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Methodological Guidance for Costing of Structural Reforms (Costing Guidance)

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I. Introduction

1.1. Background and justification

Economic Reform Programmes (ERP) and their predecessors have for more than two decades been the main documents produced by EU candidate countries and potential candidates on an annual basis as a background for their macroeconomic dialogue with the European Union. The documents have traditionally been fiscally focused and therefore also the subject of structural reforms has always been looked at primarily through their fiscal implications logic. The main idea has always been that structural reforms with significant fiscal implications are well integrated into the medium-term fiscal framework of the country.

The focus of ERPs on structural reforms and consequently on their costing, or more broadly fiscal implications, has dramatically increased since the financial crisis in 2008, in close association with (i) the changed narrative about the subject (structural reforms as a precondition for sustained economic growth and competitiveness have turned into a high-priority subject), and (ii) the changed ERP management structure within the EC (before, DG ECFIN was responsible for the whole document; since a few years ago, the responsibility is shared between DG ECFIN (for macro and fiscal chapters), and DG NEAR (for structural reform chapters).

Structural reforms and their fiscal implications is a complex subject. DG NEAR has over the recent years, with OECD's assistance, significantly strengthened the methodological framework for the structural reform chapter of ERPs. The European Commission's Guidance for ERPs now provides much clearer guidance about the definition of structural reforms, structural reform areas and priority structural reform measures. With the assistance of the OECD, countries in the region were provided with methodological tools for assessing obstacles to growth, articulating and prioritizing reform policy measures as well as monitoring their implementation.

Before 2018, the European Commission's methodological guidance for ERPs did not provide sufficient explanations with respect to measuring the fiscal implications of structural reforms, while TAIEX's technical assistance on this subject, without having a common methodological framework, could only partially address this issue. In these circumstances, EU candidate countries and potential candidates had been facing a variety of challenges with how to cost individual structural reform measures, and capacity limitations in line ministries to address the subject.

To address the limitations of the previous ERP guidance for measuring the fiscal implications of structural reforms, the European Commission substantially upgraded this segment of its Guidance for the ERP preparation in 2018. With input from the CEF, the European Commission's Guidance for ERPs 2019–2021 introduced a redesigned and methodologically strengthened framework for the costing of structural policy measures as well as for their financing. **Annex 1** summarizes how the methodological guidance for measuring the fiscal implications of structural reforms under ERPs has improved with the enhanced framework.



1.2. Objectives of the document (and its limitation)

The **overall objective** of the *Methodological Guidance for Costing of Structural Reforms under ERPs (Costing Guidance)* is to improve the overall quality of the structural reform chapter of the ERP by providing a consistent and user-friendly framework for the costing of structural reform measures.

More specifically, the Costing Guidance has **two objectives**:

- to outline the key conceptual features of a redesigned and methodologically strengthened framework for measuring the costs of structural reforms measures under ERPs, and
- to present consistent and user-friendly instructions for quantification of the costs of structural reform measures to be calculated by EU candidate countries and potential candidates as an integral part of their structural reform chapters under ERPs.

It should be underlined that the Costing Guidance addresses exclusively the costing side of structural reform measures and public finance sources of their financing. The Costing Guidance does not deal with the issue of articulation of structural reform measures or their prioritization. Experiences with ERP preparations from previous years indicate clearly that if structural reform measures are for some reason not articulated well in substance terms, then also their costing can only be done in a suboptimal way or cannot be done at all. The costing of a structural reform measure is only the final phase of a process based on strong involvement of the respective line ministry. It must be preceded by a phase in which the policy reform measure is not only identified but also articulated and elaborated in terms of objectives, activities and inputs required for its implementation.

1.3. Process of document preparation, its methodology and information sources

The Costing Guidance is based on and fully consistent with the European Commission's Guidance for ERPs 2019–2021, and has been prepared under the auspices of the CEF and within the framework of the multi-annual and multi-beneficiary IPA project *Strengthening Line Ministries' Capacities to Assess Fiscal Implications of Structural Reforms (FISR)*. It was drafted in early 2019 by the project's Expert Advisory Group, and incorporates feedback from experts and key officials from FISR beneficiary countries participating in the CEF seminar *Enabling Officials as Trainers and Learning Facilitators*, which took place in Bohinjka Bistrica, Slovenia on 19–21 March 2019.

The key methodological inputs used for preparing the Costing Guidance include (by chronological order):

- the costing of structural reforms under the national program for acquis harmonization and implementation in Montenegro (2013),
- the *Fiscal Impact Assessment of Structural Reforms (FIASR)* project of the CEF (2013),
- the costing of structural reforms under the national program for the adoption of the acquis in Serbia (2014 and 2017),



- the costing of structural reforms under the national development strategy in Kosovo (2017), and
- guidance on the costing of public administration reforms by RESPA (2017).

