal risk from local authorities, covering transfers from the state budget to the local budgets, deviations between planned and executed expenditures, arrears and guarantees issued by local authorities on foot of borrowings. It also contains a section on SOEs regarding financial stability. The monitoring information on SOEs and local authorities is not as robust as audited financial statements, which are finalised 6-9 months after the end of the financial year. Owing to limited resources within the Court of Accounts, only the largest local authorities and SOEs are audited.

The analysis in the Report is comprehensive, and risks are quantified where possible with mitigation measures. However, the Report recognises the difficulty of quantifying fiscal risks owing to the uncertainty

regarding the likely occurrence of a fiscal risk. The Report classifies fiscal risks as low, medium and high to show the potential magnitude of the risk, where low is less than 1% of GDP, medium is between 1% and 3% of GDP and high is more than 3% of GDP.

### **1.1.6. Interactions with local government**

Local authorities have several responsibilities in budgeting, including the preparation of measures for increasing the fiscal base and for assuring the sustainability of the local budgets on a medium-term and long-term basis. Nevertheless, local authorities are heavily reliant on transfers from the state budget. The OBL provides for both general transfers and earmarked transfers from the state budget to the local budgets. About 70% of local authorities' total expenditure is funded by state transfers; about 25% is funded own revenues; and the remaining 5% amount is funded by debt subject to approval by the MoF.

The approval by the MoF is to maintain the government's overall public debt position. If an approval is received, local authorities can engage in both short-term borrowing for gaps in operational expenditures and long-term borrowing for capital investment. All capital investments require the mandate of the MoF. The MoF tightly controls borrowing within the legislative framework of the Law on Local Public Finances No. 397/2003 which states that expenditures for servicing of debt and capital investment shall not exceed 20% of own revenues of local public budgets (Articles 14-18).

Local authority budgets are based on past budgets, updated for local strategies, and contain projections for the upcoming years. The MoF co-ordinates the budget process and scrutinises the local authority budgets. The annual budget circular is sent to the local authorities which must follow the criteria contained therein when formulating their budgets. There is no specified procedure to take the own revenues of local authorities into account when distributing transfers across local authorities but in cases where own revenues are high, the transfer agreed by the MoF will be less. The starting point for the transfer calculation is that budget year  $n$ , the transfer amount is based on actual expenditure in year  $n-2$ . Variations from this starting point depend on the own revenue of each local authority.

### **1.1.7. Annual budget**

Since 2011, the Moldovan Budget has been formulated within a rolling three-year medium-term budgetary framework. The framework aims to ensure the sustainability of public finances by stating the government's medium-term macroeconomic and fiscal forecasts and fiscal policy targets over the three years following the current year.

The fiscal year in Moldova runs from January to December and the formulation of the Budget is divided into two parts: the establishment of the MTBF in the first half of the year is followed by the annual budget process in the second half. The OBL and OMF No. 209 of 2015 establish the key stages for the budget process and are outlined in Table 2.

**Table 2. Calendar of the fiscal year**

Budget task	Timetable
Setting the medium term budgetary framework	<ul style="list-style-type: none"> <li>In January, the State Chancellery sets the policy objectives to be included in the MTBF, after which a co-ordinating group is established under the MoF</li> <li>In February, the MoF issues the MTBF Circular to the budget organisations.</li> <li>By 15 May, the MoF submits the draft MTBF to the Government for its approval</li> <li>By 1 June, the Government approves the MTBF</li> </ul>
Developing and approving the annual budget law	<ul style="list-style-type: none"> <li>By 1 June, the MoF issues the annual budget circular to the CPAs, which includes top-down expenditure ceilings for the following three years</li> <li>By 1 July, the CPAs submit their initial proposals to the MoF</li> <li>By 15 September, the Government submits to the Parliament the mid-year report on the execution of the national public budget and its components for the current budget year</li> <li>By 15 October, the Government approves and presents to Parliament the draft budget laws for the upcoming year</li> <li>By 1 December, the Parliament adopts the budget laws for the upcoming year</li> </ul>

The Cabinet approves the MTBF by 1 June, after which the Ministry of Finance issues the annual budget circular. The budget circular sets the parameters and three-year spending limits within which the CPAs must prepare their estimates. The CPAs have until 1 July to submit their initial requests and they can do this through the Financial Management Information System (FMIS). Requests for new policies are presented separately from requests for existing policies. Following negotiations with the MoF, new policy requests will be accepted, depending on the available fiscal space. The negotiations generally are between civil servants although some discussions may be finalised with the Prime Minister. The budget appropriations are closely aligned with the MTBF. The aggregate expenditure in the annual budget for 2023 only differed by 0.3% from the aggregate figure in the MTBF 2023-25. In the years up to 2023, however, actual expenditure varied significantly from the planned appropriations in the Budget, mainly due to crises arising from COVID-19, the Russian war of aggression against the Ukraine, and energy inflation.

Once agreement has been reached on the spending allocations, the Government approves the draft budget by 15 October and submits it to Parliament for adoption by 1 December although this is not always the case (see below). The documentation associated with the annual budget is comprehensive. There are 10 annexes to the draft law, including an explanation of the macro-fiscal developments, the policies underpinning the National Public Budget and non-financial performance targets for institutions and programmes. It presents the budget on administrative, economic and functional classification. The economic classification is aligned with Government Finance Statistics (GFS) 2001 and the functional classification is aligned with the Classification of the Functions of Government (COFOG) standard. A programme classification with programme performance budgets is also presented. The programmes are not voted on by the Parliament; they are prepared for presentation purposes and internal management.

For several years prior to 2023, the need to reach agreement on the policies that are within the IMF's support facilities to Moldova, has resulted in key deadlines in the budget calendar being missed, which in turn has resulted in very short timeframes at key stages of the budget process, specifically the time available to CPAs to prepare and negotiate budget allocations and the time available for the Parliament to review and approve the final Budget. By way of illustration, the MTBF for 2023-25 was produced in October 2022 rather than in June when it should have been finalised according to the budget calendar. Also in 2022, the draft budget was submitted to the Parliament on 7 December, nearly two months after the deadline. The Parliament adopted the budget on 22 December, which meant that it took two weeks rather than the usual six weeks to debate and approve the budget. While a six week period for parliamentary debate on the budget is short by OECD usual standards, two weeks is insufficient. This lack of observance of the timetable diminishes the role of Parliament in the budget approval process. It also leads to uncertainty in CPAs as planning for the forthcoming year is impacted adversely. Observance of the timetable is a necessary foundation of a good budget system and should be a priority in future.

## 1.2. Budget preparation

The OECD found that the foundations of modern budgeting practices were in place in Moldova for the preparation of the government's budget. This finding was evident from initiatives that have introduced performance budgeting, spending reviews, and gender budgeting. Significant reforms have also been undertaken to strengthen the capital expenditure framework.

