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COMMUNICATION FROM THE COMMISSION TO THE COUNCIL

Follow-up to the Council Decision 2010/320/EU addressed to Greece, with a view to reinforcing and deepening fiscal surveillance and giving notice to Greece to take measures for the deficit reduction judged necessary to remedy the situation of excessive deficit

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1. INTRODUCTION

This Communication assesses the measures implemented by Greece in the period between November 2010 and mid-February 2011 to comply with the Council Decision 2010/320/EU.[1] Action taken up to November was assessed in the Communication dated 9 December 2010.[2] Together with a companion Commission staff's report, prepared in liaison with the ECB,[3] it also contributes to the assessment of compliance with the MEFP and the MoU,[4] in the context of the loan facility agreement between Greece and the other euro-area Member States.

This assessment is based on the report submitted to the Council and the Commission by Greece,[5] and on the mission conducted by European Commission staff together with IMF and ECB in the context of the economic adjustment programme which is being financed by bilateral loans by the euro-area Member States and an IMF's stand-by arrangement. The report submitted by Greece on 12 February 2011 discusses not only the fiscal measures that aim at reducing the government deficit ratio in 2011, but also the wide-ranging structural reforms that are being adopted and implemented by the Greek government.

2. THE COUNCIL DECISION OF 10 MAY 2010

On 10 May 2010, the Council adopted Decision 2010/320/EU, under Articles 126(9) and 136 TFEU, addressed to Greece, with a view to reinforcing and deepening the fiscal surveillance and giving notice to take measures for the deficit reduction judged necessary to remedy the situation of excessive deficit by 2014.

The Council Decision requires Greece to adopt a number of specific measures with the aim of keeping general government deficit below the following ceilings:

- EUR 18 508 million (8.1 percent of GDP, on the basis of the recently available official GDP data) in 2010;

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1 OJ L 145, 11.6.2010, p. 6-11.

2 COM (2010) 739 final.

3 'The Economic Adjustment Programme for Greece – Third Review,' *European Economy–Occasional Paper N° 77* (February 2011). The reader is referred to that document for a more detailed assessment of macroeconomic, financial, fiscal and structural reform developments.

4 Memorandum of Economic and Financial Policies, and Memorandum of Understanding of Specific Economic Policy Conditionality of 3 May, updated 22 November 2010.

5 *The Economic Adjustment Programme for Greece – Report submitted in accordance with Council Decision – February 2011.* The report was submitted by the Greek government on 12 February 2011. It is available at: http://ec.europa.eu/economy_finance/eu/countries/greece_en.htm.

- EUR 17 065 million (7.6 percent of GDP) in 2011;
- EUR 14 916 million (6.5 percent of GDP) in 2012;
- EUR 11 399 million (4.8 percent of GDP) in 2013 and
- EUR 6 385 million (2.6 percent of GDP) in 2014.[6]

The Decision was then amended on 7 September 2010 (Decision 2010/486/EU)[7] and 20 December 2010 (Decision 2011/57/EU).[8] However, the aforementioned ceilings for the general government deficit were kept unchanged.

3. BUDGETARY EXECUTION

The ESA-based government deficit target for 2010 has been missed. While the deficit ceiling as established in the Council Decision was EUR 18 billion (8 percent of GDP) for 2010, the deficit is estimated to have reached EUR 22 billion (9.6 percent of GDP), though some uncertainty remains on the accuracy of this outcome. The margins of uncertainty are mainly related to the performance of state-owned enterprises and extra-budgetary funds classified in general government, social security and local government, for which hard infra-annual data are not available yet. There are also uncertainties on the differences between cash payments and underlying expenditure. The first complete set of ESA-based annual data will not be available before end-March 2011, to be published and validated by Eurostat in April.

The ceiling for state primary payments (cash basis) for end-year (as established in the MEFP and MoU) has been respected. The outcome was EUR 61.1 billion against a ceiling of EUR 67 billion. The over-performance of the criterion reflects under-execution of spending, which is largely related to effective savings, but also, to a postponement or delay of payments; information on expenditure pending payments is still substandard. According to available information, the amount of arrears accumulated in 2010 stands at above EUR 1.5 billion and will have to be settled in the course of 2011.

