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Recommendation for a

**COUNCIL RECOMMENDATION**

**on Romania's 2014 national reform programme**

**and delivering a Council opinion on Romania's 2014 convergence programme**

{SWD(2014) 424 final}

Recommendation for a

## **COUNCIL RECOMMENDATION**

**on Romania's 2014 national reform programme**

**and delivering a Council opinion on Romania's 2014 convergence programme**

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Articles 121(2) and 148(4) thereof,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies<sup>1</sup>, and in particular Article 9(2) thereof,

Having regard to the recommendation of the European Commission<sup>2</sup>,

Having regard to the resolutions of the European Parliament<sup>3</sup>,

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

Having regard to the opinion of the Economic and Financial Committee,

Having regard to the opinion of the Social Protection Committee,

Having regard to the opinion of the Economic Policy Committee,

Whereas:

- (1) On 26 March 2010, the European Council agreed to the Commission's proposal to launch a new strategy for growth and jobs, Europe 2020, based on enhanced coordination of economic policies, which will focus on the key areas where action is needed to boost Europe's potential for sustainable growth and competitiveness.
- (2) On 13 July 2010, the Council, on the basis of the Commission's proposals, adopted a recommendation on the broad guidelines for the economic policies of the Member States and the Union (2010 to 2014) and, on 21 October 2010, adopted a decision on guidelines for the employment policies of the Member States, which together form the 'integrated guidelines'. Member States were invited to take the integrated guidelines into account in their national economic and employment policies.
- (3) On 29 June 2012, the Heads of State or Government decided on a Compact for Growth and Jobs, providing a coherent framework for action at national, EU and euro area levels using all possible levers, instruments and policies. They decided on

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<sup>1</sup> OJ L 209, 2.8.1997, p. 1.

<sup>2</sup> COM(2014) 424 final.

<sup>3</sup> P7\_TA(2014)0128 and P7\_TA(2014)0129.

action to be taken at the level of the Member States, in particular expressing full commitment to achieving the objectives of the Europe 2020 Strategy and to implementing the country-specific recommendations.

- (4) On 9 July 2013, the Council adopted a recommendation on Romania's 2013 national reform programme and delivered its opinion on Romania's 2013 convergence programme for 2012-2016.
- (5) On 13 November 2013, the Commission adopted the Annual Growth Survey<sup>4</sup>, marking the start of the 2014 European Semester of economic policy coordination. On the same day on the basis of Regulation (EU) No 1176/2011, the Commission adopted the Alert Mechanism Report<sup>5</sup>.
- (6) On 20 December 2013, the European Council endorsed the priorities for ensuring financial stability, fiscal consolidation and action to foster growth. It underscored the need to pursue differentiated, growth-friendly fiscal consolidation, to restore normal lending conditions to the economy, to promote growth and competitiveness, to tackle unemployment and the social consequences of the crisis, and to modernise public administration.
- (7) On 6 May 2014, Romania submitted its 2014 national reform programme and on 5 May 2014 its 2014 convergence programme. In order to take account of their interlinkages, the two programmes have been assessed at the same time.
- (8) On 22 October 2013, the Council adopted Decision 2013/531/EU providing medium-term financial assistance to Romania of up to EUR 2 billion until September 2015. Precautionary medium-term financial assistance for Romania under the balance-of-payments facility for non euro-area Member States was considered appropriate due to unstable capital flows affecting in particular emerging markets, risks to the macroeconomic scenario, and remaining vulnerabilities in the banking sector. While, under present market conditions, Romania does not intend to request the disbursement of any instalment, the precautionary assistance is expected to help consolidate macroeconomic, budgetary and financial stability and, through the pursuit of structural reforms, to increase the resilience and the growth potential of the Romanian economy. The Memorandum of Understanding of 6 November 2013 and its subsequent supplements laying down the conditions to be fulfilled under the EU precautionary assistance complement and support the country-specific recommendations of the European Semester. The EU precautionary assistance will be conditional upon the implementation of a comprehensive economic policy programme, with a particular focus on structural reform measures including those country-specific recommendations relating to administrative capacity, product market reforms, the business environment, labour markets, pensions, state-owned enterprises, and healthcare. This agenda does not exempt the Romanian government from fully implementing all the country-specific recommendations. The policy prioritisation, implementation and coordination necessary for implementing the Memorandum of Understanding and the country specific recommendations, should be dealt with where priority decisions are made, in a coherent way.
- (9) The objective of the budgetary strategy outlined in the 2014 Convergence Programme is to achieve the medium-term objective of a structural deficit of 1% of GDP in 2015, which reflects the requirement of the Stability and Growth Pact, and to