1.4. Structure of the document

The document consists of an introduction, two main chapters and annexes. The second chapter outlines the main conceptual features of the Costing Guidance while the third chapter provides a detailed guidance for filling out those tables of the European Commission's Guidance for ERPs that are aimed first at quantification of costs of structural reform measures, and second at identification of funding sources for covering these costs (Tables 10a and 10b within the European Commission's Guidance for ERPs).

The main text of the Costing Guidance is accompanied with several annexes.

- Annex 1 provides information on how costs of structural reform measures under ERPs were quantified in the past and what had been the weaknesses.
- Annex 2 is a template table for standardized prices that can be used for quantification of costs of structural reform measures.
- Annex 3 provides detailed guidance on a bottom-up approach to costing that is needed in filling out Table 10a under the European Commission's Guidance for ERPs.
- Annex 4 provides a more detailed explanation of what is meant under the term "funds to be realistically provided" to be applied in filling out Table 10b under the European Commission's Guidance for ERPs.
- Annex 5 presents a selection of case studies on the costing of structural reforms as prepared by the FISR Expert Advisory Group and discussed at the CEF seminar on *Enabling Officials as Trainers and Learning Facilitators* in March 2019.



II. Conceptual features on which the Costing Guidance is based

The main objective of this chapter is to outline the key conceptual features of the redesigned and methodologically strengthened approach for measuring the costs of structural reform measures under ERPs and for identifying financial sources for their funding. These “new” features are presented in a way that they are contrasted with the respective “old” features.

There are several important conceptual features in which the “new” approach of the European Commission’s Guidance for ERPs towards the costing of structural reform measures and their financing is substantially different from the concept under the pre-2018 guidance (see **Annex 1**, for main questions / ambiguities of the pre-2018 guidance). The main features of this “new” approach articulated in the Costing Guidance are the following:

- **Focus on the costs of structural reform measures only:** In contrast to the pre-2018 guidance, based on a rather vague concept of fiscal implications of structural reforms that de facto addresses both sides of public finances, i.e. their costs as well as revenues, the Costing Guidance focuses clearly on the costing side of structural reform measures. The revenue side of public finances is therefore not addressed under this Guidance or, more precisely, is addressed only sporadically.
- **Focus on the additional costs of structural reform measures only:** In contrast to the pre-2018 guidance, where it was not clear which costs of structural reform measures are expected to be calculated, the Costing Guidance focuses exclusively on the additional costs of a structural reform measures, i.e. on the costs that are additional to the circumstances where this measure would not be introduced. The Costing Guidance is therefore not aimed at calculating the total costs of structural reform measures but only at those costs that are additional to the status quo scenario and measured vis-à-vis the base year of the reform. The base year is always the year before the year in which the priority reform measure was introduced.
- **Focus on the direct, first-level fiscal effects of structural reform measures only:** In contrast to the pre-2018 guidance that was rather unclear on what type of effects are to be calculated, the Costing Guidance focuses clearly and exclusively on the direct, first-level fiscal effects of structural policy measures that are being introduced. The Costing Guidance therefore does not address the indirect, secondary-level fiscal effects of structural reform measures, i.e. the effects that contribute to higher economic growth and consequently to higher volume of public finance revenues or the effects that contribute to lower unemployment and hence to lower expenditures for social benefits. These effects are no doubt important but they are to be addressed within ERPs through ‘structural reform’-based scenarios in macroeconomic projections and consequently in fiscal scenarios.
- **Systematic classification of costs under structural reform measures:** In contrast to the pre-2018 guidance with no cost classification, the European Commission’s Guidance for ERPs introduces under the “new” approach a template table (Table 10a in this Guidance) with a classification of the costs on conventionally agreed sub-groups. The Costing Guidance provides a detailed methodological framework for filling the template table (see Chapter III), including an orientation table with standardized prices for selected cost items.



- **Systematic classification of sources for funding structural reform measures:** In contrast to the pre-2018 guidance, where financing of structural reform measures was addressed less precisely, the European Commission's Guidance for ERPs addresses this subject under the "new" approach much more systematically through a template table (Table 10b in this Guidance), outlining the funding sources foreseen for each individual structural reform measure. The Costing Guidance provides a detailed methodological framework for filling the template table (see Chapter III). All possible public finance sources, not only the central budget, can be tapped for financing structural reform measures.

III. Instructions for ERP template tables 10a and 10b on the costs of structural reform measures and their financing

The European Commission's Guidance for ERPs contains two tables that are related to the costing aspects of structural reform measures articulated within the framework of the *Chapter IV* of the ERP. The first table – Table 10a – is aimed at the costing of an individual structural reform measure articulated by the authorities of a EU candidate country or potential candidate over the three years under the ERP, while the second table – Table 10b – gives an overview of public finance sources from which the costs of the structural reform measure quantified in the previous table are planned to be financed.

