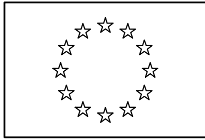

COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 24.06.2009
SEC(2009) 864

COMMISSION OPINION

on the existence of an excessive deficit in Poland

Application of Article 104(5) of the Treaty establishing the European Community

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THE APPLICATION OF THE STABILITY AND GROWTH PACT IN THE CURRENT CRISIS SITUATION

1. Many EU countries are presently facing general government deficits above the 3% of GDP reference value set in the Treaty. The often strong deterioration in the deficit as well as the debt positions must be seen in the context of the unprecedented global financial crisis and economic downturn. Several factors are at play. First, the economic downturn brings about declining tax revenue and rising social benefit expenditure (e.g. unemployment benefits). Second, recognising that budgetary policies have an important role to play in the current extraordinary economic situation, the Commission called for a fiscal stimulus in its November 2008 European Economic Recovery Plan (EERP), endorsed by the European Council in December. The Plan explicated that the stimulus should be timely, targeted and temporary and differentiated across Member States, with more room for manoeuvre for those Member States that have achieved sustainable public finance positions and improved their competitive positions. It also called for structural reforms that support demand and promote resilience in the short term, while paying special attention to actions in the four priority areas of the Lisbon strategy. Finally, several countries have taken measures to stabilise the financial sector, some of which impact on the debt position or constitute a risk of higher deficits and debt in the future, although some of the costs of the government support could be recouped in the future.

2. The Stability and Growth Pact requires the Commission to initiate the excessive deficit procedure (EDP) whenever the deficit of a Member State exceeds the 3% of GDP reference value. The amendments to the Stability and Growth Pact in 2005 aimed at ensuring that in particular the economic and budgetary background was taken into account fully in all steps in the EDP. In this way, the Stability and Growth Pact provides the framework supporting government policies for a prompt return to sound budgetary positions taking account of the economic situation, and thereby ensuring long-term sustainability of public finances.

LEGAL BACKGROUND

3. Article 104 of the Treaty lays down an excessive deficit procedure (EDP). This procedure is further specified in Council Regulation (EC) No 1467/97 “on speeding up and clarifying the implementation of the excessive deficit procedure”[1], which is part of the Stability and Growth Pact.

[1] OJ L 209, 2.8.1997, p. 6. Account is also taken of the Opinion of the Economic and Financial Committee on the “Specifications on the implementation of the Stability and Growth Pact and guidelines on the format and content of stability and convergence programmes”, endorsed by the ECOFIN Council of 11 October 2005, available at: http://ec.europa.eu/economy_finance/other_pages/other_pages12638_en.htm

4. According to Article 104(2) of the Treaty, the Commission has to monitor compliance with budgetary discipline on the basis of two criteria, namely: (a) whether the ratio of the planned or actual government deficit to gross domestic product (GDP) exceeds the reference value of 3% (unless either the ratio has declined substantially and continuously and reached a level that comes close to the reference value; or, alternatively, the excess over the reference value is only exceptional and temporary and the ratio remains close to the reference value); and (b) whether the ratio of government debt to GDP exceeds the reference value of 60% (unless the ratio is sufficiently diminishing and approaching the reference value at a satisfactory pace).

5. Article 104(3) stipulates that, if a Member State does not fulfil the requirements under one or both of these criteria, the Commission has to prepare a report. This report also has to "take into account whether the government deficit exceeds government investment expenditure and take into account all other relevant factors, including the medium-term economic and budgetary position of the Member State".

6. On the basis of the data notified by the Polish authorities in April 2009[2] and subsequently validated by Eurostat[3] and taking into account the Commission services' spring 2009 forecast, the Commission adopted a report under Article 104(3) for Poland on 13 May 2009[4].

7. Subsequently, and in accordance with Article 104(4), the Economic and Financial Committee formulated an opinion on the Commission report on 28 May 2009.

8. Article 104(5) of the Treaty requires the Commission to address an opinion to the Council if the Commission considers that an excessive deficit in a Member State exists or may occur. In order to reach a conclusion on whether an excessive deficit exists or may occur, the Commission considers that account should be taken of: (i) the conclusions of its report under Article 104(3) and (ii) the opinion of the Economic and Financial Committee on this report. On the basis of these elements, the Commission has established a number of considerations for Poland.