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<sup>4</sup> COM(2013) 800 final.

<sup>5</sup> COM(2013) 790 final.

remain at it thereafter. Romania is benefitting in 2014 from the possibility of a temporary deviation from the adjustment path towards the medium-term objective allowed for jointly financed projects. The temporary deviation has to be compensated in the following year. The programme plans a stabilisation of the (recalculated) structural balance in 2014 and an improvement of 0.8% of GDP in 2015. Expenditure is forecast to grow at a pace consistent with the expenditure benchmark in both 2014 and 2015. The debt to GDP ratio is forecast to reach 40% in 2015, and to decrease in 2016-2017. Overall, the budgetary strategy outlined in the programme is in line with the requirements of the Stability and Growth Pact. The macroeconomic scenario underpinning the budgetary projections is plausible. It is broadly in line with the Commission 2014 spring forecast. However the potential GDP estimate underlying the Convergence Programme is slightly higher, mainly on account of a more optimistic labour market outlook. There are downside risks to the 2014 budgetary plans related to expenditure control and lower-than-envisaged tax collection. Moreover, for 2015 and beyond, the measures underpinning the proposed fiscal path are not yet specified. According to the Commission forecast, despite a small deterioration in the structural balance in 2014, Romania is compliant with the Stability and Growth Pact requirements in 2014, taking into account the temporary deviation allowed for jointly financed projects. For 2015, there is a risk of a significant deviation from the required structural adjustment, taking into account the necessary compensation for the temporary deviation allowed for jointly financed projects). Moreover, Romania is forecast to deviate from the expenditure benchmark in 2015. Based on its assessment of the programme and the Commission forecast, pursuant to Council Regulation (EC) No 1466/97, the Council is of the opinion that the programme presents risks of a significant deviation from the requirements of the preventive arm in 2015.

- (10) Tax fraud and tax avoidance in the areas of VAT, including cross-border schemes, excises, social security contributions and income taxation remain a major challenge. Tangible progress in fighting undeclared work is limited, while the effectiveness of the tax compliance strategy is hampered by the lack of realistic and binding implementation measures and insufficient focus on prevention. A reform of the tax administration to increase its efficiency is ongoing; cross-border administrative cooperation, in particular in the VAT area, remains weak. The tax wedge on low and middle-income wage earners remains high and encourages undeclared work and under-declared earnings. There has been some progress in the field of environmental taxation, as the vehicle taxation system was improved and excise duties on fuel were increased and are now automatically indexed. Romania faces long-term sustainability risks, mainly due to age-related expenditure. There are concerns as regards the sustainability and adequacy of the pension system due to the low ratio of employed contributors to people drawing pensions. Romania has taken steps to equalise the pensionable age for women and men as of 2035.
- (11) Inefficient use of resources and poor management increase the fiscal sustainability risk in the health sector. Widespread informal payments in the public healthcare further hinder the accessibility, efficiency and quality of the system. Reforms to improve the efficiency of the healthcare sector and its financial sustainability have begun but continuous efforts are needed. Some of the measures are incurring delays and suffer from insufficient funding and the services' low capacity. Reducing the excessive use of hospital in-patient care and strengthening primary care and referral systems will increase cost-effectiveness. Further reforms of the healthcare system

aimed at improving the health of the population by promoting, among other things, equitable access to quality health services has been launched.

