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Greece: Request for Stand-By Arrangement

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International Monetary Fund
Washington, D.C.

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington DC

Athens, May 3, 2010

Dear Mr. Strauss-Kahn:

The attached Memorandum of Economic and Financial Policies (MEFP) outlines the economic and financial policies that the Greek government and the Bank of Greece, respectively, will implement during the remainder of 2010 and in the period 2011–2013 to strengthen market confidence and Greece's fiscal and financial position during a difficult transition period toward a more open and competitive economy. The government is fully committed to the policies stipulated in this document and its attachments, to frame tight budgets in the coming years with the aim to reduce the fiscal deficit to below 3 percent in 2014 and achieve a downward trajectory in the public debt-GDP ratio beginning in 2013, to safeguard the stability of the Greek financial system, and to implement structural reforms to boost competitiveness and the economy's capacity to produce, save, and export. In this regard, the government is also fully and equally committed to the policies stipulated in the Decision and Recommendation issued by the EU Council on February 16, 2010.

The government is strongly determined to lower the fiscal deficit, including by achieving higher and more equitable tax collections, and constraining spending in the government wage bill and entitlement outlays, among other items.

In view of these efforts and to signal the commitment to effective macroeconomic policies, the Greek government requests that the Fund supports this multi-year program under a Stand-By Arrangement (SBA) for a period of 36 months in an amount equivalent to SDR26.4 billion (3,212 percent of quota; €30 billion). A parallel request for financial assistance to euro area countries for a total amount of €80 billion has been sent.

The implementation of the program will be monitored through quantitative performance criteria and structural benchmarks as described in the attached MEFP and Technical Memorandum of Understanding (TMU). There will be twelve quarterly reviews of the program supported under the SBA by the Fund, in coordination with the European Commission and the ECB, to begin with the first review that is expected to be completed in the course of the third calendar quarter of 2010, and then every quarter thereafter until the last quarterly review envisaged to be completed during the second calendar quarter of 2013, to assess progress in implementing the program and reach understandings on any additional measures that may be needed to achieve its objectives. Each review will include an in-depth assessment of program financing in light of the joint financing of this program by the bilateral funding arrangement of the euro area member states for Greece.
The Greek authorities believe that the policies set forth in the attached memorandum are adequate to achieve the objectives of the economic program, and stand ready to take any further measures that may become appropriate for this purpose. The authorities will consult with the Fund in accordance with its policies on such consultations, and with the European

Commission and the ECB on the adoption of these measures and in advance of revisions to the policies contained in the MEFP. All information requested by the Fund, the European Commission, and ECB to assess implementation of the program will be provided.

This letter is copied to Messrs. Juncker, Rehn, and Trichet.

Sincerely,

/s/

George Papaconstantinou
Minister of Finance

/s/

George Provopoulos
Governor of the Bank of Greece

GREECE—MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES
May 3, 2010

I. RECENT DEVELOPMENTS

1. **The economic downturn accelerated coming into 2010.** Greek real GDP declined by 2 percent in 2009 and indicators suggest that activity will weaken further in 2010. Following the Greek elections in October, the realization that the fiscal and public debt outturn for 2008 and 2009 were significantly worse than had been reported by the previous government caused confidence to drop, financing costs to increase, and growth and employment to suffer.

2. **The crisis exposed the weak fiscal position.** The deficit of 5.1 percent of GDP in 2007, at the top of the cycle, shows that Greece entered the downturn with a large underlying public deficit. With weak revenue policies and tax administration, especially leading up to the 2009 elections and aggravated by the recession, revenues declined notably. Spending, meanwhile, increased significantly, especially on wages and entitlements, reflecting weak spending discipline and monitoring and control, which also led to new arrears. The deficit jumped to an estimated 13.6 percent of GDP while the public debt rose to over 115 percent of GDP in 2009. The monitoring and control deficiencies delayed the implementation of corrective fiscal policies.

3. **The financial system has been adversely affected.** With the deteriorating fiscal results came downgrades of government bonds by rating agencies, and investors started backing out of Greek bonds, driving up their yields. Furthermore, it is clear that the deep macroeconomic and structural problems combined with unavoidable strong fiscal adjustment over the medium term are likely to weigh on activity for some time. This combination of factors affects negatively the banking system. Impaired loans are rising while borrowing costs in the interbank and wholesale markets have increased, putting pressure on bank profitability.

4. **Despite the recession, the external deficit is declining only gradually.** Inflation and domestic costs have increased well above those of Greece's euro partners over the last decade and Greece has lost competitiveness. As a result, the external current account deficit at end 2009 was still over 11 percent of GDP, and the net international investment position is over negative 83 percent of GDP. The external interest bill on the foreign debt has increased to over 5 percent of GDP, so it will take a surplus in trade of goods and services to return the current account to a more sustainable position. This will require a strengthening of economic policies and competitiveness to lay the foundations for a growth model that relies more on investment and exports.

II. Key Objectives and the Outlook

5. **The main objectives of the program are to correct fiscal and external imbalances and restore confidence.** Without regaining confidence in the sustainability of fiscal and economic developments, the cost of funding the economy is bound to stay high if not increase further. The fiscal and the external imbalances need to be corrected. Facing these two tasks at the same time is challenging, requiring a major reorientation in the economy. Growth is unlikely to be buoyant as the initial corrective fiscal measures are implemented, but with financial sector policies to preserve the soundness of the banking sector and strong medium-term fiscal and structural policies, the economy will emerge from this experience in better shape than before with higher growth and employment.

6. **The government foresees an extended adjustment period:**

- **Real GDP growth** is set to contract significantly in 2010–2011, but should gradually recover thereafter. The economic program assumes negative growth of 4 percent in 2010 and 2½ percent in 2011. While fiscal consolidation is bound to weigh on economic activity at first, it is expected that confidence effects from the front-loaded fiscal measures and the strong medium-term economic program in combination with comprehensive structural reforms will create the conditions for a return to growth from 2012 onward.

- **Inflation** needs to be reduced significantly below the euro area average for Greece to regain swiftly price competitiveness. Domestic demand tightening, both through fiscal adjustment and efforts to moderate wages and pensions, together with cost-cutting measures in the economy, will be essential to bring inflation down in a meaningful way. In this regard, addressing oligopolistic structures to reduce high markups in some sectors will also be important.

- **The external deficit** is projected to decline gradually over the medium term as domestic demand and inflation moderate and the economy responds to structural reforms to improve the supply of exports and reduces the dependence on imports. This process will naturally take several years, while the interest costs on the substantial external debt will pressure the current account for some time.

III. Economic Policies

7. **To achieve the program objectives, all available fiscal, financial, and structural policies will be used.** The economy needs a strong and sustained adjustment program to correct fiscal imbalances and place debt on a downward path in the medium term, maintain banking sector stability, and restore competitiveness:

- **Fiscal adjustment will have to be the cornerstone of the program.** The government is committed to put in place durable adjustment measures, on top of those already announced in March this year, of 11 percent of GDP in cumulative terms through 2013, with additional remedial measures in 2014 to reduce the deficit to well below 3 percent of GDP. This large adjustment is needed to put the debt-GDP ratio on a downward trajectory from 2013 onward, which will be sustained after the program by keeping primary balances in a sizeable surplus (at least 5 percent of GDP) up to 2020. To sustain fiscal consolidation over the medium term, the government also is committed to strengthening the fiscal policy framework and fiscal institutions.

- **Incomes and social security policies need to buttress the fiscal adjustment effort and restoration of competitiveness.** Realigning incomes to sustainable levels is necessary to assist fiscal correction, support a reduction in inflation well below the euro area average, and improve price and cost competitiveness on a lasting basis. Social security programs need to be strengthened to confront underlying structural imbalances that result from the ageing of the population, where growth in entitlement costs for Greece is projected to be among the highest in the European Union with current policies. As the largest annual overruns in the budget consistently come from the social security funds, reforms cannot be postponed any longer to safeguard the viability of the system.

- **Financial sector policies need to maintain stability.** While currently capital buffers in the banking system are reassuring, bank supervisors will need to monitor closely liquidity and nonperforming loans at individual banks. The Bank of Greece and the government will further strengthen and clarify the key elements of Greece's supervisory and financial crisis framework to assist the banking system through this period of lower growth.

- **Structural reforms that boost the economy's capacity to produce, save, and export will be critical for the medium-term recovery.** Greece's openness is lagging euro-area peers. The government is determined to implement an ambitious program of reforms to modernize the public sector and render product and labor markets more efficient and flexible, create a more open and accessible environment for domestic and foreign investors, and reduce the state's direct participation in domestic industries.

8. **The government is committed to fairness in the distribution of the adjustment burden.** Our resolve to protect the most vulnerable in society from the effects of the economic downturn was taken into account in the design of the adjustment policies. In consolidating government finances, larger contributions will be raised from those who have traditionally not carried their fair share in the tax burden. With regard to the reduction in public wages and in pensions, the minimum earners have been protected:

- Pension reductions: The elimination of the 13th and 14th pensions is compensated, for those receiving less than €2500 a month, by introducing a new flat bonus of €800 a year. The benefit reduction is weighted toward the higher pension earners.

- Wage bill reductions. The 13th and the 14th wage payments will be eliminated for all employees. To protect the lower income segment, here too, for those receiving less than €3000 a month, a flat bonus payment of €1000 a year per employee will be introduced, which will be financed through cutting salary allowances for higher income segments.

Further, minimum pensions and family support instruments will not be cut, and the most vulnerable will be compensated for the possible adverse impact of policies. To explain and forge consensus on policies to overcome the crisis, the government will invite representatives of businesses and labor to sign a social pact for the duration of the program. The spirit of the above considerations is to maintain strong social cohesion, fight poverty, and maintain employment.

A. Fiscal Policies

9. **The Greek government recognizes the need to implement a frontloaded multiyear adjustment effort given Greece's very high and still growing debt ratio and large fiscal deficit**. All the necessary measures to strengthen market confidence and convince creditors that Greece will regain control over the debt dynamics will be taken. A difficulty is that policies to restore external price competitiveness, which in a monetary union have to rely on reductions in domestic costs and prices, will initially weigh on economic activity, government revenue and debt dynamics. Therefore, the effort has to take place in a period of contracting economic activity, naturally slowing revenues, and cyclically high expenditure. However, it is imperative to place fiscal policies, and the economy, on a sound path for future growth. It is clear that the public sector has become too large and costly and has to become smaller, more efficient and agile, and oriented to providing better services to citizens.

10. **The fiscal strategy is anchored in placing the debt-GDP ratio on a declining path from 2013 onward and reducing the general government deficit to well below 3 percent of GDP by 2014**. To avoid reform fatigue and boost market confidence, the government's strategy is strongly to frontload the fiscal adjustment. All the fiscal measures for the remainder of 2010–2012 have been identified, and most of them will be adopted in the coming weeks. Fiscal measures for 2013 have also been identified with some residual gap remaining that will need to be addressed in coming reviews.

11. **A very strong start has already been made leading to a significant reduction in the 2010 first quarter deficit. For the remainder of 2010 additional measures will be implemented beyond those stipulated in the EU Council Decision and Recommendation of 16 February 2010 and those announced in March 2010** (Table 1**)**. The three biggest

upfront measures are an immediate cut in the public sector wage bill, and in pension outlays, and further increases in the VAT and selected excises (together with other steps yielding 2½ percent of GDP in further savings already in 2010). This will assure that the deficit, notwithstanding the recession, drops from an estimated 13.6 percent of GDP in 2009 to 8.1 percent of GDP in 2010. These very large upfront efforts show the government's resolve in responding to the recent deterioration in market sentiment and the large fiscal challenges, and will help overcome the adverse developments on revenue and support payments such as higher unemployment outlays. These large measures come on top of those already undertaken, which include the first installment of lowering the government's wage bill and selected social security benefits (while safeguarding the minima), the substantial reductions in operating expenditures in all ministries, and significant permanent revenue measures and special taxes on highly profitable enterprises and large properties, and on luxury goods. Thus, the government's resolve is unwavering and every effort will be made to distribute the burden equitably.

12. **For 2011 and beyond, further revenue and expenditure measures have been identified to secure fiscal targets**. Together with the full-year effect of the advance measures taken in mid-2010, these will cover the adjustment needs for 2011 projected at 4 percent of GDP. Adjustment measures in 2012 will continue at a pace of 2½ percent of GDP and in 2013 they are projected to be 2 percent of GDP. Given the expected weakness in GDP, the headline deficit in percent of GDP is expected to drop to 7½ percent in 2011, with more significant headline declines in subsequent years when economic growth resumes.

- **Expenditures will be cut by the equivalent of around 7 percent of GDP through 2013.** Since adoption of the euro, Greece has increased its noninterest expenditures by 8 percentage points of GDP, including with public wages, consumption, and social transfers imposing an overly large burden on the state. This needs to be reversed. As a result, wage and entitlement program costs need to be curtailed as they represent the bulk of the primary budget expenditures, and thereafter wages and pensions will be subsequently frozen in nominal terms for the duration of the program. The government has also planned other reductions in government spending, including by replacing over time only 20 percent of retiring employees, and by consolidating municipalities and local councils. It is essential that the burden of the adjustment on the expenditure side be distributed over multiple programs, so even investment spending will need to be rationalized and shifted to more intensive and efficient use of EU structural and cohesion funds, as feasible. Independent reviews will be launched, conducted by internationally renowned experts, of the public administration and of existing social programs to help identify actions to rationalize the organization of public administration and improve targeting of social programs so that resources are channeled to the most vulnerable.

- **Revenues will be increased by the equivalent of around 4 percent of GDP through 2013.** Revenue from higher income segments of society will include a boost in (presumptive) taxation on liberal professions, an increase in luxury goods taxation, and (temporary) surcharges on highly profitable entities and high valued properties as well as other measures to combat tax evasion included in the recently adopted tax reform legislation. Other revenue increases will include broadening the VAT base, increasing rates and raising excise taxes where Greece is below the euro area average and collection efficiency is low. Green taxes and "health" taxes (such as on consumption of alcohol and tobacco) will also play a part in the revenue raising effort.

13. **Besides these direct fiscal steps for the budget, the government also has initiated a series of important structural fiscal reforms**. These will boost sustainability by helping to strengthen control over revenues and expenditures:

- **Pension reform.** The current pension system is unsustainable and will become insolvent if responsible measures are not taken to place it on a sound footing. The government has initiated a reform which should be adopted before end-June 2010. The National Actuarial Authority will produce a report to verify that the parameters of the new system ensure long-term actuarial balance. The existing pension funds will be merged in three funds. The reform will introduce a new system to strengthen the link between contributions and benefits, with uniform rules that will apply pro-rata to all current and future workers. The normal retirement age will be set to 65 years, increasing in line with life expectancy. Benefits will be indexed to prices. The reform will also restrict early retirement, including for those insured before 1993, and reduce the list of heavy and arduous professions. The new system will also include a means-tested social pension for all citizens above the normal retirement age so that an important safety net is provided, consistent with fiscal sustainability.

- **Health sector reform.** The government will implement double-entry accrual accounting in hospitals, the regular publication of audited accounts, and improvements in pricing and costing mechanisms. The government also plans to separate health funds from administration of pensions, merge the funds to simplify the overly fragmented system, and bring all health-related activities under one ministry.

- **Tax reform.** The government has obtained passage of a tax bill that includes important components to make the tax system more efficient and equitable. The income tax system has become more progressive; exemptions and deductions have been reduced to broaden the tax base; and a number of reforms have been introduced to fight tax evasion, including the tightening of obligations to issue receipts for VAT and to document living expenses, and the introduction of presumptive taxation. The government will further review the tax system to simplify it and increase efficiencies as necessary.

- **Tax administration.** Tax administration improvements are being implemented for which technical assistance has already been received from the IMF. In the short run, the government's strategy will focus on safeguarding revenue from the largest taxpayers, stronger enforcement and auditing of high-wealth individuals and self-employed (where risk of evasion is largest) and prosecuting the worst offenders, strengthening enforcement of VAT filing and payment, and collecting on the large stock of tax arrears. For the medium-term, the government will design a program of structural reforms in key tax compliance and administration areas, including: developing and maintaining a comprehensive compliance risk management framework (notably preparing a compliance strategy for 2012); developing taxpayer service capacity to support compliance improvement efforts; substantially improving enforcement operations, particularly in audit, using risk-based approaches; and building headquarters strategic management and planning capabilities in tax and customs administration.

- **Public financial management and fiscal framework.** Technical assistance from the IMF and the European Commission on public financial management and longer-term budgeting reforms will be re-prioritized to address the short-term challenges we are facing. In this context, the General Accounting Office (GAO) will be responsible for monitoring and reporting of general government data; the government will introduce standardized commitment control procedures for all public entities to prevent the re-emergence of arrears; ensure that all budgets are prepared within a medium-term fiscal strategy for the general government and presented before the start of the fiscal year; introduce top-down budgeting with expenditure ceilings, a sufficient contingency reserve, and a medium-term expenditure framework for the State budget; require a supplementary budget for any overruns above this contingency provision; and amend the 1995 budget management law to give effect to the above. The government will continue to work with the technical assistance teams of the IMF and the European Commission to implement the recommendations already received, and to make further improvements over the course of the program, including the creation of an independent fiscal agency attached to parliament.

- **Debt management framework.** The government will update its debt management strategy and the tools to ensure that risk is adequately managed. To enhance market confidence and communication, the government plans to review the operational and risk management framework for debt management to ensure the transparency and predictability of our actions. The government has already sought technical assistance in this area from the IMF.