CONSIDERATIONS CONCERNING POLAND

9. An EDP for Poland was initiated by the Commission in May 2004 with the adoption of a report under Article 104(3) in view of a deficit of 4.1% of GDP in 2003. On the Commission's recommendation, the Council decided in July 2004, in conformity with Article 104(6), that an excessive deficit existed in Poland and consequently, pursuant to Article 104(7), issued a recommendation to the Polish authorities with a view to bringing the situation of an excessive deficit to an end by 2007, at the latest. On 28 November 2006, the Council decided under Article 104(8), on a recommendation from the Commission, that action taken until then by the Polish

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[2] According to Council Regulation (EC) No 3605/93, Member States have to report to the Commission, twice a year, their planned and actual government deficit and debt levels. The most recent notification of Poland can be found at: http://epp.eurostat.ec.europa.eu/portal/page/portal/government_finance_statistics/procedure/edp_notification_tables.

[3] Eurostat news release No 56/2009 of 22 April 2009.

[4] All EDP-related documents for Poland can be found at the following website: http://ec.europa.eu/economy_finance/netstartsearch/pdfsearch/pdf.cfm?mode=_m2.

authorities was inadequate. On 27 February 2007, the Council issued a new recommendation under Article 104(7) confirming the 2007 deadline for the correction. After assessment of the measures taken, the Council decided on 8 July 2008 to abrogate its decision on the existence of an excessive deficit in Poland.

10. After a general government deficit of 1.9% of GDP in 2007, on the back of very high GDP growth of 6.6% that year, in 2008 public finances deteriorated again, despite still high GDP growth of 4.9%, mainly on account of higher than planned government consumption and lower than assumed non-tax revenues other than social contributions.

11. According to the April 2009 EDP notification by the Polish authorities, subsequently validated by Eurostat, the general government deficit in Poland reached 3.9% of GDP in 2008, thus exceeding the 3% of GDP reference value. The Commission report under Article 104(3) considered that the deficit was not close to the 3% of GDP reference value and that the excess over the reference value cannot be qualified as exceptional within the meaning of the Treaty and the Stability and Growth Pact. In particular, it does not result from an unusual event in the sense of the Treaty and the Stability and Growth Pact. Moreover, it does not result from a severe economic downturn in 2008 in the sense of the Treaty and the Stability and Growth Pact. Despite the slowing down in growth to 3.3% year-on-year in the last quarter of 2008, which affected revenue collection in the last quarter of the year and added to the worse-than-expected deficit outcome, overall GDP growth was still relatively robust of 4.9% in 2008. Potential GDP growth is estimated to be in the order of 4½% and the output gap to have reached about 3½% of potential GDP in that year, indicating favourable cyclical conditions. Furthermore, the excess over the reference value cannot be considered temporary. According to the Commission services' spring 2009 forecast, the general government deficit is expected to reach 6.6% of GDP in 2009 and 7.3% in 2010 (against a GDP contraction of 1.4% in 2009 and GDP growth of 0.8% in 2010). The deficit is expected to increase in 2009 also according to the Polish authorities, who on 22 June announced that the general government deficit may significantly exceed the 4.6% of GDP figure planned for the current year in the Spring 2009 EDP notification[5]. Therefore, the deficit criterion in the Treaty is not fulfilled.

12. General government gross debt remains below the 60% of GDP reference value and stood at 47.1% of GDP in 2008. However, due to high expected deficits, the general government debt is likely to reach almost 60% in 2010 according to the Commission services' spring 2009 forecast.

13. In line with the provisions in the Stability and Growth Pact, the Commission in its report gave due consideration to systemic pension reforms introducing a multi-pillar system that includes a mandatory, fully funded pillar. While the implementation of these reforms leads to a temporary deterioration of the budgetary position, the long-term sustainability of public finances clearly improves. Based on the estimates of the Polish authorities, the net cost of this reform amounted to 2.9% of GDP in 2008, rising to 3.2% of GDP in 2009 and 2010. According to the Stability and Growth Pact, these can be taken into account on a linear degressive basis for a transitory

[5] Letter from Finance Minister Mr Rostowski to Commissioner Almunia.

period and only in case where the deficit remains close to the reference value. Since the deficit does not remain close to the reference value in 2008-2010, the cost of the pension reform cannot be taken into account.

14. In line with the provisions in the Treaty and the Stability and Growth Pact, the Commission also analysed in its report “relevant factors”. According to the Stability and Growth Pact, these can only be taken into account in the steps leading to the decision on the existence of an excessive deficit if the deficit satisfies the double condition of closeness and temporariness. In the case of Poland, this double condition is not met. Considered on their own merit, the relevant factors in the case of Poland, on balance, present a mixed picture.

15. The opinion of the Economic and Financial Committee in accordance with Article 104(4) of the Treaty is consistent with the assessment in the Commission report under Article 104(3).

CONCLUSION

16. The monitoring of the budgetary situation in Poland and, in particular, the examination of the compliance with the criteria laid down in Article 104(2) has led the Commission to prepare a report in accordance with Article 104(3) of the Treaty. The Commission, having taken into account its report and the opinion of the Economic and Financial Committee, is of the opinion that an excessive deficit exists in Poland.