The government primary balance (on a cash basis according to the definition that are monitored under the MEFP and MoU) reached EUR 5.5 billion, against the ceiling of EUR 5.7 billion. In the previous communication, the estimate was that the criterion could be missed by up to EUR 1.5 billion (0.6 percent of GDP), based on the assumption of zero accumulation of arrears.

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6 The ratios to GDP are indicative. In the Council Decision, the ratios-to-GDP refer to the nominal GDP figures available in May: 8.0, 7.6, 6.5, 4.9 and 2.6 percent of GDP for 2010 to 2014, respectively. The adjustment path established by the Decision requires that the annual increase in the general government consolidated gross debt does not exceed: EUR 34 058 million in 2010; EUR 17 365 million in 2011; EUR 15 016 million in 2012; EUR 11 599 million in 2013 and EUR 7 885 million in 2014. Taking into account the revised debt figures at the end of 2009 and the latest nominal GDP projections, this corresponds to debt ratios of 145, 155, 159, 159 and 157 percent of GDP for 2010 to 2014, respectively.

7 OJ L 145, 11.6.2010, p. 6.

8 OJ L 26, 29.1.2011, p. 15.

Table 1: State budget execution

cash basis (EUR million)	2009 Jan - Dec	2010 Jan - Dec	2010 % change	2010 May-2010 plans
Total revenue	50531	54240	7,3	55715
Revenue before refunds	53443	56147	5,1	57800
Tax refunds	4952	4979	0,5	5100
Capital revenue	2040	3072	50,6	3015
Total expenditure	81403	73694	-9,5	75187
Primary expenditure	57992	51679	-10,9	52633
Interest	12325	13223	7,3	13209
Capital expenditure	9588	8447	-11,9	9000
Other	1498	345	-77,0	345
State Budget balance	-30872	-19454	-37,0	-19472

Source: General Accounting Office.
Note: This table does no include payments for military procurement (EUR 1 billion in 2010, declining by more 30 percent as compared to 2009.

The general government debt-to-GDP ratio in 2010 reached 142.5 percent, compared with the original target of 133 percent of GDP. The difference is mainly stemming from the reclassification of public entities in the general government, included for the first time in 2009 fiscal accounts, but also from the worse than anticipated deficit performance in 2010. However, the ceiling for the increase in the government debt established by the Decisions has been respected (ceiling: EUR 34 058 million; estimated outcome: EUR 28 870 million).

4. PROSPECTS FOR 2011 AND 2012-2014

The Greek Government has confirmed its commitment to meet the fiscal target for 2011 established by the Council Decision. With higher-than-expected starting deficit and debt levels, and lower-than-expected GDP, larger consolidation efforts are necessary. The fiscal strategy remains anchored on the consolidation path agreed in May 2010. The Greek Government therefore decided to fully recoup the ground lost in 2010, in order to restore rapidly a sustainable fiscal position, keep financing needs in line with the programme, and support market confidence. The 2011 budget– adopted by the Greek Parliament on 22 December 2010 – contains 2'O percent of GDP in new deficit-reducing measures. This brings total fiscal consolidation measures in 2011 – including those agreed in May – to 5'Y percent of GDP. About two thirds of the new measures agreed in November are on the expenditure side, and most of them are of a structural nature; EUR 0.7 billion (or 0.3 percent of GDP) of measures are temporary.

Most of the fiscal measures underpinning the 2011 deficit target have been legislated and started being implemented. Measures include cuts in unproductive and untargeted spending, reduction in short-term contracts in the public sector, better targeting of universal household subsidies (like subsidies for heating fuel and family allowances), and better management and use of state assets, particularly in the collection of taxes in arrears. The 2011 budget also starts tackling two key structural problems – excessive health spending and losses by state-owned enterprises. The achievement of the 2011 budgetary targets implies an increase in total tax revenue of more than EUR 1.5 billion (or some ′Y percent of GDP), compared with 2010, which is a challenging task and relies much on concrete results from the fight against tax evasion and the increase in the efficiency of the mechanism

According to the 2011 budget, the government deficit (ESA95) would be EUR 16.8 billion (7.6 percent of GDP). However, based on the latest available information the Commission services forecast that the 2011 ESA95 deficit could be at EUR 18.8 billion, (cut-off date for this forecasts 11 February 2011). Therefore, unless action is taken, the 2011 deficit would be ′Y of a percentage point of GDP above the ceiling. With the January 2011 state budget execution (cash basis) performing below the monthly target, mainly due to a still weakening revenue side, the implied annual fiscal gap stems mainly from less favourable expectations for the tax bases growth, updated estimates for the fiscal measures to be implemented in the course of the year, as well as a base effect from the worse-than-expected 2010 outcome of several revenue categories. Moreover, interest expenditure is expected to be higher than budgeted.

