Algemene administratie van de THESAURIE

Administratie Internationale en Europese Financiële Aangelegenheden

Administration Générale de la TRESORERIE

Administration Questions Financières Internationales et Européennes

Brussels, 22 October 2018

Mr. Marco Buti,
Director General
European Commission – DG ECFIN
Rue de la Loi, 170
B-1040 Brussels

Dear Mr. Buti,

In response to your letter dated 19 October 2018 and with reference Ares(2018)5388020, concerning the 2019 Draft Budgetary Plan, I would like to emphasize the following points:

Since it came into power in 2014, the current Belgian Government embarked on a series of very important reforms such as the tax shift, the pension reform, labour market reforms and recently the corporate tax reform and public administration reform. All of this was done in order to restore competitiveness and fiscal sustainability and create growth and jobs. The positive impact of some of these reforms can already be seen in the economic environment, the thousands of new jobs that were created, the economic resilience of the Belgian economy and the growth figure. Many of these reforms, however, have in the short term a negative impact on expenditures and for some of them it takes several years before the positive impact is visible. The objective of the Belgian government has always been to find an equilibrium between structural reforms, investment and fiscal sustainability. The recent launch of the Belgian plan for strategic investments is part of this policy.

Furthermore, the current government reduced the nominal deficit from 3.1% in 2014 to 0.9% (according to the recent figure of the INA) in 2017. Compared with the estimated figures of updated Stability Programmes, Belgium always performed better (e.g. Estimated nominal deficit of 1.6% in the 2017, while the outcome is only 0.9%), this demonstrates clearly the conservative approach applied by the Belgian Government

Concerning the debt figures, the tables show that debt is again on a declining path and will continue to do so:

	2007	2008	2009	2010	2011	2012	2013	2014
Debt Ratio	87,0	92,5	99,5	99,7	102,6	104,3	105,5	107,6
Debt Evolution	-4,0	5,5	7,0	0,2	2,9	1,7	1,1	2,1

	2015	2016	2017	2018	2019
Debt Ratio	106,5	106,1	103,4	102,3	100,6
Debt Evolution	-1,1	-0,4	-2,7	-1,1	-1,7
Endogenous Debt Evolution	-0,4	-1,0	-2,6	-1,6	-2,3
Exogenous Debt Evolution	-0,7	0,6	-0,1	0,5	0,5

In 2008-2009, the debt ratio increased drastically due to, among other things, the government support measures for the financial sector. In the following years, the debt ratio continued to increase gradually to 107.6% of GDP in 2014. Since 2015, however, this upward trend has been stopped and reversed. Between 2014 and 2017, the debt ratio decreased from 107.6% to 103.4%. In 2019, the debt ratio is projected to further decline to 100.6%

According to the European Commission's Spring forecast a further decline in the debt ratio is also expected for the coming years. The European Commission states that "the debt ratio is projected to continue falling, from 103,1 % of GDP in 2017 to 100,2 % in 2019".

For the government, reducing the debt ratio is an important condition for guaranteeing the long-term sustainability of public finances and for reducing the costs of ageing.

2018

The NSSO's report of 18 September on the monitoring of the overall management of salaried workers, indicates that the achievements for 2018 are largely in line with the government's forecast for social matters.

Moreover, health care expenditure may be further reduced by EUR 57 million compared to the 2018 budget review of July.

At the level of primary expenditure, the overall target for under-utilisation has been set at EUR 1,143 million. The FPS BOSA (Budget) calculated that, on the basis of current estimates and past achievements, the objective will be met. Since 2015, the under-utilisation targets have always been reached and even exceeded.

