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Subject:	Recommendation for a COUNCIL RECOMMENDATION on the 2016 national reform programme of Spain and delivering a Council opinion on the 2016 stability programme of Spain

Delegations will find attached the above mentioned draft Council Recommendation, as revised and agreed by various Council committees, based on the Commission proposal COM(2016) 329 final.

COUNCIL RECOMMENDATION

of …

on the 2016 National Reform Programme of Spain

and delivering a Council opinion on the 2016 Stability Programme of Spain

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,

Having regard to the resolutions of the European Parliament,

Having regard to the conclusions of the European Council,

[1] OJ L 209, 2.8.1997, p. 1.
[2] OJ L 306, 23.11.2011, p. 25.

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 November 2015, the Commission adopted the Annual Growth Survey, marking the start of the 2016 European Semester for economic policy coordination. The priorities of the Annual Growth Survey were endorsed by the European Council on 17-18 March 2016. On 26 November 2015, on the basis of Regulation (EU) No 1176/2011, the Commission adopted the Alert Mechanism Report, in which it identified Spain as one of the Member States for which an in-depth review would be carried out. On the same day, the Commission also adopted a recommendation for a Council Recommendation on the economic policy of the euro area. This Recommendation was endorsed by the European Council on 18-19 February 2016 and adopted by the Council on 8 March 2016[3]. As a country whose currency is the euro and in view of the close interlinkages between the economies in the economic and monetary union, Spain should ensure the full and timely implementation of the Recommendation.

[3] OJ C 96, 11.3.2016, p. 1.

(2) The 2016 country report for Spain was published on 26 February 2016. It assessed Spain's progress in addressing the country-specific recommendations adopted by the Council on 14 July 2015 and Spain's progress towards its national Europe 2020 targets. It also included the in-depth review under Article 5 of Regulation (EU) No 1176/2011. On 8 March 2016, the Commission presented the results of the in-depth review. The Commission analysis leads it to conclude that Spain is experiencing macroeconomic imbalances. In particular, high external and internal debt, both public and private, continue to constitute vulnerabilities in a context of high unemployment. The need for action to reduce the risk of adverse effects on the Spanish economy and, given its size, of negative spillovers to the economic and monetary union, is important. Despite improvement in the current account balance, net external liabilities are not projected to reach prudent levels in the short term. Private sector deleveraging is on track, supported partly by favourable growth conditions, but deleveraging needs are large and public debt remains high. Measures have been taken in the financial sector and in corporate and personal insolvency frameworks, but further action is needed on innovation and skills and on compliance with the Stability and Growth Pact.

(3) On 29 April 2016, Spain submitted its 2016 National Reform Programme and on 30 April 2016 it submitted its 2016 Stability Programme. In order to take account of their interlinkages, the two programmes have been assessed at the same time.

(4) Relevant country-specific recommendations have been addressed in the programming of the European Structural and Investment Funds for the 2014-2020 period. As foreseen in Article 23 of Regulation (EU) No 1303/2013 of the European Parliament and of the Council[4], where it is necessary to support the implementation of relevant Council recommendations, the Commission may request a Member State to review and propose amendments to its Partnership Agreement and relevant programmes. The Commission has provided further details on how it would make use of this provision in guidelines on the application of the measures linking effectiveness of the European Structural and Investment Funds to sound economic governance.

[4] Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006 (OJ L 347, 20.12.2013, p. 320).