The main objective of this chapter is to provide consistent and user-friendly instructions for filling out the two tables. The chapter starts with methodological instructions how to fill out the table on the costing of a structural reform measure (Table 10a) and continues with methodological instructions for filling out the table on the financing of this measure (Table 10b).

For each of the structural policy measures to be included in the ERP, the EU candidate country or potential candidate is expected to fill both tables: one on the costing of the measure (Table 10 a) and another one for its financing (Table 10b). The tables should be filled out in EUR.

3.1. Methodological instructions for filling out the table on costing a structural reform measure (Table 10a)

Methodological instructions for filling out Table 10a are divided into two groups. The first one presents the main conceptual features of the costs associated with structural reform measures to be integrated into the table. They include the following (broadly presented already in Chapter II of this text):

- **Only additional costs vis-à-vis the base year are to be included in the table:** This means that only those costs are to be included in the table that are additional to the status quo situation, i.e. to the situation without the structural reform measure. The additional costs are to be measured vis-à-vis the base year, which is always the last year before the year in which the priority reform measure was introduced. The year which is taken as a base year for the structural reform measure should be specified in a footnote to the table.



- **Registration of “additional costs” in the table:** In case that the total costs associated with the implementation of a structural reform measure in any of the three years covered by the ERP are higher than in the base year, these “additional costs” should be registered in the table with a positive sign. In case that the total costs associated with the implementation of a structural reform measure in any of the three years covered by ERP are lower than in the base year, these “cost savings” should be registered in the table with a negative sign. For example, if the total costs of a structural reform measure in the base year were 100 and the total costs for this measure in the first year under ERP (year X) are planned to be 70, then in Table 10a - 30 (minus 30) for the year X should be marked.
- **Only direct, first-level costs are to be included in the table:** This means that only those additional costs are to be included in the table that are caused directly (they therefore represent first-level costs) by the implementation of the structural reform measure. In case that the implementation of a structural reform measure does not involve additional costs, then all spaces in the table should be filled with “0” (zero). In case that a structural reform measure generates first-level implications on the revenue side of public finances (e.g. an increase of budget revenues or an increase of contributions for the pension fund), this should be explained and quantified in a footnote to the table.
- **Internationally accepted classification applied for the classification of costs:** Though differences among various countries of the region exist with respect to the classification of public finance expenditures, the classification of these expenditures on the four main categories of costs – “salaries”, “goods and services”, “subsidies and transfers” and “capital expenditure” – is a generally accepted international classification.

The second group of methodological instructions provides an explanation for each individual heading of Table 10a in the European Commission’s Guidance for ERPs presented below.

ERP Table 10a: Costing of structural reform measure: (NAME OF THE MEASURE) (in EUR) (Fill in one per reform)

Year	Salaries	Goods and services	Subsidies and transfers	Capital expenditure	Total
Year X					
Year X+1					
Year X+2					

- **“Year”:** The category distinguishes among three years under the ERP, namely year X, year X+1 and year X+2. Year X is the first year of the period under the ERP. In case of the ERP for the period 2019–2021, year X means the year 2019. The base year against which the additional costs are calculated is always the last year before the year in which the priority reform measure was introduced (see **Annex 5**, for various cases). The year which is taken as a base year for the structural reform measure should be specified in a footnote to the table.
- **“Salaries”:** The category is composed of costs for salaries to be paid for hiring additional staff that is needed to implement the structural reform measure. The costing

of the additional staff has to take into account not only the number of new staff members but also their qualifications as well as salary increases for the existing staff members. It is highly recommended that standardized salaries for different categories of new staff members are applied (see **Annex 2**).

- **“Goods and services”**: The category is composed of the following sub-categories of costs: (i) training, (ii) expertise, (iii) office equipment, and (iv) utilities (rent, electricity, travel). It is highly recommended that standardized costs are applied for as many sub-categories of goods and services as feasible (see **Annex 2**). If standardized costs are neither available nor appropriate, expert opinion should be applied.
- **“Subsidies and transfers”**: The category includes different types of subsidies and transfers that the beneficiaries of the measure may receive (e.g. the amount of subsidies to be provided for agricultural households or innovative enterprises, or the amount of additional transfers provided to beneficiaries of employment or social protection measures). Expert opinion should be used for calculating this category of costs.
- **“Capital expenditures”**: The category includes capital expenditures associated with the implementation of a structural reform measure. Expert opinion should be used for calculating the forecasted expenditures under this category of costs.
- **“Total”**: This category is a sum of the above four categories.

If a measure is composed of several activities, a sub-table for each of them has to be prepared as an input for the summary table that shows costing for the structural reform measure as a whole – these sub-tables do not have to be included in the ERP. This instruction from the ERP Guidance suggests that a bottom-up approach should be used for costing. The bottom-up approach to costing and its limitations are explained in **Annex 3**.