- **Fiscal and other public sector reporting of information, including statistical aspects.** Upon taking office in October 2009, the new government immediately disclosed that the fiscal deficit for 2008 was under-reported and needed to be revised. Working closely with Eurostat on fiscal data processing and reporting, the government has already taken remedial measures to prevent the reoccurrence of such problems and has designed jointly with the European Commission an action plan to address outstanding statistical issues. Among these, full independence has been granted to the Greek Statistical Office and sufficient resources will be devoted in the coming years to improve statistical systems and seek appropriate resident technical assistance to ensure rapid progress. To that end, the measures in the joint Greek government and European Commission Statistical Action Plan will be fully implemented. Going forward, we feel confident that we are in a position to provide accurate fiscal data to the Fund and our European partners Further, since January 2010, timely monthly central government budget reports on a cash basis have been published. The GAO will also start publishing monthly data on expenditures pending payment, including arrears, from July 2010. Efforts will also be intensified to improve the collection and processing of general government data compiled according to the European System of National and Regional Accounts (ESA) required under the existing EU legal framework, and compile comprehensive data on employment in the general government. Detailed information will be furnished to the European Commission, the ECB and the Fund on the operating accounts and balance sheets of key public enterprises.

14. **The program will be closely monitored and measures will be taken as necessary.** There are risks to the program from lower revenue, higher social transfers, further downward revisions of growth, additional fiscal liabilities from the public and financial sector, and higher interest costs. However, these can be managed and the government stands ready to take appropriate measures to preserve the program objectives, including by reducing discretionary spending, as necessary. At the same time, there is some upside potential. Our 2010–2011 projections include cautious estimates of the measures taken, positive confidence effects could boost GDP growth and reduce market risk premia, and our revenue administration efforts could start to yield more revenue gains than currently assumed in the program. Should confidence rebound and the market support Greece earlier than expected, or the supply response from reforms comes in more vigorously, these benefits will be saved and the intended deficit will be brought forward to achieve a speedier return to fiscal sustainability.

B. Financial Sector Policies

15. **Despite a strong solvency position, at present, the Greek banking system is facing challenges**. The system's equity base was substantially strengthened in 2009, jumping from €24 to €33 billion, including through capital injections from the government, for €3.8 billion, capital increases from the owners, and retained earnings. All banks are in compliance with the capital adequacy requirement of 8 percent, and the average capital adequacy ratio rose to 11.7 percent at end 2009. However, the fiscal crisis and a weakening economic environment resulted in a reversal in credit growth and an increase in non-

performing loans, which reached 7.7 percent at end-2009 while profitability declined and might become negative this year.

16. **The immediate challenge for the banks is to manage carefully the current tight liquidity conditions.** In the general context of the turbulence affecting the debt markets for the Greek government, the Greek banks have lost wholesale market access to fund their operations since end-2009. Maturing interbank liabilities have not been renewed, or only at high costs, and some moderate deposit outflows were noted during the first months of 2010, which has put pressure on the liquidity position of many Greek banks. As a result, the banks have increasingly relied on Eurosystem credit operations. To assist the banks in these difficult times the government has extended the banking assistance package of early 2009 (€28billion of which €11 billion had been used by end-2009)), to provide a substantial €17 billion in additional liquidity and the government is implementing another extension of this support facility subject to approval by decision of the European Commission. Within the existing Euro system framework, national central banks may give support to temporarily illiquid, but solvent institutions. In the event that such support is given by the Bank of Greece, it will be fully guaranteed by the Greek state in a manner that is consistent with relevant ECB and EU requirements.

17. **The government and the Bank of Greece are also putting in place a new safety net to preserve the sound level of bank equity, and thus improve conditions to support the real economy.** Anticipating that banks profits may decline further, possibly impacting their equity position, the government will establish (by June 30, 2010, as a structural benchmark), through specific legislation and in consultation with the IMF, the European Commission, and the ECB, a fully independent Financial Stability Fund (FSF). The FSF's key decision makers will be persons of recognized standing in financial matters, appointed by the government and the Governor of the Bank of Greece (who will make most of the appointments).

18. **The primary purpose of the FSF is to preserve the financial sector's soundness and thus its capacity to support the Greek economy, by providing equity support to banks as needed.** Whenever supervisory assessments conclude that a bank's capital buffer might fall below adequate levels, the shareholders will be required to immediately bring additional capital or take bridging capital support from the FSF. If banks are then not able to expeditiously raise additional capital on their own and repay the FSF, a restructuring process will take place under the lead of the FSF, in line with EU competition and state aid requirements.

19. **Other elements of the safety net for the financial sector will also be strengthened.** Corporate debt restructuring legislation, and the current proposal for a personal debt restructuring law, will be in line with international best practices, to ensure that credit discipline is maintained, that creditor and consumer rights are protected, and that relevant information concerning borrowers' track record is preserved.

20. **The Bank of Greece will implement intensified supervision and increase the resources dedicated to banking supervision.** This will include an increase in the frequency and speed of data reporting, and the further development of a comprehensive framework for regularly stress-testing financial institutions. Staffing will be increased both for on-site inspections and off-site review, also taking into account the new responsibilities of the Bank of Greece with respect to insurance supervision. Additional flexibility will be introduced in the management of human resources, and all Bank of Greece staff will be granted strong legal protection for actions performed in good faith.

21. **Close coordination will be maintained with home and host country supervisors within the EU framework for cross-border bank supervision.** In this context, the authorities are fully aware of the significant presence of Greek banks in South Eastern European (SEE) countries; a number of MoUs with the host supervisory authorities (both EU and non-EU) have been signed. Communication with regulators in SEE regarding risk assessments and liquidity contingency plans are also intensifying.

C. Structural Policies

22. **Structural policies are strengthened in order to boost competitiveness and emerge from the crisis quickly**. These will enhance the flexibility and productive capacity of the economy, ensure that wage and price developments restore and then sustain international competitiveness, and progressively alter the economy's structure towards a more investment and export-led growth model. The Greek government will work closely with the European Commission and the ECB to pursue reforms as specified in the MoU attached to this MEFP. In particular:

- **Modernizing public administration.** Fragmented employment practices will be reformed by reorganizing recruitment procedures and finalizing the single payment authority for wages. A simplified remuneration system will be introduced, in a cost-saving manner that will cover basic wages and all allowances which apply to all public sector employees. Procurement practices will be strengthened to generate efficiency gains and ensure transparency. The health care system, where there have been major expenditure overruns, will be overhauled through reforms in management, accounting and financing systems. A reorganization of sub-central government will be implemented to reduce the number of local administrations and elected/appointed officials. The government will collaborate with the EC to launch an independent external functional review of public administration at the central government level. These reforms will help prioritize government activities and, strengthen the fight against waste and corruption throughout the public administration.

- **Strengthening labor markets and income policies.** In line with the lowering of public sector wages, private sector wages need to become more flexible to allow cost moderation for an extended period of time. Following consultation with social partners and within the frame of EU law, the government will reform the legal framework for wage bargaining in the private sector, including by eliminating asymmetry in arbitration. The government will adopt legislation for minimum entry level wages in order to promote employment creation for groups at risk such as the young and long-term unemployed. In parallel, the government will implement the new control system for undeclared work and modernize labor market institutions. Employment protection legislation will be revised, including provisions to extend probationary periods, recalibrate rules governing collective dismissals, and facilitate greater use of part-time work. The scope for improvements in the targeting of social expenditures will be revised in order to enhance the social safety net for the most vulnerable.

- **Improving the business environment and bolstering competitive markets.** The government will shortly adopt legislation establishing one-stop shops for starting new enterprises to cut procedures, costs and delays. Legislation will be introduced to cut licensing and other costs for industry. The government will fully implement key steps of the EU Services Directive in 2010, especially in priority areas such as tourism, education and retail. Over the course of next year, restricted professions will be opened by reducing fixed tariffs and other restrictions in the legal, pharmacy, notary, engineering, architect, road haulage, and auditing professions. The role of the Hellenic Competition Commission (HCC) will also be strengthened. Network industries will be progressively liberalized, especially in the transport and energy sector while strengthening regulators in these sectors in line with EU policies.

- **Managing and divesting state enterprises**. These need to be subject to greater transparency to increase efficiency and reduce losses. As a first step, 2009 financial statements audited by chartered accountants of the ten largest loss makers will be published on the internet. A time table and action plan for improving the financial performance of main loss-makers, most notably in the railway and public transportation companies will be produced. This action plan will include concrete steps to reduce costs, including by streamlining the networks serviced and increasing tariffs. The government will review the role for divesting state assets, including of land owned by public enterprises or the government. The government will further review the scope for improving corporate governance, and enhancing oversight of state-ownership.

- **Improving the absorption of EU structural and cohesion funds.** The government will work closely with the EC to raise the absorption rate of Structural and Cohesion Funds, including by establishing targets for payment claims based on Management Information System (MIS) data every six months to be measured by certified data and a system of "fast track project production" which includes deadlines for each step of the approval and implementation of projects. A minimum of ten major projects per annum will be submitted. Within the overall public investment envelope agreed in this program, a central account will be established to be used for budgetary appropriations for the national co-financing of Structural and Cohesion Funds. A specific Task Force will be established with the Commission to ensure the faster delivery of high-quality projects.

IV. Program Financing

23. **We anticipate covering the program's financing requirements with financial support from euro-area member states and the IMF while strengthening access to the private capital markets**. Notwithstanding the significant fiscal adjustment, we project a public financing gap of around €110 billion, for the program period, which we expect to cover through matching bilateral lending support from euro area member states (€80 billion) and through IMF support (€30 billion). Greece will draw on these resources in parallel throughout the program period, drawing on the bilateral and IMF financing in a ratio of 8 to 3 in each disbursement (measured at the program exchange rate). We are confident that resolute implementation of our economic program will help our economy recover and bolster market sentiment. If fiscal consolidation proceeds faster than expected or if market conditions improve significantly during the program period, we would refrain pari passu from drawing on the full bilateral and IMF support.

V. Program Monitoring

24. Progress in the implementation of the policies under this program will be monitored through quarterly (and continuous) quantitative performance criteria (PCs) and indicative targets, structural benchmarks, program reviews and consultation clauses. These are detailed in Tables 2 and 3. The attached TMU contains definitions. Quantitative targets up to December 2010 are PCs. Targets for 2011-2013 are indicative and for 2011 will be converted into PCs at the time of the second review before end-2010. A joint EC/ECB MoU specifies, notably, the structural policies recommended in the MEFP, and sets a precise time frame for their implementation.

In the context of the arrangement, the Bank of Greece will undergo a safeguards assessment in accordance with the IMF safeguards policy. In this regard, and to facilitate a timely completion of the assessment, the authorities have provided the information requested for the assessment to commence, and have also authorized the external auditors to provide information to and hold discussions with the staff of the IMF. As a related matter, and given that financing from the IMF will be used to provide direct budget support, a memorandum of understanding between the government and the Bank of Greece will establish a clear framework on the modalities for the repayment of IMF financing and the servicing of interest payments and other charges. As part of these arrangements, Fund disbursements will be deposited into the government's single treasury account at the Bank of Greece pending their use.

Table 1: Greece: Fiscal Measures included in the Program 1/
(in millions of Euros)

	2010	2011	2012	2013	Cum	% GDP
I. Revenue measures						
VAT rates increase by 10 percent (10% to 11%; 21% to 23%)	800	1,000	0	0	1,800	0.8
Broadening VAT base	0	1,000	500	0	1,500	0.7
Excise tax on fuel	200	250	0	0	450	0.2
Excise tax on cigarettes	200	300	0	0	500	0.2
Excise tax on alcoholic beverages	50	50	0	0	100	0.0
Excise goods on non-alcoholic beverages	0	0	300	0	300	0.1
Excise tax on luxury goods	0	100	0	0	100	0.0
Green taxes	0	300	0	0	300	0.1
Gaming royalties	0	200	400	0	600	0.3
Gaming licenses	0	500	225	-725	0	0.0
Special levy on highly profitable firms	0	600	0	0	600	0.3
Presumptive taxation of professionals	0	400	100	0	500	0.2
Taxation of wage in kind (cars)	0	150	0	0	150	0.1
Book specification of incomes	0	50	0	0	50	0.0
Increase legal value real estate	0	400	200	100	700	0.3
Amnesty land use violations	0	500	0	0	500	0.2
Taxation of unauthorized establishments	0	800	0	0	800	0.3
II. Expenditure measures						
Reduce wage bill by cutting bonuses/allowances	1,100	400	0	0	1,500	0.7
Workforce reduction beyond 5:1 (add. 20,000)	0	0	600	500	1,100	0.5
Savings from introduction of unified public sector wages	0	100	0	0	100	0.0
Eliminate pension bonuses (except for minimum pensions)	1,500	500	0	0	2,000	0.9
Additional pension reduction above a certain threshold	350	150	0	0	500	0.2
Nominal pension freeze	0	100	250	200	550	0.2
Means test unemployment benefit	0	0	500	0	500	0.2
Cancel second installment of solidarity allowance	400	0	0	0	400	0.2
Cut intermediate consumption	700	300	0	0	1,000	0.4
Kalikrates	0	500	500	500	1,500	0.7
Cut in transfers to public enterprises	0	0	1,500	0	1,500	0.7
Cut domestically funded investment spending	500	500	500	0	1,500	0.7
Yet to be quantified yield from structural reform initiatives	0	0	0	4,200	4,200	1.8
Total annual measures	**5,800**	**9,150**	**5,575**	**4,775**	**25,300**	**11.0**
Revenue measures	1,250	6,600	1,725	-625	8,950	3.9
Expenditure measures	4,550	2,550	3,850	5,400	16,350	7.1
Total measures (in percent of GDP)	**2.5**	**4.1**	**2.4**	**2.0**		**11.0**
Revenue measures	0.5	3.0	0.8	-0.3		3.9
Expenditure measures	2.0	1.1	1.7	2.3		7.1
Memorandum item:						
Nominal GDP	231	224	228	235		229

Source: Greece authorities, and IMF staff estimates.
1/ Yield of measures relative to the previous year.

Table 2. Greece: Quantitative Performance Criteria (in billion of Euros, unless otherwise indicated)

	Performance Criteria			Indicative Targets					
	Jun-10 Progr. 1/	Sep-10 Progr. 1/	Dec-10 Progr. 1/	Jun-10 Progr. 1/	Sep-10 Progr. 1/	Dec-10 Progr. 1/	Dec-11 Progr. 2/	Dec-12 Progr. 3/	Dec-13 Progr. 4/
1. Floor on the modified general government primary cash balance	-5.0	-4.0	-5.7	...	...	...	-2.1	2.4	7.4
2. Ceiling on State Budget primary spending	34	50	67	...	...	...	67	68	69
3. Ceiling on the accumulation of new domestic arrears by the general government 5/	...	...	...	0	0	0	0	0	0
4. Ceiling on the overall stock of central government debt	342	342	342	...	...	...	365	...	...
5. Ceiling on the new guarantees granted by the central government	2.0	2.0	2.0	...	...	...	1.0	0.0	0.0
6. Ceiling on the accumulation of new external payments arrears on external debt contracted or guaranteed by general government 5/	0	0	0	...	...	...	0	0	0

1/ Cumulatively from January 1, 2010 (unless otherwise indicated).
2/ Cumulatively from January 1, 2011 (unless otherwise indicated).
3/ Cumulatively from January 1, 2012 (unless otherwise indicated).
4/Cumulatively from January 1, 2013 (unless otherwise indicated).
5/ Applies on a continuous basis from April [30] onward.

Greece. Table 3. Greece: Structural Conditionality for 2010 1/

Measures	Date	Macrocritical relevance
	Prior actions	
1. Reduce public wage bill by cutting bonuses/allowances; and pension bonuses (except minimum pensions).		Improves fiscal sustainability; has signaling effect for private sector wage setting.
2. Increase standard VAT rate from 21 to 23 percent and reduced rate from 10 to 11 percent and excise tax rates on alcohol, tobacco, and fuel with a yield of at least €1.25 billion in the remainder of 2010.		Improves fiscal sustainability.
3. Appoint staff team and leader in GAO responsible for general government in-year cash reporting.		Establishes in-year oversight responsibilities of general government fiscal policy.
Structural benchmarks	**End-June 2010**	
1. Establish the independent Financial Stability Fund (FSF) to preserve the financial sector's soundness and thus its capacity to support the Greek economy by providing equity support to banks as needed.		Enhances financial stability.
2. Adopt and start to implement a reorganization of sub-central government with the aim to reduce the number of local administrations and elected/appointed officials (Kalikrates).		Improves fiscal sustainability.
3. Submit to parliament amendments to Law 2362/1995 to (i) require the MoF to present a three-year fiscal and budget strategy, (ii) introduce top-down budgeting with expenditure ceilings for the State budget and multi-year expenditure estimates by line ministry, (iii) introduce standard contingency margins, (iv) require a supplementary budget for any overspending above the contingency, (v) and introduce commitment controls. The amended law should be immediately effective, including in the context of the 2011 budget.		Improves credibility of the budget and fiscal consolidation program.
4. The National Actuarial Authority to produce a report to assess whether the parameters of the new system significantly strengthen long-term actuarial balance.		Reduces budgetary costs of ageing and improves long-term fiscal sustainability. Increases labor force participation.
	End-September 2010	
1. Adopt a comprehensive pension reform that reduces the projected increase in public spending on pensions over the period 2010-60 to 2½ percent of GDP.		Improves fiscal sustainability.
2. Establish a commitment register in all line ministries and public law entities. Begin publishing monthly data on general government in-year fiscal developments (including arrears).		Reduces budget overruns.
3. Publish 2009 financial statements of the ten largest loss-making public enterprises, audited by chartered accountants, on the official website of the Ministry of Finance.		Increases transparency of fiscal risks to fiscal sustainability.
4. Put in place an effective project management arrangement (including tight MOF oversight and five specialist taskforces) to implement the anti-evasion plan to restore tax discipline through: strengthened collection enforcement and recovery of tax arrears—coordinated with the social security funds—of the largest debtors; a reorganized large taxpayer unit focused on the compliance of the largest revenue contributors; a strong audit program to defeat pervasive evasion by high-wealth individuals and high income self-employed, including prosecution of the worst offenders; and a strengthened filing and payment control program.		Achieves revenue targets and enhances sustainability of the consolidation by increasing burden sharing of the adjustment.
	End-December 2010	
1. Publish a detailed report by the ministry of finance in cooperation with the single payment authority on the structure and levels of compensation and the volume and dynamics of employment in the general government.		Reduces wage escalation. Improves transparency of public sector employment.
2. Adopt new Regulation of Statistical Obligations for the agencies participating in the Greek Statistical System.		Enhance confidence in fiscal reporting and support the formulation of fiscal policy.
3. Prepare a privatization plan for the divestment of state assets and enterprises with the aim to raise at least 1 billion euro a year during the period 2011-2013.		Reduces state intervention in the real economy; improves market efficiency; and cuts fiscal contingencies.

