VALSTYBĖS KONTROLĖ
BUDGET MONITORING

To the Seimas of the Republic of Lithuania

OPINION ON THE COMPLIANCE WITH THE FISCAL DISCIPLINE RULES OF MUNICIPAL BUDGETS DURING 2024–2025

12 June 2025 No BPE-3

Vilnius

ALL MUNICIPALITIES COMPLIED WITH THE FISCAL DISCIPLINE RULES IN 2024, BUT NOT ALL BUDGETS MEET REQUIREMENTS IN 2025

The National Audit Office implementing the function of the fiscal institution (hereinafter – NAO FI), submits to the Seimas an opinion on the assessment of compliance with the rules of fiscal discipline (hereinafter – FDR) of municipal budgets attributed to the general government sector, in accordance with the Constitutional Law on the Implementation of the Fiscal Treaty of the Republic of the Republic of Lithuania (hereinafter – the Constitutional Law).

Municipal fiscal discipline rules contribute to the sustainability of public finances. The risks of non-compliance with the FDRs identified by the *ex-ante* assessment of the NAO FI allow municipalities to assess and, if necessary, adjust their budgets before the end of the current year in order to avoid non-compliance with the FDRs at the time of the *ex-post* (actual) assessment. It also provides insight into the calculation of municipal budget balances, which municipalities can plan without violating the limits set by law.

The *ex-post* evaluation shows that in 2024, all municipal budgets were implemented in line with their requirements. The *ex-ante* evaluation found that two municipalities' initial budgets for 2025 did not meet their requirements. The assessments are subject to data reliability problems year after year. For the sustainability of public finances and the growth of municipal investment, municipalities need to address them, for if the rules are not followed, the flexibility rule that allows for higher borrowing may no longer be applied.

A more detailed assessment of compliance with the rules can be found in the MS *excel* spreadsheets provided with the opinion at https://www.valstybeskontrole.lt/LT/BiudzetoStebesena.

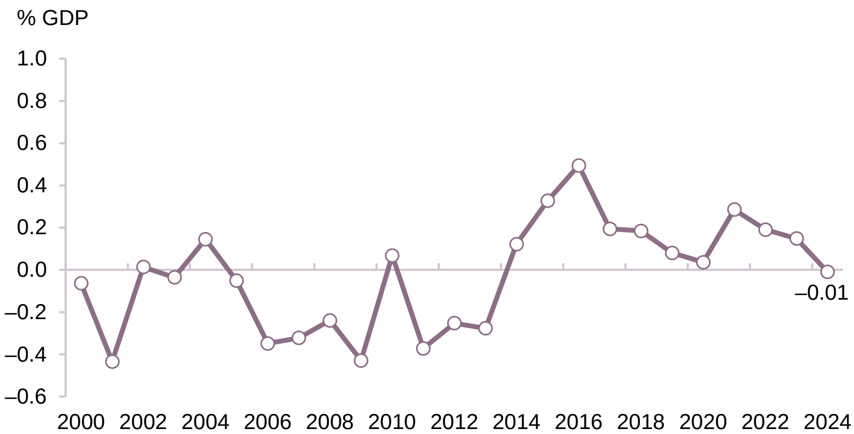
Key messages of the opinion:

- **In 2024, budgets of all municipalities were in line with their requirements.**
- **According to the planned municipal budgets for 2025, there is a risk that 2 municipalities will not comply with their fiscal discipline rules.**
- **If the assessment were based on unrevised data, the 2025 budgets of 5 municipalities would be considered as non-compliant with fiscal discipline rules.**

ASSESSING COMPLIANCE WITH MUNICIPAL FISCAL DISCIPLINE RULES FOR 2024–2025

For the first time since 2013, the local government sub-sector is in deficit in 2024 (Figure 1). In 2024, the deficit of the local government sub-sector was –7.7 million EUR (0.01% of GDP). This is the first time since 2013, when the deficit was 0.3% of GDP. With the economy below potential and the flexibility provided by the Constitutional Law (CL), municipalities could run deficits.

