DECISIONS

COUNCIL DECISION (EU) 2017/984

of 8 August 2016

giving notice to Spain to take measures for the deficit reduction judged necessary in order to remedy the situation of excessive deficit

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 126(9) thereof,

Having regard to the recommendation from the European Commission,

Whereas:

(1) According to Article 126 of the Treaty on the Functioning of the European Union (TFEU), Member States are to avoid excessive government deficits.

(2) The Stability and Growth Pact is based on the objective of sound government finances as a means of strengthening the conditions for price stability and for strong sustainable growth conducive to employment creation. The Stability and Growth Pact includes Council Regulation (EC) No 1467/97 ([1]), which was adopted in order to further the prompt correction of excessive general government deficits.

(3) On 27 April 2009, the Council decided, in accordance with Article 104(6) of the Treaty establishing the European Community (TEC), that an excessive deficit existed in Spain and issued a recommendation to correct the excessive deficit by 2012 at the latest, in accordance with Article 104(7) of that Treaty. Since then, the Council has issued three new recommendations to Spain (on 2 December 2009, 10 July 2012 and 21 June 2013) on the basis of Article 126(7) TFEU, which extended the deadline for correcting the excessive deficit to 2013, 2014 and 2016 respectively. In all three recommendations, the Council considered that Spain had taken effective action, but unexpected adverse economic events with major unfavourable consequences for government finances had occurred ([2]).

(4) According to Article 126(8) TFEU, the Council decided on 12 July 2016 that Spain had not taken effective action in response to the Council Recommendation of 21 June 2013.

(5) According to Article 10(2) of Regulation (EC) No 1467/97, if action by a participating Member State is not being implemented or, in the Council's view, is proving to be inadequate, the Council shall immediately take a decision under Article 126(9) TFEU.

(6) The Commission has updated its 2016 spring forecast with information available up to 19 July 2016. On this basis, the real GDP growth forecast for 2016 has been revised upwards by 0,3 percentage points in comparison to the spring forecast, to 2,9 %, and downwards for 2017 (2,3 % vs. 2,5 % in spring). For 2018, real GDP is forecast to grow by 2,1 %. This compares to growth of 3,2 % in 2015. Economic growth is therefore set to ease but to remain robust, still benefitting from reforms undertaken in response to the crisis and the successful completion of the financial assistance programme. The recovery continues to be accompanied by strong job creation, in a context of continued wage moderation and benefitting from the labour market reforms. Low oil prices also support growth. At the same time, inflation is expected to be — 0,3 % in 2016. There are, however, downside risks to the growth forecast, especially as from 2017, related among others, to the outcome of the referendum in the United Kingdom on its membership of the Union, which has increased uncertainty, with potential negative implications for trade and domestic demand.

([1]) Council Regulation (EC) No 1467/97 of 7 July 1997 on speeding up and clarifying the implementation of the excessive deficit procedure (OJ L 209, 2.8.1997, p. 6).

([2]) All documents related to the excessive deficit procedure of Spain can be found at: http://ec.europa.eu/economy_finance/economic_governance/sgp/deficit/countries/spain_en.htm

(7) According to the updated Commission 2016 spring forecast, the general government deficit is expected to narrow to 4,6 % of GDP in 2016, 3,3 % of GDP in 2017 and 2,7 % of GDP in 2018 (compared to Stability Programme targets of 3,6 %, 2,9 % and 2,2 % of GDP in 2016, 2017 and 2018, respectively and a projected deficit outcome of 3,9 % of GDP in 2016 and 3,1 % of GDP in 2017 in the spring forecast). The higher deficit forecast is due partly to the fact that the updated Commission forecast takes on board a lower amount of measures to contain expenditure at central and regional government level in response to the March 2016 Commission Recommendation (0,2 % of GDP) than the Stability Programme forecast (0,4 % of GDP) on account of the fact that some of these measures have not yet been sufficiently specified to be included in the Commission forecast on the basis of the usual no-policy-change assumption. However, most of the difference stems from changes made to the corporate income tax legal framework, leading to lower advanced payments by companies (*'pagos fraccionados'*) in 2016. The shortfalls in advanced payments were not quantified in the Stability Programme and only became apparent in April, at the time of the first instalment, after the cut-off date of the spring forecast. The updated Commission 2016 spring forecast estimates these shortfalls at 0,5 % of GDP in 2016. As the abovementioned changes create a permanent delay in the payment of taxes, but not to a change in the tax rate or tax base, they would not affect revenue from corporate income taxes in a new steady state (starting in 2017). They result in a temporary loss of tax collection in 2016, which has been treated as a one-off in the updated spring forecast.