According to the Greek organic budget law, the government should prepare the medium-term fiscal strategy for 2012–15. The government will design the fiscal policy to be implemented over the medium term, with the view to reduce the general government deficit below 3 percent of GDP by 2014 and further afterwards. Commission services' estimates suggest that the fiscal gap between a baseline no-policy scenario and the 2014 target set in the Council Decision currently stands at around 8 percent of GDP (table 2), out of which, fiscal measures of some 2 percent of GDP had already been identified in May, though revisions of their budgetary impact should not be excluded.

The government has already announced the first broad lines of the medium-term budget strategy, a draft of which will be available by end-March, adopted by the Council of Ministers by mid-April and voted by Parliament by mid-May. The main elements of the strategy paper will include: (i) prudent macroeconomic forecasts; (ii) baseline revenue and expenditure projections for the state and for the other government entities; (iii) a description of permanent fiscal measures, their timing and quantification; (iv) annual spending ceilings for each ministry and fiscal targets for other government entities through 2014; (v) post-measures fiscal projections for general government in line with the deficit and debt targets; (vi) longer-term debt projections based on prudent macroeconomic projections, stable primary surpluses from 2014 on, and privatisation plans. A number of ongoing or planned fiscal structural reforms will be embedded in the medium-term strategy, including: (i) the reform of state-owned enterprises; and of (ii) extra-budgetary funds (legal entities of the public sector and earmarked accounts); (iii) the tax policy reforms; (iv) the reforms in the public wage system and the public administration; (v) the rationalisation of the social spending; (vi) and cost-effective planning for the public investment; and (vii) military spending.

Table 2: Deficit accounting: Deficit from the previous year to the next

	EUR million	Cumulative measures 2010-2014	Cumulative measures 2012-2014	% of GDP	Cumulative measures 2010-2014	Cumulative measures 2012-2014
2009 Deficit	**36150**			**15,4**		
Nominal deficit drift in 2010	3880			1,7		
Measures implemented in 2010	18000	18000		7,8	7,8	
Impact on ratio of nominal GDP growth	--			0,2		
2010 Deficit	**22030**			**9,6**		
Nominal deficit drift in 2011	9226			4,1		
Measures implemented in 2011	12450	30450		5,5	13,5	
Unidentified measures	1741	1741		0,7	0,7	
Impact on ratio of nominal GDP growth	--			0,1		
2011 Deficit (target)	**17065**			**7,6**		
Nominal deficit drift in 2012	5455			2,4		
Identified measures for 2012*	5575	36025	5575	2,4	15,7	2,4
Unidentified measures for 2012	2029	3770	3770	0,9	1,6	1,6
Impact on ratio of nominal GDP growth	--			-0,1		
2012 Deficit (target)	**14916**			**6,4**		
Nominal deficit drift in 2013	2218			0,9		
Identified measures for 2013*	575	36600	6150	0,2	15,5	2,6
Unidentified measures for 2013	5160	8931	8930	2,2	3,8	3,8
Impact on ratio of nominal GDP growth	--			-0,2		
2013 Deficit (target)	**11399**			**4,8**		
Nominal deficit drift in 2014	491			0,2		
Identified measures for 2014*	-1050	35550	5100	-0,4	14,6	2,1
Unidentified measures for 2014	5573	14504	14504	2,3	5,9	5,9
Impact on ratio of nominal GDP growth	--			-0,6		
2014 Deficit (target)	**6385**			**2,6**		

* Measures for 2012, 2013 and 2014 identified and quantified in the original programme of May are subject to revision.

Deficit in year t equals deficit in year t-1 plus nominal deficit drift in year t minus identified measures minus unidentified measures (and for the ratios: plus impact on ratio of nominal GDP).