In millions	*2017*	*2016*	*2015*
Under-utilisation achieved	*1,314*	*1,087*	*941.1*
Under-utilisation target	*920.5*	*910*	*832.0*

For 2018, fiscal revenues are on track. Notwithstanding a slight slowdown of economic growth due to a weakening external environment, fiscal revenues are performing strongly. After 8 months, year-on-year growth amounts to 7,5% whereas the fiscal target comprised in the Draft Budgetary Plan of October 2018 equals 4,5%, already an upward revision of the 3,6% target comprised in the last budget of May 2018. This solid performance is partly explained by the boost in revenues from advance corporate tax payments that show a year-on-year growth of 27%, or +2,8 billion EUR, after three quarters. However, also other revenue categories are performing well. Most notably, the raise in personal income withholding tax, which is currently at +1,4%, is exceeding the fiscal target of +1%. We would like to emphasise that these revenues are directly related to the 2018-phase of the tax shift including a 1,5 billion EUR personal income tax cut.
This implies that these revenues perform better than what the macro-economic parameters would suggest and is therefore another sign that the structural reforms implemented by the current government aiming at additional job creation are already bearing fruit. This is also supported by the rising purchasing power of households in 2018 and 2019 that benefit from the strong labour market performance in recent years. The performance of revenue growth this year could also be partially explained by the higher tax compliance due to efforts undertaken in the fight against tax fraud and tax evasion in recent years. An impressive number of measures have been implemented, both legal and operational, to improve tax collecting. In 2019 additional measures are foreseen, as explained further." To sum up, the 2018 estimate of fiscal revenues is very prudent. Currently, the year-on-year growth overshoots the fiscal target and creates a comfortable buffer to cope with potential shortfalls in corporate income tax assessments due to a shift from assessments in year T to advance tax payments in year T-1. Upward risks underlying fiscal revenues were already identified by the Commission in its assessment of the Stability Program in May 2018. At that time, the Commission concluded that "there is no sufficient evidence to conclude that Belgium is non-compliant with the required adjustment path towards the MTO in 2017 and over 2016 and 2017 together". Given the strong fiscal performance thanks to a strong increase in corporate income tax revenues which is considered largely as one-off by the European Commission, we believe these conclusions still hold.

2019

On your question regarding the 0.2% effort for 2019, taking into account the better than predicted results in the previous years, the Belgian government is of the opinion that its cautiously predicted effort for 2019 is credible and realistic. To demonstrate this, you will find below different measures that are in the process of adoption and will be implemented in 2019.

In terms of primary expenditure and non-tax revenue, measures were taken for a total amount of EUR 375 million. Among others, these include:

- The volume effects forecast in the context of asylum and migration, have been revised downwards, for a total of EUR 141 million;
- An increase in dividends of EUR 112 million has been factored in;
- A further decrease in interest charges of EUR 98 million following the most recent assessment by the Federal Debt Agency.

With regard to employment, the government assumes that the "job deal", which mobilizes all the key players for the implementation of 28 strong measures (see annex), will lead to the creation of 12,500 additional FTE jobs in 2019. The overall budgetary gain of this policy for 2019 is estimated at EUR 505 million. For companies under restructuring or in difficulty, the age of access to the unemployment regime with company supplement (RCC), has been raised to 59 years. This will generate a positive return of EUR 20 million in 2019. Finally, concerning starter jobs, a positive return of EUR 12 million is expected.

At the level of pensions, the volume effects were revised downwards for an amount of EUR 132 million. The procedure for retirement on grounds of physical incapacity is being reviewed in order to strengthen the possibilities for professional reintegration. This is expected to generate EUR 39 million. In terms of social security, the expected return on the reform of the preferential directors' fees and hardship will be EUR 29 million. Other measures related to the health capital of the FPSs will generate a return of EUR 17 million.

Several measures regarding tax fraud have been taken, these should result in a net return of EUR 150 million (including a cost of EUR 3 million to guarantee this return). They include, the obligation to provide a form for the allocation of free or discounted shares and other benefits of all kinds, the harmonization of recovery procedures, the development of measures based on the Panama recommendations and initiatives within the judiciary to strengthen the fight against tax fraud in public prosecutors' offices.