The OECD's recommendations to the MoF focus on ways to build on the progress achieved to date to improve the quality of the budget preparation process and the quality of information that informs budget decisions, in particular by:

- Improving budget transparency by providing narrative statements in budget documents on the context of budget decisions and by improving the accessibility features in budget documents, including visualisation, and summarisation of key points, to facilitate a clearer understanding of the budget.
- Aligning sectoral objectives, strategies and programmes with the MTBF and the budget by standardising budgetary classifications to better align them with the country's overall goals.
- Strengthening the assessment of budget performance and expanding spending reviews by establishing a programme of spending reviews to cover all expenditure over a specified number of years.
- Enhancing green and gender considerations in budget processes by adopting green budgeting and gender budgeting in the annual budget cycle.

To enhance the effectiveness of the capital budgeting system, three key areas to focus on are:

- A multi-year budgeting approach for capital projects to increase the predictability of budgets and the certainty of implementation,
- Establishing safeguards to control commitments by setting a cap on the value of contractual agreements that line ministries may make for each subsequent year, with exceptions subject to approval from the MoF.
- A methodology for project selection and management, and training resources for staff who prepare proposals for capital projects.

### 1.2.1. Structure of the budget

The State budget is cash based and it is structured according to five classifications:<sup>1</sup> i) organisational classification, ii) functional classification (COFOG), iii) classification of programmes, iv) economic classification, v) classification of sources. The structure of the budget classification, the components and the methodology were designed and approved by the MoF, approved in Parliament, and published in two volumes.

The economic classification is used to report government spending and to show the size and composition of the CPA budgetary operations. The COFOG classifies spending into broad areas of activity, such as defence, health and education. The functional classification is accompanied by informative notes describing the execution of the budget and the forecast budget for the following year. However, it does not include narrative on public policy and budget allocations by policies or projects, which would provide a better understanding of where and how government funds are being used. Both classifications are published in Volume 1.

The programme classification is published in Volume 2. It is for information purposes, and it is not used for appropriation. The programme classification comprises 188 Excel sheets, each of which contains a brief paragraph explaining the purpose of the programme and several budget lines. The sheets do not include detailed statements on policy, budget execution, trends, and targets.

From an OECD perspective, the narrative statements in a country's budget provide important context to the fiscal decisions being made by government officials and the public. They outline the reasons why certain decisions were made, an economic analysis of the decision, an assessment of the impact that locating funds in different programmes will have, and an explanation as to how money will be used to achieve different objectives. By linking the state's budget to specific strategies based on budgetary programmes, decision-makers can better understand how the budget supports the state's objectives, and make meaningful decisions based on that understanding.

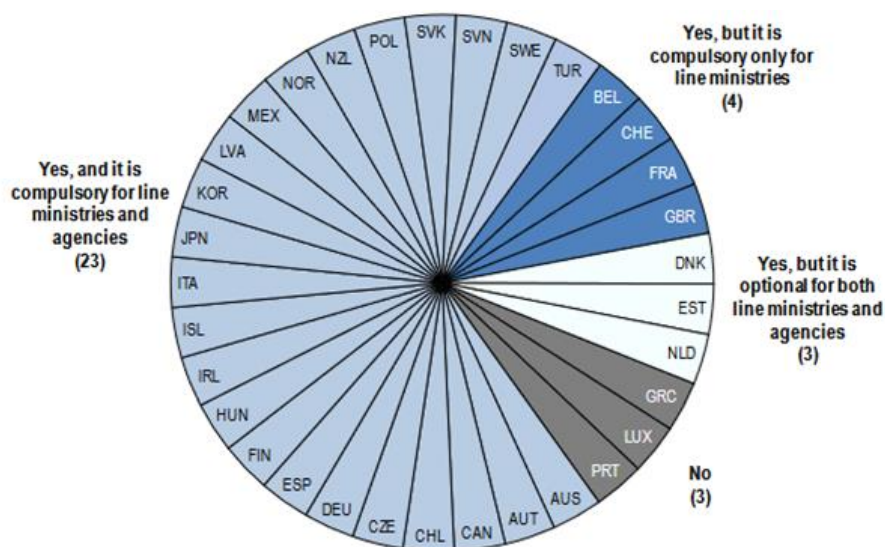
To provide better context of fiscal decisions, the Moldovan budget documentation should:

- **Provide more analysis:** The synthesis should include analysis of the impact of changes in the budget and how they will affect citizens.
- **Highlight variations:** Present comparisons between current and past budgets to highlight variations (e.g. in programmes), whether the variations are positive or negative. This can help explain what is happening to the budget and why changes are taking place.
- **Provide summaries of important points:** A summary of key points would make the budget more accessible to Parliamentarians and the public.
- **Summarise the economic impacts of the budget:** The budget should explain its estimated impact on the economy and citizens.
- **Increase the use of visual aids:** Fiscal reports and synthesised budget documents should include visuals such as charts and graphs that provide readers with an overview of the data.

### ***1.2.2. Programme and performance budgeting***

The use of performance budgeting is common among OECD countries (Figure 1). OECD countries have adopted performance budgeting practices to improve the efficiency, effectiveness, and accountability of government spending. Each OECD country tailors its approach to its specific governance structure, priorities, and contextual circumstances while sharing the common goal of delivering better results for citizens. For performance budgeting to be effective, it is important to develop programmes of expenditure under each ministry according to policy objectives of that ministry and to develop relevant performance indicators for those programmes. This helps decision makers compare costs and benefits of expenditure relative to the results that were achieved. Brief descriptions of performance budgeting approaches in selected OECD countries are included in Box 1.

Figure 1. Performance budgeting in OECD countries



Source: (OECD, 2019<sup>[2]</sup>)

In 2012, Moldova started a budget reform to modernise its budgeting system and improve the efficiency of budget management. Since 2012, the budget has been presented according to national priorities and strategies, by programmes and sub-programmes. Each programme is linked to a CPA. However, they are not aligned fully with the government's strategic objectives.

The OBL prescribes that the budgets will be drawn up and reported on performance-based programmes. It also assigns responsibility for this to the CPAs so each CPA proposes indicators when preparing budget proposals for submission to the MoF. The performance information developed during the budget process is for information purposes and is not published systematically. While Parliament has access to the information, other stakeholders do not.

The MTBF describes the medium-term fiscal strategy and the budget gives a broad outline of the programmes undertaken by each ministry. The OECD found that it can be difficult to reconcile the budget with the MTBF, for example to show how a budget allocation contributes to a medium-term policy objective. The MoF should establish a clearer link between the MTBF and the annual budget to show how the annual budget aligns to the Government's fiscal strategy.

The Government should publish the budget performance information that is submitted to Parliament to support the Parliament's access to expert and informed views regarding the draft budget. Similarly, at the end of the budget year, CPAs should publish performance information to report on the delivery of results and strengthen budget accountability. This would allow stakeholders, including the public, access to information on the authority's effectiveness in achieving results.

The MoF does not organise formal meetings and negotiations with CPAs on budget performance. The MoF does not systematically benchmark, challenge, or negotiate the targets. Additionally, there is no specific documentation which explains the performance methodology followed by line ministries regarding objectives, targets, and indicators. Having meetings on budget performance between the MoF and the line ministries during the budget negotiations would help to strengthen performance budgeting in Moldova. The meetings would clarify the priorities, objectives, indicators and targets of each ministry, and develop them beyond a bureaucratic exercise to which little attention is paid. They would also enable ministry representatives to demonstrate the case for budget proposals.