Deficit drift includes the increase in the deficit level that would take place without measures. It includes in particular the structural increase in pension expenditure, the increase in interest expenditure and other structural increase in spending. The deficit drift has been calculated assuming wage freeze and the implementation of the 1-to-5 rule between recruitments and exits. It also reflects the increase/decrease in revenue due to developments in tax bases.

5. PROGRESS WITH STRUCTURAL REFORMS

The structural reform agenda in Greece is being implemented. Progress has been achieved in structural fiscal reforms, though in some cases slower than planned. The government is strengthening the legislative framework to fight tax evasion and to modernise the tax administration. Budgetary institution reforms, including the General Accounting Office, are progressing - the government has set expenditure ceilings for the State and deficit targets for the general government and it has made progress in ensuring a timely provision of fiscal data, although quality and scope need to improve further. Fiscal management on the expenditure side of the budget also needs to improve, in particular with respect the investment budget and military procurement. Progress has been made with the healthcare reform - a first package of reforms having been adopted in mid-February 2011. However, a number of fiscal structural measures have been delayed, including simplifying the public sector remuneration system and making fully effective the Single Payment Authority (SPA). Albeit with some delay, the preparation of the functional reviews of central administration and social programmes is now making progress.

The Government has committed to publish an inventory of state-owned assets, including stakes in listed and non-listed enterprises and commercially viable real estate and land. This will contribute to accelerate privatisation, the proceeds of which have been scaled up by the government to EUR 50 billion in 2011-2015, of which EUR 15 billion in 2011-2012.

Progress with other structural reforms is ongoing, but as with fiscal structural reforms, there have been delays. With the adoption of the labour law in December and the legislative proposals on the opening of closed professions, Greece has effectively launched a new wave of structural reforms. An independent taskforce of education policy experts is being set up as a first step towards a reform in education. Legislative acts are adopted or are expected to be adopted shortly which aim to remove existing restrictions on the freedom to provide services, reform the energy sector, simplify legislation and accelerate the process of licensing undertakings, industrial activities and professions, as well as modify the institutional framework of the Hellenic Competition Commission (HCC).

6. Completeness of required Information

The report submitted by Greece, and data regularly transmitted to the Commission, include most of the information requirements established by the Council Decision. In particular, the report contains detailed information on concrete measures implemented (and to be implemented) in order to comply with the Decision and their respective budgetary impact.

Data on the monthly state budget execution have been timely provided by the General Accounting Office, with the latest (for January 2011) having been published on 12 February 2011. Moreover, data on the monthly evolution of arrears for the state and a large part of the non-state sectors of the general government is also provided, following the monthly updates published by the General Accounting Office. Although the level of detail for the annual data for the non-state sectors of the government has been improved, the provision of monthly data on the budgetary implementation by social security funds, extra-budgetary bodies and local governments remains incomplete. The report presents the development of the number of permanent staff in the public sector since the end of 2009, including permanent staff of the central administration, public entities, local authorities, state legal entities of private law, security forces, military personnel and clergy. The report contains the required information in relation to debt issuance and reimbursements, and on the financial situation of the largest state-owned enterprises. Moreover, the report contains a wealth of information concerning the implementation of structural reforms in response to the Council Recommendation of 16 February 2010[9] and to comply with the MEFP and MoU.

7. Conclusion

The government deficit (ESA95 basis) ceiling for 2010 established by the Council Decision is estimated to have been missed by around EUR 4.1 billion and to have amounted to EUR 22 billion (9.6 percent of GDP), instead of EUR 18.5 billion (8 percent of GDP). This amounts, however, to a reduction in the deficit ratio of almost 6 points as compared to 2009. The government debt ratio is estimated to have increased from 127 percent of GDP at the end 2009 to 141 percent in 2010.

For 2011, the budget adopted by Parliament is in line with the Council Decision ceilings, though further action will be needed to stick to the deficit ceiling. The Government is currently elaborating further durable measures that will be necessary to keep reducing the deficit in subsequent years. In particular, the government has already announced the broad lines of a medium-term budget strategy, a draft of which will be available by end-March, adopted by the Council of Ministers by mid-April and voted by Parliament by mid-May. In the context of the medium-term strategy, permanent fiscal consolidation measures of at least 8 percent of GDP shall be needed, of which 6 percent of GDP still needs to be identified, to ensure the achievement of deficit targets up to 2014, and that the debt-to-GDP ratio is put on a sustainable downward path. A scaled-up privatisation plan is expected to reduce the debt ratio by almost 20 percentage points of GDP in five years.