- (12) High inactivity, insufficient utilisation of labour potential and the need to increase the quality and productivity of the work force remain key challenges of the Romanian labour market. The quality of public job search and retraining services is still low, despite some small-scale measures. Limited resources within the public employment service and a lack of measurement of performance constrain the efficient delivery of personalised services to jobseekers, employer services and the integration of active and passive labour market policies. Romania has a high and increasing percentage of young people not in employment, education or training (17.3% in 2013). A national Active Ageing Strategy to support an increase in the employment rate of older workers has been delayed and now is due by the end of 2014.
- (13) There is no transparent guideline for minimum wage setting involving social partners aiming at supporting employment and competitiveness and safeguarding labour income in a sustainable way.
- (14) The Education Reform of 2011, which set a long-term agenda for upgrading the quality of education at all levels, is not yet fully operational, due to insufficient financial and human resources. Following sharp decline in vocational education and training in the last twenty years, several reforms and pilot projects have been initiated in recent years but the availability of vocational education and training, its relevance to the labour market and business involvement in work-based learning and apprenticeships remains low. Important skills mismatches persist for tertiary graduates and the link between business and academia remains weak, as shown by a high unemployment rate and many university graduates being employed either in professions not corresponding to their training or in jobs requiring lower levels of qualification. Participation in lifelong learning activities continues to be among the lowest in the EU. The early school leaving rate continues to be one of the highest in the EU and is now higher than prior to 2010, affecting in particular Roma. Female employment is hindered by low provision of and limited access to affordable quality childcare facilities, in particular for the 0-3 years old.
- (15) Poverty reduction remains a major challenge. , Despite the relatively stable employment situation, gross household incomes have been declining and income inequalities have been growing. Families with children are particularly exposed. There was only limited progress in speeding up the transition from institutional to alternative care for children deprived of parental care. There is still a high number of persons with disabilities in large residential institutions, while community services for the disabled are not sufficiently developed.. The low take-up, coverage and adequacy of social benefits remain a challenge for the efficiency of social benefits in reducing poverty. The introduction of the Minimum Insertion Income combining three existing social benefits (the Guaranteed Minimum Income, the family allowance and the heating benefits)planned for 2015 has been delayed. The implementation of the National Roma Integration Strategy started in 2012, but financial allocation for the implementation of key action plans was insufficient and the results are modest. The revision of the Strategy and the implementation of the revised action plans are delayed.
- (16) The weak capacity of the public administration to develop and implement policies remains a core challenge for Romania, hampering overall development of the

country, the business environment and the capacity for public investment, while not allowing for the provision of public services of sufficient quality. The structural causes that led to a low administrative capacity were analysed in 2013. Based on this, a 2014-20 strategy on strengthening public administration is currently under preparation and is expected to be finalised by mid-2014.

- (17) Despite important progress, the absorption rate for EU funds remains one of the lowest in the EU. Continuously weak management and control systems and public procurement practices may negatively impact the preparations for and implementation of the next generation of programmes. Public procurement legislation suffers from instability and a lack of coherence. The institutional set-up, with multiple actors and frequently overlapping responsibilities is not equipped to tackle the shortcomings and provide appropriate guidance to contracting authorities. Corruption and conflicts of interests continue to be concerns for contracting authorities. A system for ex-ante checks for conflicts of interest in the award process of public procurement contracts is expected to become operational by the end of 2014.
- (18) Poor quality of regulations and the lack of transparency and predictability of the regulatory framework hinder businesses and citizens. Procedures for obtaining electricity, dealing with construction permits and paying taxes are still complex. Unclear land ownership rights represent a further challenge for Romania's business environment; less than 50 % of real estate are recorded in the land book system and only around 15 % of real estate records are verified and registered digitally. Romania has made some progress in improving the quality, independence and efficiency of the Romanian justice system and in the fight against corruption, but these issues remain a concern for businesses seeking effective redress. Resistance to integrity and anti-corruption measures at political and administrative levels is still strong.
- (19) Price regulation in the electricity market for industrial customers ended in 2013 and phasing-out of gas and electricity price regulation is ongoing. Efficiency and transparency of governance of the state-owned enterprises in these sectors represent a major challenge. Energy price deregulation is expected to bring incentives to enhance energy efficiency, although concrete measures and resource commitments are needed to further improve energy efficiency in the housing, district heating, industry and urban transport sectors. The integration of Romania's electricity and gas markets in the EU markets remains incomplete and substantial barriers remain for the implementation of cross-border connections for gas, which would contribute to enhancing diversification of supply.
- (20) The underdeveloped basic transport infrastructure continues to be a bottleneck to growth in Romania. High growth of the vehicle fleet and the low quality of the road infrastructure hamper businesses and the economy. Poor maintenance of the railway network has affected safety and reliability. Freight transport on inland waterways remains far below its potential, particularly on the Danube. The inefficiency and untransparent governance of state-owned enterprises in the transport sector hinder the development of network infrastructures.
- (21) In the context of the European Semester, the Commission has carried out a comprehensive analysis of Romania's economic policy. It has assessed the convergence programme and the national reform programme. It has taken into account not only their relevance for sustainable fiscal and socio-economic policy in Romania but also their compliance with EU rules and guidance, given the need to