(5) [Spain is currently in the corrective arm of the Stability and Growth Pact. In its 2016 Stability Programme, Spain plans to achieve headline deficit targets of 3,6 % of GDP in 2016 and 2,9 % of GDP in 2017. The excessive deficit is thus planned to be corrected one year later than currently recommended by the Council, the fiscal effort and headline targets having been missed in 2014 and 2015. These targets assume the full implementation of 0,4 % of GDP in permanent savings at central and regional government level announced in response to the Autonomous Commission recommendation of 9 March 2016. The deficit is planned to continue declining thereafter, to 1,6 % of GDP in 2019. However, the medium-term objective of a balanced budgetary position in structural terms is not planned to be reached within the time horizon of the Stability Programme. In particular, the recalculated structural balance is projected to improve only marginally in 2016 and 2017 to around -2½ % of GDP, and decline slowly to reach -2¾ % of GDP in 2019. The government debt-to-GDP ratio declined only marginally in 2015 to 99,2 % of GDP and is expected to decline slightly in 2016 and 2017 and more decisively in the following two years, to 96 % of GDP in 2019, as the primary balance turns into a surplus. The macroeconomic scenario underpinning these budgetary projections is plausible for 2016 and 2017 and somewhat optimistic thereafter; it has been endorsed by Spain's Independent Fiscal Institution (AIReF). The Commission 2016 spring forecast projects the deficit at 3,9 % of GDP in 2016 and 3,1 % of GDP in 2017, above the headline targets in the Stability Programme. Spain is thus not projected to correct the excessive deficit by 2016 as recommended by the Council. Risks to the deficit targets in the programme largely stem from uncertainties surrounding the implementation of the savings from the March/April 2016 measures. As the structural deficit is projected to slightly increase in both years, the fiscal effort is not in line with the requirements of the Stability and Growth Pact. Based on its assessment of the Stability Programme and taking into account the Commission's 2016 spring forecast, the Council is of the opinion that there is a risk that Spain will not comply with the provisions of the Stability and Growth Pact. Therefore, further measures are needed to ensure compliance in 2016 and 2017.

(6) Pursuant to Article 10(1) of Council Regulation (EC) No 1467/97[5], the Commission will regularly monitor the implementation of action taken by Spain in response to the last recommendation made by the Council under Article 126(7) TFEU: the Commission will therefore recommend to the Council the appropriate steps to be taken in the framework of the excessive deficit procedure.**]**

(7) Since 2012, Spain's fiscal framework has been strengthened in order to, among other things, prevent deviations and ensure compliance by all government levels with their respective deficit, debt and expenditure targets. In addition, a rule for application (on a voluntary basis and, in 2016, made compulsory for most regions) at regional level was approved in mid-2015 to limit growth in expenditure on healthcare and pharmaceutical products, and an agreement between the Government and the pharmaceutical industry was signed in November 2015 to help rationalise spending on pharmaceuticals. Despite this, in 2015, most regions as well as the social security sector fell significantly short of meeting their domestic fiscal targets. The stability law's expenditure rule was not observed by the central, regional and local government subsectors and growth in expenditure of pharmaceutical products, namely in hospitals, strengthened further, even excluding the impact of new anti-hepatitis C treatments.

(8) In the field of public procurement, Spain performs well concerning the quality of the legislation and the availability of review procedures. Efforts have been made to rationalise public purchasing, in particular via joint procurement mechanisms. However, there are disparities in the implementation of public procurement across administrations and insufficient control mechanisms hinder the correct application of public procurement rules. The number of presumed breaches of EU public procurement legislation brought to the Commission’s attention in recent years has been relatively high. Furthermore, the Spanish Court of Auditors has pointed to some weaknesses such as the frequent use of the negotiated procedure without publication, the repeated modification of contracts, the splitting of contracts into smaller ones and the insufficient precision and clarity of some tender documents and administrative decisions.

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5 Council Regulation (EC) No 1467/97 of 7 July 1997 on speeding up and clarifying the implementation of the excessive deficit procedure (OJ L 209 , 02.08.1997, p. 6).

(9) Spain has made substantial progress in restructuring the financial sector. The law on savings banks to strengthen their governance and reduce controlling stakes held by banking foundations has been implemented. The implementation of plans for restructuring state-aided banks is well advanced. The Bank of Spain has amended the existing accounting regime for credit institutions and adopted a new framework for SAREB, the Spanish asset management company. The new framework will allow SAREB to achieve a proper treatment of impairments and help in adapting its deleveraging policies to credible market assumptions.

