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Recommendation for a

COUNCIL RECOMMENDATION

on Bulgaria's 2012 national reform programme

and delivering a Council opinion on Bulgaria's convergence programme for 2012-2015

{SWD(2012) 302 final}

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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[1], and in particular Article 5(2) thereof,

Having regard to Regulation (EU) No 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances[2], and in particular Article 6(1) thereof,

Having regard to the recommendation of the European Commission[3],

Having regard to the resolutions of the European Parliament,[4]

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

After consulting the Economic and Financial Committee,

Whereas:

(1) On 26 March 2010, the European Council agreed to the European Commission's proposal to launch a new strategy for jobs and growth, 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 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

[1] OJ L 209, 02.08.1997, p. 1
[2] OJ L 306, 23.11.2011, p. 25
[3] COM(2012)302 final
[4] P7_TA(2012)0048 and P7_TA(2012)0047

Member States[5], 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 12 July 2011, the Council adopted a recommendation on Bulgaria's national reform programme for 2011 and delivered its opinion on Bulgaria's updated convergence programme for 2011-2014.

(4) On 23 November 2011, the Commission adopted the second Annual Growth Survey, marking the start of the second European Semester of ex-ante and integrated policy coordination, which is anchored in the Europe 2020 strategy. On 14 February 2012, the Commission, on the basis of Regulation (EU) No 1176/2011, adopted the Alert Mechanism Report[6], in which it identified Bulgaria as one of the Member States for which an in-depth review would be carried out.

(5) On 2 March 2012, the European Council endorsed the priorities for ensuring financial stability, fiscal consolidation and action to foster growth (in line with the Council's conclusions of 9 December 2011 and further to the Commission's Annual Growth Survey). 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.

(6) On 2 March 2012, the European Council also invited the Member States participating in the Euro Plus Pact to present their commitments in time for inclusion in their stability or convergence programmes and their national reform programmes.

(7) On 13 April 2012, Bulgaria submitted its convergence programme covering the period 2012-2015 and its 2012 national reform programme. In order to take account of their interlinkages, the two programmes have been assessed at the same time. The Commission has also assessed, in an in-depth review under Article 5 of Regulation (EU) No 1176/2011, whether Bulgaria is affected by macroeconomic imbalances. The Commission concluded in its in-depth review[7] that Bulgaria is experiencing an internal macroeconomic imbalance, although not excessive.

(8) According to the first 2012 notification of deficit and debt figures by Bulgaria for the years 2008-2011 for the application of the excessive deficit procedure (EDP), the general government deficit in 2011 was below the 3% of GDP reference value of the Treaty. Moreover, the Commission's 2012 spring forecast projects the general government deficit to stay below the reference value of the Treaty and to further decline over the forecast period. As a result, and in line with the provisions of the Stability and Growth Pact, on 30 May the Commission adopted a recommendation for a Council decision abrogating the decision on the existence of an excessive deficit under Article 126(12) of the Treaty.

(9) Based on the assessment of the 2012 convergence programme pursuant to Council Regulation (EC) No 1466/97, the Council is of the opinion that the macroeconomic

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5 Council Decision 2012/238/EU of 26 April 2012

6 COM(2012) 68 final

7 SWD(2012)151 final

scenario underpinning the budgetary projections in the programme is optimistic for the 2012-13 period, when annual growth is expected to reach 1.4% in 2012 and 2.5% in 2013. The Commission's 2012 spring forecast foresees a GDP growth of 0.5% in 2012 and 1.9% in 2013. After the correction of the excessive deficit in 2011, the objective of the budgetary strategy outlined in the programme is to achieve a budgetary position which is close to balance, both in terms of the structual and headline budget balances, by the end of the programme period. The medium-term budgetary objective (MTO), defined in structural terms, has been marginally revised from a deficit of 0.6% of GDP to a deficit of 0.5% of GDP. The new MTO adequately reflects the requirements of the Stability and Growth Pact. Based on the (recalculated) structural deficit[8], Bulgaria plans to achieve its MTO over the programme period. . In 2012-14, the growth rate of government expenditure, taking into account discretionary revenue measures, would respect the expenditure benchmark of the Stability and Growth Pact, yet breach it in 2015. Panned fiscal consolidation faces important risks stemming from (i) lower revenue given the optimistic macroeconomic scenario as well as less tax-rich underlying growth structure of the economy and (ii) inefficiencies in the public sector, particularly in healthcare and education, which may lead to considerable expenditure pressures. The debt ratio is below 60% of GDP and, according to the programme, it is expected to peak at close to 20% of GDP in 2012 and then to decrease over the programme period. There is considerable scope for improvement in tax compliance and advancing in this area would allow Bulgaria to support higher growth enhancing expenditures. A requirement to keep the budget deficit below 2 % and limiting government expenditure to 40 % of GDP was adopted as an amendment to the Organic Budget Law, thus strengthening the binding nature of the fiscal framework and improving the predictability of budgetary planning. However, challenges remain with respect to further improving the contents of the medium-term budgetary framework and strengthening the reporting on accrual basis.