3.2. Methodological guidance for filling out the table on the financing of a structural reform measure (Table 10b)

Similarly, as in sub-chapter 3.1, also methodological instructions for filling out Table 10b are divided into two groups. The first one presents the main conceptual features of funding sources to be tapped for the financing costs quantified in Table 10a. These features include the following (broadly presented already in Chapter II above):

- **All public finance sources are to be included in the table**: All domestic and foreign public finance sources – and not only central budget funds – could be tapped for the financing costs of a structural reform measure quantified in Table 10a.
- **An internationally accepted classification for the classification of funding sources is to be applied in the table**: All available funding sources – domestic ones as well as international ones – could be tapped for financing costs of a structural reform measure quantified in the Table 10a (broadly presented already in Chapter II above).
- **Disbursements are to be entered into the table**: Planned disbursements of funds – not their commitments – are to be entered into the table for respective funding sources categories.



The second group of methodological instructions provides an explanation for each individual heading of Table 10b of the European Commission’s Guidance for ERPs presented below.

ERP Table 10b: Financing of structural reform measure: (NAME OF THE MEASURE) (in EUR) (Fill in one per reform)

Year	Central budget	Local budgets	Other national public finance sources	IPA funds	Other grants	Project loans	To be determined	Total
Year X								
Year X+1								
Year X+2								

- **“Year”**: The category has the same meaning as in Table 10a. It therefore distinguishes among three years under the ERP, namely year X, year X+1 and year X+2. Year X is the first year of the period under the ERP. In case of the ERP for the period 2019–2021, year X means the year 2019 and the base year is always the last year before the year in which the priority reform measure was introduced (see **Annex 5**, for various cases). The year which is taken as a base year for the structural reform measure should be specified in a footnote to the table.
- **“Central budget”**: The category includes funds to be realistically provided (disbursed) from the central budget either from national public finance revenues or from borrowing in the form of financial loans. For year X, the funds are actually available under the budget adopted for this year.
- **“Local budgets”**: The category includes funds to be realistically provided (disbursed) from budgets at sub-national level: at a regional level and/or municipal level.
- **“Other national public finance sources”**: The category includes funds to be realistically provided (disbursed) from other national public finance sources (apart from central budget and local budget revenues), such as contributions for the health fund or pension funds, or investments financed by publicly-owned enterprises.
- **“IPA funds”**: The category includes funds to be realistically provided (disbursed) from IPA funds.
- **“Other grants”**: The category includes funds to be realistically provided (disbursed) in the form of grants from all multilateral and bilateral donors; the category excludes IPA funds.
- **“Project loans”**: The category includes funds to be realistically provided (disbursed) from foreign multilateral and bilateral lenders in the form of project loans. As explained above under the **“Central budget”**, financial loans are integrated into this category.
- **“To be determined”**: The category quantifies that portion of funds which is needed for the implementation of the structural policy measure concerned, but for which the funding source(s) is/are yet to be determined. The category should be calculated as a residual between the category **“Total”** and the sum of categories for all already known funding sources for the structural policy measure concerned.





- **“Total”**: The category is the sum of all the above seven categories and must be equal to the category **“Total”** in Table 10a for each respective year.

Instructions require that the table includes only funds that will realistically be provided. **Annex 4** provides a set of simple rules on what is to be considered as "realistically provided" in order to minimize the subjectivist bias and differences across measures.



ANNEXES

Annex 1: Challenges faced before 2018 in quantifying structural reform measures under ERPs

Before 2018, ERP authors had faced several challenges in preparing the specific part of the document, which addresses the quantification of fiscal implications of structural reforms, including the following:

- *Should the calculation be focused on narrowly defined budget implications or on more broadly defined public finance implications (i.e. should the calculation focus exclusively on implications on the national and local budgets or also on other segments of government finances such as health funds, pension funds, etc.)?*
- *Should the calculation be limited to direct implications only? Or should indirect implications be addressed as well?* (Though the European Commission's Guidance for ERPs explained in a footnote to the respective table that only direct, first-level effects should be included, ERP drafters sometimes include in the table also the indirect, second-level effects in the form of increased revenues caused by higher economic growth.)
- *Should the calculation address implications on the revenue and the expenditure side of the budget or only the latter?* (The European Commission's Guidance for ERPs was open to both, but in practice a large majority of first-level implications of structural reform measures has a form of an expenditure increase. If this is the case, then it would be more appropriate to call the whole calculation exercise "costing of structural reform measures" rather than "fiscal implications of structural reform measures".)
- *Which costs should be the subject of calculation?* (It has not been clarified in the European Commission's Guidance on ERPs which costs should be calculated: total costs or only additional costs, i.e. the difference between the total costs of a policy or programme already in place *plus* the cost of the proposed new measure (reform of the said policy or programme) or *only* the additional cost of the new measure.)
- *Whether to include expenditure reductions and tax expenditures or not? If yes, how to do it?* (It has not been clarified how to present the effects of a reform that leads to a reduction of budgetary costs, e.g. a reform of public enterprises, or how to present the effects of a reform that results in reduced revenues, e.g. a tax allowance for investment in research and development.)
- *How to integrate extra-budgetary sources into the table?* (Donations / project loans should be integrated into a national budget, but experiences show that this is not always the case.)
- *What figures on extra-budgetary funding sources should be presented in the table (commitments or forecasted disbursements; for the projects as a whole or on an annual basis)?*