(10) Labour market reforms undertaken in recent years have made employment more responsive to growth and job creation has resumed, supported by increased flexibility and continued wage moderation. Collective agreements have been supportive of this trend, also owing to the inter-professional agreement signed in June 2015. The recent increase in overall employment has been driven mainly by temporary contracts, although the number of newly signed open-ended contracts is slowly rising. However, the take-up of incentives for new permanent hiring remains limited, and the proportion of temporary workers remains one of the highest in the Union, while the opportunities for temporary workers to move to a permanent contract remain low. The short duration of temporary contracts limits incentives to invest in human capital, hampering productivity growth. Although decreasing rapidly, unemployment remains very high, in particular among young people and its average duration is also very high. Persistently high long-term unemployment implies that unemployment risks becoming entrenched, negatively affecting working and social conditions. Nearly 60 % of the long-term unemployed are low-skilled, which calls for appropriate active and passive labour market and training policies to tackle pervasive skills mismatches and prevent skills depreciation among this group. Interaction with employers in the design of training programmes is still weak..

(11) The effectiveness of activation and active labour market measures depends heavily on the capacity of employment services to design and offer individualised support to beneficiaries. The implementation of recent reforms of active labour market policies is progressing slowly and the capacity of the public employment services to provide effective, individualised counselling and job search assistance is still limited. Cooperation between the regional public employment services and private placement agencies remains limited. Moreover, cooperation between employment and social services is uneven across regions, hampering the provision of coordinated assistance for those further away from the labour market, in particular minimum income beneficiaries. There are significant disparities across regions as regards income support schemes, for example in delivery arrangements, eligibility requirements, coverage and adequacy, while difficulties in transferring social benefits hamper inter-regional job mobility. In addition, information about the transition to employment from minimum income schemes is quite limited. Spain is currently preparing a map of national and regional income support schemes in the country, covering national and regional levels. While some measures have been introduced, the effectiveness of family and housing benefits in reducing poverty remains limited, and the lack of adequate and affordable child care and long-term care provision discourages women, in particular, from taking up a job.

(12) The increasingly rapid change in the sectoral composition of employment that Spain has been witnessing since 2008 has been accompanied by an increase in skills mismatches. The low overall skills level constrains the transition towards higher value-added activities and hampers productivity growth. Despite a high level of tertiary education attainment, skills supply is not sufficiently aligned with labour market needs and employability rates for recent tertiary graduates are among the lowest in Europe, with a significant proportion employed in jobs that do not require a university degree. Furthermore, despite a slight improvement over the past five years, partly supported by initiatives to increase business representation on university governing boards, cooperation between universities and businesses remains weak. The reduced mobility of academics, the rigidity of the university governance system and the administrative barriers faced by the Offices for the Transfer of Research outcomes (*Oficinas de transferencia de resultados de investigación*) compound obstacles to closer cooperation.

(13) Research and innovation policy in Spain faces several challenges. Interaction between public and private research is weak. Spain's R&D intensity (spending on R&D relative to GDP) and innovation performance keeps declining, against the backdrop of a relatively low number of innovative firms and limited incentives for collaboration between public research and business. Spain underperforms in respect of most business innovation indicators. The gap on spending on R&D intensity compared to the Union as a whole is especially significant as regards investment in R&D by the private sector (0,6 % in Spain compared to 1,3 % in the Union as a whole). Venture capital is still not widely used in Spain, in particular at seed stage. Weak coordination of R&I policies in Spain and a fragmented regional landscape of bodies and programmes to promote innovation activities and foster science-business cooperation create significant challenges for businesses, especially for smaller firms. Low business involvement in innovation activities could point to a lack of absorptive capacity, innovation-friendly framework conditions and incentives. As highlighted in the 2014 ERAC (European Research Area Committee) Peer Review of the Spanish Research and Innovation System, most successful public research systems are driven by higher degrees of evaluation and accountability than are found in Spain. In this context, the allocation of public institutional funding for universities and public research bodies is usually not based on R&I performance, thus reducing the incentives to improve the quality and relevance of scientific outputs.

