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COMMISSION STAFF WORKING DOCUMENT

Analysis of the draft budgetary plan of LUXEMBOURG

Accompanying the document

COMMISSION OPINION

on the draft budgetary plan of LUXEMBOURG

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1. INTRODUCTION

Luxembourg has submitted its Draft Budgetary Plan (DBP) for 2015 on 15 October 2014 in compliance with Regulation (EU) No 473/2013 of the Two-Pack. Luxembourg is subject to the preventive arm of the Pact and should preserve a sound fiscal position ensuring compliance with the medium term objective (MTO).

Section 2 of this document presents the macroeconomic outlook underlying the Draft Budgetary Plan and provides an assessment based on the Commission forecast. The following section presents the recent and planned fiscal developments, according to the DBP, including an analysis of risks to their achievement based on the Commission forecast. In addition, it includes an assessment of the measures underpinning the draft budgetary plan. Section 4 assesses the recent and planned fiscal developments in 2014-2015 (also taking into account the risks to their achievement) against the obligations stemming from the Stability and Growth Pact. Section 5 provides an analysis on the implementation by Luxembourg of fiscal and structural reforms in response to the latest country-specific recommendations adopted by the Council on 8 July 2014, including those to reduce the tax wedge. Section 6 summarises the main conclusions of the document.

2. MACROECONOMIC DEVELOPMENTS UNDERLYING THE DRAFT BUDGETARY PLAN

According to the macroeconomic scenario underpinning the DBP, economic prospects would remain favourable both in 2014 and 2015, with real GDP growth estimated at 2.8% and 2.7%, respectively. This compares with a 3.2% growth rate projected for both years in the 2014 Stability Programme. The downward revision broadly reflects more recent information regarding the second quarter of the year, which also points to the risks of a potential subdued economic environment, notably in the euro area, for the second half of the year. In addition, it factors in the risk that the current external weaknesses could be further protracted in 2015. It compares with the more optimistic macroeconomic scenario in the most recent Stability Programme, which assumes sustained growth in the euro area during the period 2015-2018.

Moreover, the macroeconomic scenario underlying the DBP was established before the national account data for the second quarter of 2014 were released. These data brought forward a sizeable upward revision in output expansion for the first quarter and pointed to sustained growth for the second quarter. On these grounds, the Commission 2014 autumn forecast projects real GDP to grow at a rate of 3% in 2014. In 2015, a lower economic growth of 2.4% is projected under the assumption of a less dynamic external environment, notably in the euro area, where output expansion is projected to be more subdued than assumed in the DBP.

Table 1. Comparison of macroeconomic developments and forecasts

	2013	2014			2015		
	COM	SP	DBP	COM	SP	DBP	COM
Real GDP (% change)	2.0	3.2	2.8	3.0	3.2	2.7	2.4
Private consumption (% change)	1.5	1.7	2.1	1.7	3.0	1.1	1.8
Gross fixed capital formation (% change)	-4.5	2.2	6.4	-0.6	-3.2	0.2	3.4
Exports of goods and services (% change)	5.6	4.9	3.4	2.4	4.7	3.9	4.0
Imports of goods and services (% change)	5.8	4.2	3.7	1.7	3.8	3.3	4.4
<i>Contributions to real GDP growth:</i>							
- Final domestic demand	0.5	1.3	2.4	0.9	0.8	1.0	1.6
- Change in inventories	0.0	0.0	0.0	0.0	0.0	0.0	0.0
- Net exports	1.5	1.9	0.3	2.1	2.4	1.7	0.8
Output gap ¹	-3.1	-2.0	-2.1	-2.1	-0.9	-1.5	-1.9
Employment (% change)	2.0	1.9	2.2	2.3	2.3	2.1	2.1
Unemployment rate (%)	5.9	6.2	6.1	6.1	6.3	6.4	6.2
Labour productivity (% change)	0.0	1.2	0.5	0.7	0.7	0.4	0.3
HICP inflation (%)	1.7	1.0	0.9	1.0	2.7	2.0	2.1
GDP deflator (% change)	1.4	3.3	2.5	1.9	2.7	1.2	2.6
Comp. of employees (per head, % change)	3.6	2.1	2.3	1.9	2.9	2.8	3.0
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	4.7	n.a.	n.a.	5.1	n.a.	n.a.	5.3
Note:							
¹ In percent of potential GDP, with potential GDP growth recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.							
<i>Source:</i>							
<i>Stability programme 2014 (SP); Draft Budgetary Plan 2015 (DBP); Commission 2014 autumn forecast (COM); Commission calculations.</i>							

Box 1: The macro economic forecast underpinning the budget in Luxembourg

The macroeconomic forecasts underlying the draft budgetary plan have been prepared by the Direction "Etudes, prévisions et recherche" of the national statistical office STATEC¹, which also provided the methodology for the calculation of the output gap. STATEC is an autonomous entity placed under the authority of the Ministry of Economy.