### Box 1. Examples of performance budgeting in OECD countries

**New Zealand:** New Zealand is known for its performance-based budgeting approach, which includes the use of "output budgeting." Departments and agencies are required to identify outputs and set performance targets, allowing for a focus on results and outcomes.

**Norway:** Norway's budgeting system focuses on performance through its "Responsibility and Results Framework." Agencies are required to set performance targets and are held accountable for achieving them.

**Sweden:** Sweden uses a results-based budgeting system where government agencies are required to set objectives, outcomes, and performance indicators at the programme level. The government assesses and evaluates the performance of agencies, and funding is allocated based on the achievement of results.

**United Kingdom:** The United Kingdom introduced the "Public Service Agreements" and "Sustainable Development Indicators" to align budget allocations with key government priorities and sustainability goals. The use of the "Three Es" framework (economy, efficiency, and effectiveness) is common in performance assessments.

### 1.2.3. Spending reviews

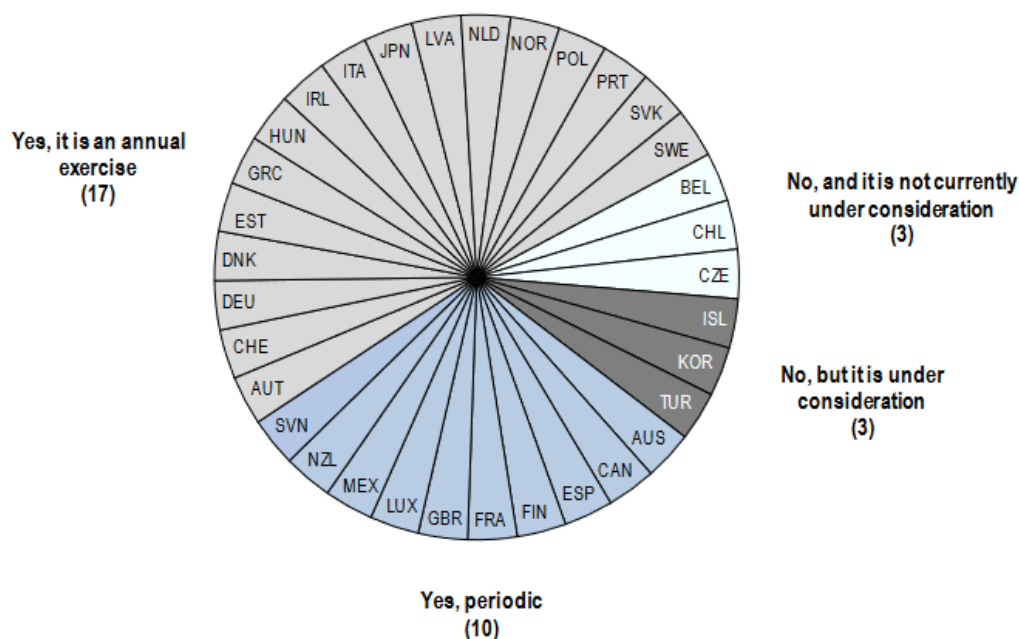
The government's existing baseline of expenditure is often the *de facto* starting point from which a government prepares its budget. Spending reviews look at this stock of existing expenditure and have a crucial role in helping governments manage public spending through reallocation of fiscal resources. The purposes of a spending review include:

- Enabling the government to manage the aggregate level of expenditure;
- Identifying savings and/or reallocation measures; and
- Improving effectiveness and efficiency within programmes and policies.

Spending reviews exist in nearly all OECD countries (Figure 2), though procedures vary from one nation to another (Tryggvadottir, 2022<sup>[3]</sup>). Spending reviews can concentrate on all government spending, or they can be more selective and focus on spending in particular sectors.



**Figure 2. Use of spending reviews by country**



Source: (OECD, 2019<sup>[2]</sup>)

During the period 2018-2022, Moldova piloted spending reviews on higher education, agriculture, and health. The main objective was to improve spending effectiveness and identify savings within programmes for approximately 0%-5% of total government spending. The recommendations from those reviews were finalised prior to the budget formulation process and included in the multi-annual expenditure baselines. However, the spending reviews were not carried out on an annual basis, and formal working groups were not used to resource the spending review processes.

Integrating spending reviews systematically within the annual budget process increases the likelihood of resources being allocated efficiently and effectively. The annual review process provides a structured approach to ensure that the proposed budget is based on accurate and up-to-date information and allows for any discrepancies to be identified and addressed. The spending review process also supports accountability by providing a feedback mechanism on how budget proposals from previous budgets were implemented.

The MoF should work with line ministries to develop a programme of spending reviews to ensure that all spending is subject to review over a specified number of years. In addition, attention should be given to including tax expenditure within the scope of spending reviews. Tax expenditure is a form of expenditure and can impact on the efficiency and effectiveness of government programmes. Brief descriptions of spending reviews in Denmark and the Netherlands are included in Box 2.

## Box 2. Examples of spending reviews Denmark and the Netherlands

### Spending reviews in Denmark

Denmark has conducted spending reviews since the 1980s. Built off close engagement and interest from political leaders, spending reviews have become an integral part of the Danish budgeting process over the past 40 years. The consistent application and use of spending reviews contributes to the budget process and has allowed successive governments to improve the quality of public spending by creating efficiencies and aligning spending programmes towards the key priorities of the government. The Danish spending review process aims to create fiscal space (“offensive reviews”), accommodate emerging budget pressures (“defensive reviews”), ensure value for money and review structural issues in the performance of spending entities (“opening black boxes”). Spending reviews are conducted on both a selective and periodic basis.

### Spending reviews in the Netherlands

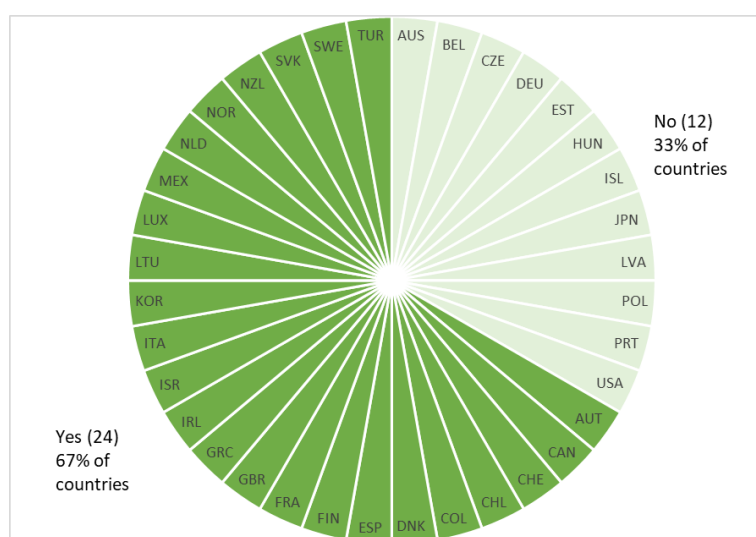
The Netherlands have conducted over 300 spending reviews since 1981. Like many OECD countries, the Netherlands conducted spending reviews to review, cut and focus government expenditure along the key priorities of the government following economic crisis in the late 1970s. With over 40 years of practice, spending reviews have become an integral tool for budgeting and actively feed into policy discourse and decision-making. Key elements of the Dutch system include an analysis of the existing strengths and weaknesses of existing policies, assessments of implementation costs, analysis of the role of government in effecting policies and policy options for spending cuts and improvements in efficiency and effectiveness. Specifically, they include the provision of policy options for savings, improving the approach to existing policy challenges, increasing effectiveness and efficiency, and addressing future policy challenges (i.e. pensions, climate change).