(14) The small average size of Spanish firms helps explain the economy's persistently low productivity. Firm growth, combined with improvements in human capital, innovation, technology, access to finance and efficient justice could spur aggregate productivity. In 2015, business investment strengthened, underpinned by dynamic demand conditions, low borrowing costs and ongoing balance sheet repair by the corporate sector and households. Spain has taken various measures to ease business growth. For example, a recent law on business financing is expected to facilitate access to finance for small and medium-sized enterprises (SMEs). Furthermore, prior assessment of the potential impact of new legislation on SMEs has now become compulsory. However, the time and number of permits required for starting up a business and launching certain economic activities remains relatively high.

(15) Spain's considerable differences across regions in regulatory practices, including on business licencing, may limit firms' capacity to grow. The law on market unity aims to reduce barriers to access to and the exercise of economic activities across Spanish regions and to improve regulation. It could potentially have a significant impact on removing barriers to investment and facilitate business licensing, business operations and company growth. The implementation of the law on market unity requires full involvement of all administrations. However, in its third year of application, it is being implemented slowly by regional governments. Likewise, the benefits of the retail sector reform of 2014 depend on regional governments adopting the necessary implementing acts. Furthermore, tackling obstacles to access to the professional services sector is likely to improve productivity in other sectors that use those inputs. Apart from the transposition of the Services Directive into Spanish law, there has been no progress on a horizontal reform of the regulatory framework for regulated professions and professional associations, other than in the area of professional board certification of projects. The reform planned in successive National Reform Programmes was not adopted. This reform aimed at defining the professions requiring registration in a professional organisation, increasing transparency and accountability of professional bodies, opening up unjustified reserved activities and safeguarding market unity in the access to and exercise of professional services in Spain.

(16) In the context of the European Semester, the Commission has carried out an analysis of Spain’s economic policy and published it in the 2016 country report. It has also assessed the Stability Programme and the National Reform Programme and the follow-up given to the recommendations addressed to Spain in previous years. It has taken into account not only their relevance for sustainable fiscal and socioeconomic policy in Spain but also their compliance with EU rules and guidance, given the need to strengthen the EU’s overall economic governance by providing EU-level input into future national decisions. The recommendations under the European Semester are reflected in recommendations (1) to (4) below.

(17) In the light of this assessment, the Council has examined the Stability Programme, and its opinion[6] is reflected in particular in recommendation (1) below.

(18) In the light of the Commission's in-depth review and this assessment, the Council has examined the National Reform Programme and the Stability Programme. The recommendations under Article 6 of Regulation (EU) No 1176/2011 are reflected in recommendations (1) to (4) below.

[6] Under Article 5(2) of Regulation (EC) No 1466/97.

HEREBY RECOMMENDS that Spain take action in 2016 and 2017 to:

1. **[**Ensure a durable correction of the excessive deficit by 2017~~,~~ reducing the general government deficit to 3,7 % of GDP in 2016 and to 2,5 % of GDP in 2017, by taking the necessary structural measures and by using all windfall gains for deficit and debt reduction. This is consistent with an improvement in the structural balance of 0,25 % of GDP in 2016 and of 0,5 % of GDP in 2017. Implement at all government levels the tools set out in the fiscal framework law. Enhance control mechanisms for public procurement and coordination of procurement policies across government levels.**]**

2. Take further measures to improve labour market integration, by focusing on individualised support and strengthening the effectiveness of training measures. Enhance the capacity of regional employment services and reinforce their coordination with social services. Address gaps and disparities in minimum income schemes and improve family support schemes, including access to quality childcare and long-term care.

3. Take further measures to improve the labour market relevance of tertiary education, including by incentivising cooperation between universities, firms and research institutions. Increase performance-based funding of public research bodies and universities and foster R&I investment by the private sector.

4. Accelerate the implementation of the law on market unity at regional level. Ensure implementation by the autonomous regions of the reform measures adopted for the retail sector. Adopt the planned reform on professional services and associations.

Done at Brussels,

For the Council
The President