Its mandate and organisation were revised by the law of 10 July 2011², which explicitly highlights STATEC's scientific and administrative independence, its ability to access to appropriate information to carry out its mandate and its capacity to communicate freely. Its director is appointed by the Grand-Duke. Its statutes contain provisions supporting independence of the institution as a body producing macroeconomic forecasts.

¹ Institut national de la statistique et des études économiques du Grand-Duché du Luxembourg.

² Loi du 10 juillet 2011 portant organisation de l'Institut national de la statistique et des études économiques et modifiant la loi modifiée du 22 juin 1963 fixant le régime des traitements des fonctionnaires de l'État.

3. RECENT AND PLANNED FISCAL DEVELOPMENTS

3.1. Deficit developments

According to the October 2014 EDP notification, the general government surplus for 2013 was revised upwards to 0.6% of GDP, being substantially higher than initially estimated in the most recent update of the Stability Programme (0.1% of GDP). The revision is only marginally explained by the introduction of the new European System of National and Regional Accounts (ESA 2010), which mainly impacted on the government deficit and debt through the reclassification within the government of the SNCI (Société Nationale de Crédit et d'Investissement). Instead, the better-than-expected outcome is mostly due to an upward revision of revenue as expenditure has remained broadly unchanged.

However, according to the DBP, the surplus of the general government balance is projected to decline to 0.2% of GDP in 2014, despite the implementation of the consolidation package – equivalent to 0.4% of GDP –, the positive base effect of the higher surplus in 2013 being almost completely offset by expenditure overruns. However, this deterioration represents a slightly better outcome compared to the target surplus of 0.1% of GDP set in the Stability Programme. The revised outcome for the 2014 surplus is in line with that projected in the Commission 2014 autumn forecast.

Concerning 2015, the DBP projects the general government balance to turn into a deficit of 0.2% of GDP, mostly as a result of the expected decrease in e-VAT revenues stemming from the change in the e-commerce legislation. The underlying fiscal loss is estimated at around 1.5% of GDP and will be only partially compensated by the consolidation measures specified in the DBP. This budget balance compares to a deficit of 0.5% of GDP contained in the most recent Stability Programme. The difference is largely explained by: i) a base effect, as the 2014 surplus has been revised upwards by 0.1% of GDP, and ii) a slight revision of the consolidation package, the size of which has been increased to 1.1% of GDP (0.1% of GDP more than in the Stability Programme). The Commission 2014 autumn forecast projects the headline balance to post a deficit of 0.4% of GDP in 2015, the difference from the government forecast being largely due to a weaker underlying economic scenario. Moreover, in the Draft Budgetary Plan the apparent elasticity of revenues to GDP, notably for taxes on income and wealth, is slightly higher than the one used in the Commission forecast.

In structural terms, the DBP projects the general government balance³ to post a surplus of 1.2% of GDP in 2014. This surplus will then decline to 0.5% of GDP in 2015. By comparison, in the Stability Programme, the structural balance was estimated at 1.1% of GDP for 2014 and -0.1% of GDP for 2015. In the Commission 2014 autumn forecast developments in the structural balance are very close to those planned in the DBP.

The main risk to the fiscal outlook as projected by the Commission and in the DBP relates to the actual size of the e-VAT revenue loss. The current estimation, factored in by both the national and Commission forecasts, of an amount of about EUR 700 million (1.5% of GDP) is based on a central scenario, where the majority of companies concerned by the change in legislation will remain registered in Luxembourg for all their services. In the worst-case scenario, where all concerned companies would choose to leave the country, the losses could exceed 2% of GDP.

³ Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission services on the basis of the information provided in the Draft Budgetary Plan, using the commonly agreed methodology.