### 1.2.4. Green budgeting

Moldova’s climate policy is focussed on taking the necessary measures to reduce the volume of greenhouse gases released into the atmosphere and to support the country’s adaptation to climate change. This policy focuses on energy efficiency, renewable energy, transport, adaptation to climate change, sustainable agriculture and forestry, and hydropower. The government has set an ambitious target of reducing emissions by at least 20% between 2009 and 2030 and has committed to achieving 30% renewable energy by 2025. To support adaptation, Moldova has created a National Climate Change Adaptation Plan for 2020-2030, which includes energy efficient policies, such as mandatory energy efficiency labels for new appliances, incentives for investments in energy efficiency measures, and fiscal incentives for renewable energy technology.

Despite these ambitious policy objectives, there has been little progress on the development of green budgeting in Moldova. In 2023, the topic was being discussed by the MoF and the Ministry of the Environment. Green budgeting is an approach to managing public finances with sustainability as a primary consideration. It considers climate and environmental factors when allocating resources and considers long-term objectives. Green budgeting should be integrated into the annual budget cycle to advance Moldova’s EU accession by showing the relationship between fiscal resources and policy objectives on climate change and the environment (European Commission/IMF/OECD, 2021<sup>[4]</sup>). By 2022, 24 OECD countries out of 38 had introduced green budgeting (Figure 3).

**Figure 3. Green budgeting in OECD countries**



Source: (OECD, 2024<sup>[5]</sup>).

Green budgeting practices vary among OECD countries for a variety of reasons. Each country tailors its approach to green budgeting based on its specific circumstances, policy objectives, and levels of commitment to environmental sustainability. The most prevalent budgetary tools refer to carbon pricing mechanisms (22 countries, + 83% compared to 2021), environmental impact assessments (18 countries, + 33% compared to 2021), and green tagging (13 countries). These are all options from which the Moldovan Government could choose. The important thing is that introduction of green budgeting should be implemented gradually and with regard to the resources and capacities that are available. Box 3 contains relevant examples of green budgeting in OECD countries.

### Box 3. Examples of green budgeting in OECD countries

**Ireland:** Since 2018, Ireland developed several tools such as environmental impact assessments of individual budget measures, green budget tagging, environmental cost benefit analysis in its public spending code and an environmental tax reform. In 2022, Ireland adopted a carbon budget programme that comprises three, five-year economy-wide carbon budgets. The carbon budgets were approved by both Houses of the Oireachtas in 2022. The total emissions allowed under each budget, as well as the average annual reduction for each five-year period.

**Lithuania:** The implementation of green budgeting is monitored through the performance of environmental indicators that are set when developing budget programmes. The government's National Progress Plan is to contain information on the progress and performance of environmental objectives and includes monitoring information.

**United Kingdom:** The Green Book, a central government guidance on the appraisal and evaluation of public policies, programmes, and activities, uses a performance and programme-based budget structure. This document provides information on the evaluation process from design to evaluation, and also includes a climate and environmental lens focus. Furthermore, the Treasury itself offers training to both business leaders and government ministries regarding the application of the Green Book.

### 1.2.5. Gender budgeting

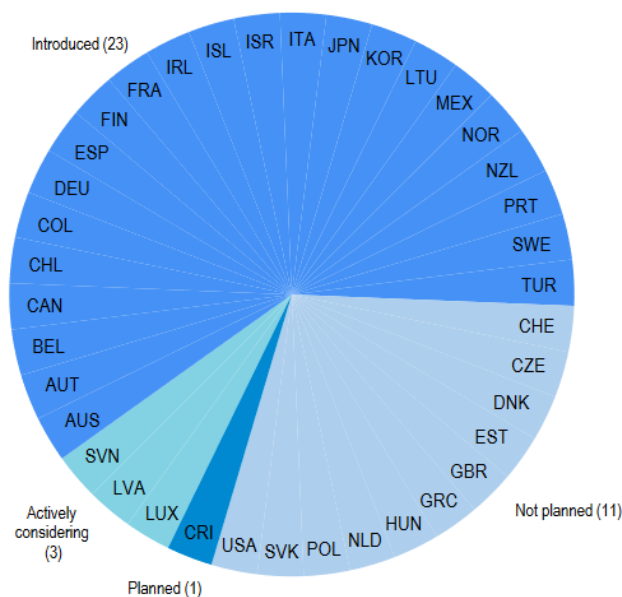
There are several initiatives in Moldova aimed at eliminating gender inequality in the country. These initiatives include education about gender equality and promoting the full participation of women in the workforce and society in general. This includes providing broader access to education, resources, and services for women, as well as implementing laws and policies that promote gender equality. The Ministry of Labour and Social Protection has the lead role in this policy area.

An increasing number of OECD countries are recognising the power of gender budgeting as a tool to help close gender gaps. The benefits of gender budgeting include:

- An improved evidence base upon which resource allocations decisions can be made.
- Improvements to the effectiveness of the budget in closing gender gaps.
- Removal of inherent gender biases from key government processes and tools.
- Greater transparency on the impact of the budget on different groups across the population (OECD, 2023<sup>[6]</sup>).

Similar to the majority of OECD countries (Figure 4), Moldova has also made some efforts to introduce gender budgeting. For example, since 2019, Moldova included gender indicators in its budget circular, such as the number of women and men affected by particular policies. The Ministry of Finance also has a gender budgeting project for 2023-2027 which the Government approved in April 2023, with the objective of integrating a gender sensitivity framework for health, education, labour market, social protection, entrepreneurship, refugees and rural development into the budget.

**Figure 4. Gender budgeting in OECD countries**



Source: (OECD, 2023<sup>[7]</sup>)

It is laudable that gender budgeting is being taken forward in Moldova but there is opportunity to strengthen the approach in order for it to be an effective tool. The OECD publication *Designing and Implementing Gender Budgeting* sets out a framework for an effective and enduring gender budgeting practice, based on the following elements:

- **Institutional and strategic framework:** The political commitment and governance arrangements for an enduring approach to gender budgeting, including a legal framework, institutional roles and responsibilities and national gender equality goals.
- **Methods and tools of implementation:** The tools used to apply a “gender lens” at various stages of the budget process.
- **Supportive enabling environment:** The supportive elements which help ensure a more effective gender budgeting practice, including guidance, capacity building and independent oversight mechanisms (Downes and Nicol, 2020<sup>[8]</sup>).

Several developments would help Moldova align its gender budgeting project with the OECD framework. For example, a legal underpinning for gender budgeting would help solidify the approach and ensure its sustainability over time. In addition, the Ministry of Finance could have a more prominent role leading gender budgeting. As of 2023, the Ministry of Labour and Social Protection was taking the lead in developing a roadmap for the implementation of gender budgeting, but the Ministry of Finance would be better placed to do this in co-ordination with the Ministry of Labour and Social Protection. In designing and implementing its approach to gender budgeting, it could be useful for Moldova to consider experiences in OECD countries (Box 4).