In the context of the fight against social fraud, the Council of Ministers of 28 September 2018 decided on a series of new measures. The latter must generate a net return of EUR 100 million. In total, more than 10 measures have been adopted to address the different aspects of social fraud:

- improvement of the processing of cross-border social fraud cases,
- a targeted IT policy to standardize and digitalize the documents of the Social Inspection services,
- strengthening the CLS,
- the continued fight against fictitious social security benefits or the introduction of an independent tax assessment aimed at creating new information flows with social insurance funds so that the offsetting of debts currently used in the FPS Finance also applies to social debts collected by INASTI and the social insurance funds.

For 2019, fiscal revenue growth is estimated at +2,1% vis-à-vis 2018, backed by a 3,3% nominal growth of the economy. Two elements are expected to drag growth in fiscal revenue.

A first element is the 2019-phase of the tax shift, the last phase impacting personal income tax revenues. Taxes on labour are reduced by 1.85 billion EUR of which 1.5 billion EUR reduction in personal income taxes and the remaining via a reduction of employers' social contributions. The tax shift implemented over the period 2015-2020 is responding to the 2014 and the 2015 country-specific recommendation of the European Commission to shift taxes away from labour towards other less-distortive tax bases. This major tax reform temporarily affects revenues but is expected to generate large positive economic returns. A study of the National Bank of Belgium in April 2017 estimated that these positive returns are expected to improve the primary

government balance by 4.2 billion EUR by 2021[1]. These sizeable economic returns may even be larger since a recent academic study shows that the impact on employment might be up to 92.000 additional jobs instead of 52.100 as forecasted by the National Bank. Also post 2021, economic returns are likely to be largely positive as the latest phase of the tax shift is only implemented in 2020. As part of an extensive structural reform agenda, comprising also a pension reform, labour market flexibilization, a corporate tax reform and a reform of the statute of the civil service, Belgium therefore would like to apply for the structural reform clause allowing a temporary deviation of the structural adjustment path towards the MTO. For the moment we are working on more detailed information.

A second element is the estimated impact of the shift from corporate tax assessments towards corporate advance tax payments as a result of the policy measure to amplify the tax increase in case of insufficient advance tax payments. This increase is linked to market interest rates and followed their downward trend. In the 2019 budget, revenues from tax assessments are estimated to be negatively affected by 1 215 million EUR compared to 2018.

Given these two elements that are factored in the estimates for fiscal revenues 2019, we believe that our forecast is very prudent. Moreover, note that a better than expected result for 2018 may positively impact 2019 and provides a safety margin towards the budget 2019.

Some additional information regarding the most important fiscal measures for 2019:

- The planned modification of the law concerning building a social liability; the budgetary impact of this measure will be spread over the next 5 years (+ EUR 210 million) ;
- Implementation of a series of measures in the fight against tax fraud; decision taken at the Council of Ministers of October 2018 – one of these measures is the replacement of tax controllers at a rate of 1 to 1 (+ EUR 153 million);
- Implementation of the job deal, with emphasis on further labour market flexibility. This will lead to a return on investment of EUR 505 million, of which EUR 196.4 million will be linked to taxes due to the net creation of an additional 12,500 extra jobs;
- A technical correction of advance corporate tax payments: the evolution of advance corporate tax payments is very positive. The estimate of the Monitoring Committee was only based on the realised advance payments of the first trimester. A very cautious attitude was adopted with respect to the evolution of the advance payments in the second trimester and thereafter. The Government decided to not to take into account this positive evolution in 2018, but already for 2019.

Sincerely Yours,

Steven Costers

[1] Remark: The study considers the full cost of the tax shift affecting revenues at the level of Entity I and Entity II. Nevertheless, it only takes into account the explicit financing measures at the level of Entity I, but disregards the implicit financing at the level of Entity II. Entity II has fiscal autonomy to compensate their 4,8 billion EUR loss in fiscal revenues according to the study of the National Bank.