Table 2. Composition of the budgetary adjustment

(% of GDP)	2013	2014			2015			Change: 2013-2015
	COM	SP	DBP	COM	SP	DBP	COM	DBP
Revenue	44.5	42.2	43.9	44.1	41.4	44.1	43.5	-0.4
<i>of which:</i>								
- Taxes on production and imports	13.3	12.9	13.2	13.2	11.9	12.2	12.3	-1.1
- Current taxes on income, wealth, etc.	14.6	14.0	14.4	14.5	14.3	14.9	14.6	0.3
- Capital taxes	0.2	0.1	0.2	0.1	0.1	0.2	0.1	0.0
- Social contributions	12.3	11.9	12.2	12.3	11.9	12.7	12.5	0.4
- Other (residual)	4.0	3.3	3.9	4.0	3.2	4.1	4.0	0.1
Expenditure	43.8	42.1	43.7	44.0	41.9	44.3	44.0	0.5
<i>of which:</i>								
- Primary expenditure	43.4	41.6	43.3	43.6	41.5	43.9	43.6	0.5
<i>of which:</i>								
Compensation of employees	8.4	8.2	8.4	8.4	8.1	8.5	8.6	0.1
Intermediate consumption	3.8	3.6	3.8	3.9	3.6	3.9	3.8	0.1
Social payments	21.1	20.5	21.0	21.0	20.0	21.4	20.6	0.3
Subsidies	1.8	1.7	2.0	2.0	1.7	1.9	2.0	0.1
Gross fixed capital formation	3.5	3.1	3.6	3.5	3.5	3.8	3.9	0.3
Other (residual)	4.8	4.5	4.5	4.7	4.6	4.4	4.7	-0.4
- Interest expenditure	0.4	0.5	0.4	0.4	0.4	0.4	0.4	0.0
General government balance (GGB)	0.6	0.1	0.2	0.2	-0.5	-0.2	-0.4	-0.8
Primary balance	1.1	0.6	0.6	0.5	-0.1	0.2	-0.1	-0.9
One-off and other temporary	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
GGB excl. one-offs	0.6	0.1	0.2	0.2	-0.5	-0.2	-0.4	-0.8
Output gap ¹	-3.1	-2.0	-2.1	-2.1	-0.9	-1.5	-1.9	1.5
Cyclically-adjusted balance ¹	2.0	1.1	1.2	1.1	-0.1	0.5	0.4	-1.5
Structural balance (SB)²	2.0	1.1	1.2	1.1	-0.1	0.5	0.4	-1.5
Structural primary balance ²	2.4	1.5	1.6	1.5	0.3	0.9	0.8	-1.5
Notes:								
¹ Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission on the basis of the programme scenario using the commonly agreed methodology.								
² Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.								
Source:								
Stability programme 2014 (SP); Draft Budgetary Plan 2015 (DBP); Commission 2014 autumn forecast (COM); Commission calculations.								

3.2. Debt developments

In the DBP, the national authorities reiterate their commitment to maintain the public debt-to-GDP ratio under the national threshold of 30% and therefore, well below the Treaty threshold of 60%. The debt-to-GDP ratio is projected to increase only slightly to 24.1% in 2015 from 23.6% in 2013. This increase is slightly lower than that projected by the Commission in its 2014 autumn forecast and largely explained by the difference in the assumed nominal deficit. In 2015, the public debt is forecast to increase, although the primary balance is set to remain positive. This is explained by the different developments in the government sub-sectors. Indeed, the breakdown of the general government balance shows that, while the social security sector traditionally posts a surplus of more than 1% of GDP, the central government records a deficit of nearly the same size, and the balance of the local government sector is broadly neutral. However, according to the law, the surpluses of the social security sector are

allocated to a reserve fund (the so-called "*Fonds de compensation commun au régime général de pension*") with the aim to cover future pension expenditure and they cannot be used to finance the needs of the central government. As a consequence, the latter needs to issue new debt. In the Commission forecast, the central government is projected to be able to finance its needs without issuing new debt in 2014. Instead, in 2015 new debt issuance is estimated at around 2% of GDP.