#### Box 4. Examples of gender budgeting in OECD countries

**Canada:** Canada’s Gender Budgeting Act in 2018 made gender budgeting a permanent part of the federal budget-making process. It calls upon the Government of Canada to enhance its financial operations by taking into consideration gender and diversity when making budgetary decisions. The Act requires the Minister of Finance and the President of the Treasury Board to provide reports publicly on the effects of gender-oriented analysis of all fiscal measures, tax exemptions and expenditure programmes in order to make sure accountability and transparency prevail.

**Ireland:** In 2018, the Irish Government launched a pilot initiative for equality budgeting and all 18 departments within the country now actively participate in the initiative. An Equality Budgeting Advisory Group has been created to facilitate the implementation of equality budgeting, with senior representatives from within government as well as experts from outside government.

**Spain:** The Constitution of Spain, established in 1978, proclaims the equal rights of all individuals and outright bans any discriminatory practices. In 2007, the Spanish government established a legal obligation to conduct *ex ante* gender assessments as well as the practice of gender budgeting to ensure the inclusion of a gender perspective in the design, implementation, and evaluation of policies, laws, and programmes.

### 1.2.6. Capital investment

Capital spending in Moldova was a source of concern for several years, with under-developed appraisal, evaluation and monitoring procedures. Following the 2019 IMF Public Investment Management Assessment report, new legal requirements were adopted in 2022<sup>2</sup> to underpin a more robust public investment management and capital budgeting system. This development should result in better value for

money from public investment although it is not yet fully operational and it does not cover capital investments by various budget funds such as the Road Fund, and the Environment Fund.

Under the new procedures, the Working Group for Public Capital Procedures chaired by the MoF has overall direction of the capital spending processes. The aim is to have a standardised approach to the selection of capital projects. Projects must be submitted to the Working Group and must be accompanied by justifications and costings. Depending on the size of the project, supporting analysis (e.g. projects over MLD 200 million must contain a cost-benefit analysis) is also required. Any new capital investment proposals must be in line with the Government's strategic plan and the sectoral strategic plans. The MoF proposes the allocation of capital spending based on the government's existing commitments to complete capital projects, and new projects subject to available resources. Once approved by the Cabinet, the details can then be included in the MTBF and the annual budget. One of the aims of the new system is to establish a pipeline of projects and to move away from an *ad hoc* approach to managing capital expenditure.

The ministry that proposes a capital project is responsible for monitoring its implementation and submitting progress reports each March to the MoF. Under the new procedures there is provision for an *ex ante* review of projects although this feature has yet to be implemented.

One of the issues that remain in the capital budgeting system is the inability to provide multi-annual funding for capital projects, with funding being allocated on an annual basis. There is also no provision to carry-over of funds where there was a delay in a project. The approach hampers the implementation of projects and budgets. To address this issue, investment projects should be agreed on a multi-year budget basis. This would provide more stability and certainty for implementation of capital projects and budgets. Consideration by the MoF should be given to the allowing carry over funds (subject to specified limit) where this has occurred due to delays in a project. Without the certainty of multi-year budgeting, the government may struggle to maintain consistent funding for important projects or may have to delay or cancel projects if the budget is unexpectedly cut.

Even where there is agreement on a ministry's multi-annual allocation, there should be a limit on contractual commitments or binding agreements. This limitation would ensure that the value of binding agreements made by a line ministry in the current year would not exceed in respect of each of the subsequent three year's allocation, for instance, 75% in the first year, 60% in the second year and 50% in the third year. These limits would be rolled over each year. If the ministry believes the limits need to be exceeded, they should be discussed with the MoF to ascertain whether the limit should be exceeded on an exceptional basis.

The standardised approach to assessing projects for selection could be strengthened by developing a methodology for project assessment and training of staff in bodies that will be submitting projects. MoF should seek support for a training programme to develop skills in the public service in this regard. It may be beneficial for the MoF to consider good practices internationally and the documentation available in countries that could be adapted to the Moldovan context, such as the Irish Public Spending Code (Department of Public Expenditure and Reform of Ireland, 2019<sup>[9]</sup>).

### 1.3. Budget oversight

The OBL provides the Parliament with powers to carry out its role regarding the consideration and approval of the budget. The most significant limitation to this role is the time available for Parliament to consider the draft budget. A parliamentary budget office is a proven mechanism to provide support to parliamentary committees, and members generally, when considering the draft budget.

The establishment of an independent fiscal council would also strengthen fiscal governance, bolster oversight capacity of the Parliament and increase public awareness on the fiscal sustainability of public finance.

The OECD found that the Court of Accounts operates under well-developed legal and institutional arrangements. The Court completes a consistently high volume of audits, and the audit reports are submitted to Parliament in a timely manner to support the Parliament's consideration of the coming year's draft budget. Further progress is possible on the rate at which the government implements the Court's recommendations.

#### 1.3.1. Role of parliament

In accordance with the Constitution and the OBL, the Government must submit for parliamentary approval the annual budget law, any laws amending the budget and any laws establishing extrabudgetary funds. There are two standing committees that are responsible for budgetary matters. The Committee for Economy, Budget and Finance co-ordinates the consideration of draft budgets. The Standing Committee for Control of Public Finance is responsible for examining annual reports including the reports on the executed budgets of the state budget, the social insurance fund, and the medical insurance fund.

The OBL provides that the annual budget is presented to the Parliament by 15 October each year for adoption by 1 December (Table 3). This means Parliament has just six weeks to review the budget, which is not in line with the *OECD Best Practices for Budget Transparency* that recommends a minimum of three months for parliamentary scrutiny of a draft budget (OECD, 2002, p. 8<sub>[10]</sub>). The actual practice can result in a period shorter than six weeks. For instance, the 2023 budget was submitted to the Parliament on 7 December 2022 and was approved on 22 December 2022.

The relatively short period to consider the budget is mitigated to some extent by the requirement for the MTBF, which contains the pre-budget fiscal policy statement, to be submitted to Parliament by 1 June. While the MTBF is submitted for information purposes, its availability means that parliamentarians and other stakeholders can make use of the information when considering the proposals that are contained in the budget. In addition, the OBL provides that the Court of Accounts tables in Parliament the audited annual reports on the execution of the state budget, the state social insurance budget and the mandatory medical assistance insurance funds by 1 June for approval by 15 July, which further adds to the information available to parliamentarians when they consider the upcoming year's draft budget. The reports are published on-line.

**Table 3. Parliamentary approval of the budget**

Budget Task	Timetable
Developing and approving the annual budget law	<ul style="list-style-type: none"> <li>By 1 June, the MTBF including pre-budget fiscal policy statement, is presented to Parliament for information purposes</li> <li>By 15 October: the <b>draft budget</b> is submitted to Parliament</li> <li>By 1 December: the <b>State Budget Law</b> is approved by Parliament</li> </ul>
Audit of budget execution	<ul style="list-style-type: none"> <li>By 1 June (year n+1), the Court of Accounts submits annual audited report on the executed budget to Parliament</li> <li>By 15 July (year n+1), the Parliament approves the audited report</li> </ul>

Article 54.4 of the OBL empowers Parliament to amend the draft budget provided the amendments comply with the “principles and budgetary fiscal rules established by this law”. This means not breaching the fiscal rule limiting the deficit to 2.5% of GDP and ensuring that the costs of amendments are met by offsetting savings. Historically, the government has accepted amendments put forward by the Parliament if they comply with these requirements.