Figure 1. For the first time in 10 years, the local government subsector was in deficit in 2024



Source: State Data Agency, calculations by the National Audit Office, implementing the function of the fiscal institution

According to the Constitutional Law, municipalities are divided into two groups. According to Article 4(2) and (4) of this law, municipalities with appropriations exceeding 0.3% of GDP are required to balance their budgets cyclically, while the appropriations of the remaining municipalities may exceed revenues by up to 1.5% when the economy is below its potential level. The assessment of the compliance of municipal budgets with fiscal discipline rules also takes into account the flexibility provided for in Article 4(5) of the CL, i.e. the appropriations for co-financing of European Union and other international financial assistance, as well as the unused part of the accrued revenue of the municipal budget that is used for appropriations.

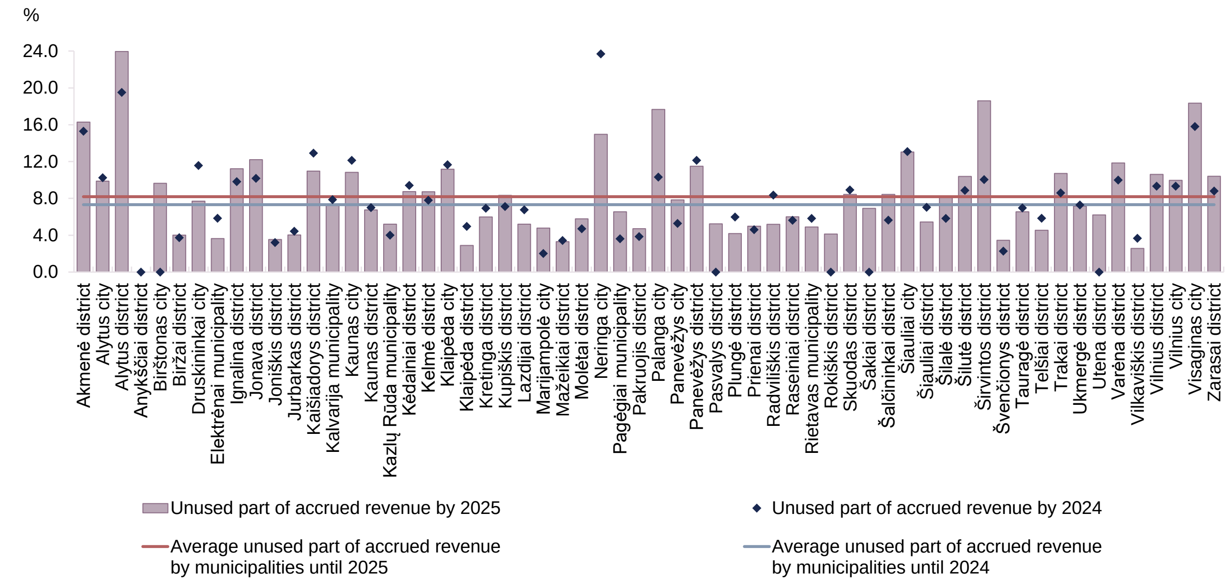
The possibility to add to revenue unused part of the accrued revenue significantly increases the ability of municipalities to finance expenditure. The average unused part of the accrued revenue accumulated by 2024[1] among municipalities was 7.3% and by 2025 8.2%[2] of their revenue (Figure 2). This indicator increased in 43 out of 60 municipalities. Across all municipalities, the unused part of the accrued revenue rose from €547 million (0.7% of GDP) in 2024 to €592 million[3] in 2025. Thus, the possibility to add these amounts to revenue has extended the possibilities for municipalities to plan higher expenditure without breaching fiscal discipline rules. It should be noted that this amount does not increase municipal debt, as the needs are financed with financial resources already accumulated. However, as municipalities are part of the general government, this additional flexibility may have a negative impact on the overall general government balance, which is constrained by both national and EU legislation.

[1] Including the unused part of the accrued revenue until 2023 but excluding the 2024 part.

[2] The unused part of the accrued revenue in 2025 is compared with the projected revenue in 2025.