Annex 2: Orientation template table for standardized prices that can be used for the quantification of costs of structural reform measures under ERPs

In preparation of Table 10 a, a candidate country may consider to design its own table of standardized prices per unit of selected cost categories. The following template is provided to be used as a general orientation for the preparation of country specific tables of standardized prices. The quantification of costs of structural reform measures (to be included in Table 10a) based on an application of standardized prices is expected to improve significantly the consistency of cost data across line ministries as well as the overall transparency of the process.

Category	Measuring unit	Price
1. Salaries		
• Senior level	Month	
• Middle level	Month	
• Junior level	Month	
2. Good and services		
• Training		
○ Abroad	person / year	
○ In the country	person / year	
• Expertise		
○ Local	person / day	
○ International	person / day	
• Office equipment	person / year	
• Utilities	person / year	

The template table should provide information on at least the following two categories of costs:

- **“Salaries”**: It would be advisable to apply standardized costs for the payment of salaries to various categories of staff classified upon their seniority (junior level staff, middle level staff, and senior / management level staff).
- **“Goods and services”**: It would be advisable to apply standardized costs as many sub-categories of “goods and service” as feasible. The most logical sub-categories appropriate for cost standardization are payments for: (i) office equipment, (ii) utilities, (iii) various types of training (in the country and abroad), (iv) and expertise (local and international).

The costing of the remaining two cost categories – “*subsidies and transfers*” and “*capital expenditure*” – is by their very nature less appropriate to be done via a ‘standardized prices’ approach but will largely remain based on professional expertise.

Annex 3: The bottom-up approach to costing

The ERP Guidance for filling the costing Table 10a includes the following instruction:

If a measure is composed of several activities, a sub-table for each of them has to be prepared as an input for the summary table that shows costing for the structural reform measure as a whole – these sub-tables do not have to be included in the ERP.

Indeed, ERP measures usually consist of several activities that often span over 2 or 3 years. The cited instruction strongly suggests that a bottom-up approach should be used for the costing of measures. The bottom-up approach means that each activity should first be costed separately, and then the total cost of the measure should be calculated as the sum of costs of all activities.

The following table may be used for bottom-up costing:

Costing of measure X (short name of the measure) (in EUR)					
Year	Salaries	Goods and services	Subsidies and transfers	Capital expenditure	Total
Activity 1 (short description)					
X					
X+1					
X+2					
Activity 2 (short description)					
X					
X+1					
X+2					
Activity 3 (short description)					
X					
X+1					
X+2					
<i>(continued for all activities of the measure)</i>					
Total costs of measure X					
X	sum	sum	sum	sum	sum
X+1	sum	sum	sum	sum	sum
X+2	sum	sum	sum	sum	sum

Once the table is completed, the entries in the last three rows (total cost of the measure) may be copied into the ERP Annex Table 10a.

In order to estimate the costs correctly and fully before they are entered into the table, the bottom-up costing must proceed in three consecutive steps.

The first step in bottom-up costing is to articulate the activities as clearly and precisely as possible. Ideally, as best practice, each activity should be clearly defined in terms of its expected or targeted outputs (deliverables). Outputs are the direct products of the implementation of an activity. Whenever possible, outputs should be expressed in quantitative terms. For example, typical outputs of the activities in ERP measures include:

- legislative and policy documents drafted and approved (e.g. a new, amended or simplified law, regulation, instruction, strategy, new curricula for schools)
- administrative databases created or completed (e.g. land registry, registry of social aid recipients)
- IT systems created and in operation (e.g. e-procurement system, portal for e-government services, information system for education, labour market or social policy)
- trainings delivered (e.g. number of trainings, number of person trained)
- support services provided to enterprises (e.g. number of enterprises supported, total sum of advisory days provided)
- new subsidies and grants disbursed to SMEs, agricultural holdings, research institutions, students or other beneficiaries (e.g. number of beneficiaries, total value of subsidies disbursed)
- support services provided to job seekers (e.g. number of beneficiaries of active labour market measures)
- new transfers provided to social aid recipients, unemployed, students or other beneficiaries (e.g. number of beneficiaries, the increase in the value of benefits provided)
- physical objects constructed (e.g. coverage of the new broadband network, length of the new gas pipeline or power interconnection line, area of land under newly constructed irrigation system)