The government may propose amendments to the annual budget subject to several conditions, one of which is that the process must be the same as for the approval of the annual budget. This means that parliamentary approval is required and that the proposal can be amended. In addition, the proposal must be accompanied by an information note that explains the necessity of the proposal and its impact on the MTBF. Another condition is that there can be no more than two amendments in a fiscal year and that, in general, amendments cannot be adopted prior to 1 July and later than 15 November.

The fiscal rule can be set aside in exceptional circumstances. During such a period, the Government must report to the Parliament every six months on the budget position and the measures it is undertaking to bring the deficit below the 2.5% limit.

The OBL requires (Article 53.7) that the budgets are presented for approval according to an organisational classification, a programme classification, and an economic classification “to ensure the control of certain budgetary indicators by the Parliament”. Potential areas to strengthen in the application of the Article are the focus on programmes, performance indicators and the medium-term perspective.

### **1.3.2. Parliamentary committees**

The Committee for Economy, Budget and Finance is responsible for the consideration and approval of the draft budget. It is not the only committee that analyses the draft budget because debates on the draft budget take place in several parliamentary committees before its presentation to the plenary. However, it co-ordinates all inputs and proposals from the other committees.

There are two readings of the draft law. At the first reading the Committee presents the report on the draft budget and the total revenue, expenditure and budget balance are approved. For the second reading, the Committee prepares a report that contains proposed amendments from parliamentarian, proposals from the other committees and the Government’s responses to the proposed amendments. Government ministers and officials may be asked to explain and answer questions on their budget requests. Other entities, including the autonomous institutions, and experts from academia or civil society, can also be invited to give views.

Despite the wide-ranging responsibilities of the Committee and the complexity of budgetary information, the technical support available to the members is limited to two full-time and experienced officials. As such, it places a priority on arranging contributions from experts and other stakeholders during committee hearings. Topics that are relevant to the Committee’s report include expert views on the outcomes that are to be achieved from spending proposals and the relevance of the performance information that forms part of the budget documentation.



The establishment of the Committee for Public Finance Control in 2020 strengthened parliamentary scrutiny of the audit reports produced by the Court of Accounts. The Committee examines the annual reports of the government on the execution of the state budget and the insurance funds on behalf of the Parliament, which is responsible for approving them. In 2020, it examined 45 reports of the Court of Accounts. Each report on the budget by the Committee can be accompanied by recommendations for improvement and all reports are published. The members consider that the relationship with the Court of Accounts works well.

Consideration could be given to establishing a parliamentary budget office to provide independent expertise to parliamentarians in the budget process. In several OECD countries, parliamentary budget offices have boosted parliamentary scrutiny and quality of debate on budgeting and public finance (Box 5).

### Box 5. Parliamentary Budget Offices in Austria and Ireland

In Austria, the Parliamentary Budget Office (*Budgetdienst*) directly supports the Budget Committee to improve the ability of Parliament and the Budget Committee to engage with the budget process and providing analysis of budget documents (particularly performance budgeting). Specifically, the Parliamentary Budget Office provides independent analyses on all budget-related documents focussed on fiscal policy, development of income and expenditure, tax revenue and the adequacy of budget allocations in relation to economic forecasts, performance information and gender budgeting (von Trapp, Lienert and Wehner, 2016<sup>[11]</sup>).

In Ireland, two bodies – the Oireachtas Parliamentary Budget Office and the Fiscal Advisory Council – provide independent analysis to inform budget debate and provide transparency and accountability (von Trapp, Lienert and Wehner, 2016<sup>[11]</sup>).

### 1.3.3. A fiscal council

Supplementing the role of a parliamentary budget office is a fiscal council. With the Parliament having limited internal capacity to undertake independent analysis of the budget, the views of a fiscal council can inform budget debates, contribute to better decisions, and increase public awareness on the fiscal sustainability of public finance.

Although Moldova does not have a fiscal council, the establishment of such a body has been considered. A report on this subject, *Report on a possible Fiscal Council for Moldova and options for its institutional setup*, is available on the MoF website (Ministry of Finance, n.d.<sup>[12]</sup>). The report highlights the key factors in establishing a fiscal council and suggests two options. However, it also emphasises that its establishment is a medium- to long-term concept because it is also important to build capacities of the MoF.

The importance of addressing capacity challenges in the MoF notwithstanding, the development of a fiscal council in the context of the EU accession process is important because it is a requirement for EU members to establish such a council. Based on the OECD's analysis in this review, Moldova should work towards the creation of an independent fiscal council to support its EU accession and credible fiscal management. Ultimately, a Fiscal Council would instil confidence in Moldova's level of economic preparedness for EU accession, helping to ensure a smoother transition.

While institutions such as the MoF and the Central Bank should not find themselves competing with a fiscal council for a limited pool of available expertise, other small countries have managed this concern through secondment arrangements and developing junior officials from within the organisation in readiness for more senior responsibilities.

### 1.3.4. Court of Accounts

The Moldovan Court of Accounts (*Curtea de Conturi a Republicii Moldova, CCRM*) is responsible for audits and reviews of government bodies and other public sector entities. The Court consists of 161 officials, including seven board members. According to the Law on the Organisation and Functioning of the Court of Accounts of the Republic of Moldova No. 260/2017, the Court is responsible for providing independent assurance that government entities are accountable for their use of public funds, and that these funds are being allocated, managed, and used efficiently and effectively. The Court also has responsibility for developing and implementing audit standards, systems, and procedures to support its mission.

The legislative framework assures the independence of the members and the President, along with the functional independence of the Court. In practice, there has been no moves to remove members and the law provides that parliamentary approval would be required if such an attempt were to take effect. Also, the law provides that the Court conducts its role independently of the Government. However, the financial independence is not absolute. As with the other independent institutions, the Court's draft budget is passed to the MoF before being approved by Cabinet and submitted to Parliament for adoption. The Court has the right to appeal its draft budget to Parliament if it considers the allocation is inadequate.

From 2020-2021, the Court encountered difficulties in accessing information. It informed the Public Finance Control Committee on the matter, and in 2023 the President of the Committee raised the matter in Parliament. This led to the matter being raised with the government and since then, access to information has improved. The process, however, can still be slow. Delays in the process whereby public authorities transmit information to the Court can be improved by:

- The Court should regularly review its procedures to ensure requests for information are not duplicative or unnecessarily detailed.
- Transmission of information could be sped-up if the Court and the relevant entity could use an automated interface to transfer information electronically instead of relying on paper.
- The Court could provide feedback throughout the process to improve the speed with which information is transmitted.