(10) The Bulgarian government has made considerable progress on some of the pension-reform measures including those on the pensionable age for both men and women and on the length of service for army and police-sector employees. However, addressing the shortcomings in the adequacy of pension provision remains a key challenge in the medium term. The changes do not envisage steps to make the statutory retirement age the same for men and women. Also, they fall short in reducing early retirement options for employees. A key challenge remains the inclusion of people not paying contributions, as well as tightening controls and criteria for the allocation of invalidity pensions.

(11) Bulgaria has the highest rate of people at risk of severe material deprivation in the EU, with the elderly and children being particularly affected. Comprehensive measures are needed. Priority should be given to making social transfers more effective. Only half of the economically active Roma are employed. The recently adopted National Strategy for Roma Integration targets multiple barriers but still needs to be underpinned by a detailed Action Plan if it is to be operational over the period 2015-2020.

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[8] Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission services on the basis of the information provided in the programme, using the commonly agreed methodology.

(12) The crisis has had a particularly strong impact on low-skilled workers (who account for almost 70 % of the unemployed) and has significantly raised youth unemployment. Moreover, since 2009, the increase in long-term unemployment has been significantly faster than in the rest of EU and principally reflecting an increase in skills and geographical mismatches as job cuts were concentrated in the low-skilled segment. A review of the system setting minimum thresholds for social security contributions should be undertaken to balance the need to reduce undeclared work and to ensure that low-skilled workers are not priced out. Measures undertaken by the government to freeze public sector wage bill in 2010-12 have been a relevant and adequate response, also contributing to bring labour costs closer to productivity levels. A national initiative has been launched to comprehensively address the integration of young people in the labour market. Public employment services are still of relatively low quality and staff training should be intensified, in particular "Roma mediators". Further measures are needed to improve services dealing with activation, job search, matching, retraining and individualised services for the low-skilled.

(13) Bulgaria has the highest share of low achievers in reading and in mathematics and science in the EU (according to PISA 2009), indicating the existence of considerable structural obstacles to ensuring quality education. The low educational achievements are linked to weak access to education of disadvantaged groups, in particular the Roma population, insufficient autonomy of schools, lack of incentives for better performance, a poor national assessment system and insufficient accountability. In higher education, progress remains very limited even though some promising efforts have been made recently. The planned amendments to the Higher Education Act need to be implemented as a top priority for growth and accompanied by adequate governance, investment and political determination.

(14) Bulgaria has a low level of research and innovation. Research and innovation (R&I) investment needs to be raised to reach the 2020 target and an appropriate strategy for innovation must be established. The R&I administration in Bulgaria is fragmented. Bulgaria needs to strengthen its universities and develop a strategy to engage higher education institutions in innovation activities. Frameworks fostering collaboration between universities and the private sector do not exist, and funding should be allocated in a competitive, merit-based and transparent way. Bottlenecks remain for start-up companies and innovative SMEs seeking bank finance. Public financial instruments and guarantees for young and innovative enterprises are not effective enough to help SMEs match EU Structural Funds and secure the required co-financing via bank loans.

(15) Currently, the administrative capacity of Bulgaria is insufficient to properly manage and maintain road, rail and water infrastructures projects. The administrative reform has focused mainly on reducing public sector staff with limited attempts to remove other sources of inefficiency. The use of EU funds remains low despite consistent progress in the last two years. The main reasons are the existence of complicated administrative procedures and the difficulty encountered by enterprises in securing co-financing. Significant challenges also remain in terms of further improving the business and regulatory environment and achieving progress in increasing the administrative capacity of the public sector. The implementation of e-government has been delayed many times. The tax system in Bulgaria is characterised by significant tax evasion and low administrative efficiency. Administrative costs for tax collection are high, as are the time costs for businesses of paying taxes.