reinforce the overall economic governance of the European Union by providing EU-level input into future national decisions. Its recommendations under the European Semester are reflected in recommendations (1) to (8) below.

- (22) In the light of this assessment, the Council has examined Romania's convergence programme, and its opinion<sup>6</sup> is reflected in particular in recommendation (2) below.

HEREBY RECOMMENDS that Romania take action within the period 2014-2015 to:

1. Implement the EU/IMF financial assistance programme by fully addressing the policy conditionality included in the Memorandum of Understanding of 6 November 2013 and its subsequent supplements that complements and supports the implementation of these country specific recommendations.
2. Implement the budgetary strategy for 2014, significantly strengthen the budgetary effort to ensure reaching the medium-term objective in 2015 in line with commitments under the Balance of Payments programme and as reflected in the 2014 convergence programme, in particular by specifying the underlying measures, and remain at the medium-term objective thereafter. Improve tax collection by continuing to implement a comprehensive tax compliance strategy, stepping up efforts to reduce VAT fraud. Fight undeclared work. Reduce tax burden for low- and middle-income earners in a budget-neutral way. Finalise the pension reform started in 2010 by equalising the pensionable age for men and women.
3. Step up reforms in the health sector to increase its efficiency, quality and accessibility, including for disadvantaged people and remote and isolated communities. Increase efforts to curb informal payments, including through proper management and control systems.
4. Strengthen active labour-market measures and the capacity of the National Employment Agency. Pay particular attention to the activation of unregistered young people. Strengthen measures to promote the employability of older workers. Establish, in consultation with social partners, clear guidelines for transparent minimum wage setting, taking into account economic and labour market conditions.
5. Increase the quality and access to vocational education and training, apprenticeships, tertiary education and of lifelong learning and adapt them to labour market needs. Ensure better access to early childhood education and care.
6. In order to alleviate poverty, increase the efficiency and effectiveness of social transfers, particularly for children, and continue reform of social assistance, strengthening its links with activation measures. Step up efforts to implement the envisaged measures to favour the integration of Roma in the labour market, increase school attendance and reduce early school leaving, through a partnership approach and a robust monitoring mechanism.
7. Step up efforts to strengthen the capacity of public administration, in particular by improving efficiency, human resource management, the decision-making tools and coordination within and between different levels of government; and by improving transparency, integrity and accountability. Accelerate the absorption of EU funds, strengthen management and control systems, and improve capacity for strategic planning, including the multi-annual budgetary element. Tackle persisting shortcomings in public procurement. Continue to improve the quality and efficiency

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<sup>6</sup> Under Article 9(2) of Council Regulation (EC) No 1466/97.

of the judicial system, fight corruption at all levels, and ensure the effective implementation of court decisions.

8. Promote competition and efficiency in energy and transport industries. Accelerate the corporate governance reform of state-owned enterprises in the energy and transport sectors and increase their efficiency. Improve and streamline energy efficiency policies. Improve the cross-border integration of energy networks and enable physical reverse flows in gas interconnections as a matter of priority.

Done at Brussels,

*For the Council*  
*The President*