The Audit Law provides the Court with a mandate to conduct financial, compliance and performance audits in accordance with the International Standards of Supreme Audit Institutions (ISSAI), and to audit all public entities and resources. The Court does not audit the State's consolidated account because it is not submitted by the government. However, it audits the annual reports on the Execution of the State Budget, the two insurance funds and the CPAs' consolidated financial reports. In 2021, the Court conducted 61 audits, compared with 54 in 2019. The audits concerned compliance (28 audits, compared with 10 in 2019), financial (26 audits, compared with 34 in 2019) and performance (6 audits, compared to 5 in 2019), while there was one follow up audit compared to five in 2019. In 2021, the Court submitted 1 215 recommendations. As of 2022, 235 had been implemented (19%), 255 had been partially implemented (21%) and 725 remained unimplemented (60%). Monitoring the implementation of its recommendations is an integral part of the Court's activity. It has developed its own information system to monitor recommendations to which the audited institutions have access for recording progress with implementation. (OECD, 2023<sup>[13]</sup>)

To ensure the quality of audits, the Court has measures in place including the use of manuals, which are in line with ISSAI requirements, for each of the three types of audit. There is also a Quality Management Guide for ensuring quality management procedures. The Audit Law provides the Court with the responsibility for the certification of public auditors, along with a training and development process.

## 1.4. Budget execution, control and transparency

The Ministry of Finance maintains a robust operational framework for cash management, budget flexibility and execution. Cash management benefits from strong cash flow planning. The financial systems in Moldova prevent the government from entering unfunded commitments and arrears are low.

The reliance on supplementary budgets at a relatively early stage of the fiscal year indicates the potential to improve the sequence of events in the budget calendar and strengthen capacities in macro-fiscal forecasting.

A robust legal framework is in place for internal controls and internal audit, but the implementation of the framework would benefit from further development across central government and local authorities. There should also be greater monitoring of the extra-budgetary operations in the central government which are around 6% of annual expenditure. These operations should be brought within the budget and have the same accountability arrangements that apply to CPAs.

Budget transparency has improved since 2017 and is consistent with OECD countries in the region. Areas to improve focus on the explanatory information monitoring reports, notably the mid-year report. Adhering to the six-week period in the budget calendar for the Parliament to consider and approve the proposed budget would help to ensure public engagement by parliamentary committees during that period.

### 1.4.1. Cash management

The OBL specifies that there is a Treasury Single Account (TSA) and that all revenues are paid into it. The account is operated by the Central Bank. All budget users including the Social Insurance Fund, the Health Insurance Fund and local authorities are included in the TSA. Accounts with commercial banks are not used by central budget bodies nor by local authorities (although some publicly funded bodies who are outside the remit of the central government do use commercial banks).

Cash flow projections are developed in January of each year. These projections are developed by the Treasury with input from the constituent bodies. The projections are updated every month and, subsequently, adjusted weekly forecasts are developed over the year. The social insurance and health insurance funds submit their cash flow reports to the Treasury every month. The published cash flow reports are not detailed by budget organisation or administrative unit but rather on an economic classification basis.

Arrears are low in Moldova. According to the authorities, the stock of arrears (central government and local authorities) account for less than 0.1% of overall spending. Arrears are classified as payment due beyond a 60-day threshold, this having been increased from 30 days in 2016. In general, most arrears are at the local level. The local authorities report monthly on arrears. In the analysis of Fiscal Risks, the main causes of arrears are listed and include such reasons as insufficient budget allocations and non-financing of repair works and capital investments. Arrears for the State-Owned Enterprises are reported to the National Board of Statistics which publishes the data.

### 1.4.2. Budget flexibility and execution

In terms of spending, the OBL allows the reallocation of spending during the year subject to various rules. As is normal in OECD countries, minor changes are allowed without MoF approval while larger transfers require either the approval of the MoF or the Cabinet. Budget spending is not apportioned on a monthly basis by the MoF. The level of spending is controlled by the Treasury based on available funds including

commitments. Any new commitments which a spending unit wishes to incur will only be allowed if it does not exceed the remaining balance in its annual allocation.

Supplementary budgets are a fixture in Moldova. There have been 2-3 per year in the last three years. This was expected during the COVID-19 pandemic and the impact of the war of aggression against the Ukraine. However, according to the MoF it is normal to have a supplementary budget in July each year, subject to additional resources becoming available. There is also normally a supplementary budget late in the year which would be a more normal feature of budgeting in OECD countries.

There should not be a need for a supplementary budget in July unless there is an emergency where unforeseen circumstances arise. The annual budget should be sufficiently accurate to cater for normal planned spending over a budget year. The authorities should ensure that the annual budget provides sufficient funding to only require a supplementary towards the end of the year to deal with normal reallocations and adjustments. This requires more accurate and timely forecasts so that the annual budget can allocate sufficient funds and avoid multiple supplementary budgets in a given year, except in exceptional circumstances.

### **1.4.3. Internal control and audit**

The Central Harmonisation Unit in the MoF co-ordinates and supports the development of internal control and internal audit structures of both central and local government institutions. The National Internal Control Standards provide detailed instructions for the management of CPAs on the implementation of internal controls, and the application of the standards includes the insurance funds and local authorities. The MoF's PFM Strategy 2023-2030 contains development targets for internal control, with reform proposals to enhance managerial accountability. The development of internal controls includes the CPAs as well as the MoF.

The MoF compiles an annual consolidated report on public internal financial control (PIFC) using information from the CPAs which are required to provide information to the MoF. The report provides information on each institution and highlights progress by comparing relevant data with the preceding year. The report is tabled at Cabinet, and the Government can issue specific actions to improve internal controls.

There are significant challenges, however, in the implementation of internal controls at the management level. Basic managerial accountability mechanisms are not yet in place throughout the institutions. The delegation of routine tasks beyond ministers or state secretaries is low. Risk management is not practiced consistently. There is a government decision requiring institutions to report on irregularities but some major institutions do not report on such irregularities.

For internal audit, legislation prescribes the operational arrangements. This includes a minimum of three staff in an internal audit unit and a provision for internal audit arrangements to differ depending on the type and size of the institution. Internal audit units are established in all ministries, in both insurance funds and about 90% of local authorities. The consolidated PIFC report shows that most recommendations are implemented or are in the process of being implemented. However, only 76 of 131 established units are reported to be functioning. Just under 40% of functioning units prepare a strategic plan and about 70% prepare annual audit plans.

Of 134 internal auditors in the public sector, only 54 people hold professional qualifications. However, a continuous professional development programme is being implemented. Of even greater concern is that the national requirements for minimum staffing levels for internal audit are met by only three of the 13 ministries, including the MoF and both insurance funds, and only three of the 35 second level local authorities. There is a formal external quality assurance process but only three units applied this process in the most recent year.

Overall, there is a sound legislative framework for internal control and internal audit but the implementation of both is under-developed. Applying fundamental activities of internal control by management and upgrading the number of qualified personal the internal audit units should be priorities for the authorities. Addressing internal audit capacity constraints within the institutions will help to safeguard the quality and integrity of the budget process. Enhancing senior management awareness of the importance of accountability can help to develop performance management across the public administration.

#### **1.4.4. Financial monitoring and reporting**

In Moldova, the financial reporting framework is a set of rules, systems, and processes used to measure, assess, and report financial information. The framework includes guidance on how financial information should be presented, organised, and analysed. The framework includes a set of reporting formats that require a consistent method of financial reporting for every ministry to ensure that all budget-related information is presented in the same format and gives clarity to financial information. The framework has its own set of key elements to be reported, such as cash flows, revenue, expenses, assets, liabilities, and shareholders' equity. The financial reporting framework also dictates how the reported information should be presented, such as whether to use International Financial Reporting Standards (IFRS).