1/ Structural benchmarks for 2011 will be determined in the reviews for end-September and end-December 2010.

GREECE: TECHNICAL MEMORANDUM OF UNDERSTANDING

May 3, 2010

1. This Technical Memorandum of Understanding (TMU) sets out the understandings regarding the definitions of the indicators subject to quantitative targets (performance criteria and indicative targets), specified in the Letter of Intent (LOI). It also describes the methods to be used in assessing the program performance and the information requirements to ensure adequate monitoring of the targets. We will consult with the Fund, European Commission and ECB before modifying measures contained in this letter, or adopting new measures that would deviate from the goals of the program, and provide the European Commission, ECB and the Fund with the necessary information for program monitoring.

2. For program purposes, all foreign currency-related assets, liabilities, and flows will be evaluated at "program exchange rates" as defined below, with the exception of the items affecting government fiscal balances, which will be measured at current exchange rates. The program exchange rates are those that prevailed on April 30, 2010. In particular, the exchange rates for the purposes of the program are set €1 = 1.3315 U.S. dollar, €1 = 125.81 Japanese yen, €1.135 = 1 SDR.

General Government

3. **Definition**: For the purposes of the program, the general government includes:

- The entities covered under the State Budget as defined in Chapter 2 of the Law 2362/1995 regarding "Public Accounting, Auditing of Government Expenditures and Other Regulations."
- Local authorities comprising municipalities, prefectures, and regional governments including their basic and special budgets, including all agencies and institutions attached thereto, which are classified as part of local authorities according to ESA 95.
- Social security funds comprising all funds that are established as social security funds in the registry of the National Statistical Service.
- This definition of general government also includes any new funds, or other special budgetary and extra budgetary programs that may be created during the program period to carry out operations of a fiscal nature as defined in the IMF's *Manual on Government Finance Statistics 2001*. The authorities will inform IMF, European Commission and ECB staff of the creation of any such new funds or programs immediately.

4. **Supporting material:** The Ministry of Finance (MoF) will provide to the European Commission, ECB and IMF detailed information on monthly revenues and expenditures, domestic and foreign debt redemptions, new domestic and foreign debt issuance, change in

the domestic and foreign cash balances of the central government at the central bank of Greece, all other sources of financing including capital transactions, and arrears of the general government. Data will be provided within 30 days. The Bank of Greece will provide detailed monthly data on assets and liabilities of local authorities and social security funds in line with monetary survey data.

I. Quantitative Performance Criteria, Indicative Ceilings, and Continuous Performance Criteria: Definitions and Reporting Standards

A. Floor of the Modified General Government Primary Cash Balance (Performance Criterion)

5. **Definition**: The modified general government primary cash balance (MGGPCB) is defined as the modified general government cash balance (MGGCB) minus interest payments by the state budget. The MGGCB is defined as the sum of the cash balances of the ordinary state budget, the cash balance of the investment state budget, the change in net financial assets of local authorities and the change in net financial assets of social security funds. Privatization receipts will be excluded from cash receipts. Net lending operations by the state budget will be recorded as cash expenditures.

- **The cash balance of the ordinary state budget.** The cash balance of the ordinary state budget will be measured from above the line, based on ordinary budget revenues (recurrent revenue plus non-recurrent revenue minus tax refunds) minus ordinary budget expenditures (ordinary budget expenditures will exclude amortization payments and capital transfers to social security funds by bonds but include salaries and pensions; grants to social security funds, medical care and social protection; operational and other expenditure; returned resources; payments in exchange of claims of insurance fund for the personnel working in the Public Electricity Company; interest payments; payments for military equipment procurement; and NATO expenses) of the ordinary state budget as published monthly on the official website of the General Accounting Office of the Ministry of Finance, and in line with the corresponding line items established in the ordinary state budget.

- **The cash balance of the investment state budget.** The cash balance of the investment state budget will be measured from above the line, based on investment budget revenues minus investment budget expenditures of the investment state budget as published monthly on the official website of the General Accounting Office of the Ministry of Finance, and in line with the corresponding line items established in the investment state budget.

- **Net financial assets of local authorities** are defined as financial assets minus financial liabilities of local authorities. Financial assets include deposits of local authorities in the Bank of Greece and deposits of local authorities in the commercial domestic banking sector. Deposits will be measured at face value excluding accrued interest in line with recording for monetary survey data. Financial liabilities include short and long term loans from the domestic banking system to local authorities, measured at face value, consistent with recording for monetary survey data.

- **Net financial assets of social security funds** are defined as financial assets minus financial liabilities of social security funds.

    - Financial assets include

        - Deposits of social security funds in the Bank of Greece and direct deposits of social security funds in the domestic commercial banking system and indirect deposits held by the IKA mutual fund. Deposits are measured at face value excluding accrued interest, consistent with reporting requirements for monetary survey data.

        - Holdings of direct shares or indirect shares (through the IKA mutual fund), held by social security funds quoted on the Athens Stock Exchange. Holdings of shares will be measured at the end-of-month market value.

        - Direct or indirect holdings of Mutual Fund units issued by Greek management companies (other than the IKA mutual fund). Holdings of holdings will be measured at the end-of-month market value.

        - Holdings of central government bonds, including short and long-term securities issued domestically, long-term securities issued abroad operated from Bank of Greece accounts, and indirect holdings through the IKA mutual fund. Holdings will be measured at nominal value.

    - Financial liabilities include the short and long term loans from the domestic banking system to the social security funds, measured consistently with monetary survey data.

6. **Adjustments.** For the purpose of the program, the primary expenditure of the central government that is monitored excludes payments related to bank support, when carried out under the program's banking sector support and restructuring strategy. Costs that may be excluded from the balance include loans to financial institutions and investments in equity of financial institutions (requited recapitalization); unrequited recapitalization; and purchases of troubled assets. However, any financial operation by central government to support banks, including the issuance of guarantees or provision of liquidity, will be immediately reported to IMF, European Commission and ECB staff. Further, this performance criterion will be adjusted upward for any possible revenue overperformance in the central government against the current projection as indicated below:

7. Central government revenue (Cumulative from January 1, 2010)

8. June 2010: €25,056 million

9. September 2010: €41,232 million

10. December 2010: €58,382 million.

11. **Supporting material**.

- Data on cash balances of the ordinary and state budgets will be provided to the European Commission, ECB and IMF by the General Accounting Office in the Ministry of Finance within three weeks after the end of the month. Data will include detailed information on revenue and expenditure items, in line with monthly reports that are published since January 2010 on the official website of the Ministry of Finance.

- Data on net financial assets of local authorities and social security funds will be provided to the IMF, European Commission and ECB by the Statistics Department of the Bank of Greece within four weeks after the end of the month.

B. Ceiling of State Budget Primary Spending (Performance Criterion)

12. **Definition**: The state budget primary spending consists of state budget spending (spending of the ordinary state budget plus spending of the investment budget) minus interest expenditures paid by the state budget, in line with the definitions provided above. Primary expenditure of the central government that is monitored for the PC excludes any cash payments related to bank restructuring, when carried out under the program's banking sector restructuring strategy. Costs that may be excluded from the balance include loans to financial institutions and investments in equity of financial institutions (requited recapitalization); unrequited recapitalization; and purchase of troubled assets. However, any financial operation by central or general government to support banks, including the issuance of guarantees or provision of liquidity, will be immediately reported to European Commission, ECB and IMF staff.

13. **Supporting material**. The General Accounting Office of the Ministry of Finance will provide monthly expenditure data of the ordinary and investment state budget, as defined above.

C. Non-accumulation of Domestic Arrears by the General Government (Continuous Indicative Target)

14. **Definition**. For the purpose of the program, domestic arrears are defined as accounts payable to domestic suppliers past due date by 90 days. Data will be provided within four

weeks after the end of the month. The stock of arrears as of end-April stood at 5.6 billion euro.

15. **Supporting material.** The Ministry of Finance will provide data on monthly expenditure arrears of the general government, as defined above. Data will be provided within four weeks after the end of the month.

D. Ceiling on the Overall Stock of Central Government Debt (Performance Criterion)

16. **Definition**. The overall stock of central government debt will refer to debt that corresponds to the activities of the state budget and will be defined for the purposes of the program as the total outstanding gross debt liabilities of the central government. It will include, but not be limited to, liabilities in the form of securities and loans. The program exchange rate will apply to all non-euro denominated debt. For the purposes of the program, the ceiling on the stock of central government debt will exclude debt arising from payments for bank restructuring, when carried out under the program's banking sector restructuring strategy. This includes loans to financial institutions and investments in equity of financial institutions (requited recapitalization); unrequited recapitalization; and purchase of troubled assets. However, any financial operation by the central government to support banks, including the issuance of guarantees or provision of liquidity, will be immediately reported to IMF, European Commission and ECB staff.

17. **Adjusters**. The ceiling on the overall stock of central government debt will be adjusted upward (downward) by the amount of any upward (downward) revision to the stock of end-December 2009 central government debt.

18. **Supporting material**. Data on the total stock of central government debt will be provided to the European Commission, ECB and IMF staff by the General Accounting Office consistent with the debt published in the public debt bulletin no later than 30 days after the end of each month.

E. Ceiling on New Central Government Guarantees (Performance Criterion)

19. **Definition**. The ceiling on the new central government guarantees shall exclude guarantees to support banks and exclude guarantees related to EIB financed loans.

20. **Supporting material**. All new central government guarantees will be reported in detail, identifying amounts and beneficiaries. The General Accounting Office will provide the data on a monthly basis within three weeks after the end of each month.

F. Non-accumulation of External Debt Payments Arrears by the General Government (Continuous Performance Criteria)

21. **Definition**. For the purposes of the program, an external debt payment arrear will be defined as a payment on debt contracted or guaranteed by the general government, which has not been made within seven days after falling due. The performance criterion will apply on a continuous basis throughout the program period.

22. **Supporting material**. The stock of external arrears of the general government system will be provided by the General Accounting Office with a lag of not more than seven days after the test date.

G. Overall Monitoring and Reporting Requirements

23. Performance under the program will be monitored from data supplied to the EC, ECB and IMF by the Ministry of Finance, the General Accounting Office, and Bank of Greece. The authorities will transmit promptly to the IMF, EC and ECB staff any data revisions in a timely manner.

H. Monitoring of Structural Benchmarks

24. **Pension reform**. The government has initiated a pension reform which should be adopted by the end of September 2010. In preparing this reform, the authorities will consult with EC/IMF/ECB experts and the National Actuarial Authority will produce a report to assess whether the parameters of the new system significantly strengthen long-term actuarial balance. The draft law for the new and actuarially-balanced system should be available by the end of June, 2010.

25. **Expectations for the Pension Reform**. The reform will:

- Merge pension funds in three funds by 2018.
- Introduce a new system to strengthen the link between contributions and benefits, with uniform rules that will apply pro-rata (as a sum of the accrued rights under the old system and the benefits accrued under the new system) to all current and future workers. Workers retiring in and after 2015 will collect benefits from this system.
- Set the normal retirement to age 65 across all systems, including for those insured before 1993 and women in the public sector, by 2015. After 2020, the normal retirement age will increase in line with life expectancy.

- Restrict early retirement to age 60 by 2011, including for those insured before 1993, workers in heavy and arduous professions, and those with 35 or more years of contributions.

- Index benefits to changes in the consumer price index, starting in 2014 (benefits will be frozen 2010–2013).

- Include a means-tested pension for all citizens older than the normal retirement age so that an important safety net is provided, consistent with fiscal sustainability.

- Lengthens the years over which the pensionable earnings base is calculated from the top 5 out of the last 10 years of earnings to lifetime earnings.

- Review conditions for disability pensions by the end of March of 2011 and introduce stricter conditions for eligibility by December of 2011, including periodic re-examination of those with disability pensions.

Athens, May 3, 2010

Mr. Jean-Claude Juncker
President
Eurogroup

Mr. Olli Rehn
Commissionner
European Commission

Mr Trichet
President
European Central Bank

Dear Messrs. Juncker, Rehn and Trichet,

The attached Memorandum of Economic and Financial Policies (MEFP) outlines the economic and financial policies that the Greek Government and the Bank of Greece, respectively, will implement during the remainder of 2010 and in the period 2011–2013 to strengthen market confidence and Greece's fiscal and financial position. An annexed Memorandum of Understanding (MoU) specifies detailed economic policy measures that will serve as benchmarks for assessing policy performance in the context of the quarterly reviews under the financial assistance programme.

The authorities will work closely with the European Commission and the European Central Bank to pursue reforms to meet our conditionality. We will fully implement the policies included in the Decision and the Recommendation addressed by the European Union on 16 February 2010, frame tight budgets in the coming years with the aim to reduce our deficit significantly below 3 percent of GDP in 2014, achieve a downward trajectory in the public debt-GDP ratio in 2013, safeguard the stability of the financial system, and implement structural reforms to boost the economy's capacity to produce, save, and export.

The authorities are particularly determined to lower the fiscal deficit, including by implementing a significant effort to achieve higher and more equitable tax collections, and by constraining spending in the government wage bill and entitlement outlays, among other items.

In view of these efforts and to signal our commitment to effective macroeconomic policies, we request financial assistance from euro area Member States for a total amount of €80 billion over a 36 months period, in support of our ambitious multi-year policy programme. We sent a parallel request for financial assistance to the IMF for a total amount of €30 billion (SDR 26.4 billion).

The implementation of our program will be monitored through quantitative performance criteria and structural benchmarks as described in the attached MEFP, and through the detailed and specific economic policy criteria in the MoU. There will be quarterly reviews of the arrangement, in coordination with the IMF. The first review is expected to be completed in the course of the third calendar quarter of 2010. The reviews will assess progress in implementing the program and reach understandings on any additional measures that may be needed to achieve its objectives. Each review will include an in-depth assessment of program financing in light of the joint financing of this program by the IMF.

The Greek authorities believe that the policies set forth in the attached memorandum are adequate to achieve the objectives of our economic program, but stand ready to take any further measures that may become appropriate for this purpose. The authorities will stay in very close contact and consult with the European Commission, the ECB and the Fund on the adoption of these measures and in advance of revisions to the policies contained in the MEFP and the MoU. All information requested by the European Commission, the ECB and the Fund to assess implementation of the program will be provided.

We are copying this letter to Mr. Strauss-Kahn, Managing Director of the IMF.

Sincerely,

/s/	/s/
George Papaconstantinou Minister of Finance	George Provopoulos Governor of the Bank of Greece

GREECE

Memorandum of Economic and Financial Policies

May 3, 2010

I. Recent Developments

1. **The economic downturn accelerated coming into 2010.** Greek real GDP declined by 2 percent in 2009 and indicators suggest that activity will weaken further in 2010. Following the Greek elections in October, the realization that the fiscal and public debt outturn for 2008 and 2009 were significantly worse than had been reported by the previous government caused confidence to drop, financing costs to increase, and growth and employment to suffer.

2. **The crisis exposed the weak fiscal position.** The deficit of 5.1 percent of GDP in 2007, at the top of the cycle, shows that Greece entered the downturn with a large underlying public deficit. With weak revenue policies and tax administration, especially leading up to the 2009 elections and aggravated by the recession, revenues declined notably. Spending, meanwhile, increased significantly, especially on wages and entitlements, reflecting weak spending discipline and monitoring and control, which also led to new arrears. The deficit jumped to an estimated 13.6 percent of GDP while the public debt rose to over 115 percent of GDP in 2009. The monitoring and control deficiencies delayed the implementation of corrective fiscal policies.

3. **The financial system has been adversely affected.** With the deteriorating fiscal results came downgrades of government bonds by rating agencies, and investors started backing out of Greek bonds, driving up their yields. Furthermore, it is clear that the deep macroeconomic and structural problems combined with unavoidable strong fiscal adjustment over the medium term are likely to weigh on activity for some time. This combination of factors affects negatively the banking system. Impaired loans are rising while borrowing costs in the interbank and wholesale markets have increased, putting pressure on bank profitability.

4. **Despite the recession, the external deficit is declining only gradually.** Inflation and domestic costs have increased well above those of Greece's euro partners over the last decade and Greece has lost competitiveness. As a result, the external current account deficit at end 2009 was still over 11 percent of GDP, and the net international investment position is over negative 83 percent of GDP. The external interest bill on the foreign debt has increased to over 5 percent of GDP, so it will take a surplus in trade of goods and services to return the current account to a more sustainable position. This will require a strengthening of economic

policies and competitiveness to lay the foundations for a growth model that relies more on investment and exports.

II. Key Objectives and the Outlook

5. **The main objectives of the program are to correct fiscal and external imbalances and restore confidence.** Without regaining confidence in the sustainability of fiscal and economic developments, the cost of funding the economy is bound to stay high if not increase further. The fiscal and the external imbalances need to be corrected. Facing these two tasks at the same time is challenging, requiring a major reorientation in the economy. Growth is unlikely to be buoyant as the initial corrective fiscal measures are implemented, but with financial sector policies to preserve the soundness of the banking sector and strong medium-term fiscal and structural policies, the economy will emerge from this experience in better shape than before with higher growth and employment.

6. **The government foresees an extended adjustment period:**

- **Real GDP growth** is set to contract significantly in 2010–2011, but should gradually recover thereafter. The economic program assumes negative growth of 4 percent in 2010 and 2½ percent in 2011. While fiscal consolidation is bound to weigh on economic activity at first, it is expected that confidence effects from the front-loaded fiscal measures and the strong medium-term economic program in combination with comprehensive structural reforms will create the conditions for a return to growth from 2012 onward.

- **Inflation** needs to be reduced significantly below the euro area average for Greece to regain swiftly price competitiveness. Domestic demand tightening, both through fiscal adjustment and efforts to moderate wages and pensions, together with cost-cutting measures in the economy, will be essential to bring inflation down in a meaningful way. In this regard, addressing oligopolistic structures to reduce high markups in some sectors will also be important.