The second step in bottom-up costing is to estimate the inputs that will be required to produce the expected output of each activity. The detail in which the inputs need to be planned – in order to be costed – will depend on the nature of the activity. For legislative and administrative outputs, the key question is whether they can be produced by the existing staff, or whether new employment or external technical assistance will be required. For support measures (subsidies, grants, transfers, labour market measures, trainings, and business support services), the key question should be how much of these different types of support is needed to have a meaningful impact on reality. Physical objects and IT systems are often an indivisible whole which may best be costed in total, but the construction and hence the costs may be spread over several years, sometimes even beyond the ERP's three-year horizon.

The final step in bottom-up costing is to estimate the costs of required inputs for each activity. It is recommended that as many inputs as possible are costed based on unified reference prices, which enables comparability of costs across measures and simplifies the estimation. When reference prices are not or cannot be provided, expert judgement – e.g. by budget officers in the line ministry responsible for implementation, or in the budget directorate of the Ministry of Finance – may be used. The costs of inputs should be costed using the cost



categories defined by the ERP guidance, and the total cost of an activity should be entered into the bottom-up costing table as presented above.

Some important difficulties and limitations are often encountered with the bottom-up approach to costing:

1. **Line ministries may not be able to specify the measure and its activities in terms of quantified outputs, or may not be able to precisely identify the required inputs.** This leads to uncertainty about the realism of estimated costs. Support from officials with more experience in policy design and costing, for example from the ERP coordinator's office of the budget department at the Ministry of Finance, may be helpful in such cases to reduce the uncertainty of costs to an acceptable level. Measures that remain vaguely described and are specified only in general terms should, in principle, not be prioritized for ERPs.
2. **When costing is done completely and based on an ambitious plan of activities, it may turn out that the funds currently available from budgetary and other sources are not sufficient.** Assuming that ERP measures are a high priority for governments, the first best solution in such cases is to try to secure additional funds, for example by reducing expenditures for policies or programmes of a lower priority. When this cannot be done, or not to the required extent, the scope of activities and the measure needs to be adjusted to the available funding.
3. **Some measures or activities may come with pre-defined budgets.** This may be the case when the major part of funding comes from a fixed international grant or loan, or when the funding for a given policy has already been allocated by a mid-term budgetary document that cannot be easily amended. In such cases, the bottom-up costing is effectively replaced by the top-down allocation of funds, or, put differently, the key question becomes how much can be achieved with available funds (rather than how much funding is needed to implement a pre-defined measure). Still, also in such cases, the good practice of policy design requires the line ministry to plan activities and outputs that will be achieved with available funds.

In conclusion, it needs to be emphasized that the staff involved in the costing process in line ministries should have sufficient technical knowledge of the nature of the planned activities and their likely costs. This requires close collaboration between officials from policy departments and the budgetary department (or general secretariat) within the line ministry, whereas the ERP coordinator and the budget department of the Ministry of Finance should provide support to and ensure the quality of the costing process.



Annex 4: Realistic planning of available funding

The ERP Guidance for filling the financing Table 10b stresses that only funds that will "realistically be provided" should be entered into the table. This solicits the question of a more precise clarification of the term "realistically provided", in order to minimize the subjective bias and differences in approach across measures. This Annex provides a list of tentative criteria for each source of financing.

Central budget: For year X (the current year), only the funds allocated in the officially approved budget for year X should be included in the table. For years X+1 and X+2, only the funds which are in line with the valid official mid-term expenditure planning document should be entered in the table. The best practice is to have the entries on budgetary financing checked and approved by the budgetary department of the Ministry of Finance.

Local budgets: For year X (the current year), only the funds allocated in the officially approved municipal budget for year X should be included in the table. An exception to this may be made when the local budgets have not yet been approved but the activities of the measure will be financed directly from a grant provided by the central budget. For years X+1 and X+2, only the funds which are in line with the valid official mid-term expenditure planning document at the national level should be entered in the table. The best practice is to have the entries on local financing checked and approved by the sub-national budgets unit in the budgetary department of the Ministry of Finance.

Other national public finance sources: Only the funds allocated for financing of the measure in the officially approved financial plan of the institution expected to provide financing should be included in the table. When such financial plans do not cover years X+1 and X+2, increases of financing from this source compared to year X should not be included in the table.

IPA funds: Only funds from already existing IPA projects should be planned in the table. Exceptions can be made for projects which are in the pipeline close to the start of implementation (e.g. in the tendering procedure), or when an officially approved IPA planning document makes a firm commitment to provide funds for the implementation of the measure. In these exceptional cases, funds planned for year X should be distributed between years X and X+1 to provision for possible delays in funding procedures. The best practice is to have the entries on international financing checked by the government unit responsible for the coordination of international financial assistance.