Budget execution reports are on a monthly, semi-annual and annual basis. They are produced by the treasury system, and they show deviations from the approved budget, as well as comparisons with budget execution in the previous year. While monthly reports do not analyse deviations from the budget, the semi-annual and annual reports are more comprehensive.

The Report on Execution of the State Budget is prepared annually in accordance with the Law on the State Budget for the relevant fiscal year and OMF No. 216/2015 and OMF No. 44/2018.<sup>3</sup> The annual financial report is comprehensive for the central government and is published within six months of the end of the financial year. The format mirrors the presentation format of the budget. It notes and explains variations from the original budget allocation. It contains an analysis of state assets and liabilities, including state guarantees and contingent liabilities, including information on transfers and disposals.

The budget and the year-end financial report are on a cash-basis. Starting from 1 January 2016, accounting and financial reporting in all CPAs are in accordance with the Chart of Accounts for the Budgetary System under OMF No. 216/2015. The Chart of Accounts is aligned with economic classifications in the budget and GFS 2001. Work has been ongoing with external assistance to develop new accounting standards based on IPSAS and this is one of the PFM reform objectives.

The CPAs, including the National Social Insurance Fund and the National Medical Insurance Fund, prepare financial reports based on the 2014 Accounting Law (Article 74, Law No. 181) and in accordance with the terms and requirements established by the Ministry of Finance. The records of the receipts and payments of the National Social Insurance Fund and the National Medical Insurance Fund are based on each institution's own accounting plans, with the use of information systems specific to the fields of activity in the 2014 Accounting Law.

The MoF monitors the implementation of the budget during the year and publishes monthly reports. However, these reports simply outline the receipts and expenditure and give no detailed commentary on the progress of the budget or on future commitments. They comprise a short (4 pages) summary report and several excel sheets. The reports compare the figures for the current year with those of the previous year and the planned annual amounts for the current year. The MoF does not prepare a forecast early in the year for the expected monthly evolution of the budget detailed by budget user or revenue category against which the monthly spending and revenue figures can be gauged. The monthly figures are not broken down by ministry/budget body. The two main funds (Medical and Social Insurance) are included in the figures.

Quarterly reports are also prepared but these are not published although they are used by the MoF for budgetary analysis. The two large funds – for social insurance and for medical insurance also send quarterly execution reports to the MoF, but these are paper based and switching to digital reports would speed up integration of their data into the various MoF reports.

The MoF prepares a more detailed half yearly report which is usually published in September (although the budget calendar specifies its publication in mid-August). This report covers macroeconomic developments, developments on the evolution of the state budget, including changes to public debt and remuneration. The half yearly report would be better published in July rather than in August/September as it could feed into the budget preparations and provide more up to date information on the evolution of the current year budget for budget users and the MoF. It would also be useful to budget users and other stakeholders for the quarterly reports to be distributed within government and/or published on the MoF's website. The MoF should prepare a forecast at the beginning of the year on the likely monthly figures for both revenue and expenditure to inform budget implementation and cash management.

There are significant extrabudgetary operations that are outside the national public budget. These are not reported during the budget execution process and are not subject to scrutiny by the MoF. There are 160 units of central government that are in receipt of budget funding but also have extrabudgetary operations. These units are self-managed institutions that are subordinated to ministries and CPAs but are in receipt of fees and charges which they are not required to report in the budget documents. These receipts are not included in the MTBF or annual budget figures. Furthermore, these amount to about 6% of the total state budget, which is material. It should be noted that all public bodies including the self-managed units are required to use the TSA and they are prohibited from operating accounts in commercial banks.

As stated above, the local budgets are monitored by the MoF, however the MoF does not monitor the financial statements of local authorities. The MoF publishes an annual consolidated local budget execution report, and also a similar monthly report so there is regular monitoring and reporting. However, currently the Court of Accounts has capacity to carry out audits of only a small number of these institutions each year and it focuses on the largest ones.

Although the SOEs are subject to audit, the Court of Accounts does not carry out regular audits and the audits are mainly compliance audits. In addition, the financial reports of SOEs are often published between six and nine months after the financial year ends, which means that financial pressures may only come to the attention of the MoF with a delay. Nevertheless, SOEs are required to report quarterly to the MoF and so they are subject to regular monitoring.

#### **1.4.5. Budget transparency**

In Moldova, the MoF publishes extensive public expenditure information, with monthly updates for some headline budgetary aggregates. The MoF publishes a Citizens Budget, which presents the key aspects of the budget in a format that can be easily understood by citizens (Ministry of Finance, 2023<sup>[14]</sup>). It also publishes a Citizens Report on the financial statements of the government, which contains data on revenue and expenditure, public debt, and foreign assistance (Ministry of Finance, 2022<sup>[15]</sup>).

A significant amount of information is presented in a PDF format, which makes it difficult to search and time-consuming to download. Efforts to consolidate information in a simplified format could make information more accessible to the public. Furthermore, the level of detail in the published documentation could be increased, relative to the budget reports prepared in OECD countries. For instance, the Moldovan budget reports could include information on new policy initiatives, performance indicators, and long-term projections (five years or more) for capital expenditure.

The PFM Reform Strategy 2023-2030 recognises the importance of transparency at all stages of the budget process. It specifically states the need to improve Moldova's rating in the Open Budget Survey Transparency Index (International Budget Partnership, 2021<sup>[16]</sup>). Its rating in the most recent (2021) survey

is 65 out of 100, which compares well with several EU countries but is below the rating of countries such as Sweden, Italy and France. The Strategy includes several activities to enhance transparency such as the inclusion in the TSA of the revenues and expenditures of the self-managed subordinate institutions and the annual publication of performance information by all CPAs. In the long term, the welcome objective is to improve the rating in the Open Budget Transparency Index and to publish evaluations of the efficiency and effectiveness of service provisions by most ministries every five years.

In terms of citizen engagement during the approval stage of the budget process, hearings by standing committees are held in public but there is no other means of engagement between the public and Parliament. The tight budget timetable limits the opportunity for public engagement on the draft budget by the Parliament. Observing the six-week period in the budget calendar for the Parliament's consideration of the proposed budget would assist consideration of ways to expand public engagement during the approval stage.

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## Notes

<sup>1</sup> Article 26. of the law no. 181 on public finances and budgetary-fiscal responsibility from 25 July 2014.

<sup>2</sup> Government Decision 684 of 2022

<sup>3</sup> OMF No. 216/2015 on the Chart of Accounts in the Budgetary System and Methodological Norms on Accounting and Financial Reporting in the Budgetary System.

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**From:**  
**OECD Journal on Budgeting**

**Access the journal at:**  
<https://doi.org/10.1787/16812336>

**Please cite this article as:**

Finn, Brian (2024), "Budgeting in Moldova: Strengthening public finance management", *OECD Journal on Budgeting*, Vol. 24/1.

DOI: <https://doi.org/10.1787/1ae6b030-en>

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