- **The external deficit** is projected to decline gradually over the medium term as domestic demand and inflation moderate and the economy responds to structural reforms to improve the supply of exports and reduces the dependence on imports. This process will naturally take several years, while the interest costs on the substantial external debt will pressure the current account for some time.

III. Economic Policies

7. **To achieve the program objectives, all available fiscal, financial, and structural policies will be used.** The economy needs a strong and sustained adjustment program to correct fiscal imbalances and place debt on a downward path in the medium term, maintain banking sector stability, and restore competitiveness:

- **Fiscal adjustment will have to be the cornerstone of the program.** The government is committed to put in place durable adjustment measures, on top of those already announced in March this year, of 11 percent of GDP in cumulative terms through 2013, with additional remedial measures in 2014 to reduce the deficit to well below 3 percent of GDP. This large adjustment is needed to put the debt-GDP ratio on a downward trajectory from 2013 onward, which will be sustained after the program by keeping primary balances in a sizeable surplus (at least 5 percent of GDP) up to 2020. To sustain fiscal consolidation over the medium term, the government also is committed to strengthen the fiscal policy framework and fiscal institutions.

- **Incomes and social security policies need to buttress the fiscal adjustment effort and restoration of competitiveness.** Realigning incomes to sustainable levels is necessary to assist fiscal correction, support a reduction in inflation well below the euro area average, and improve price and cost competitiveness on a lasting basis. Social security programs need to be strengthened to confront underlying structural imbalances that result from the ageing of the population, where growth in entitlement costs for Greece is projected to be among the highest in the European Union with current policies. As the largest annual overruns in the budget consistently come from the social security funds, reforms cannot be postponed any longer to safeguard the viability of the system.

- **Financial sector policies need to maintain stability.** While currently capital buffers in the banking system are reassuring, bank supervisors will need to monitor closely liquidity and nonperforming loans at individual banks. The Bank of Greece and the government will further strengthen and clarify the key elements of Greece's supervisory and financial crisis framework to assist the banking system through this period of lower growth.

- **Structural reforms that boost the economy's capacity to produce, save, and export will be critical for the medium-term recovery.** Greece's openness is lagging euro-area peers. The government is determined to implement an ambitious program of reforms to modernize the public sector and render product and labor markets more efficient and flexible, create a more open and accessible environment for domestic and foreign investors, and reduce the state's direct participation in domestic industries.

8. **The government is committed to fairness in the distribution of the adjustment burden.** Our resolve to protect the most vulnerable in society from the effects of the economic downturn was taken into account in the design of the adjustment policies. In consolidating government finances, larger contributions will be raised from those who have traditionally not carried their fair share in the tax burden. With regard to the reduction in public wages and in pensions, the minimum earners have been protected:

- Pension reductions: The elimination of the 13th and 14th pensions is compensated, for those receiving less than €2500 a month, by introducing a new flat bonus of €800 a year. The benefit reduction is weighted toward the higher pension earners.

- Wage bill reductions. The 13th and the 14th wage payments will be eliminated for all employees. To protect the lower income segment, here too, for those receiving less than €3000 a month, a flat bonus payment of €1000 a year per employee will be introduced, which will be financed through cutting salary allowances for higher income segments.

- Further, minimum pensions and family support instruments will not be cut, and the most vulnerable will be compensated for the possible adverse impact of policies. To explain and forge consensus on policies to overcome the crisis, the government will invite representatives of businesses and labor to sign a social pact for the duration of the program. The spirit of the above considerations is to maintain strong social cohesion, fight poverty, and maintain employment.

A. Fiscal Policies

9. **The Greek government recognizes the need to implement a frontloaded multiyear adjustment effort given Greece's very high and still growing debt ratio and large fiscal deficit**. All the necessary measures to strengthen market confidence and convince creditors that Greece will regain control over the debt dynamics will be taken. A difficulty is that policies to restore external price competitiveness, which in a monetary union have to rely on reductions in domestic costs and prices, will initially weigh on economic activity, government revenue and debt dynamics. Therefore, the effort has to take place in a period of contracting economic activity, naturally slowing revenues, and cyclically high expenditure. However, it is imperative to place fiscal policies, and the economy, on a sound path for future growth. It is clear that the public sector has become too large and costly and has to become smaller, more efficient and agile, and oriented to providing better services to citizens.

10. **The fiscal strategy is anchored in placing the debt-GDP ratio on a declining path from 2013 onward and reducing the general government deficit to well below 3 percent of GDP by 2014**. To avoid reform fatigue and boost market confidence, the government's strategy is strongly to frontload the fiscal adjustment. All the fiscal measures for the remainder of 2010-2012 have been identified, and most of them will be adopted in the coming weeks. Fiscal measures for 2013 have also been identified with some residual gap remaining that will need to be addressed in coming reviews.

11. **A very strong start has already been made leading to a significant reduction in the 2010 first quarter deficit. For the remainder of 2010 additional measures will be implemented beyond those stipulated in the EU Council Decision and Recommendation of 16 February 2010 and those announced in March 2010** (Table 1). The three biggest

upfront measures are an immediate cut in the public sector wage bill, and in pension outlays, and further increases in the VAT and selected excises (together with other steps yielding 2½ percent of GDP in further savings already in 2010). This will assure that the deficit, notwithstanding the recession, drops from an estimated 13.6 percent of GDP in 2009 to 8.1 percent of GDP in 2010. These very large upfront efforts show the government's resolve in responding to the recent deterioration in market sentiment and the large fiscal challenges, and will help overcome the adverse developments on revenue and support payments such as higher unemployment outlays. These large measures come on top of those already undertaken, which include the first installment of lowering the government's wage bill and selected social security benefits (while safeguarding the minima), the substantial reductions in operating expenditures in all ministries, and significant permanent revenue measures and special taxes on highly profitable enterprises and large properties, and on luxury goods. Thus, the government's resolve is unwavering and every effort will be made to distribute the burden equitably.

12. **For 2011 and beyond, further revenue and expenditure measures have been identified to secure fiscal targets**. Together with the full-year effect of the advance measures taken in mid-2010, these will cover the adjustment needs for 2011 projected at 4 percent of GDP. Adjustment measures in 2012 will continue at a pace of 2½ percent of GDP and in 2013 they are projected to be 2 percent of GDP. Given the expected weakness in GDP, the headline deficit in percent of GDP is expected to drop to 7½ percent in 2011, with more significant headline declines in subsequent years when economic growth resumes.

- **Expenditures will be cut by the equivalent of around 7 percent of GDP through 2013.** Since adoption of the euro, Greece has increased its noninterest expenditures by 8 percentage points of GDP, including with public wages, consumption, and social transfers imposing an overly large burden on the state. This needs to be reversed. As a result, wage and entitlement program costs need to be curtailed as they represent the bulk of the primary budget expenditures, and thereafter wages and pensions will be subsequently frozen in nominal terms for the duration of the program. The government has also planned other reductions in government spending, including by replacing over time only 20 percent of retiring employees, and by consolidating municipalities and local councils. It is essential that the burden of the adjustment on the expenditure side be distributed over multiple programs, so even investment spending will need to be rationalized and shifted to more intensive and efficient use of EU structural and cohesion funds, as feasible. Independent reviews will be launched, conducted by internationally renowned experts, of the public administration and of existing social programs to help identify actions to rationalize the organization of public administration and improve targeting of social programs so that resources are channeled to the most vulnerable.

- **Revenues will be increased by the equivalent of around 4 percent of GDP through 2013.** Revenue from higher income segments of society will include a boost in (presumptive) taxation on liberal professions, an increase in luxury goods taxation, and (temporary) surcharges on highly profitable entities and high valued properties as well as other measures to combat tax evasion included in the recently adopted tax reform legislation. Other revenue increases will include broadening the VAT base, increasing rates and bringing up excise taxes where Greece is below the euro area average and collection efficiency is low. Green taxes and "health" taxes (such as on consumption of alcohol and tobacco) will also play a part in the revenue raising effort.

13. **Besides these direct fiscal steps for the budget, the government also has initiated a series of important structural fiscal reforms**. These will boost sustainability by helping to strengthen control over revenues and expenditures:

- **Pension reform.** The current pension system is unsustainable and will become insolvent if responsible measures are not taken to place it on a sound footing. The government has initiated a reform which should be adopted before end-June 2010. The National Actuarial Authority will produce a report to verify that the parameters of the new system ensure long-term actuarial balance. The existing pension funds will be merged in three funds. The reform will introduce a new system to strengthen the link between contributions and benefits, with uniform rules that will apply pro-rata to all current and future workers. The normal retirement age will be set to 65 years, increasing in line with life expectancy. Benefits will be indexed to prices. The reform will also restrict early retirement, including for those insured before 1993, and reduce the list of heavy and arduous professions. The new system will also include a means-tested social pension for all citizens above the normal retirement age so that an important safety net is provided, consistent with fiscal sustainability.

- **Health sector reform.** The government will implement double-entry accrual accounting in hospitals, the periodic publication of audited accounts, and improvements in pricing and costing mechanisms. The government also plans to separate health funds from administration of pensions, merge the funds to simplify the overly fragmented system, and bring all health-related activities under one ministry.

- **Tax reform.** The government has obtained passage of a tax bill that includes important components to make the tax system more equitable. The income tax system has become more progressive; exemptions and deductions have been reduced to broaden the tax base; and a number of reforms have been introduced to fight tax evasion, including the tightening of obligations to issue receipts for VAT and to document living expenses, and the introduction of presumptive taxation. The government will further review the tax system to simplify it and increase efficiencies as necessary.

- **Tax administration.** Tax administration improvements are being implemented for which technical assistance has already been received from the IMF. In the short run, the government's strategy will focus on safeguarding revenue from the largest taxpayers, stronger enforcement and auditing of high-wealth individuals and self-employed (where risk of evasion is largest) and prosecuting the worst offenders, strengthening enforcement of VAT filing and payment, and collecting on the large stock of tax arrears. For the medium-term, the government will design a program of structural reforms in key tax compliance and administration areas, including: developing and maintaining a comprehensive compliance risk management framework (notably preparing a compliance strategy for 2012); developing taxpayer service capacity to support compliance improvement efforts; substantially improving enforcement operations, particularly in audit, using risk-based approaches; and building headquarters strategic management and planning capabilities in tax and customs administration.

- **Public financial management and fiscal framework.** Technical assistance from the IMF and the European Commission on public financial management and longer-term budgeting reforms will be re-prioritized to address the short-term challenges we are facing. In this context, the General Accounting Office (GAO) will be responsible for monitoring and reporting of general government data; the government will introduce standardized commitment control procedures for all public entities to prevent the re-emergence of arrears; ensure that all budgets are prepared within a medium-term fiscal strategy for the general government and presented before the start of the fiscal year; introduce top-down budgeting with expenditure ceilings, a sufficient contingency reserve, and a medium-term expenditure framework for the State budget; require a supplementary budget for any overruns above this contingency provision; and amend the 1995 budget management law to give effect to the above. The government will continue to work with the technical assistance teams of the IMF and the European Commission to implement the recommendations already received, and to make further improvements over the course of the program, including the creation of an independent fiscal agency attached to parliament.

- **Debt management framework.** The government will update its debt management strategy and the tools to ensure that risk is adequately managed. To enhance market confidence and communication, the government plans to review the operational and risk management framework for debt management to ensure the transparency and predictability of our actions. The government has already sought technical assistance in this area from the IMF.

- **Fiscal and other public sector reporting of information, including statistical aspects.** Upon taking office in October 2009, the new government immediately disclosed that the fiscal deficit for 2008 was under-reported and needed to be revised. Working closely with Eurostat on fiscal data processing and reporting, the government has already taken remedial measures to prevent the reoccurrence of such problems and has designed jointly with the European Commission an action plan to address outstanding statistical issues. Among these, full independence has been granted to the Greek Statistical Office and sufficient resources will be devoted in the coming years to improve statistical systems and seek appropriate resident technical assistance to ensure rapid progress. To that end, the measures in the joint Greek government and European Commission Statistical Action Plan will be fully implemented. Going forward, we feel confident that we are in a position to provide accurate fiscal data to the Fund and our European partners Further, since January 2010, timely monthly central government budget reports on a cash basis have been published. The GAO will also start publishing monthly data on expenditures pending payment, including arrears, from July 2010. Efforts will also be intensified to improve the collection and processing of general government data compiled according to the European System of National and Regional Accounts (ESA) required under the existing EU legal framework, and compile comprehensive data on employment in the general government. Detailed information will be furnished to the European Commission, the ECB and the Fund on the operating accounts and balance sheets of key public enterprises.

14. **The program will be closely monitored and measures will be taken as necessary.** There are risks to the program from lower revenue, higher social transfers, further downward revisions of growth, additional fiscal liabilities from the public and financial sector, and higher interest costs. However, these can be managed and the government stands ready to take appropriate measures to preserve the program objectives, including by reducing discretionary spending, as necessary. At the same time, there is some upside potential. Our 2010–2011 projections include cautious estimates of the measures taken, positive confidence effects could boost GDP growth and reduce market risk premia, and our revenue administration efforts could start to yield more revenue gains than currently assumed in the program. Should confidence rebound and the market support Greece earlier than expected, or the supply response from reforms comes in more vigorously, these benefits will be saved and bring forward the correction to the intended deficit to achieve a speedier return to fiscal sustainability.

B. Financial Sector Policies

15. **Despite a strong solvency position, at present, the Greek banking system is facing challenges**. The system's equity base was substantially strengthened in 2009, jumping from €24 to €33 billion, including through capital injections from the government, for €3.8 billion, capital increases from the owners, and retained earnings. All banks are in compliance with the capital adequacy requirement of 8 percent, and the average capital adequacy ratio rose to 11.7 percent at end 2009. However, the fiscal crisis and a weakening economic environment resulted in a reversal in credit growth and an increase in non-performing loans,

which reached 7.7 percent at end-2009 while profitability declined and might become negative this year.

16. **The immediate challenge for the banks is to manage carefully the current tight liquidity conditions.** In the general context of the turbulence affecting the debt markets for the Greek government, the Greek banks have lost wholesale market access to fund their operations since end-2009. Maturing interbank liabilities have not been renewed, or only at high costs, and some moderate deposit outflows were noted during the first months of 2010, which has put pressure on the liquidity position of many Greek banks. As a result, the banks have increasingly relied on Eurosystem credit operations. To assist the banks in these difficult times the government has extended the banking assistance package of early 2009 (€28billion of which €11 billion had been used by end-2009), to provide a substantial €17 billion in additional liquidity and the government is implementing another extension of this support facility subject to approval by decision of the European Commission. Within the existing Euro system framework, national central banks may give support to temporarily illiquid, but solvent institutions. In the event that such support is given by the Bank of Greece, it will be fully guaranteed by the Greek state in a manner that is consistent with relevant ECB and EU requirements.

17. **The government and the Bank of Greece are also putting in place a new safety net to preserve the sound level of bank equity, and thus improve conditions to support the real economy.** Anticipating that banks profits may decline further, possibly impacting their equity position, the government will establish (by June 30, 2010, as a structural benchmark), through specific legislation and in consultation with the IMF, the European Commission, and the ECB, a fully independent Financial Stability Fund (FSF). The FSF's key decision makers will be persons of recognized standing in financial matters, appointed by the government and the Governor of the Bank of Greece (who will make most of the appointments).

18. **The primary purpose of the FSF is to preserve the financial sector's soundness and thus its capacity to support the Greek economy, by providing equity support to banks as needed.** Whenever supervisory assessments conclude that a bank's capital buffer might fall below adequate levels, the shareholders will be invited to immediately bring additional capital or take bridging capital support from the FSF. If banks are then not able to expeditiously raise additional capital on their own and repay the FSF, a restructuring process will take place under the lead of the FSF, in line with EU competition and state aid requirements.

19. **Other elements of the safety net for the financial sector will also be strengthened.** Corporate debt restructuring legislation, and the current proposal for a personal debt restructuring law, will be in line with international best practices, to ensure that credit discipline is maintained, that creditor and consumer rights are protected, and that relevant information concerning borrowers' track record is preserved.

20. **The Bank of Greece will implement intensified supervision and increase the resources dedicated to banking supervision.** This will include an increase in the frequency and speed of data reporting, and the further development of a comprehensive framework for regularly stress-testing financial institutions. Staffing will be increased both for on-site inspections and off-site review, also taking into account the new responsibilities of the Bank of Greece with respect to insurance supervision. Additional flexibility will be introduced in the management of human resources, and all Bank of Greece staff will be granted strong legal protection for actions performed in good faith.

21. **Close coordination will be maintained with home and host country supervisors within the EU framework for cross-border bank supervision.** In this context, fully aware of the significant presence of Greek banks in South Eastern European (SEE) countries; a number of MoUs with the host supervisory authorities (both EU and non-EU) have been signed. Communication with regulators in SEE regarding risk assessments and liquidity contingency plans are also intensifying.

C. Structural Policies

22. **Structural policies are strengthened in order to boost competitiveness and emerge from the crisis quickly**. These will enhance the flexibility and productive capacity of the economy, ensure that wage and price developments restore and then sustain international competitiveness, and progressively alter the economy's structure towards a more investment and export-led growth model. The Greek government will work closely with the European Commission and the ECB to pursue reforms as specified in the MoU attached to this MEFP. In particular:

- **Modernizing public administration.** Fragmented employment practices will be reformed by reorganizing recruitment procedures and finalizing the single payment authority for wages. A simplified remuneration system will be introduced, in a cost-saving manner that will cover basic wages and all allowances which apply to all public sector employees. Procurement practices will be strengthened to generate efficiency gains and ensure transparency. The health care system, where there have been major expenditure overruns, will be overhauled through reforms in management, accounting and financing systems. A reorganization of sub-central government will be implemented to reduce the number of local administrations and elected/appointed officials. The government will collaborate with the EC to launch an independent external functional review of public administration at the central government level. These reforms will help prioritize government activities and, strengthen the fight against waste and corruption throughout the public administration.