Other grants: Only funds from already approved and committed grants should be planned in the table. Exceptions can be made for grants which are in the pipeline close to approval (e.g. a draft agreement endorsed by both sides already exists). In these exceptional cases, funds planned for year X should be distributed between year X and year X+1 to provision for possible delays in funding procedures. The best practice is to have the entries on international financing checked by the government unit responsible for the coordination of international financial assistance.

Project loans: Only funds from already approved loans should be planned in the table. Exceptions can be made for loans which are in the pipeline close to approval (e.g. a draft agreement endorsed by both sides already exists). In these exceptional cases, funds planned



for year X should be distributed evenly between the years X and X+1 to provision for possible delays in funding procedures. The best practice is to have the entries on international financing checked by the government unit responsible for coordination of international financial assistance.

To be determined: This column includes the difference between the total cost of the measure (in Table 10a) and the sum of available funds entered in the first six columns of Table 10b in line with the rules specified above. The minimum requirement for inclusion of funds in the "to be determined" column is that the responsible ministry has a realistic plan for securing these funds in the near future (e.g. to propose the measure for the next IPA planning documents, or to approach a specific international donor or lender, or to reallocate budgetary funds from other budget lines). When there are no plans on how to secure the financing which is currently lacking, the scope of the measure should be adjusted to match the realistically available financing.

Footnotes: In all cases where there is some uncertainty about provision of financing (e.g. in the exceptional cases mentioned with several sources above, and for the "to be determined" column) this uncertainty should be clearly mentioned in a footnote to Table 10b and explained in the description of the measure in Chapter II in the paragraph on implementation risks.



Annex 5: Costing of structural reforms – case studies

Calculate and record the below described structural reform effects according to the above outlined methodology and ERP Tables 10a and 10b.

CASE STUDY #1A – Introduction of tax registers

Case description

In year X–1, the Law on implementation of tax registers is adopted, entering into force in year X. The Government assumes that 10,000 firms will acquire tax registers in year X and will award each business with 500 EUR of tax reliefs for this purpose. The Government further assumes that VAT will increase by 75 million EUR p.a. as a consequence of introducing tax registers, with a third of the effect observed in year X and the full effect observed in year X+1. The necessary software was already developed and paid in year X–1, while there are no additional employment or other costs needed for the implementation of the measure.

Calculation

X: –5 million tax relief (one-off) + 25 million additional revenue = net +20 million

X+1: 75 million

X+2: 75 million

NB! All the effects are to be recorded in a footnote to the table as they only affect the revenue side.

Answer

Table 10a (zeros)

Year	Salaries	Goods and services	Subsidies and transfers	Capital expenditure	Total
Year X	0	0	0	0	0
Year X+1	0	0	0	0	0
Year X+2	0	0	0	0	0

Footnote to Table 10a: The effects of the reform amount to 20 million additional revenue in year X, 75 million additional revenue in year X+1 and 75 million additional revenue in year X+2.

CASE STUDY #1B – Introduction of tax registers

Case description

In year X–1, the Law on implementation of tax registers is adopted, entering into force in year X. The Government assumes that 10,000 firms will acquire tax registers in year X and will award each business with 500 EUR of subsidies for this purpose. The Government further assumes that VAT will increase by 75 million EUR p.a. as a consequence of introducing tax registers, with a third of the effect observed in year X and the full effect observed in year X+1. The necessary software was already developed and paid in year X–1, while there are no additional employment or other costs needed for the implementation of the measure.

Calculation

X: –5 million subsidy (one-off) + 25 million additional revenue = net +20 million

X+1: 75 million

X+2: 75 million

NB! Only 5 million subsidy is to be recorded in the table in year X (subsidies and transfers; central budget). All other effects are to be included in a footnote as they only affect the revenue side.

Answer

Table 10a

Year	Salaries	Goods and services	Subsidies and transfers	Capital expenditure	Total
Year X	0	0	5,000,000	0	5,000,000
Year X+1	0	0	0	0	0
Year X+2	0	0	0	0	0

Footnote to Table 10a: The effects of the reform amount to 20 million of additional revenues in year X, 75 million of additional revenues in year X+1, and 75 million of additional revenues in year X+2.

Table 10b

Year	Central budget	Local budgets	Other national public finance	IPA funds	Other grants	Project loans	To be determined	Total
Year X	5,000,000	0	0	0	0	0	0	5,000,000
Year X+1	0	0	0	0	0	0	0	0
Year X+2	0	0	0	0	0	0	0	0

CASE STUDY #2 – Shortening of the unemployment benefit period

Case description

Currently, workers are entitled to receive an unemployment benefit (UB) for 24 months. The annual cost of a UB is 100 million, half of which is attributed to the long-term unemployed (24 months) and the other half to the short-term unemployed. The reform adopted in year X–1 shortens the UB period to 18 months, starting in X.