For 2017, the differences between the updated spring forecast and the Stability Programme stem from the worse-than-expected starting position and the fact that the savings measures taken in response to the March 2016 Commission Recommendation are not yet sufficiently specified to be taken into account on the basis of the usual no-policy-change assumption. The structural deficit is expected to increase by 0,4 % and 0,1 % of GDP in 2016 and 2017, respectively, and to remain unchanged in 2018. However, in 2016, the projected increase of the structural deficit is partly driven by the fact that the current outlook for inflation and nominal GDP growth is lower than the one underpinning the 2016 budget, which adversely affected structural government revenue while not allowing to adjust expenditure.

(8) The general government gross debt-to-GDP ratio rose from 36 % in 2007 to about 99 % in 2014. In 2015, the debt ratio was more or less stable, as net sales of financial assets offset the negative impact of the deficit growing faster than nominal GDP growth. According to the updated Commission 2016 spring forecast, the debt ratio is expected to peak at 100,6 % of GDP in 2017, whereas the spring forecast projected the debt to peak at 100,3 % of GDP in 2016. Although Spain does not appear to face immediate risks of fiscal stress arising from this high debt ratio, debt-sustainability risks will significantly increase in the medium term if the budgetary position is not improved. In the longer term, risks to fiscal sustainability are set to be reduced thanks to the positive impact of reductions in age-related expenditure.

(9) According to Article 5 of Regulation (EC) No 1467/97, in its decision to give notice to take measures for the deficit reduction in accordance with Article 126(9) TFEU, the Council is to request that the Member State achieve annual budgetary targets which, on the basis of the forecast underpinning the notice, are consistent with a minimum annual improvement of at least 0,5 % of GDP as a benchmark, in its cyclically adjusted balance net of one-off and temporary measures. However, the fact that that decision is adopted in the second half of the year amplifies the fiscal effort needed to achieve a given annual improvement of the structural balance. It is also important to bear in mind that the baseline scenario for the new adjustment path starts with a deterioration of 0,4 % of GDP of the structural deficit, which is at least in part the result of the inflation turning out lower than projected in the scenario underpinning the 2016 budget — an event that is largely outside the control of the Government. Taking this into account, it appears appropriate not to request further structural measures in 2016.

(10) Considering that no further structural measures should be requested in 2016, granting Spain one additional year for the correction of its excessive deficit, which is the rule under Regulation (EC) No 1467/97, would require an annual improvement of the structural balance in 2017 which would have a too negative impact on growth. Therefore, it seems adequate to extend the deadline for Spain to bring an end to its excessive deficit situation by two years.

(11) Therefore, a credible and sustainable adjustment path would require Spain to reach a general government deficit of 4,6 %, 3,1 % and 2,2 % of GDP in 2016, 2017 and 2018, respectively, which is consistent with a deterioration of the structural balance of 0,4 % of GDP in 2016 and a 0,5 % of GDP improvement in both 2017 and 2018. These budgetary targets also take into account the need to compensate for second-round effects of fiscal consolidation on public finances, through its impact on the wider economy.

(12) In order to reach those targets, further structural measures with an estimated impact of 0,5 % of GDP in both 2017 and 2018, are considered necessary. Savings for 2017 and 2018 could among others include the reduction of the number and scope of tax expenditures, in particular the reduced VAT rates, in order to achieve the required structural effort.

(13) In addition, strict enforcement at all government levels of the preventive and corrective mechanisms provided for in Spain's Stability Law could be conducive to a timely and durable correction of the excessive deficit. This could be achieved through greater automaticity in their implementation. Moreover, the contribution of the Stability Law's spending rule to the sustainability of public finances could be enhanced by further clarifying the coverage and definition of the spending categories needed for its computation and by explicitly calling on the non-compliant public administrations to make up for spending slippages in the year following their occurrence.