- **Strengthening labor markets and income policies.** In line with the lowering of public sector wages, private sector wages need to become more flexible to allow cost moderation for an extended period of time. Following consultation with social partners and within the frame of EU law, the government will reform the legal framework for wage bargaining in the private sector, including by eliminating asymmetry in arbitration. The government will adopt legislation for minimum entry level wages in order to promote employment creation for groups at risk such as the young and long-term unemployed. In parallel, the government will implement the new control system for undeclared work and modernize labor market institutions. Employment protection legislation will be revised, including provisions to extend probationary periods, recalibrate rules governing collective dismissals, and facilitate greater use of part-time work. The scope for improvements in the targeting of social expenditures will be revised in order to enhance the social safety net for the most vulnerable.

- **Improving the business environment and bolstering competitive markets.** The government will shortly adopt legislation establishing one-stop shops for starting new enterprises to cut procedures, costs and delays. Legislation will be introduced to cut licensing and other costs for industry. The government will fully implement key steps of the EU Services Directive in 2010, especially in priority areas such as tourism, education and retail. Over the course of next year, restricted professions will be opened by reducing fixed tariffs and other restrictions in the legal, pharmacy, notary, engineering, architect, road haulage, and auditing professions. The role of the Hellenic Competition Commission (HCC) will also be strengthened. Network industries will be progressively liberalized, especially in the transport and energy sector while strengthening regulators in these sectors in line with EU policies.

- **Managing and divesting state enterprises**. These need to be subject to greater transparency to increase efficiency and reduce losses. As a first step, 2009 financial statements audited by chartered accountants of the ten largest loss makers will be published on the internet. A time table and action plan for improving the financial performance of main loss-makers, most notably in the railway and public transportation companies will be produced. This action plan will include concrete steps to reduce costs, including by streamlining the networks serviced and increasing tariffs. The government will review the role for divesting state assets, including of land owned by public enterprises or the government. The government will further review the scope for improving corporate governance, and enhancing oversight of state-ownership.

- **Improving the absorption of EU structural and cohesion funds.** The government will work closely with the EC to raise the absorption rate of Structural and Cohesion Funds, including by establishing targets for payment claims based on Management Information System (MIS) data every six months to be measured by certified data and a system of "fast track project production" which includes deadlines for each step of the approval and implementation of projects. A minimum of ten major projects per annum will be submitted. Within the overall public investment envelope agreed in this program, a central account will be established to be used for budgetary appropriations for the national cofinancing of Structural and Cohesion Funds. A specific Task Force will be established with the Commission to ensure the faster delivery of high-quality projects.

IV. Program Financing

23. **We anticipate covering the program's financing requirements with financial support from euro-area member states and the IMF while strengthening access to the private capital markets**. Notwithstanding the significant fiscal adjustment, we project a public financing gap of around €110 billion, for the program period, which we expect to cover through matching bilateral lending support from euro area member states (€80 billion) and through IMF support (€30 billion). Greece will draw on these resources in parallel throughout the program period, drawing on the bilateral and IMF financing in a ratio of 8 to 3 in each disbursement (measured at the program exchange rate). We are confident that resolute implementation of our economic program will help our economy recover and bolster market sentiment. If fiscal consolidation proceeds faster than expected or if market conditions improve significantly during the program period, we would refrain from drawing on the full bilateral and IMF support.

V. Program Monitoring

24. Progress in the implementation of the policies under this program will be monitored through quarterly (and continuous) quantitative performance criteria (PCs) and indicative targets, structural benchmarks, program reviews and consultation clauses. These are detailed in Tables 2 and 3. The attached TMU contains definitions. Quantitative targets up to December 2010 are PCs. Targets for 2011–2013 are indicative and for 2011 will be converted into PCs at the time of the second review before end-2010. A joint EC/ECB MoU specifies, notably, the structural policies recommended in the MEFP, and sets a precise time frame for their implementation.

25. In the context of the arrangement, the Bank of Greece will undergo a safeguards assessment in accordance with the IMF safeguards policy. In this regard, and to facilitate a timely completion of the assessment, the authorities have provided the information requested for the assessment to commence, and have also authorized the external auditors to provide information to and hold discussions with the staff of the IMF. As a related matter, and given that purchases from the IMF will be used to provide direct budget support, a memorandum of understanding between the government and the Bank of Greece will establish a clear framework on the modalities for the repayment of IMF financing and the servicing of interest payments and other charges. As part of these arrangements, Fund disbursements will be deposited into the government's single treasury account at the Bank of Greece pending their use.

Table 1. Greece: Fiscal measures included in the programme

	2010	
in million EUR		% of GDP
Revenue		**0.5**
Increase in VAT rates	800	0.3
Increase in excise tax on fuel	200	0.1
Increase in excise tax on cigarettes	200	0.1
Increase in excise tax on alcohol	50	0.0
Expenditure		**1.9**
Wage bill cut by reducing the Easter, summer and Christmas bonuses and allowances	1100	0.5
Intermediate consumption	700	0.3
Pension cuts (highest pensions)	350	0.1
Elimination of solidarity allowance (second instalment)	400	0.2
Pensions cut by reducing the Easter, summer and Christmas bonuses	1500	0.6
Public investment reduction	500	0.2
TOTAL ANNUAL IMPACT	**5800**	**2.5**

2011

in million EUR		% of GDP
Carry over from last year		**1.1**
Increase the VAT rates	1000	0.4
Increase in excise tax on fuel	250	0.1
Increase in excise tax on cigarettes	300	0.1
Increase in excise tax on alcohol	50	0.0
Wage bill cut by reducing the Easter, summer and Christmas bonuses and allowances	400	0.2
Pensions cut by reducing the Easter, summer and Christmas bonuses	500	0.2
Revenue		**2.2**
Taxation on unauthorised establishments	800	0.4
Luxury goods tax	100	0.0
Book specification of income	50	0.0
Gaming royalties	200	0.1
Gaming licenses	500	0.2
Special levy on profitable firms	600	0.3
Levies on illegal buildings	500	0.2
VAT - changes in the sub-categories and broadening base	1000	0.4
Green tax	300	0.1
Presumptive taxation	400	0.2
Increase of legal values of real estate	400	0.2
Taxation of wage in kind (cars)	150	0.1
Expenditure		**1.0**
Intermediate consumption	300	0.1
Savings from the introduction of unified public sector wages	100	0.0
Pension freeze	100	0.0
Kalikrates savings	500	0.2
Pension cuts (highest pensions)	150	0.1
Public investment reduction	500	0.2
TOTAL ANNUAL IMPACT	**9150**	**4.1**

2012		
in million EUR		% of GDP
Revenue		**0.7**
Excise non-alcoholic beverages	300	0.1
Gaming licenses	225	0.1
Gaming royalties	400	0.2
VAT - broadening base	300	0.1
Presumptive taxation	100	0.0
Increase of legal values of real estate	200	0.1
Expenditure		**1.2**
Reduction in public employment in addition to the 5-to-1 replacement rule	600	0.3
Means test unemployment benefit	500	0.2
Pension freeze	250	0.1
Kalikrates savings	500	0.2
Cut transfers to public entities	800	0.4
Public investment reduction	500	0.2
Unidentified cuts in operational expenditure	900	0.4
TOTAL ANNUAL IMPACT	**5575**	**2.4**

2013

in million EUR		**% of GDP**
Revenue		-0.3
Presumptive taxation	100	0.0
Gaming licenses	-725	-0.3
Expenditure		0.5
Reduction in public employment in addition to the 5-to-1 replacement rule	500	0.2
Pension freeze	200	0.1
Kalikrates savings	500	0.2
Unidentified measures	**4200**	**1.8**
TOTAL ANNUAL IMPACT	**4775**	**2.0**

2014

in million EUR		% of GDP
Temporary measures		**-0.4**
Special levy on profitable firms (discontinuation of temporary measures)	-600	-0.2
Levies on illegal buildings (discontinuation of temporary measures)	-450	-0.2
Unidentified measures	**5750**	**2.4**
TOTAL ANNUAL IMPACT	**4700**	**1.9**
TOTAL MEASURES 2010–2014	**30000**	**13.0**

Table 2. Greece: Quantitative Performance Criteria (in billions of euros, unless otherwise indicated)

	Performance Criteria			Indicative Targets		
	juin-10 Progr. 1/	sept-10 Progr. 1/	déc-10 Progr. 1/	déc-11 Progr. 2/	déc-12 Progr. 3/	déc-13 Progr. 4/
1. Floor on the modified general government primary cash balance	-5.0	-4.0	-5.7	-2.1	2.4	7.4
2. Ceiling on State Budget primary spending	34	50	67	67	68	69
3. Ceiling on the accumulation of new domestic arrears by the general government 5/	..	..	..	0	0	0
4. Ceiling on the overall stock of central government debt	342	342	342	365	..	..
5. Ceiling on the new guarantees granted by the central government	2.0	2.0	2.0	1.0	0.0	0.0
6. Ceiling on the accumulation of new external payments arrears on external debt contracted or guaranteed by general government from multilateral or bilateral official creditors 5/	0	0	0	0	0	0

1/ Cumulatively from January 1, 2010 (unless otherwise indicated).
2/ Cumulatively from January 1, 2011 (unless otherwise indicated).
3/ Cumulatively from January 1, 2012 (unless otherwise indicated).
4/Cumulatively from January 1, 2013 (unless otherwise indicated).
5/ Applies on a continuous basis from April 30, 2010 onward.

Table 3. Greece: Structural Conditionality for 2010 1/

Measures	Date	Macrocritical relevance
	Prior actions	
1. Reduce public wage bill by cutting bonuses/allowances; and pension bonuses (except minimum pensions).		Improves fiscal sustainability; has signaling effect for private sector wage setting.
2. Increase standard VAT rate from 21 to 23 percent and reduced rate from 10 to 11 percent and excise tax rates on alcohol, tobacco, and fuel with a yield of at least €1.25 billion in the remainder of 2010.		Improves fiscal sustainability.
3. Appoint staff team and leader in GAO responsible for general government in-year cash reporting.		Establishes in-year oversight responsibilities of general government fiscal policy.
Structural benchmarks	**End-June 2010**	
1. Establish the independent Financial Stability Fund (FSF) to preserve the financial sector's soundness and thus its capacity to support the Greek economy by providing equity support to banks as needed.		Enhances financial stability.
2. Adopt and start to implement a reorganization of sub-central government with the aim to reduce the number of local administrations and elected/appointed officials (Kalikrates).		Improves fiscal sustainability.
3. Submit to parliament amendments to Law 2362/1995 to (i) require the MoF to present a three-year fiscal and budget strategy, (ii) introduce top-down budgeting with expenditure ceilings for the State budget and multi-year expenditure estimates by line ministry, (iii) introduce standard contingency margins, (iv) require a supplementary budget for any overspending above the contingency, (v) and introduce commitment controls. The amended law should be immediately effective, including in the context of the 2011 budget.		Improves credibility of the budget and fiscal consolidation program.
4. The National Actuarial Authority to produce a report to assess whether the parameters of the new system significantly strengthen long-term actuarial balance.		Reduces budgetary costs of ageing and improves long-term fiscal sustainability. Increases labor force participation.
	End-September 2010	
1. Adopt a comprehensive pension reform that reduces the projected increase in public spending on pensions over the period 2010-60 to 2½ percent of GDP.		Improves fiscal sustainability.
2. Establish a commitment register in all line ministries and public law entities. Begin publishing monthly data on general government in-year fiscal developments (including arrears).		Reduces budget overruns.
3. Publish 2009 financial statements of the ten largest loss-making public enterprises, audited by chartered accountants, on the official website of the Ministry of Finance.		Increases transparency of fiscal risks to fiscal sustainability.
4. Put in place an effective project management arrangement (including tight MOF oversight and five specialist taskforces) to implement the anti-evasion plan to restore tax discipline through: strengthened collection enforcement and recovery of tax arrears—coordinated with the social security funds—of the largest debtors; a reorganized large taxpayer unit focused on the compliance of the largest revenue contributors; a strong audit program to defeat pervasive evasion by high-wealth individuals and high income self-employed, including prosecution of the worst offenders; and a strengthened filing and payment control program.		Achieves revenue targets and enhances sustainability of the consolidation by increasing burden sharing of the adjustment.
	End-December 2010	
1. Publish a detailed report by the ministry of finance in cooperation with the single payment authority on the structure and levels of compensation and the volume and dynamics of employment in the general government.		Reduces wage escalation. Improves transparency of public sector employment.
2. Adopt new Regulation of Statistical Obligations for the agencies participating in the Greek Statistical System.		Enhance confidence in fiscal reporting and support the formulation of fiscal policy.
3. Prepare a privatization plan for the divestment of state assets and enterprises with the aim to raise at least 1 billion euro a year during the period 2011-2013.		Reduces state intervention in the real economy; improves market efficiency; and cuts fiscal contingencies.

1/ Structural benchmarks for 2011 will be determined in the reviews for end-September and end-December 2010.

Table 4. Greece: Fiscal financing gap and disbursement schedule, 2010–2013, billion euro 1/

		SUM	2010				2011				2012				2013	
		10Q2-13Q2	Jan-Apr	May-Jun	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
A.	GG deficit	48.5	6.1	3.1	4.6	4.6	4.1	4.1	4.1	4.1	3.6	3.6	3.6	3.6	2.7	2.7
B.	GG deficit + PE borrowing need	53.0	6.8	3.4	4.9	4.9	4.5	4.5	4.5	4.5	4.0	4.0	4.0	4.0	3.0	3.0
C.	Debt amortization (existing bonds)	138.3	20.1	9.5	5.4	4.4	13.8	13.1	10.8	5.4	19.1	13.2	12.6	5.5	9.8	15.6
D.	of which short-term debt	50.0	...	0.0	4.6	4.3	4.0	4.0	4.0	4.0	4.0	4.0	4.5	4.5	4.0	4.0
E.	of which long-term debt	88.3	...	9.5	0.8	0.1	9.8	9.1	6.8	1.4	15.1	9.2	8.1	1.0	5.8	11.6
F.	Stock flow adjustment	1.5	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
G.	**Public sector financing need (B+C+F)**	**192.8**	**27.0**	**13.0**	**10.4**	**9.4**	**18.4**	**17.7**	**15.5**	**10.0**	**23.2**	**17.3**	**16.7**	**9.6**	**12.9**	**18.7**
H.	Rollover of short-term debt		...	0%	87%	93%	100%	100%	113%	113%	100%	100%	111%	111%	100%	100%
I.	Rollover of long-term debt		...	0%	0%	0%	0%	0%	0%	0%	75%	75%	75%	75%	100%	100%
J.	**New GG borrowing**	**77.9**	**28.9**	**0.0**	**4.0**	**4.0**	**4.0**	**4.0**	**4.5**	**4.5**	**15.3**	**10.9**	**11.1**	**5.8**	**9.8**	**15.6**
K.	of which short-term borrowing (D*H)	47.0	...	0.0	4.0	4.0	4.0	4.0	4.5	4.5	4.0	4.0	5.0	5.0	4.0	4.0
L.	of which long-term borrowing (E*I)	30.9	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0	11.3	6.9	6.1	0.8	5.8	11.6
M.	Privatisation receipts	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
N.	PE borrowing	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
O.	Bank support scheme	10.0	0.0	5.0	5.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
P.	**Financing gap (E-G-H-I+J+O)**	**109.2**	**-1.9**	**18.0**	**11.4**	**5.4**	**14.4**	**13.7**	**11.0**	**5.5**	**7.9**	**6.4**	**5.6**	**3.8**	**3.1**	**3.1**
Q.	**Loan disbursements**	**110.0**	**0.0**	**20.0**	**9.0**	**9.0**	**15.0**	**12.0**	**8.0**	**5.0**	**10.0**	**6.0**	**6.0**	**2.0**	**6.0**	**2.0**
R.	of which IMF	30.0	0.0	5.5	2.5	2.5	4.1	3.3	2.2	1.4	2.7	1.6	1.6	0.5	1.6	0.5
S.	of which EU	80.0	0.0	14.5	6.5	6.5	10.9	8.7	5.8	3.6	7.3	4.4	4.4	1.5	4.4	1.5

1/ Data in this table are subject to revision.

GREECE: MEMORANDUM OF UNDERSTANDING ON

SPECIFIC ECONOMIC POLICY CONDITIONALITY

May 3, 2010

The quarterly disbursements of bilateral financial assistance from euro area Member States will be subject to quarterly reviews of conditionality for the duration of the arrangement. The release of the tranches will be based on observance of quantitative performance criteria, and a positive evaluation of progress made with respect to policy criteria in the MEFP and in this Memorandum, which specifies the detailed criteria that will be assessed for the successive reviews, up to the end of 2011. The detailed criteria for the years 2012 and 2013 will be specified at the occasion of the spring 2011 review.

The authorities commit to consult with the European Commission, the ECB and the IMF on adoption of policies that are not consistent with this memorandum. They will also provide them with all requested information for monitoring progress during program implementation and the economic and financial situation (Annex 1). Prior to the release of the instalments, the authorities shall provide a compliance report on the fulfilment of the conditionality.