[3] Based on data provided by the Ministry of Finance and revised by municipalities.

Figure 2. The unused part of the accrued revenue in municipalities in 2024 averaged 7.3% of their total revenue



Based on data from the reports on the execution of municipal budgets of the Republic of Lithuania (31 December 2024 and 31 March 2025). Source: https://lietuvosfinansai.lt/, data provided to the Ministry of Finance and municipalities' revised data, calculations by the National Audit Office, implementing the function of the fiscal institution

In 2024, all municipalities complied with their fiscal discipline rules. As the municipal budget deficits of the cities of Vilnius, Kaunas, Klaipėda and Šiauliai did not exceed the cyclical component[4], and the appropriations of the other municipalities did not exceed their revenues by more than 1.5%, the budgets of all the municipalities were implemented in accordance with the rules for budgets attributable to the general government sector in 2024.

According to Law on the Budget Structure, municipal councils had to approve their budgets for 2025 within two months of the adoption of the Law on Financial Indicators of the State Budget and Municipal Budgets for the current year. During the year, municipalities adjust their budgets. The NAO FI carried out an *ex-ante* evaluation by analysing the initial budgets approved by the municipal councils. The actual compliance of municipalities with the fiscal discipline rules in their 2025 budgets will be assessed in 2026[5].

According to the planned municipal budgets for 2025, 2 municipalities are at risk of non-compliance with their fiscal discipline rules (Figure 3). With the economy below potential[6], the municipalities of Vilnius, Kaunas, Klaipėda and Šiauliai were allowed to plan for deficits the size of the cyclical component, while the remaining municipalities had to ensure that appropriations did not exceed revenues by more than 1.5%. **According to the financial statements, the budgets of 5 municipalities in 2025 would be considered non-compliant with fiscal discipline rules.** On 23/05/2025, the municipalities were informed of the risk of non-compliance with the FDR and asked to inform the NAO FI of possible data discrepancies. With the inclusion of revised information on unused part of accrued revenue

[4] The cyclical component of the budget is an indicator expressed in monetary units that shows the impact of the output gap on the municipality's budget balance over the reference period. Estimates of this indicator used for the assessment can be found on the website of the Ministry of Finance. Available online: https://finmin.lrv.lt/lt/veiklos-sritys/fiskaline-politika/informacija-savivaldybems-sodrai-ir-psdf/savivaldybiu-sodros-psdf-biudzetu-cikliniu-komponenciu-dydziai.

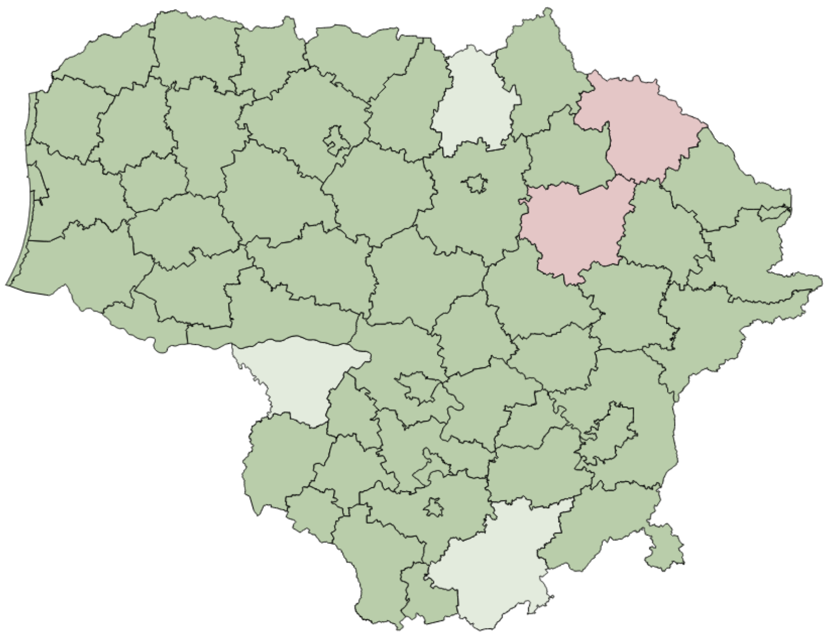
[5] According to the National Audit Office Law, a report on the compliance of municipal budgets with the rules laid down in Article 4(2), (4) to (7) of the Constitutional Law on the Implementation of the Fiscal Treaty and on the assessment of the correction of non-compliance with these rules is due by 30 June each year.