Table 3. Debt developments

(% of GDP)	2013	2014			2015		
		SP	DBP	COM	SP	DBP	COM
Gross debt ratio¹	23.6	23.3	23.0	23.0	24.0	24.1	24.3
Change in the ratio	2.1	0.1	-0.6	-0.6	0.7	1.1	1.3
<i>Contributions²:</i>							
1. Primary balance	-1.1	-0.6	-0.6	-0.5	0.1	-0.2	0.1
2. "Snow-ball" effect	-0.3	-1.0	-0.8	-0.7	-0.8	-0.5	-0.7
<i>Of which:</i>							
Interest expenditure	0.4	0.5	0.4	0.4	0.4	0.4	0.4
Growth effect	-0.4	-0.7	-0.6	-0.7	-0.7	-0.6	-0.5
Inflation effect	-0.3	-0.7	-0.6	-0.4	-0.6	-0.3	-0.6
3. Stock-flow adjustment	3.5	1.7	0.8	0.7	1.5	1.8	2.0
<i>Of which:</i>							
Cash/accruals difference		n.a.	n.a.		n.a.	n.a.	
Net accumulation of financial <i>of which privatisation proceeds</i>		n.a.	n.a.		n.a.	n.a.	
Valuation effect & residual		n.a.	n.a.		n.a.	n.a.	
Notes:							
¹ End of period.							
² The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual							
Source:							
<i>Stability programme 2014 (SP); Draft Budgetary Plan 2015 (DBP); Commission 2014 autumn forecast (COM); Commission calculations.</i>							

3.3. Measures underpinning the draft budgetary plan

In the DBP, consolidation measures equivalent to EUR 560 million (1.1% of GDP) have been specified, with the bulk of the package consisting of revenue measures (0.8% of GDP).

In particular, on the revenue side, the increase from 1 January 2015 by 2 pps. in all VAT rates, as already announced in the Stability Programme, has been confirmed. In order to soften the regressive nature of the measure, the special low rate of 3% on essential goods and services has been retained. In addition, it has been specified that the higher standard rate of 17%, rather than the reduced 3% rate, will apply on new housing investment projects, with the exclusion of primary residence acquisitions. The overall budgetary impact of the VAT increase is estimated at around EUR 250 million (0.5% of GDP). Moreover, a new contribution of 0.5% levied on personal income, worth around EUR 120 million (0.25% of GDP), will also be introduced on 1 January 2015 to contribute to the financing of education expenditure.

Table 4. Main discretionary measures reported in the DBP**A. Discretionary measures taken by General Government - revenue side**

Components	Budgetary impact (% GDP) (as reported by the authorities)		
	2014	2015	2016
Taxes on production and imports	0.0	0.5	n.a.
Current taxes on income, wealth, Capital taxes	0.0	0.1	n.a.
Social contributions	n.a.	n.a.	n.a.
Property Income	0.0	0.2	n.a.
Other	n.a.	n.a.	n.a.
Total	0.0	0.8	n.a.
<u>Note:</u> The budgetary impact in the table is the aggregated impact of measures as reported in the DBP, i.e. by the national authorities. A positive sign implies that revenue increases as a consequence of this measure. <i>Source: Draft Budgetary Plan 2015</i>			

B. Discretionary measures taken by general Government- expenditure side

Components	Budgetary impact (% GDP) (as reported by the authorities)		
	2014	2015	2016
Compensation of employees	n.a.	n.a.	n.a.
Intermediate consumption	n.a.	n.a.	n.a.
Social payments	0.0	-0.4	n.a.
Interest Expenditure	n.a.	n.a.	n.a.
Subsidies	n.a.	n.a.	n.a.
Gross fixed capital formation	n.a.	n.a.	n.a.
Capital transfers	n.a.	n.a.	n.a.
Other	n.a.	n.a.	n.a.
Total	0.0	-0.4	n.a.
<u>Note:</u> The budgetary impact in the table is the aggregated impact of measures as reported in the DBP, i.e. by the national authorities. A positive sign implies that expenditure increases as a consequence of this measure. <i>Source: Draft Budgetary Plan 2015</i>			

On the expenditure side, measures introducing savings for a total amount of around 0.4% of GDP have been specified. The measures underlying these savings are the result of the spending review exercise launched by the new government in early spring and carried out by 19 working groups. More than 250 proposals of savings have been submitted to the government. The measures appear rather heterogeneous and are expected to produce savings

with an impact on both the central government and the social security sub-sectors. Most of the measures consist of savings on social benefits.

4. COMPLIANCE WITH THE PROVISIONS OF THE STABILITY AND GROWTH PACT

4.1. Compliance with the MTO

In the most recent Stability Programme the government of Luxembourg reiterated its commitment to maintain sound public finances in the medium-term and outlined its medium-term strategy. This strategy aims inter alia to compensate for the upcoming sharp deterioration of public finances in 2015, which is broadly linked to the expected loss of VAT revenues (around EUR 700 million or 1.5% of GDP). In the trajectory set in the Stability Programme, the general government balance, in structural terms, was expected to deviate from the country's MTO in 2015, but to reach it again already in 2016 or at the latest in 2017.