1. Actions for the first review (to be completed by end Q2-2010)

i. Fiscal consolidation

Progress with the implementation of the 2010 budget and fiscal measures adopted thereafter. Progress is assessed against the (cumulative) quarterly deficit ceilings in the MEFP (including the TMU). The authorities take the following measures, generating savings for a total amount of 2.5% of GDP in 2010:

- Increase in VAT rates, with a yield of at least EUR 1800 million for a full year (EUR 800 million in 2010);
- Increase in excises for fuel, tobacco and alcohol, with a yield of at least EUR 1050 million for a full year (EUR 450 million in 2010);
- Reduction in the public wage bill by reducing the Easter, summer and Christmas bonuses and allowances paid to civil servants, with net savings amounting to EUR 1500 million for a full year (EUR 1100 million in 2010);
- Elimination of the Easter, summer and Christmas bonuses paid to pensioners, while protecting those receiving lower pensions, with net savings amounting to EUR 1900 for a full year (EUR 1500 million in 2010);
- Cancel budgetary appropriations in the contingency reserve with the aim of saving EUR 700 million;
- Reduce the highest pensions with the aim of saving EUR 500 million for a full year (EUR 350 million in 2010);
- Abolish most of the budgetary appropriation for the solidarity allowance (except a part for poverty relief) with the aim of saving EUR 400 million;
- Reduce public investment by EUR 500 million compared to plans;

- Parliament adopts, as planned in the stability programme of January 2010, a Law introducing a progressive tax scale for all sources of income and a horizontally unified treatment of income generated from labour and assets;
- Parliament adopts, as planned in the stability programme of January 2010, a Law abrogating exemptions and autonomous taxation provisions in the tax system, including income from special allowances paid to civil servants. The law applies retroactively from January 1, 2010.

ii. Structural Fiscal Reforms

Government adopts by end June 2010 a law that requires the monthly publication by the General Accounting Office (GAO) of timely monthly statistics (on a cash basis) on revenue, expenditure and financing for the State, as well as on spending pending of payment, including arrears.

iii. Financial sector regulation and supervision

The Bank of Greece, on behalf of the Government, establishes an independent Financial Stability Fund, with a strong governance structure, to deal with potential solvency issues and to preserve the financial sector's soundness and its capacity to support the Greek economy, by providing equity support to banks as needed (Annex 2).

Start implementation of intensified supervision of banks, including by allocating more human resources, also with a view to the take-over of insurance supervision, frequent reporting under tighter deadlines and quarterly solvency stress tests.

Review the private sector bankruptcy law to ensure consistency with ECB observations.

iv. Structural reforms

Authorities undertake reforms to modernise public administration:

Parliament adopts legislation reforming public administration at the local level, notably by merging municipalities, prefectures and regions with the aim of reducing operating costs and wage bill.

Parliament adopts legislation requiring online publication of all decisions involving commitments of funds in the general government sector.

To strengthen labour market institutions:

Government starts discussions with social partners in order to revise private sector wage bargaining and contractual arrangements.

To enhance competition in open markets:

Government adopts law to simplify the start-up of new businesses.

Government adopts the horizontal legislation on the Services Directive.

Government adopts a recovery plan for the railway sector with a timetable for measures which:

- specify how operational activities will be made profitable, including by closing loss-making lines;
- ensure the effective implementation of EU Directives allowing for competition amongst providers of railway services;
- provide for the restructuring of holding company, including the sale of land and other assets.

To raise the absorption rates of Structural and Cohesion Funds:

Government will put in place measures, including the implementation of Law 3840/2010, the establishment of a "fast-track project production", to achieve the six-monthly targets for payment claims targets in the absorption of Structural and Cohesion Funds set down in the table below. Compliance with the targets shall be measured by certified data. The government will take steps to achieve an annual target of submitting 10 major projects applications to Commission services.

Programming period 2007-2013	**Payment claims to be submitted between 2010 and 2013**			
(in million of euro)	**2010**	**2011**	**2012**	**2013**
European Regional Fund and Cohesion Fund	2330	2600	2850	3000
European Social Fund	420	750	880	890
Target of first half of the year		*1105*	*1231*	*1284*
Target of second half of the year		*2245*	*2499*	*2606*
Total annual target	*2750*	*3350*	*3730*	*3890*

Government establishes a technical task force in direct contact with Commission services, to ensure rapid implementation of a) major projects in transport sectors, b) environmental projects; c) financial engineering instruments and d) public administration reform, relying on increased technical assistance.

Government shall have completed steps to ensure that budgetary appropriations for the national co-financing of Structural and Cohesion Funds are channelled to a special central account that cannot be used for any other purposes and which should be available to provide co-financing to all entities in the general government.

2. Actions for the second review (to be completed by end Q3-2010)

i. Fiscal consolidation

Rigorously implement the budget for 2010 and the fiscal consolidation measures announced afterwards, including those in this Memorandum. Progress is assessed against the (cumulative) quarterly deficit ceilings in the MEFP (including the TMU).

Government submits the draft budget for 2011 to Parliament. The budget provides information and reliable projections on the entire general government sector and targets a further reduction of the general government deficit in line with the MEFP. It includes a detailed presentation of fiscal consolidation measures amounting to at least 3.2% of GDP (4.3% of GDP, if carryovers from measures implemented in 2010 are considered), and detailed information on the situation of public enterprises.

The budget includes the following measures (in exceptional circumstances, measures yielding comparable savings could be considered in close consultation with European Commission, IMF and ECB staff):

- Implement the rule of replacing only 20 percent of retiring employees in the public sector (central government, municipalities, public companies, local governments, state agencies and other public institutions);
- Reduction in intermediate consumption of the general government by at least EUR 300 million compared to the 2010 level, on top of savings envisaged in the context of reforming public administration and the reorganisation of local government (see next measure);
- Government starts implementing legislation reforming public administration and the reorganisation of local government with the aim of reducing costs by at least EUR 1500 million from 2011 to 2013, of which at least EUR 500 million in 2011.
- Freeze in the indexation of pensions, with aim of saving EUR 100 million;[7]
- Reduction in domestically-financed investments by at least EUR 1000 million, by giving priority to investment projects financed by EU structural and cohesion funds;
- Temporary "crisis levies" on highly profitable firms, yielding at least EUR 600 million in additional revenue per year in 2011, 2012 and 2013;
- Incentives to regularise land-use violations, yielding at least EUR 1500 million from 2011 to 2013, of which at least EUR 500 million in 2011;
- Enforce the presumptive taxation of professionals, with a yield of at least EUR 400 million in 2011 and increasing returns in 2012 and 2013;
- Broaden the VAT base by including services that are currently exempted and move a significant proportion (at least 30%) of the goods and services currently subject to the reduced rate to the normal rate, with a yield of at least EUR 1000 million;
- Start phasing in a "green tax" on CO_2 emissions, with a yield of at least EUR 300 million in 2011;

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[7] Adjustments may be needed in case of negative inflation.

- Collect revenue from the licensing of gaming: at least EUR 500 million in sales of licences and EUR 200 in royalties;
- Expand the base of the real estate tax by updating asset values to yield at least EUR 500 million additional revenue;
- Increase taxation of wages in kind, including by taxing car lease payments (at least EUR 150 million);
- Initiate the collection of a special tax on unauthorised establishments (at least EUR 800 million per year);
- Increase taxes on luxury goods by at least EUR 100 million;
- The budget will establish detailed expenditure ceilings for each line-ministry, local governments, and social security funds consistent with the general government deficit target. This also pertains to the medium-term fiscal framework for 2012-2013;
- The budget will contain indicative information on monthly revenue per category, and expenditure per Ministry. Updated figures will be regularly made available online.

Parliament adopts modifications to the organic budget law, if necessary, to ensure that the draft budget law for 2011 onwards contains detailed information on outturn and plans of the entire general government sector – including local government, social security, hospitals and legal entities. An annex to the budget will present key figures on the financial performance of the largest public enterprises, concomitant budgetary and tax expenditures, and related fiscal risks.

ii. Structural fiscal reforms

Parliament adopts legislation to improve the efficiency of the tax administration and controls, implementing recommendations provided by the European Commission and IMF. In particular, they put in place an effective project management arrangement (including tight MOF oversight and taskforces) to implement the anti-evasion plan to restore tax discipline through: strengthened collection enforcement and recovery of tax arrears (coordinated with the social security funds) of the largest debtors; a reorganized large taxpayer unit focused on the compliance of the largest revenue contributors; a strong audit program to defeat pervasive evasion by high-wealth individuals and high income self-employed, including prosecution of the worst offenders; and a strengthened filing and payment control program.

Parliament adopts a reform of the pension system to ensure its medium- and long-term sustainability. It should limit the increase of public sector spending on pensions, over the period 2010–2060, to under 2.5 percent of GDP. The reform will be designed in close consultation with European Commission, IMF and ECB staff, and its estimated impact on long-term sustainability will be validated by the EU Economic Policy Committee. The parameters of the system will ensure long-term actuarial balance, as determined by the National Actuarial Authority. The reform should include the following elements:

- Simplification of the fragmented pension system by merging the existing pension funds in three funds and introducing a unified new system for all current and future employees. The new universally binding rules on entitlements, contributions, accumulation rules and indexation of pension rights shall be applied pro rata to everybody from 1 January 2013;

- Introduction of a unified statutory retirement age of 65 years, including for women in the public sector (phased in immediately after adoption), to be completed by December 2013;
- Gradual increase in the minimum contributory period for retirement on a full benefit from 37 to 40 years by 2015;
- Amendment of the pension award formula in the contributory-based scheme to strengthen the link between contributions paid and benefits received, with accrual rate limited to an average annual rate of 1.2%, and pensions indexed to prices;
- Introduction of an automatic adjustment mechanism that, every three years and starting in 2020, will increase the (minimum and statutory) retirement age in line with the increase in life expectancy at retirement;
- Extend the calculation of the pensionable earnings from the current last five years to the entire lifetime earnings (while retaining acquired rights);
- Reduction of the upper limit on pensions;
- Introduction of a means-tested minimum guaranteed income for elderly people (above the statutory retirement age), to protect the most vulnerable groups, consistent with fiscal sustainability;
- Measures to restrict access to early retirement. In particular, increase the minimum early retirement age to 60 years by 1st January 2011, including for workers in heavy and arduous professions and those with 40 years of contributions. Abolish special rules for those insured before 1993 (while retaining acquired rights). Substantial revision of the list of heavy and arduous professions;
- Reduction of pension benefits (by 6% per year) for people entering retirement between the ages of 60 and 65 with a contributory period of less than 40 years;
- Introduction of stricter conditions and regular re-examination of eligibility for disability pensions.

Government adopts a reform of the GAO, including the following elements:

- Strengthening of the role of the GAO in budget planning and control;
- Provision of the necessary resources in terms of high-level personnel, infrastructure and equipment support, managerial organisation and information-sharing systems;
- Provision of safeguards for GAO staff against political interference, and personal accountability in the provision of reliable data;
- Strengthen the institutional mechanisms for providing reliable and plausible official budgetary forecasts that take into account available recent execution developments and trends; to this end, the official macroeconomic forecasts should be reviewed by external experts;.

Government takes the following measures to ensure timely provision of reliable fiscal accounts and statistics:

- GAO starts, in June 2010, the publication of timely monthly statistics (on a cash basis) on revenue, expenditure and financing and spending arrears for the "available general government" and its sub entities (state, social security, hospitals, local governments and legal entities);
- Government adopts a detailed time-bound action plan, to be agreed with Eurostat, to improve collection and processing of general government data required under

the existing EU legal framework, in particular by enhancing the mechanisms that ensure the prompt and correct supply of these data, and ensure personal responsibility in cases of misreporting; and seek appropriate resident technical assistance to ensure rapid progress;

- Government starts to publish timely information on the financial situation in public enterprises (at least the 10 largest loss-making ones) and other public entities not classified in the general government (including detailed income statements, balance sheets and data on employment and the wage bill). To this end, a regular and timely reporting mechanism is introduced.

iii. Financial sector regulation and supervision

The Bank of Greece and the Government ensure that the Financial Stability Fund is fully operational.

Review the adequacy of the insolvency framework, for banks as well as for non-financial entities.

iv. Structural reforms

Progress with reforms to modernise public administration:

Government launches the process, including the principles and timetable, for establishing a simplified remuneration system covering basic wages and allowances. It shall apply to all public sector employees, and be part of an overall reform of Human Resource management. This should lead to a system where remuneration reflects productivity and tasks.

Government launches independent functional reviews of the public administration at central level and of existing social programmes. It is to be conducted by internationally renowned and external experts. The Terms of Reference for the reviews will be agreed with European Commission, IMF and ECB staff. The objectives of the reviews are:

- To take stock of the use of resources, including human resources, to carry out government functions (e.g., employment, goods and services) in the central government and subordinated public institutions;
- To identify actions to rationalize the organisation of public administration and generate productivity gains, and quantify possible fiscal savings from implementation of these actions;
- To assess effectiveness and appropriateness of existing social programmes and make proposals for reform or cancellation of the least effective ones, while quantifying possible fiscal savings from implementation of these actions.

To strengthen competition in open markets

Authorities make the General Commercial Registry (GEMI) fully operational

Under the Services Directive, the government finalizes the review of existing sectoral legislation (screening), ensures that the point(s) of single contact is(are) operational.

Government adopts a law on road freight transport that removes restrictions not provided for in Directive 96/26/EC of 29 April 1996 on admission to the occupation of road haulage, including minimum fixed prices.

Issue a Ministerial Decree for the liberalisation of wholesale electricity market and a Ministerial Decision on rationalisation of electricity consumer tariffs.

Promoting investments and exports

Government takes measures, in line with EU competition rules, to facilitate FDI and investment in innovation in strategic sectors (green industries, ICT etc...) through a revision of the Investment Law, the adoption of measures to facilitate PPPs, action to fast-track large FDI projects and measures to strengthen export promotion policy.

3. Actions for the third review (to be completed by end Q4-2010)

i. Fiscal consolidation

1. Government achieves the programme target for the 2010 general government deficit.

Parliament adopts draft budget for 2011 targeting a further reduction of the general government deficit and including the consolidation measures specified in this Memorandum.

Government prepares a privatization plan for the divestment of state assets and enterprises with the aim to raise at least 1 billion euros a year during the period 2011–2013.

ii. Structural fiscal reforms

Government adopts draft legislation to strengthen the fiscal framework, following discussions with European Commission and IMF staff. The following elements should be part of the reform:

- Introduce a medium-term fiscal framework covering the general government based on rolling three-year expenditure ceilings for the State, social security entities and local governments;
- Strengthen the position of the Finance Minister vis-à-vis line ministers in both budget preparation and execution phases (giving him/her veto power on spending decisions and execution);
- Introduce a compulsory contingency reserve in the budget, corresponding to 10 percent of total appropriations government departments other than wages, pensions and interest; the use of the contingency reserve will be decided by the Finance Minister;
- Ensure that Parliament does not modify the overall size of the budget at the approval stage, and focus on the composition of public expenditure and revenue, and reliability of projections for expenditure and revenue;
- Introduce stronger expenditure monitoring mechanisms, particularly by implementing an appropriate control of spending commitments, through which spending entities (line ministries, local authorities, social security funds, hospital and legal entities) would report on a regular basis to the Treasury on their

outstanding expenditure commitments against their authorised appropriations in the budget law;

- Introduce a revenue rule for the general government, according to which the allocation of higher-than-expected revenues should be specified *ex-ante* in the budget law;
- Creation of a fiscal agency attached to Parliament providing independent advice and expert scrutiny on fiscal issues, and reporting publicly on the budgetary plans and execution of the spending entities of the general government, and on macroeconomic assumptions used in the budget law.

Parliament adopts reform of the public wage legislation consistent with this Memorandum.

iii. Structural reforms

To reform and modernise public administration:

Government adopts all necessary legislation and decree for the full entry into force of the local administration reform.

Government completes the creation of a Single Payment Authority for the payment of wages in the public sector. The Ministry of finance publishes a detailed report, based on information and in collaboration with the Single Payment Authority, on the structure and levels of compensation and the volume and dynamics of employment in the general government.

Authorities complete the first phase of the public procurement system reform, with a central procurement authority and involving a swift implementation of the electronic platform for public procurement and introducing the use of e-auctioning system. It should ensure a common approach and tendering procedures, *ex ante* and *ex post* controls.

Government adopts legislation and measures needed to implement the Better Regulation agenda.

To modernise the health care systems:

Government adopts legislation on the institutional framework for health supplies (Law 3580/2007), establishes new systems for the management of drugs that favour more use of generic medicines, including a new system for the electronic monitoring of doctors' prescriptions.

Government completes the programme of hospital computerisation, upgrading hospital budgeting systems, and the reform of management, the accounting (including double-entry accrual accounting) and financing systems.

Government ensures greater budgetary and operational oversight of health care spending by the Finance Minister, the publication of audited accounts and improvement in pricing and costing mechanisms.

To strengthen labour market institutions:

Following dialogue with social partners, the government proposes and parliament adopts legislation to reform wage bargaining system in the private sector, which should provide for a reduction in pay rates for overtime work and enhanced flexibility in the management of working time. Allow local territorial pacts to set wage growth below sectoral agreements and introduce variable pay to link wages to productivity performance at the firm level.

Government amends regulation of the arbitration system, (Law 1876/1990), so that both parties can resort to arbitration if they disagree with the proposal of the mediator.

Following dialogue with social partners, government adopts legislation on minimum wages to introduce sub-minima for groups at risk such as the young and long-term unemployed, and put measures in place to guarantee that current minimum wages remain fixed in nominal terms for three years.

Government amends employment protection legislation to extend the probationary period for new jobs to one year, to reduce the overall level of severance payments and ensure that the same severance payment conditions apply to blue- and white-collar workers, to raise the minimum threshold for activation of rules on collective dismissals especially for larger companies, and to facilitate greater use of temporary contracts and part-time work.

To enhance competition in open markets:

Government adopts changes to existing (sectoral) legislation in key services sectors such as tourism, retail and education services. New legislation should facilitate establishment, by significantly reducing requirements covered by Articles 15 and 25 of the Services Directive, in particular requirements relating to quantitative and territorial restrictions, legal form requirements, shareholding requirements, fixed minimum and/or maximum tariffs and restrictions to multidisciplinary activities. It should also facilitate the provision of cross-border services by implementing the freedom to provide services clause in Article 16 of the Service Directive through an approach ensuring legal certainty for services providers, i.e. by clearly setting out in the respective (sectoral) legislation which requirements can and which requirements cannot be applied to cross-border services.

Government proposes legislation to remove restrictions to trade in restricted professions including:

- the legal profession, to remove unnecessary restrictions on fixed minimum tariffs, the effective ban on advertising, territorial restrictions on where lawyers can practice in Greece;
- the pharmacy profession, covering limits on the number of pharmacies and minimum profit margins;
- the notary profession, covering fixed tariffs, limits on the number of notaries, territorial restrictions on where notaries can practice and the effective ban on advertising;
- architects, covering fixed minimum tariffs;
- engineers, covering fixed minimum tariffs;
- auditing services, covering fixed tariffs.