[6] The Ministry of Finance's 27/03/2025 report "On the Potential Gross Domestic Product and Output Gap from Potential for 2024-2028" estimated the output gap from potential in 2025 at −1.8% pot. GDP. Available online: https://finmin.lrv.lt/public/canonical/1743081035/24868/Pranesimas_del_potencialaus_2025_kovas.pdf.

and appropriations for international assistance co-financing in the assessment, there is a risk that 2 out of 60 municipalities (Anykščiai and Rokiškis) will not comply with their FDRs as projected deficits are higher than allowed by regulation. According to Article 4(10) of the CL, if the municipalities' deficits are actually higher than the FDRs allow, the deviation will have to be compensated within two years. If this is not done, the flexibility rule will no longer apply. Also, compliance with the *ex-post* fiscal discipline rules by municipalities is one of the conditions for non-repayment of the grant, as set out in the description of the procedure for allocation and repayment of grants to municipalities, approved by Decree[7].

There is a recurring problem of inaccurate data, in particular the unused part of the accrued revenue that is not reported or not accurately reported in the financial statements. It is important that municipal administrations and their audit services ensure the accuracy of the information provided in the reports. Municipalities that fail to ensure the reliability of their financial statements and compliance with fiscal discipline risk their ability to invest.

Figure 3. There is a risk that 2 municipalities will not comply with their fiscal discipline rules in 2025



Source: State Data Agency, www.lietuvosfinansai.lt, Public Sector Accounting and Reports Consolidation Information System, data provided to the Ministry of Finance and municipalities' revised data, calculations by the National Audit Office, implementing the function of a fiscal institution

When assessing the compliance of municipalities with the rules of fiscal discipline, the NAO FI takes into account the impact of the European Union and other international financial assistance on the budget balance. The impact of the European Union and international financial assistance (excluding co-financing) on the general government balance should be neutral, as it is an external source of revenue financed by the EU budget. However, a situation may arise where EU support affects the municipal balance. Normally, when a municipality prepares and executes its budget, the unused part of the EU funds is added to expenditure, but the CL does not foresee the possibility of adding it to revenue.

[7] Decree of the Minister of Finance No 1K-213 of 26 May 2016 "On Approval of the Description of the Procedure for Allocation and Repayment of Grants to Municipalities". Available online: https://e-seimas.lrs.lt/portal/legalAct/lt/TAD/a33ab890276a11e6a222b0cd86c2adfc/WqkDOTKOoe.

For the purpose of assessing fiscal discipline, the unspent part of the EU funds is not added to revenue. This has a negative impact on municipal balance, which should not be the case. For this reason, the NAO FI has made an additional correction of EU funds to neutralise this effect. As in 2024, municipalities were asked to complete a survey on EU and international financial assistance (excluding co-financing) in their budgets for 2024 and in their budget plans for 2025. It should be noted that this information could not be identified from the financial reporting documents provided by the municipalities and therefore a survey was chosen. In the future, it should be ensured that is it possible to use data from official sources for the assessment of fiscal discipline.