(16) The new legislation on public procurement is an important step towards a better system for the monitoring, prevention and sanctioning of irregularities. These efforts should be supplemented on two fronts: (i) the sanctions foreseen need to be effectively applied and (ii) ex officio powers should be entrusted to the Public Procurement Agency and the State Financial Inspection Agency.

(17) Despite initiated reforms, Bulgaria still maintains some restrictions to entry into network sectors such as rail transport, telecommunications and energy. The functioning of energy markets at both wholesale and retail levels remains problematic. Areas of particular concern in need of improvement include the lack of electricity and gas exchanges and of a functioning balancing market as well as regulated prices for consumers. Moreover, Bulgaria should ensure regulatory independence for the transmission system. Bulgaria is highly dependent on a single energy route and its domestic energy market functions inadequately, exposing it to risks of significant supply shocks. Existing measures aimed at tackling energy dependency need to be improved. So far, the construction of new gas infrastructure has been too slow. Although some desirable reforms were formally adopted and the share of renewable energy increased in 2011, their implementation remains unsatisfactory due to procurement, the capture of public polices by private interests and poor management of state-owned energy companies.

(18) Bulgaria has made a number of commitments under the Euro Plus Pact. These commitments, and the implementation of the commitments presented in 2011, relate to improved public finance sustainability, fostering employment, boosting public-sector competitiveness and reinforcing financial stability. The Commission has assessed the implementation of the Euro Plus Pact commitments. The results of this assessment have been taken into account in the recommendations.

(19) In the context of the European Semester, the Commission has carried out a comprehensive analysis of Bulgaria's economic policy. It has assessed the convergence programme and national reform programme, and presented an in-depth review. It has taken into account not only their relevance for sustainable fiscal and socio-economic policy in Bulgaria 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 (7) below.

(20) In the light of this assessment, the Council has examined Bulgaria's convergence programme, and its opinion[9] is reflected in particular in recommendation (1) below.

(21) In the light of the Commission's in-depth review and this assessment, the Council has examined Bulgaria's 2012 national reform programme and Bulgaria's convergence programme. Its recommendations under Article 6 of Regulation (EU) No 1176/2011 are reflected in particular in recommendations (3) and (5) below;

[9] Under Article 9(2) of Council Regulation (EC) No 1466/97.

HEREBY RECOMMENDS that Bulgaria should take action within the period 2012-2013 to:

1. Continue with sound fiscal policies to achieve the medium-term budgetary objective by 2012. To this end, implement the budgetary strategy as envisaged, ensuring compliance with the expenditure benchmark, and stand ready to take additional measures in case risks to the budgetary scenario materialise. Strengthen efforts to enhance the quality of public spending, particularly in the education and health sectors and implement a comprehensive tax-compliance strategy to improve tax revenue and address the shadow economy. Further improve the contents of the medium-term budgetary framework and the quality of the reporting system.

2. Take steps to reduce risks to the sustainability and to improve adequacy of the pension system by restricting access to early retirement and by making the statutory retirement age the same for men and women with full career contributions. Introduce tighter criteria and controls for the allocation of invalidity pensions.

3. Accelerate the implementation of the national Youth Employment Initiative. Ensure that the minimum thresholds for social security contributions do not discourage declared work. Step up efforts to improve the Public Employment Service's performance. To alleviate poverty, improve the effectiveness of social transfers and the access to quality social services for children and the elderly and implement the National Roma Inclusion Strategy.

4. Speed up the reform of relevant legal acts on schools and higher education and of accompanying measures by focusing on modernising curricula, improving teacher training, and ensuring access to education for disadvantaged groups. Improve the access to finance for start-ups and SMEs, in particular those involved in innovative activities.

5. Step up efforts to enhance administrative capacity and reforms by reducing red tape and the cost of tax compliance and collection, and further improving the absorption of EU funds, in particular in road and rail transport and water management. Improve the quality and independence of the judicial system and speed up the introduction of e-government. Strengthen public administrative capacity in key transport sectors and regulatory authorities.

6. Ensure sound implementation of public procurement legislation. Strengthen the prevention of irregularities and effectively apply the sanctions under the Public Procurement Law and those of the Law on Conflict of Interest.

7. Take measures to remove market barriers, guaranteed profit arrangements and price controls. Ensure the independence of transmission and distribution system operators; complete the market design in particular for the energy exchanges and balancing markets. Improve electricity and gas connections, boost energy efficiency and enhance the capacity to cope with disruptions.

Done at Brussels,

For the Council
The President