Calculation

- X: no change as all long-term unemployed have “old” entitlements for 24 months
- X+1: with the same number of unemployed, the “short-term unemployed” have the same rights (not affected by the reform), whereas the long-term unemployment benefit is shortened from 24 to 18 months, so the annual cost of this cohort is not 50 million, but 37.5 million. However, in X+1, there are still some (assumption: HALF) of “old timers” with 24 months of entitlement, so saving in this year is 6.25 million (6.25 million in X+1, subsidies and transfers)
- X+2: full effect of the reform, 12.5 million of saving (subsidies and transfers)

Answer

Table 10a

Year	Salaries	Goods and services	Subsidies and transfers	Capital expenditure	Total
Year X	0	0	0	0	0
Year X+1	0	0	-6,250,000	0	-6,250,000
Year X+2	0	0	-12,500,000	0	-12,500,000

Table 10b

Year	Central budget	Local budgets	Other national public finance sources	IPA funds	Other grants	Project loans	To be determined	Total
Year X	0	0	0	0	0	0	0	0
Year X+1	-6,250,000	0	0	0	0	0	0	-6,250,000
Year X+2	-12,500,000	0	0	0	0	0	0	-12,500,000

CASE STUDY #2 – Shortening of the unemployment benefit period – UPGRADE

Case description

Currently, workers are entitled to receive an unemployment benefit (UB) for 24 months. The annual cost of a UB is 100 million, half of which is attributed to the long-term unemployed (24 months) and the other half to the short-term unemployed. The reform adopted in year X–1 shortens the UB period to 18 months, starting in X.

Calculation

X: no change
X+1: saving of 6.25 million
X+2: full effect of the reform, –12.5 million

Note: What happens to the unemployed now, are they out of unemployment benefit?

- Some of them are entitled to social transfers
- Costing of social transfers
- Second order of the reform, not to be recorded in the tables



CASE STUDY #3 – Increasing female participation in the labour market

Case description

The unemployment rate of women is critical and so the government introduces a reform to increase female participation in the labour market. For two years, the government will offer education and skills development in the education system. For the following two years, the government will subsidize the employment of newly educated women (the firms that employ previously inactive women will receive a subsidy on the condition that these women will remain employed for at least two more years after the subsidized period). In all these years, it will also provide the additional and subsidized daily child care for the participants.

Calculation

Years X, X+1: education, skills development, cost of 100 million p.a. (80 million on teachers' salaries, 20 million on goods and services – education materials)

Years X+2, X+3: subsidies to firms that employ previously inactive women, 50 million p.a. (subsidies and transfers), at the same time a decrease of social transfers to these women, savings 20 million p.a. (subsidies and transfers)

Each of the years X to X+5: additional cost of subsidizing daily childcare, 20 million p.a.

X: 120 million of additional cost (100 million on education + 20 million on day care)

X+1: 120 million of additional cost (100 million on education + 20 million on day care)

X+2: 50 million of additional cost (50 million on subsidy to firms + 20 million on day care – 20 million social transfers, whereas additional PIT, VAT & SSC due to higher employment and higher consumption – second order effect)

X+3: 50 million of additional cost (50 million on subsidy to firms + 20 million on day care – 20 million social transfers, whereas PIT, VAT & SSC due to higher employment and higher consumption – second order effect)

X+4 and X+5: 0 (20 million on day care – 20 million social transfers, whereas additional PIT and SSC due to higher employment – second order effect)



Answer

Table 10a in ERP in year X

Year	Salaries	Goods and services	Subsidies and transfers	Capital expenditure	Total
Year X	80,000,000	20,000,000	20,000,000	0	120,000,000
Year X+1	80,000,000	20,000,000	20,000,000	0	120,000,000
Year X+2	0	0	50,000,000	0	50,000,000

Table 10a in ERP in year X+1

Year	Salaries	Goods and services	Subsidies and transfers	Capital expenditure	Total
Year X	80,000,000	20,000,000	20,000,000	0	120,000,000
Year X+1	0	0	50,000,000	0	50,000,000
Year X+2	0	0	50,000,000	0	50,000,000

Table 10a in ERP in year X+2

Year	Salaries	Goods and services	Subsidies and transfers	Capital expenditure	Total
Year X	0	0	50,000,000	0	50,000,000
Year X+1	0	0	50,000,000	0	50,000,000
Year X+2	0	0	0	0	0

Note that the duration of the reform is limited. If it is successful, the government may decide to include additional women in education in year X+2 but that would no longer be considered a reform. The reform is introducing a new measure, continuing with it is no longer a reform.