(14) Spain should also pay due attention to the qualitative aspects of public finances, including its public procurement policy. The number of wrongdoings having an impact on the application of EU public procurement legislation brought to the Commission's attention in recent years has been significant. The data show that there are disparities in the implementation of public procurement across contracting authorities and entities and that insufficient *ex ante* and *ex post* control mechanisms hinder the correct and uniform application of public procurement legislation. Spain stands out for a low publication rate of contract notices and a relatively high use of the negotiated procedure without prior publication compared with other Member States. This translates into limited competition from undertakings from other Member States and frequently, into direct awards, with implications in terms of higher general government expenditure. The limited use of centralised or joint procurement instruments prevents efficiency gains which would contribute to fiscal savings. The absence of an independent body in charge of ensuring efficiency and legal compliance in public procurement throughout the country hampers the proper implementation of procurement rules and may create opportunities for wrongdoings, both of which have negative impacts on the situation of Spain's public finances.

(15) To facilitate the success of the fiscal consolidation strategy, it will also be important to back the fiscal consolidation by comprehensive structural reforms, in line with the Council recommendations addressed to Spain in the context of the 2016 European Semester and in particular those related to the correction of its macroeconomic imbalances.

(16) According to Article 126(9) TFEU, the Council may, as part of its decision to give notice under that provision, request the Member State concerned to submit reports on the adjustment effort in accordance with a specific timetable. According to Article 5(1a) of Regulation (EC) No 1467/97, the Member State report is to include the targets for government expenditure and revenue and specify the fiscal policy measures on both the expenditure and the revenue side, as well as information on the policy actions being taken in response to the specific Council recommendations. In order to facilitate the monitoring of the deadline for compliance with the recommendations contained in this Decision, as well as the deadline for correction of the excessive deficit, Spain should submit such a report by 15 October 2016, at the same time as its 2017 Draft Budgetary Plan.

(17) Spain should also report to the Commission and the Economic and Financial Committee as required under Article 10 of Council Regulation (EU) No 473/2013 ([1]) in accordance with the specifications laid down in Commission Delegated Regulation (EU) No 877/2013 ([2]). The report should be submitted for the first time by 15 January 2017 and on a three-monthly basis thereafter,

HAS ADOPTED THIS DECISION:

Article 1

1. Spain shall put an end to the present excessive deficit situation by 2018.

([1]) Regulation (EU) No 473/2013 of the European Parliament and of the Council of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area (OJ L 140, 27.5.2013, p. 11).

([2]) Commission Delegated Regulation (EU) No 877/2013 of 27 June 2013 supplementing Regulation (EU) No 473/2013 of the European Parliament and of the Council on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area (OJ L 244, 13.9.2013, p. 23).

2. Spain shall reduce the general government deficit to 4,6 % of GDP in 2016, to 3,1 % of GDP in 2017 and to 2,2 % of GDP in 2018. This improvement in the general government deficit is consistent with a deterioration of the structural balance by 0,4 % of GDP in 2016 and a 0,5 % of GDP improvement in both 2017 and 2018, based on the updated Commission 2016 spring forecast. Spain shall also use all windfall gains to accerelate the deficit and debt reduction.

3. In addition to the savings already included in the updated Commission 2016 spring forecast, Spain shall adopt and fully implement consolidation measures for the amount of 0,5 % of GDP in both 2017 and 2018.

4. Spain shall stand ready to adopt further measures should risks to the budgetary plans materialise. Fiscal consolidation measures shall secure a lasting improvement in the general government structural balance in a growth-friendly manner.

5. Spain shall adopt measures to strengthen its fiscal framework, in particular with a view to increasing the automaticity of mechanisms to prevent and correct deviations from the deficit, debt and expenditure targets and to strengthening the contribution of the Stability Law's spending rule to public finance sustainability.

6. Spain shall set up a consistent framework to ensure transparency and coordination of public procurement policy across all contracting authorities and entities with a view to guaranteeing economic efficiency and a high level of competition. Such framework shall include appropriate *ex ante* and *ex post* control mechanisms for public procurement to ensure efficiency and legal compliance.

Article 2

The Council establishes the deadline of 15 October 2016 for Spain to take effective action and, in accordance with Article 5(1a) of Regulation (EC) No 1467/97, to submit a report to the Council and the Commission on action taken in response to this Decision. The report shall include the targets for government expenditure and revenue, and specify the discretionary measures on both the expenditure and the revenue side, as well as information on the actions being taken in response to the specific Council recommendations to strengthen its fiscal framework and its public procurement policy framework in accordance with Article 1(5) and (6).

Article 3

This Decision is addressed to the Kingdom of Spain.

Done at Brussels, 8 August 2016.

For the Council
The President
M. LAJČÁK