By comparison, the strategy outlined in the DBP for 2015 will enable the country to avoid any deviation from its MTO and to remain compliant with the relevant requirement of the preventive arm of the Stability and Growth Pact even in 2015.

According to the DBP, the headline balance is expected to turn into a deficit of 0.2% of GDP in 2015 compared to a surplus of 0.2% of GDP in 2014. Measures contained in the budget are projected to almost fully compensate for the loss in e-VAT revenues, estimated at around EUR 700 million or 1.5% of GDP. No significant one-off measures are foreseen in the draft budget.

Box 2. Council recommendations addressed to Luxembourg

On 8 July 2014, the Council addressed recommendations to Luxembourg in the context of the European Semester. In particular, in the area of public finances the Council recommended to Luxembourg to preserve a sound fiscal position in 2014; significantly strengthen the budgetary strategy in 2015 to ensure that the medium-term objective is achieved and remain at the medium-term objective thereafter, in order to protect the long-term sustainability of public finances, in particular by taking into account implicit liabilities related to ageing. Strengthen fiscal governance by speeding up the adoption of a medium-term budgetary framework covering the general government and including multi-annual expenditure ceilings,

and by putting into place the independent monitoring of fiscal rules. Further broaden the tax base, in particular on consumption.

Given that Luxembourg overachieved its MTO in 2013, the country does not face specific requirements beyond the maintenance of its structural balance at the MTO level in 2014. According to the information in the DBP, Luxembourg is projected to remain above its country-specific MTO in 2014. The structural balance (as recalculated by the Commission using the commonly agreed methodology) is set to decline from 2.0% of GDP in 2013 to 1.2% of GDP in 2014, a level still well above the country-specific MTO (of 0.5 % of GDP). These results are in line with the Stability Programme, where a structural balance of 1.1% of GDP was expected, and with the estimate from the Commission forecast of a structural balance of 1.1% of GDP. As the country achieved its MTO with a margin in 2013, the assessment of compliance with the expenditure benchmark is not needed as the latter is intended to underpin the necessary adjustment towards the MTO.

Moreover, given that Luxembourg is expected to record a structural balance above its MTO in 2014, it does not face specific requirements beyond the maintenance of its structural balance at the MTO level in 2015. According to the information in the DBP, in 2015 Luxembourg is expected to make use of its buffer with respect to the MTO, as the recalculated structural surplus is set to decrease by 0.7% of GDP and to drop from 1.2% of GDP in 2014 to 0.5% of GDP in 2015, just in line with the country-specific MTO. The drop is mostly due to the projected e-VAT revenue shortfall, which is only partially offset by the new measures planned in the DBP. In the Stability Programme, the recalculated structural balance was expected to post a deficit of 0.1% of GDP and thus to deviate from the country-specific MTO. This difference is explained by two main factors: i) a base effect as in 2014 the structural balance in the DBP is 0.1% higher than in the Stability Programme, and ii) the size of the consolidation package which in the DBP is 0.1% higher than in the Stability Programme. In the Commission forecast, the structural surplus in 2015 is projected to stand at 0.4% of GDP, marginally lower than estimated in the DBP, but still broadly remaining at the MTO.

On the basis of this assessment, it appears that Luxembourg is expected to broadly comply with the recommendation addressed to it by the Council on 8 July 2014, both in 2014 and 2015.