All in all, despite the 2010 fiscal slippage, Greece is getting ready to take the necessary actions and to implement the required policies to remain on track, with a view to putting an end to the excessive deficit by 2014, as required in the Council Decision. Therefore, the Commission concludes that Greece is satisfactorily complying with the Council Decision of 10 May 2010, responding to the Council Recommendation of 16 February 2010 and implementing the measures outlined in the updated MEFP and MoU of 22 November 2010.

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9 Council Recommendation (2010/190/EU) to Greece of 16 February 2010 with a view to ending the inconsistency with the broad guidelines of the economic policies in Greece and removing the risk of jeopardising the proper functioning of the economic and monetary union (OJ L 83, 30.3.2010, p. 63).

ANNEX I: MEASURES REQUIRED BY THE COUNCIL DECISION, TO BE ADOPTED BY END-DECEMBER 2010

Measures (as required by Article 2(3) of the Council Decision)	State of progress
"Greece shall adopt the following measures by the end of December 2010:	
(a) the final adoption of the measures referred to in paragraph 2(a);	**Observed.**
(b) the implementation of legislation strengthening the fiscal framework. This should, in particular, include the establishment of a medium-term fiscal framework, the creation of a compulsory contingency reserve in the budget corresponding to 5 percent of total appropriations of government departments, other than wages, pensions and interest, the creation of stronger expenditure monitoring mechanisms and the establishment of a budget office attached to Parliament;	**Partially observed.** The new organic budget law legislated in September 2010, has already been applied with the 2011 budget law. The Government shall adopt by May 2011 the medium-term fiscal budgetary framework which will be the basis for the 2012 budget. The budget office attached to Parliament, while legislated, has not been created yet.
(f) a significant increase in the absorption rate of structural and cohesion funds;	**Observed.**
(i) legislation simplifying and accelerating the process of licensing undertakings, industrial activities and professions;	**Partially observed, delayed.** The licensing law is expected to be voted in Parliament shortly.
(j) a modification of the institutional framework of the Hellenic competition authority (HCC) with a view to increasing its independence, establishing reasonable deadlines for the investigation and issue of decisions and entrusting it with the power to reject complaints;	**Ongoing, delayed**. To be submitted to Parliament shortly.
(k) a better management of public assets, with the aim of raising at least EUR 7 billion during the period 2011- 2013, of which at least EUR 1 billion in 2011 and proceeds from the sale of assets (real estate and financial assets) shall be used to redeem debt and will not reduce the fiscal consolidation efforts to comply with the deficit ceilings in Article 1(2);	**Observed.** The government has announced the assets it intends to privatise in the course of 2011-13. The plan should be revised in line with the government's intention of scaling up privatisation receipts to EUR 50 billion in 2011-2015.
(l) measures aiming at removing existing restrictions on the freedom to provide services;	**Ongoing with delay**. Several measures to be legislated shortly.
(m) a decree disallowing local governments to run deficits at least until 2014; reduction in transfers to local government in line with planned savings and transfers of competences;	**Observed.**