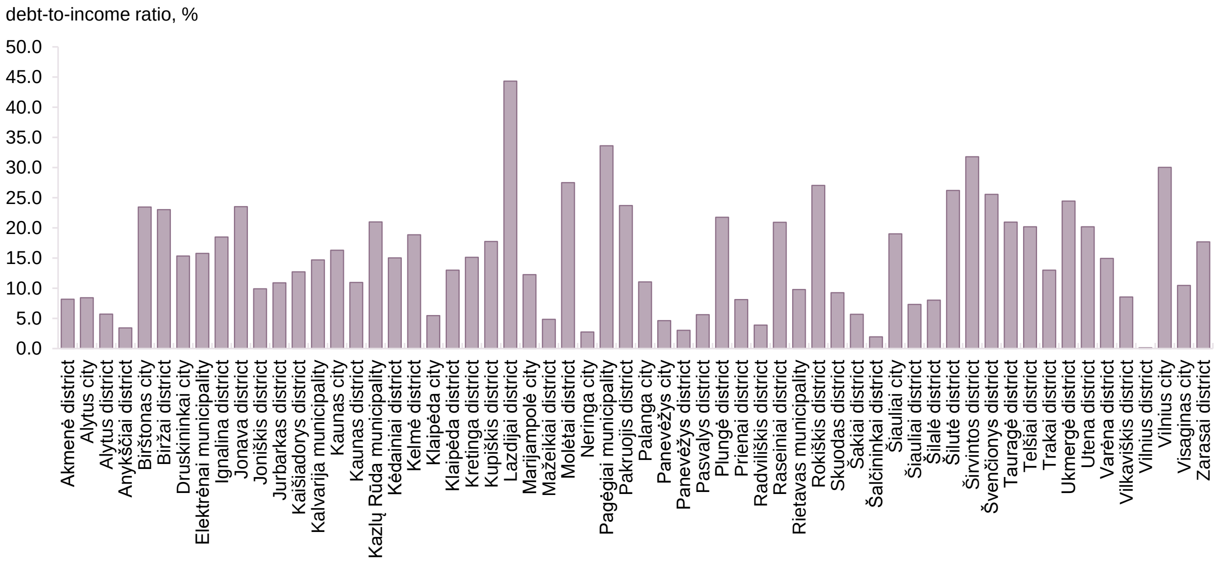
Not all municipalities provide accurate information on estimated accounts payable. According to the Law on Budgetary Structure, municipal councils are required to approve the planned annual amount of the change in arrears (accounts payable, except for repayment of loans). Information on the planned accounts payable can be found in the explanatory notes to the budgets of all municipalities, but a few did not provide this information accurately. For example, one municipality's budget explanatory note states: "To set the planned annual amount of change in arrears (accounts payable, other than loan repayments) at 31 December 2025 at no more than the amount on 31 December 2024". This description does not indicate the exact amount forecast. In the opinion of the NAO FI, the amount of the change to be approved should be precise or, if no increase in arrears is planned, should be shown as zero at the time of approval.

MUNICIPAL DEBTS AND GUARANTEES IN 2024

No municipality exceeded its debt limit in 2024. According to the OECD[8], low municipal borrowing autonomy can be a barrier to cooperation between municipalities on large-scale infrastructure projects. However, a change to the Constitutional Law, which entered into force in 2023, has increased the borrowing capacity of municipalities, not only by introducing more flexibility in the size of the balance, but also by changing the calculation of the debt limit[9]. In the Law on the Approval of Financial Indicators of the State Budget and Municipal Budgets of the Republic of Lithuania, the debt-to-revenue ratio was calculated on the basis of the projected personal income tax, while under the new wording of the Constitutional Law, it is calculated on the basis of the total municipal revenues. It should be noted that if a municipality exceeded the limits set by the law, the flexibility rule would no longer apply. The application of the flexibility rule is of particular relevance for the purpose of accessing wider investment opportunities. In 2024, no municipality exceeded its debt limit (Figure 4).

[8] Available online: https://www.oecd.org/en/publications/enabling-inter-municipal-shared-service-provision-in-lithuania_f8ad6859-en.html.
[9] Municipal debt cannot exceed 60% (75% in Vilnius) of revenue.