Table 5. Compliance with the requirements of the preventive arm

(% of GDP)	2013	2014		2015	
Initial position¹					
Medium-term objective (MTO)	0.5	0.5		0.5	
Structural balance ² (COM)	2.0	1.1		0.4	
Structural balance based on freezing (COM)	2.0	1.1		-	
Position vis-a-vis the MTO³	At or above the MTO	At or above the MTO		At or above the MTO	
(% of GDP)	2013	2014		2015	
	COM	DBP	COM	DBP	COM
Structural balance pillar					
Required adjustment ⁴	0.0	0.0		0.0	
Change in structural balance ⁵	-0.3	-0.8	-0.9	-0.7	-0.7
<i>One-year deviation from the required adjustment after considering the relevant factors⁶</i>	0.9	0.7	0.6	-0.1	-0.1
Two-year average change in structural balance ⁵	0.2	-0.6	-0.6	-0.7	-0.8
<i>Two-year average deviation from the required adjustment after considering the relevant factors⁶</i>	1.1	0.8	0.8	0.3	0.3
Expenditure benchmark pillar					
Applicable reference rate ⁷	1.8	1.1		1.1	
<i>One-year deviation⁸</i>	n.a.				
<i>Two-year average deviation⁸</i>	(structural balance above the MTO)				
Conclusion					
Conclusion over one year	Compliance				
Conclusion over two years					
Notes					
¹ The most favourable level of the structural balance, measured as a percentage of GDP reached at the end of year t-1, between Spring forecast (t-1) and the latest forecast, determines whether there is a need to adjust towards the MTO or not in year t. A margin of 0.25 percentage points (p.p.) is allowed in order to be evaluated as having reached the MTO.					
² Structural balance = cyclically-adjusted government balance excluding one-off measures.					
³ Based on the relevant structural balance at year t-1.					
⁴ Based on the position vis-à-vis the MTO, the cyclical position and the debt level (See European Commission: Vade mecum on the Stability and Growth Pact, page 28.).					
⁵ Change in the structural balance compared to year t-1. Ex post assessment (for 2013) is carried out on the basis of Commission 2014 spring forecast.					
⁶ The difference of the change in the structural balance and the required adjustment corrected for the clauses, the possible margin to the MTO and the allowed deviation in case of overachievers.					
⁷ Reference medium-term rate of potential GDP growth. The (standard) reference rate applies from year t+1, if the country has reached its MTO in year t. A lower rate applies as long as the country is adjusting towards its MTO, including in year t. The reference rates applicable to 2014 onwards have been updated in 2013.					
⁸ Deviation of the growth rate of public expenditure net of discretionary revenue measures and revenue increases mandated by law from the applicable reference rate in terms of the effect on the structural balance. The expenditure aggregate used for the expenditure benchmark is obtained following the commonly agreed methodology. A negative sign implies that expenditure growth exceeds the applicable reference rate.					
<i>Source :</i>					
<i>Draft Budgetary Plan 2015 (DBP), Commission 2014 autumn forecast (COM), Commission calculations</i>					

5. IMPLEMENTATION OF FISCAL-STRUCTURAL REFORMS

The Draft Budgetary Plan provides a list of the measures that have been already adopted or are planned to be adopted in order to ensure an adequate follow-up of the 2014 country-specific recommendations (CSRs).

As regards the fiscal recommendation (see Box 2), which called for a reinforcement of fiscal governance, the Draft Budgetary Plan indicates that the law⁴ transposing the provisions of the Fiscal compact was finally adopted by the Parliament on 12 July 2014. The law contains provisions that introduce a multi-annual financial programming law covering all three sub-sectors of the general government and thereby ensuring a complete overview of public finances developments. The law aims to cover five years, including the year when the budget law is drafted. Its provisions have already been put in place as the government has deposited before the Parliament a draft multi-annual financial programming law, covering the period 2014-2018, together with the DBP. The law also contains provisions about the set-up of a newly created body, called "*Conseil National des Finances Publiques*", in charge of ensuring an independent monitoring of the implementation of fiscal rules.

Moreover, the DBP stressed that the above-mentioned increase in VAT rates ensures an adequate follow-up to the Council recommendation to broaden the tax base, in particular on consumption. The decision to shift to the 17% rate to be applicable to real estate transactions, rather than the reduced rate of 3% and, the general increase of 2 pps. of all VAT rates is indeed in line with the Council's recommendation.

Box 3. Addressing the tax wedge

The tax burden on labour in the euro area is relatively high, which weighs on economic activity and employment. Against this background, the Eurogroup has expressed its commitment to effectively reduce the tax burden on labour. It will take stock of Member States' plans for reductions of the tax burden when discussing the draft budgetary plans.

The tax wedge in Luxembourg is well below the EU average. The tax wedge for a single person without children earning 50% of the average wage was 26% compared to an EU average of 34% in 2013, for 67% of the average wage it was 29.9% (EU average: 37.7%) and for the average wage it was 37% (EU average: 41.1%).

The Draft Budgetary Plan does not include any plans that affect the tax wedge on labour.

6. OVERALL CONCLUSION

Luxembourg is projected to over-achieve its MTO in 2014. In 2015, Luxembourg is expected to make use of its buffer as the surplus of structural balance is set to deteriorate, while still broadly remaining at the MTO. The deterioration in the structural balance is mostly due to the e-VAT revenue shortfall, which is only partially compensated by the new measures planned in the Draft Budgetary Plan.

⁴ Draft law No. 6597 relative to the coordination and the governance of the public finances.