(n) publication of interim long-term projections of pension expenditure up to 2060 as set out in the July 2010 legislative reform covering the main pension schemes (IKA, including the pension scheme for civil servants, OGA and OAEE);	**Observed.**
(o) implementation of a uniform e-prescribing system; publication of the complete price list for the medicines in the market; application of the list of non-reimbursed medicines and of the list of over- the-counter medicines; publication of the new list of reimbursed medicines using the new reference price system; the use of the information made available through e-prescribing and scanning for the collection of rebates from pharmaceutical companies; introduction of a monitoring mechanism allowing for pharmaceutical expenditure to be assessed on a monthly basis; enforcement of co-payments for regular outpatient services of EUR 5 and extension of co-payments to unwarranted visits to emergency departments; publication of audited accounts for hospitals and health centres; and creation of an independent taskforce of health policy experts whose task is to produce, by end May 2011, a detailed report for an overall reform of the health system aimed at improving efficiency and effectiveness in the health system;	**Ongoing.** Several measures being legislated or implemented.
(q) further reduction in operational expenditure by at least 5 percent yielding savings of at least EUR 100 million;	**Observed.**
(r) further reduction in transfers yielding savings for the government as a whole of at least EUR 100 million. The beneficiary public entities will ensure the concomitant reduction in expenditure so that there is no accumulation of arrears;	
(s) means-testing of family allowances from January 2011 on yielding savings of at least EUR 150 million (net of the respective administrative costs);	**Observed.**
(t) reduction in the purchase of military equipment (deliveries) by at least EUR 500 million compared to the actual 2010 level;	**Planned.** To be assessed by end-year.
(u) reduction in pharmaceutical expenditure by social security funds by EUR 900 million owing to an additional reduction in drug prices and new procurement procedures and by hospitals (also including expenditure in equipment) by at least EUR 350 million;	**Observed.**
(v) changes in the management, pricing and wages of public enterprises yielding savings of at least EUR 800 million;	**Observed.**
(w) equalisation of taxation on heating oil and diesel oil after 15 October 2011, with the aim of fighting fraud and yielding at least EUR 400 million in 2011 net of specific measures to protect the less prosperous population strata;	**Not observed.** The act to equalise the taxation of heating oil and diesel oil has not yet been legislated. The specific tax benefit to heating oil to be revoked applies only in autumn and winter, so that a delay in the adoption the act until now has no

	material impact on tax revenue and tax expenditure.
(x) increase in the reduced rates of VAT from 5,5 % to 6,5 % and from 11 % to 13 %, yielding at least EUR 880 million and reduction in the VAT rate applicable to medicines and hotel accommodation from 11 % to 6,5 % with a cost not exceeding EUR 250 million, net of savings for social security funds and hospitals that result from the lower VAT rate on medicines;	**Observed.**
(y) intensification of the fight against smuggling on fuel (at least EUR 190 million);	
(z) increase in court trial fees (at least EUR 100 million);	
(aa) implementation of an action plan to accelerate the collection of tax arrears (at least EUR 200 million);	
(bb) speeding up tax penalty collection (at least EUR 400 million);	
(cc) collection of revenue that results from the new framework of tax disputes and trials (at least EUR 300 million);	
(dd) revenue from the renewal of telecommunication licences that are about to expire (at least EUR 350 million);	
(ee) revenue from concessions (at least EUR 250 million);	
(ff) a restructuring plan for the Athens transportation network (OASA). The objective of the plan shall be to reduce operational losses of the company and make it economically viable. The plan shall include cuts in operational expenditure of the company and tariff increases. The required actions shall be implemented by March 2011;	**Ongoing**. Draft business plan available.
(gg) an act that limits recruitment in the whole general government to a ratio of not more than one recruitment for five retirements or dismissals, without sector exceptions, and including staff transferred from public enterprises under restructuring to government entities;	**Observed**
(hh) acts to strengthen labour market institution and establish that: firm-level agreements prevail over those under sector and occupational agreements without undue restrictions; firm-level collective agreements are not restricted by requirements regarding the minimum size of firms; the extension of sector and occupational agreements to parties not represented in negotiations is eliminated; the probationary period for new jobs is extended; temporal limits in the use of temporary working agencies are eliminated; impediments for greater use of fixed-term contracts are removed; the provision that establishes higher hourly remuneration to part- time workers is eliminated; and a more flexible working-time management including part-time shift work is allowed for.	**Partially observed.** Law 3899/2010 establishes that firms and their employees may agree special firm-level collective agreements (SFLCA) that deviate *in peius* from sector agreements. The new OMED board is in the process of being constituted. The requirements on extending the probationary period for new jobs to one year, eliminating temporal limits in the use of temporary working agencies and eliminating the provision that establishes higher hourly remuneration to part-time workers have been observed. The required elimination of the extension of

	sector and occupational agreements to parties not represented in negotiations has not taken place. The requirements to adopt legislation to remove impediments for greater use of fixed-term contracts and to allow for a more flexible working-time management have not been fulfilled.