Government adopts legislation and takes all necessary measures to complete the full and effective transposition of EU rules on recognition of professional qualifications, including the transposition of the Professional Qualifications Directive (Directive 2005/36/EC) including compliance with ECJ rulings.

Government adopts legislation to simplify and accelerate the process of licensing enterprises, industrial activities and professions, which inter alia revises Law 3325/05, makes Law 3335/05 for business areas, and operationalises the spatial plan.

Government adopts a law modifying the existing institutional framework of the Hellenic Competition Commission (HCC) which abolishes the notification system for all agreements falling within the scope of Article 1 of Law 703/1977, gives the HCC the power to reject complaints, to increase the independence of HCC members, and to establish reasonable for the investigation and issuance of decisions.

Promoting investments and exports

Government carries out in depth evaluation of all R&D and innovation actions, including in various Operational Programmes, in order to adjust the national strategy.

Government creates an external advisory council financed through the 7th R&D programme, to consider how to foster innovation, how to strengthen links between public research and Greek industries and the development of regional industrial clusters.

To raise the absorption rates of Structural and Cohesion Funds

Government to meet targets for payment claims (to be measured against certified data) and for the submission of large projects.

4. Actions for the fourth review (to be completed by end Q1-2011)

i. Fiscal consolidation

Rigorously implement the budget for 2011 in line with this memorandum, and the fiscal consolidation measures in the budget. Progress is assessed against the (cumulative) quarterly deficit ceilings in the MEFP (including the TMU).

ii. Structural fiscal reforms

Parliament adopts legislation to strengthen the fiscal framework, consistent with this memorandum.

iii. Structural reforms

To reform and modernise public administration:

Government completes effective transposition of Directive 2007/66/EC on public procurement regarding remedies, and at the same time ensures that responsibility for the review of award procedures be vested with the administrative courts. Government completes the transposition of Directives 2009/81 on defence and security expenditure.

Reforms to improve the business environment:

Government fully implements the recovery plan for the railway sector to make operational activities profitable, implement EU Directives and restructure the holding company.

Parliament adopts legislation unbundling electricity and gas activities.

Government adopts measures, in line with EU requirements to strengthen the independence and capacity of the Energy Regulatory Authority and further unbundle the transmission system operators DESMIE (electricity) and DESFA (gas), including by bringing forward transparent criteria and procedure to govern the selection of the chair and members of RAE.

5. Actions for the fifth review (to be completed by end Q2-2011)

i. Fiscal consolidation

Rigorously implement the budget for 2011 in line with this memorandum, and the fiscal consolidation measures in the budget. Progress is assessed against the quarterly deficit ceilings in the MEFP (including the TMU).

ii. Structural reforms

Reforms to modernise public administration:

Government adopts legislation/decrees establishing a simplified remuneration system covering basic wages and allowances that applies to all public sector employees ensuring that remuneration reflects productivity and tasks: this reform should be part of an overall reform of Human Resource management in the public sector.

On the findings of the external and independent functional review of public administration at central level, the government adopts legislation and measures to rationalize the use of resources, the organisation of the public administration and social programmes.

Authorities take the following measures to strengthen labour market institutions:

Government completes the reform to strengthen the Labour Inspectorate, which should be fully resourced with qualified staff and has quantitative targets on the number of controls to be executed.

Government adapts the legislation on tackling undeclared work to require the registration of new employees before they start working.

Review the scope for improvements in the targeting of social expenditures to enhance the social safety net for the most vulnerable.

To strengthen competition in open markets:

Government adopts specific legislation to in restricted professions including for the legal profession, the pharmacy profession, the notary profession, architects, engineers and auditing services.

To raise the absorption rates of Structural and Cohesion Funds:

Government to meet targets for payment claims to be measured against certified data.

6. Actions for the sixth review (to be completed by end Q3-2011)

i. Fiscal consolidation

Rigorously implement the budget for 2011 in line with this memorandum, and the fiscal consolidation measures in the budget. Progress is assessed against the quarterly deficit ceilings in the MEFP (including the TMU).

Government adopts draft budget for 2012 aiming at a further reduction of the general government deficit in line with the programme and including the detailed presentation of consolidation measures amounting to at least 2.2% of GDP, including the following measures (in exceptional circumstances, measures yielding comparable savings could be considered in close consultation with European Commission, IMF and ECB):

- Reduce public employment on top of the rule of 1 recruitment for each 5 retirements in the public sector; the reduction in public employment on top of the 5-to-1 rule should allow savings of at least EUR 600 million;
- Establish excises for non alcoholic beverages, for a total amount of at least EUR 300 million;
- Continue the expansion of the base of the real estate tax by updating asset values to yield at least EUR 200 million additional revenue;
- Continue the reorganisation of local government, to generate at least EUR 500 million in savings;
- Nominal freeze in pensions;
- Continue to increase the effectiveness of the presumptive taxation of professionals, with the aim of collecting at least additional EUR 100 million;
- Reduction of transfers to public enterprises by at least EUR 800 billion following their restructuring;
- Make unemployment benefits means-tested (aiming at savings of EUR 500 million);
- Collect further revenue from the licensing of gaming: at least EUR 225 million in sales of licences and EUR 400 in royalties;
- Further broadening of VAT base, by moving goods and services from the reduced to the normal rate, with the aim of collecting at least additional EUR 300 million.

ii. Structural reforms

Reforms to modernise public administration:

Government ensures full operation of the Better Regulation Agenda to reduce administrative burden by 20% compared with 2008 level, and sends report to the Commission.

Improve the business environment:

Government changes legislation to mitigate tax obstacles to mergers and acquisitions such as the non-transfer of accumulated losses, together with the company and the complex computation of "excessive benefit" (Law 3522/2006, Article 11) in the transfer of private limited companies.

Government takes decisions to simplify the process to clear customs for exports and imports and give larger companies or industrial areas the possibility to be certified to clear cargo for the customs themselves; Government abolishes the requirement of registration with the exporter's registry of the chamber of commerce for obtaining a certificate of origin.

7. Actions for the seventh review (to be completed by end Q4-2011)

i. Fiscal consolidation

2. Government achieves the programme target for the 2011 general government deficit.

Parliament adopts draft budget for 2012 a further reduction of the general government deficit and including consolidation measures amounting to at least 2.2% of GDP, in line with Memorandum.

ii. Structural reforms

To raise the absorption rates of Structural and Cohesion Funds:

Government to meet targets for payment claims (to be measured against certified data) and for the submission of large projects.

Introduced of web-based open-access monitoring tool of procedures for approval of project proposals and for implementation of public projects.

Ensure that the managerial capacity of all Managing Authorities and Intermediate Bodies of operational programmes under the framework of the National Strategy Reference Framework 2007-2013 has been certified by the International Organization for Standardization according to the standard ISO 9001:2008 (Quality Management).

Annex 1. Provision of data

During the programme, the following indicators and reports shall be made available to the European Commission, the ECB and the IMF by the authorities on a regular basis. In general, reporting information provided to other multilateral and bilateral lenders involved in the programme of financial assistance of which the assistance provided by the Community forms part shall at the same time also be provided to the Commission, unless the Commission has indicated that this is not specifically required. The authorities shall provide the Commission and the ECB with compliance reports on the fulfilment of conditionality immediately after test dates.

To be provided by the Ministry of Finance	
Preliminary monthly data on the state budget execution (including functional breakdown by main categories of revenue and expenditure and by line ministry)	Monthly, 15 days after the end of each month; these data should also be included in subsequent transmissions in case of revision
Updated monthly plans for the state budget execution for the remainder of the year, including functional breakdown by main categories of revenue and expenditure and by line ministry	Monthly, 30 days after the end of each month
Preliminary monthly cash data on general government entities other than the State	Monthly, 30 days after the end of each month, these data should also be included in subsequent transmissions in case of revision
Monthly data on the public wage bill (of general government, including a functional breakdown in nominal wage and allowances paid to government employees per line ministry and public entity), number of employees (including a functional breakdown per ministry and public entities outside the central government) and average wage (including the relative shares of the base wage, allowances and bonuses). A functional breakdown of these data into the main public entities will be added.	Monthly, 30 days after the end of each month (starting in June 2010)
Quarterly data on general government accounts, and general government debt as per the relevant EU regulations on statistics	Quarterly accrual data, 90 days after the end of each quarter
Weekly information on the Government's cash position with indication of sources and uses as well of number of days covered as well as information on the main government spending and receipt items	Weekly on Friday, reporting on the previous Thursday
Data on below-the-line financing for the general government	Monthly, no later than 15 days after the end of each month, ; these data should also be included in subsequent transmissions in case of revision
Data on expenditure pending payment (including arrears) of the general government, including the State, local government, social security, and legal entities	Quarterly, within 55 days after the end of each quarter
Data on expenditure pending payment (arrears) of the State and hospitals	Monthly, 30 days after the end of each month
Public debt, and new guarantees issued by the general government to public enterprises and the private sector	Monthly, within one month
Income and expenditure statement and balance sheets of 30 largest public enterprises by total expenditures	Quarterly, three months after the end of the quarter

Data on EU project grants (reimbursements and advances), capital expenditures and subsidies covered by EU advances or eligible for EU reimbursement on EU supported projects specifically agreed with the EU	Monthly, within three weeks of the end of each month
Monthly statement of the transactions through off-budget accounts	Monthly, at the end of each month
Monthly statements of the operations on the special account	Monthly, at the end of each month
Report on progress with fulfilment of policy conditionality	Monthly, at the end of each month
To be provided by the Bank of Greece	
Assets and liabilities of the Bank of Greece	Weekly, next working day
Assets and liabilities of the Greek banking system - aggregate monetary balance sheet of credit institutions	Monthly, 30 days after the end of each month
Evolution of the external funding provided by Greek banks to their subsidiaries abroad[8]	Monthly, 15 days after the end of each month
External funding flows for the banking, corporate and government sector, including also expected developments in the 12 months ahead	Monthly, 30 days after the end of each month
Report on banking sector liquidity situation	Weekly, next working day
Report on the evolution of financial stability indicators	Quarterly, 15 days after the end of each quarter depending on data availability
Report on results from the regular quarterly solvency stress tests	Quarterly, 15 days after the end of each quarter depending on data availability
Detailed report on the balance sheet of the Financial Stability Fund with indication and explanation of changes in the accounts	Weekly, next working day

[8] All forms of debt instruments and capital, as well as net deposits provided to subsidiaries abroad.

Annex 2. Financial Stability Fund

General

- The purpose of the Financial Stability Fund (the 'Fund') is to maintain the stability of the Greek banking system by providing equity capital in case of a significant decline of capital buffers.
- The Fund will not provide liquidity support, which will be provided under existing arrangements.
- The equity will be provided in the form of preference shares to credit institutions authorised to operate in Greece by license from the Bank of Greece. The preference shares will be convertible into ordinary shares at a later stage under certain conditions to be further specified in the legislation establishing the Fund.
- Participation in the Fund will be mandatory, based on a trigger linked to the minimum required level of capital adequacy requirements, as established for specific credit institutions by the Bank of Greece, in its capacity as the competent supervisory authority, if no private solution has been found.
- If banks are then not able to expeditiously raise additional capital on their own and repay the Fund, a restructuring process will take place under the lead of the Fund, in line with EU competition and state aid requirements
- The Fund will be established by specific Greek legislation.
- An initial lifespan of seven years will be set for the Fund. After the end of the lifespan of the Fund, the ownership of the Fund rests with the Greek state to the extent of its shareholding in the Fund

Legal status

- The Fund will be established as a private law legal entity in order to enhance its flexibility and efficiency (e.g., to facilitate the recruitment and remuneration of appropriately qualified staff).
- The legal structure of the Fund should allow for private participation.

Funding

- The FSF will be fully funded by the government out of the resources available under the EU-IMF program for this purpose in the amount of EUR 10 billion. This implies that the risk of losses arising out of the Fund's operations would lie exclusively with the Greek Government, as the primary shareholder in the Fund. The purchase of preference shares by the Fund shall be made in cash.

Organizational issues

- The Fund will be managed by a Governing Council composed of (1) a Chairperson, a Chief Executive and three directors appointed by the Governor of the Bank of Greece and (2) two ex officio directors who represent the Minister of Finance and the Governor of the Bank of Greece. The European Commission and the ECB will each nominate an observer who would have a right to participate, without voting, in meetings of the Governing Council (without prejudice, in the case of the Commission observer, to the application by the Commission of state aid and competition rules).

- The Chairperson, Chief Executive and the non-ex officio directors will be required by law to be persons of recognised standing in banking or financial matters in Greece, the EU or internationally.
- Each of the Chairperson and the non-ex officio directors will be appointed to a five year term of office, renewable for a further two years, and may only be compulsorily removed from office by an appropriate Greek court on application of either the Governor of the Bank of Greece or the Governing Council of the Fund where (1) no longer capable of fulfilling the conditions required for the performance of the duties of office or (2) guilty of serious misconduct.
- No member of the Governing Council may be represented on the board of directors of any credit institution.
- The legislation establishing the Fund will provide that, when exercising the powers and carrying out the tasks and duties conferred upon them under the legislation, neither the Governor of the Bank of Greece nor the members of the Governing Council of the Fund shall seek or take instructions from the Greek Government or any other State entity, institution, body or undertaking.
- The Governing Council will present a semi-annual report to the Greek Parliament, the European Commission, the ECB and the IMF.
- The operating expenses will be covered by the Fund.

Powers of the Fund

- In order to fulfil its purposes the Fund will enjoy certain powers over credit institutions receiving capital from the Fund, to be exercised following consultation of the BoG. These powers will be without prejudice to the supervisory powers of the Bank of Greece, and will include, without limitation, the power:
    - to require the BoG to provide the Fund with all information on financial institutions necessary for it to fulfil its tasks;
    - to appoint a member of the Board of Directors of a credit institution;
    - to require a credit institution to present a restructuring plan;
    - to veto key decisions of a credit institution (e.g., business strategy, dividend distributions, salary caps, liquidity and asset-liability management, etc.);
    - to call a general shareholders' meeting for a credit institution in accordance with Greek company law;
    - to require conversion of preference shares into ordinary shares insofar as a credit institution fails to meet (1) the minimum required level of capital adequacy requirements established for credit institutions generally under applicable regulatory requirements or (2) certain financial conditions to be established in the restructuring plan for the credit institution; the legislation establishing the Fund will further specify an objective procedure to be followed in establishing a market-based conversion price, taking account of the impact of the Fund's intervention, the rights of shareholders under Greek law and EU state aid requirements; and
    - to conduct diagnostic studies and special audits with the help of outside consultants to assess the solvency of a credit institution where the Fund considers this necessary.

- Each of the Bank of Greece, in its capacity as the competent authority for the supervision of credit institutions, and the Fund will be authorised to exchange confidential information with one another to the fullest extent permitted by EU law.

<u>Conditions applicable to capital increases</u>

- The conditions <u>applicable to any capital increases</u> should be aligned with the Commission Decision of 19.11.2008 (N 560/2008 support measures for the credit institutions in Greece). The granting of equity capital is made subject to the following conditions in particular.
- The credit institutions will be expected to pay a market-oriented, non-cumulative remuneration unless an analysis of the restructuring plan warrants an alternative approach. A market-oriented, non-cumulative remuneration can either be 10% as stipulated in the above decision or depending on the risk profile of the credit institution and the quality of the capital, between 7% and 9.3%, whereas core tier 1 capital for fundamentally sound credit institutions should normally be remunerated at not less than 9%.
- The credit institutions will not pay dividends or coupon on hybrid capital, unless they are legally obliged to do so, which is typically the case when a credit institution is profit making (the credit institution should however not be allowed to use reserves to book a profit).
- Preference shares shall be repurchased by the credit institution for an amount that is equivalent to the amount originally invested in the credit institution. After five years the shares shall be repurchased or be remunerated at penal rates. If they cannot be repurchased because the capital adequacy requirements are not fulfilled, the preference shares shall be converted into ordinary shares.

<u>Approval of restructuring plan by European Commission</u>

- Any restructuring plan needs to be in accordance with State aid rules and approved by decision of the European Commission ensuring that the credit institutions will restore viability at the end of the restructuring period, burden sharing of shareholders is achieved and distortion of competition is limited.

<u>Follow-up</u>

- The Greek authorities would prepare the necessary legislation implementing the details of the above by the end of June 2010, at the latest.