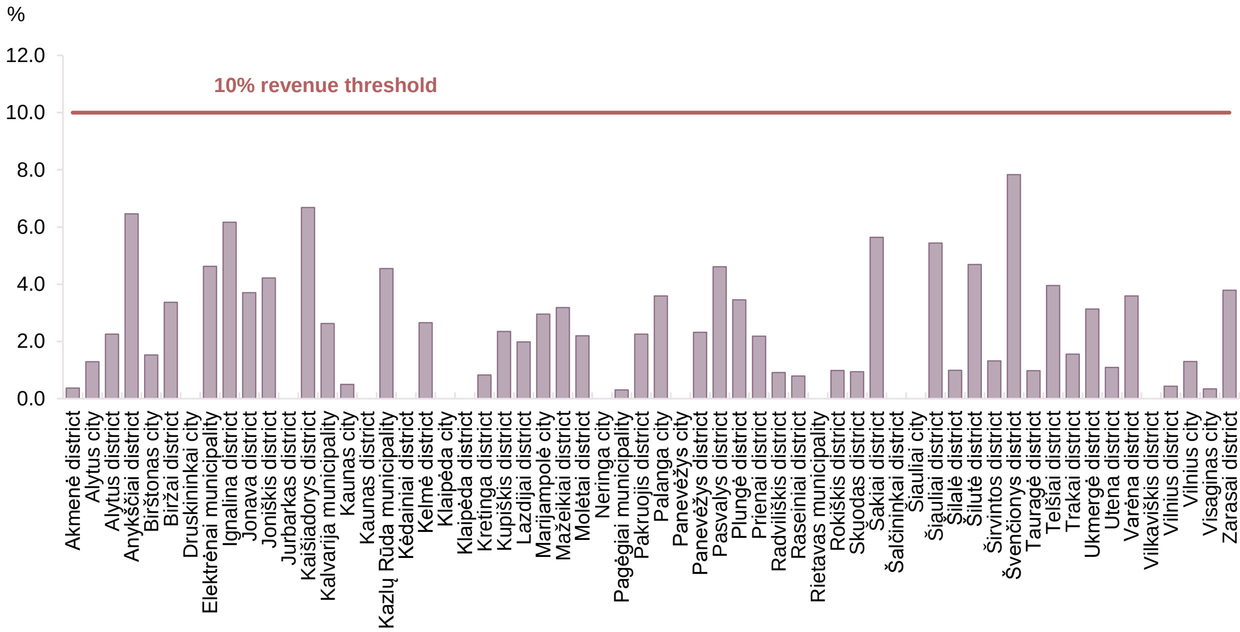
Figure 4. No municipality exceeded its debt limit in 2024



Source: https://lietuvosfinansai.lt/, Public Sector Accounting and Reports Consolidation Information System, calculations by the National Audit Office, implementing the function of a fiscal institution

In 2024, no the municipality's guarantees exceeded the 10% of revenue threshold. According to Article 4(7) of the Constitutional Law, the municipality's guarantees cannot exceed 10% of the sum of the municipality's personal income tax revenue forecast for that year and the municipality's budget revenue for the most recently completed year (excluding personal income tax revenue and state budget grants). In 2024, no municipality exceeded the guarantee limit (Figure 5).

Figure 5. In 2024, no municipality's guarantees exceeded the 10% of revenue threshold provided for in the Constitutional Law



Source: https://lietuvosfinansai.lt/, Public Sector Accounting and Reports Consolidation Information System, Law on the Approval of Financial Indicators of the State Budget and Municipal Budgets of the Republic of Lithuania for the Year 2024, municipalities' adjusted data, calculations by the National Audit Office, implementing the function of the fiscal institution

The National Audit Office, implementing its functions of the budget policy monitoring institution, is responsible for the monitoring of the compliance with fiscal discipline rules established in the Constitutional Law on the Implementation of the Fiscal Treaty of the Republic of Lithuania, as well as for monitoring the implementation of the assignments and is authorised to prepare and present independent opinions to the Seimas of the Republic of Lithuania on the compliance with fiscal discipline rules and macroeconomic developments. Pursuant to Article 4(2), (4) to (7) of the Constitutional Law on the Implementation of the Fiscal Treaty *of the Republic of Lithuania and Article 8(7)(7) of the Law on the National Audit Office, the National Audit Office shall submit an opinion to the Seimas of the Republic of Lithuania.*

Head of Budget Monitoring Department Jurga Rukšėnaitė