Annex 3. Structural reforms conditionality

STRUCTURAL REFORMS: CONDITIONALITY		
	Action	**Time frame**
PUBLIC ADMINISTRATION REFORMS		
Simplify the remuneration system for public sector employees	- launch a process to create a simplified remuneration system to cover basic wages and all allowances applying to all public sector employees and ensuring that remuneration reflects productivity and tasks	*September 2010*
	- establish a fully operational Single Payment Authority to centralize the payment of all salaries paid to civil servants at all levels of government	*December 2010*
	- adopt legislation for a simplified remuneration system	*June 2011*
Public procurement	- complete the first phase of the public procurement system for all sectors and levels of government with a fully operational electronic platform introducing the use of e-auctioning systems	*December 2010*
	- implement EU Directives and have an effective appeals system	*March 2011*
Transparency of public spending decisions	- adopt legislation to ensure transparency by requiring online publication of all government expenditure decisions	*June 2010*
Local administration reform	- adopt legislation reforming public administration at the local level	*June 2010*
	- adopt all legislation and decrees for full entry force of the reform on 1 January 2011 involving transfer of responsibilities and resources across entities	*December 2010*
Independent functional review of the central		*September 2010*

	STRUCTURAL REFORMS: CONDITIONALITY	
	Action	**Time frame**
government	- launch an independent and external review of the organization and functioning of the central administration - adopt legislation and measures to rationalize the use of resources, the organisation of the public administration and the effectiveness of social programmes	 *June 2011*
Better Regulation	-adopt legislation to implement the Better Regulation agenda - ensure full implementation to reduce administrative burden by 20 compared with 2008 level and submit a progress report to the Commission	*December 2010* *September 2011*
LABOUR MARKET and WAGES		
Start discussion with social partners	To prepare the revision of private sector wage bargaining and contractual arrangements	*June 2010*
Reform Employment Protection Legislation	- extend the probationary period for new jobs to one year - reduce the overall level of severance payments which should apply equally to blue and white collar workers - raise the minimum threshold for activating rules on collective dismissals especially for larger companies - put measures in place to guarantee that current minimum wages remain fixed in nominal terms for 3 years - facilitate use of temporary contracts and part-time work	*December 2010*
Reform minimum wages	- following dialogue with social partners, government to adopt legislation on minimum wages to introduces sub-minima for groups at risk such as the young and long term unemployed, - guarantee that current minimum wages remain fixed in nominal	*December 2010*

STRUCTURAL REFORMS: CONDITIONALITY		
	Action	**Time frame**
	terms for three years	
Reform private wage bargaining system to ensure wage moderation	- adopts legislation to reform wage bargaining system in the private sector, including local territorial pacts to set wage growth below sectoral agreements - introduce variable pay to link wages to productivity performance at the firm level - amend regulation of the arbitration system	*December 2010*
Increase the flexibility of working hours	- adjust legislation to introduce annual time accounts and reduce overtime pay	*December 2010*
Fight undeclared work	- strengthen legislation to enforce the registration of new employees - ensure the Labour Inspectorate is fully staffed and quantitative controls targets are in place	*June 2011*
Review social safety net	Review the scope for improvements in the targeting of social expenditures to enhance the social safety net for the most vulnerable	*June 2011*
PENSIONS		
Reform pension system	Government to adopt a new simplified system (pro rata) for all current and future employees including: - by December 2015, a unified statutory retirement age of 65 years, including for those insured before 1 Jan 1993 - an increased retirement age of women in the public sector to 65 by 2013 - strengthened link between contributions and benefits	*June 2010*

STRUCTURAL REFORMS: CONDITIONALITY		
	Action	**Time frame**
	- pension earnings calculated on the entire lifetime - an average annual accrual rate of 1.2 - price indexation of pensions - an automatic adjustment mechanism that links the retirement age with increases in life expectancy at retirement - an increased minimum contribution period from 37 to 40 years by 2015 - restricted access to early retirement and increased minimum retirement age of 60 years by 1st January 2011, including for workers in heavy and arduous professions, and those with 40 years of contributions - a revised disability scheme - reduced (by 6 per year) pension benefits for people retiring between the ages of 60 and 65 with less than 40 years of contribution - no special rules for those insured before 1 Jan 1993 - substantial cuts in the list of heavy and arduous professions (to no more than 10 of employees) - a means-tested minimum guaranteed pension for people aged above 65 years of age - a reduction in the number of funds to 3 Parliament adopts the pension reform	 *September 2010*
HEALTHCARE		
Healthcare reform	Complete reforms to improve management and procurement systems of health system: complete move to double accounting systems, establish operational oversight by the Finance Minister, the publication of audited accounts	*December2010*
BUSINESS ENVIRONMENT		
Facilitate business start ups	Simplify the start up of new businesses and make the General Commercial Registry (GEMI) fully operational	*June 2010* *September 2010*

STRUCTURAL REFORMS: CONDITIONALITY		
	Action	**Time frame**
Simplify the licensing of industrial units and reduce the costs of doing business	- simplify and accelerate the process of licensing enterprises, industrial activities and professions through legislation and by making the spatial plans operational	*December 2010*
	- Government to change legislation to mitigate tax obstacles to mergers and acquisitions, and lower costs associated with customs	*September 2011*
Implement the Services Directive	- adopt horizontal legislation, finalize screening of sectoral legislation	*June 2010*
	- make single points of contact operational	*September 2010*
	- adopt measures in key service sectors such as tourism, retail and education	*December 2010*
Open up restricted professions	- propose sector-specific legislation to remove restrictions to trade in the legal profession, the pharmacy profession, the notary profession, architects, engineers, auditing services	*December 2010*
	- implement the Professional Qualifications Directive so that qualifications from third countries are recognized	*December 2010*
	- adopt legislation to open up restricted professions	*June 2011*
Reform road freight transportation	Liberalize road freight transport by removing all unnecessary restrictions on admission to the occupation of road haulage, including minimum fixed prices	*September 2010*
Competition policy framework	Modify the existing institutional framework of the Hellenic	*December 2010*

STRUCTURAL REFORMS: CONDITIONALITY		
	Action	**Time frame**
	Competition Commission, including to allow prioritisation on important cases and to strengthen the independence of HCC members	
Railways	- prepare a recovery plan for the railway sector to restore profitability to operational services, ensure compliance with EU Directives, and specify a timetable for the restructuring of the holding company including the sale of land and other assets - implement fully the recovery plan for the railway sector	*June 2010* *March 2011*
Energy	-finalise plans for the liberalization of the wholesale electricity market and commence with the rationalization of consumer tariffs -adopt legislation to unbundle electricity and gas activities, including measures - adopt measures to strengthen the independence and capacity of the Energy Regulatory Authority	*September 2010* *March 2011* *March 2011*
PROMOTING INVESTMENT AND EXPORTS		
Promoting FDI and investment in strategic sectors	Government to take measures to facilitate FDI and investment in innovation in strategic sectors (green industries, ICT etc...), through a revision of the Investment Law, the adoption of measures to facilitate PPPs, action to fast-track large FDI projects and measures to strengthen export promotion policy	*September 2010*
R&D and innovation	- Carry out in depth evaluation of all R&D and innovation actions, including in various Operational Programmes, in order to adjust the national strategy	*December 2010*

STRUCTURAL REFORMS: CONDITIONALITY		
	Action	**Time frame**
	- create an Advisory Council financed through the 7th R&D programme, to consider how to foster innovation, how to strengthen links between public research and Greek industries and the development of regional industrial clusters	*December 2010*
STRUCTURAL AND COHESION FUNDS		
Increase absorption of Structural and Cohesion Funds	- put in place measures to achieve binding targets for payment claims of Structural and Cohesion Funds and for submission of large projects - establish Task Force with the Commission to speed-up the development of high quality projects, through better coordination and other actions - complete steps to prioritize public investment spending for projects benefiting from EU funds, including the introduction of a central bank account	*June 2010*
	- meet targets for payment claims (measured against certified data) and large projects	*December 2010 and every six months thereafter*
	- introduce a web-based open access monitoring tool of procedures for approval of project proposals and for implementation of public projects	*December 2011*
	- ensure that the managerial capacity of all Managing Authorities and Intermediate Bodies of operational programmes	*December 2011*

GREECE: TECHNICAL MEMORANDUM OF UNDERSTANDING

May 3, 2010

1. This Technical Memorandum of Understanding (TMU) sets out the understandings regarding the definitions of the indicators subject to quantitative targets (performance criteria and indicative targets), specified in the Letter of Intent (LOI). It also describes the methods to be used in assessing the program performance and the information requirements to ensure adequate monitoring of the targets. We will consult with the Fund, European Commission and ECB before modifying measures contained in this letter, or adopting new measures that would deviate from the goals of the program, and provide the European Commission, ECB and the Fund with the necessary information for program monitoring.

2. For program purposes, all foreign currency-related assets, liabilities, and flows will be evaluated at "program exchange rates" as defined below, with the exception of the items affecting government fiscal balances, which will be measured at current exchange rates. The program exchange rates are those that prevailed on April 30, 2010. In particular, the exchange rates for the purposes of the program are set €1 = 1.3315 U.S. dollar, €1 = 125.81 Japanese yen, €1.135 = 1 SDR.

General Government

3. **Definition**: For the purposes of the program, the general government includes:

- The entities covered under the State Budget as defined in Chapter 2 of the Law 2362/1995 regarding "Public Accounting, Auditing of Government Expenditures and Other Regulations."
- Local authorities comprising municipalities, prefectures, and regional governments including their basic and special budgets, including all agencies and institutions attached thereto, which are classified as part of local authorities according to ESA 95.
- Social security funds comprising all funds that are established as social security funds in the registry of the National Statistical Service.
- This definition of general government also includes any new funds, or other special budgetary and extra budgetary programs that may be created during the program period to carry out operations of a fiscal nature as defined in the IMF's *Manual on Government Finance Statistics 2001*. The authorities will inform IMF, European Commission and ECB staff of the creation of any such new funds or programs immediately.

4. **Supporting material:** The Ministry of Finance (MoF) will provide to the European Commission, ECB and IMF detailed information on monthly revenues and expenditures, domestic and foreign debt redemptions, new domestic and foreign debt issuance, change in the domestic and foreign cash balances of the central government at the central bank of Greece, all other sources of financing including capital transactions, and arrears of the general government. Data will be provided within 30 days. The Bank of Greece will provide detailed monthly data on assets and liabilities of local authorities and social security funds in line with monetary survey data.

VI. Quantitative Performance Criteria, Indicative Ceilings, and Continuous Performance Criteria: Definitions and Reporting Standards

A. Floor of the Modified General Government Primary Cash Balance (Performance Criterion)

5. **Definition**: The modified general government primary cash balance (MGGPCB) is defined as the modified general government cash balance (MGGCB) minus interest payments by the state budget. The MGGCB is defined as the sum of the cash balances of the ordinary state budget, the cash balance of the investment state budget, the change in net financial assets of local authorities and the change in net financial assets of social security funds. Privatization receipts will be excluded from cash receipts. Net lending operations by the state budget will be recorded as cash expenditures.

- **The cash balance of the ordinary state budget.** The cash balance of the ordinary state budget will be measured from above the line, based on ordinary budget revenues (recurrent revenue plus non-recurrent revenue minus tax refunds) minus ordinary budget expenditures (ordinary budget expenditures will exclude amortization payments and capital transfers to social security funds by bonds but include salaries and pensions; grants to social security funds, medical care and social protection; operational and other expenditure; returned resources; payments in exchange of claims of insurance fund for the personnel working in the Public Electricity Company; interest payments; payments for military equipment procurement; and NATO expenses) of the ordinary state budget as published monthly on the official website of the General Accounting Office of the Ministry of Finance, and in line with the corresponding line items established in the ordinary state budget.

- **The cash balance of the investment state budget.** The cash balance of the investment state budget will be measured from above the line, based on investment budget revenues minus investment budget expenditures of the investment state budget as published monthly on the official website of the General Accounting Office of the Ministry of Finance, and in line with the corresponding line items established in the investment state budget.

- **Net financial assets of local authorities** are defined as financial assets minus financial liabilities of local authorities. Financial assets include deposits of local authorities in the Bank of Greece and deposits of local authorities in the commercial domestic banking sector. Deposits will be measured at face value excluding accrued interest in line with recording for monetary survey data. Financial liabilities include short and long term loans from the domestic banking system to local authorities, measured at face value, consistent with recording for monetary survey data.

- **Net financial assets of social security funds** are defined as financial assets minus financial liabilities of social security funds.

    - Financial assets include

        - Deposits of social security funds in the Bank of Greece and direct deposits of social security funds in the domestic commercial banking system and indirect deposits held by the IKA mutual fund. Deposits are measured at face value excluding accrued interest, consistent with reporting requirements for monetary survey data.

        - Holdings of direct shares or indirect shares (through the IKA mutual fund), held by social security funds quoted on the Athens Stock Exchange. Holdings of shares will be measured at the end-of-month market value.

        - Direct or indirect holdings of Mutual Fund units issued by Greek management companies (other than the IKA mutual fund). Holdings of holdings will be measured at the end-of-month market value.

        - Holdings of central government bonds, including short and long-term securities issued domestically, long-term securities issued abroad operated from Bank of Greece accounts, and indirect holdings through the IKA mutual fund. Holdings will be measured at nominal value.

    - Financial liabilities include the short and long term loans from the domestic banking system to the social security funds, measured consistently with monetary survey data.

6. **Adjustments.** For the purpose of the program, the primary expenditure of the central government that is monitored excludes payments related to bank support, when carried out under the program's banking sector support and restructuring strategy. Costs that may be excluded from the balance include loans to financial institutions and investments in equity of financial institutions (requited recapitalization); unrequited recapitalization; and purchases of troubled assets. However, any financial operation by central government to support banks, including the issuance of guarantees or provision of liquidity, will be immediately reported to

IMF, European Commission and ECB staff. Further, this performance criterion will be adjusted upward for any possible revenue overperformance in the central government against the current projection as indicated below:

7. Central government revenue (Cumulative from January 1, 2010)

8. June 2010: €25,056 million

9. September 2010: €41,232 million

10. December 2010: €58,382 million.

11. **Supporting material**.

- Data on cash balances of the ordinary and state budgets will be provided to the European Commission, ECB and IMF by the General Accounting Office in the Ministry of Finance within three weeks after the end of the month. Data will include detailed information on revenue and expenditure items, in line with monthly reports that are published since January 2010 on the official website of the Ministry of Finance.

- Data on net financial assets of local authorities and social security funds will be provided to the IMF, European Commission and ECB by the Statistics Department of the Bank of Greece within four weeks after the end of the month.

B. Ceiling of State Budget Primary Spending (Performance Criterion)

12. **Definition**: The state budget primary spending consists of state budget spending (spending of the ordinary state budget plus spending of the investment budget) minus interest expenditures paid by the state budget, in line with the definitions provided above. Primary expenditure of the central government that is monitored for the PC excludes any cash payments related to bank restructuring, when carried out under the program's banking sector restructuring strategy. Costs that may be excluded from the balance include loans to financial institutions and investments in equity of financial institutions (requited recapitalization); unrequited recapitalization; and purchase of troubled assets. However, any financial operation by central or general government to support banks, including the issuance of guarantees or provision of liquidity, will be immediately reported to European Commission, ECB and IMF staff.

13. **Supporting material**. The General Accounting Office of the Ministry of Finance will provide monthly expenditure data of the ordinary and investment state budget, as defined above.

C. Non-accumulation of Domestic Arrears by the General Government (Continuous Indicative Target)

Definition. For the purpose of the program, domestic arrears are defined as accounts payable to domestic suppliers past due date by 90 days. Data will be provided within four weeks after the end of the month. The stock of arrears as of end-April stood at 5.6 billion euro.

14. **Supporting material.** The Ministry of Finance will provide data on monthly expenditure arrears of the general government, as defined above. Data will be provided within four weeks after the end of the month.

D. Ceiling on the Overall Stock of Central Government Debt (Performance Criterion)

15. **Definition**. The overall stock of central government debt will refer to debt that corresponds to the activities of the state budget and will be defined for the purposes of the program as the total outstanding gross debt liabilities of the central government. It will include, but not be limited to, liabilities in the form of securities and loans. The program exchange rate will apply to all non-euro denominated debt. For the purposes of the program, the ceiling on the stock of central government debt will exclude debt arising from payments for bank restructuring, when carried out under the program's banking sector restructuring strategy. This includes loans to financial institutions and investments in equity of financial institutions (requited recapitalization); unrequited recapitalization; and purchase of troubled assets. However, any financial operation by the central government to support banks, including the issuance of guarantees or provision of liquidity, will be immediately reported to IMF, European Commission and ECB staff.

16. **Adjusters**. The ceiling on the overall stock of central government debt will be adjusted upward (downward) by the amount of any upward (downward) revision to the stock of end-December 2009 central government debt.

17. **Supporting material**. Data on the total stock of central government debt will be provided to the European Commission, ECB and IMF staff by the General Accounting Office consistent with the debt published in the public debt bulletin no later than 30 days after the end of each month.

E. Ceiling on New Central Government Guarantees (Performance Criterion)

18. **Definition**. The ceiling on the new central government guarantees shall exclude guarantees to support banks and exclude guarantees related to EIB financed loans.

19. **Supporting material**. All new central government guarantees will be reported in detail, identifying amounts and beneficiaries. The General Accounting Office will provide the data on a monthly basis within three weeks after the end of each month.

F. Non-accumulation of External Debt Payments Arrears by the General Government (Continuous Performance Criteria)

20. **Definition**. For the purposes of the program, an external debt payment arrear will be defined as a payment on debt contracted or guaranteed by the general government, which has not been made within seven days after falling due. The performance criterion will apply on a continuous basis throughout the program period.

21. **Supporting material**. The stock of external arrears of the general government system will be provided by the General Accounting Office with a lag of not more than seven days after the test date.

G. Overall Monitoring and Reporting Requirements

23. Performance under the program will be monitored from data supplied to the EC, ECB and IMF by the Ministry of Finance, the General Accounting Office, and Bank of Greece. The authorities will transmit promptly to the IMF, EC and ECB staff any data revisions in a timely manner.

H. Monitoring of Structural Benchmarks

24. **Pension reform**. The government has initiated a pension reform which should be adopted by the end of September 2010. In preparing this reform, the authorities will consult with EC/IMF/ECB experts and the National Actuarial Authority will produce a report to assess whether the parameters of the new system significantly strengthen long-term actuarial balance. The draft law for the new and actuarially-balanced system should be available by the end of June, 2010.

25. **Expectations for the Pension Reform**. The reform will:

- Merge pension funds in three funds by 2018.
- Introduce a new system to strengthen the link between contributions and benefits, with uniform rules that will apply pro-rata (as a sum of the accrued rights under the old system and the benefits accrued under the new system) to all current and future workers. Workers retiring in and after 2015 will collect benefits from this system.
- Set the normal retirement to age 65 across all systems, including for those insured before 1993 and women in the public sector, by 2015. After 2020, the normal retirement age will increase in line with life expectancy.

- Restrict early retirement to age 60 by 2011, including for those insured before 1993, workers in heavy and arduous professions, and those with 35 or more years of contributions.

- Index benefits to changes in the consumer price index, starting in 2014 (benefits will be frozen 2010–2013).

- Include a means-tested pension for all citizens older than the normal retirement age so that an important safety net is provided, consistent with fiscal sustainability.

- Lengthens the years over which the pensionable earnings base is calculated from the top 5 out of the last 10 years of earnings to lifetime earnings.

- Review conditions for disability pensions by the end of March of 2011 and introduce stricter conditions for eligibility by December of 2011, including periodic re-examination of those with disability pensions.