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Recommendation for a

COUNCIL RECOMMENDATION

on the 2015 National Reform Programme of Germany

and delivering a Council opinion on the 2015 Stability Programme of Germany

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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,

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. The strategy focuses 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 it adopted a decision on guidelines for the employment policies of the Member States. Together these form

1 OJ L 209, 2.8.1997, p. 1.
2 OJ L 306, 23.11.2011, p. 25.
3 COM(2015) 256
4 P8_TA(2015)0067, P8_TA(2015)0068, P8_TA(2015)0069.

the 'integrated guidelines' which Member States were invited to take into account in their national economic and employment policies.

(3) On 8 July 2014, the Council adopted a Recommendation on Germany's national reform programme for 2014 and delivered its opinion on Germany's updated stability programme for 2014. On 28 November 2014, in line with Regulation (EU) No 473/2013[5], the Commission presented its opinion on Germany's draft budgetary plan for 2015[6].

(4) On 28 November 2014, the Commission adopted the Annual Growth Survey[7], marking the start of the 2015 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[8], in which it identified Germany as one of the Member States for which an in-depth review would be carried out.

(5) On 18 December 2014, the European Council endorsed the priorities for boosting investment, accelerating structural reforms and pursuing responsible growth-friendly fiscal consolidation.

(6) On 26 February 2015, the Commission published its 2015 country report for Germany[9]. This assessed Germany's progress in addressing the country-specific recommendations adopted on 8 July 2014. The country report also includes the results of the in-depth review under Article 5 of Regulation (EU) No 1176/2011. The Commission's analysis leads it to conclude that Germany is experiencing macroeconomic imbalances which require decisive policy action and monitoring. Risks have increased in light of the persistence of insufficient private and public investment, which represents a drag on growth and contributes to the very high current account surplus which continues to require close attention. The need for action to reduce the risk of adverse effects on the German economy and, given its size, on the economic and monetary union more widely, is particularly great.

(7) On 28 April 2015, Germany submitted its 2015 National Reform Programme and on 16 April 2015 its 2015 Stability Programme. To take account of their interlinkages, the two programmes have been assessed at the same time.

(8) Germany is currently in the preventive arm of the Stability and Growth Pact and subject to the debt rule. In its 2015 Stability Programme, the Government plans to maintain a budgetary surplus. The medium-term objective – a structural deficit of 0.5% of GDP – continues to be met throughout the programme period. The government debt-to-GDP ratio is expected to gradually decline to 61.5% in 2019. The macroeconomic scenario underpinning these budgetary projections, which has not been endorsed by an independent body, uses cautious growth assumptions. Based on the Commission's 2015 spring forecast, the structural balance is projected to remain above the medium-term objective. Gross debt is forecast to remain on a firm downward path beyond the requirement of the debt rule. This creates the fiscal space to boost investment. Based on its assessment of the Stability Programme and taking into account the Commission's 2015 spring forecast, the Council is of the opinion

5 OJ L 140, 27.5.2013, p. 11.
6 C(2014) 8801 final.
7 COM(2014) 902.
8 COM(2014) 904 final.
9 SWD(2015) 25 final.

that Germany is expected to comply with the provisions of the Stability and Growth Pact.

(9) The federal government has increased expenditure on education and research, but the share of public spending on education as a proportion of GDP is still below the EU average and total expenditure on education and research may fall short of the national target of 10 % of GDP by 2015. Germany intends to increase public investment until 2018, including additional amounts of EUR 10 billion for infrastructure and EUR 5 billion to support investment by financially weak municipalities. However, these positive steps appear insufficient to address the overall investment backlog. Taking advantage of its fiscal space would enable Germany to invest in the economy's future growth potential and to address the public investment backlog, which is particularly evident in infrastructure and at municipal level. Germany has made no progress in improving the efficiency of the tax system. Overall, the scope for shifting taxes to more growth-friendly revenue sources appears underused. The revenues from recurrent property taxes remain comparatively low (0.5 % of GDP in 2012 vs. 1.5 % in the EU-28) and the valuation of property is outdated, dating back to market values of 1963/64 in the western *Länder* and 1935 in the eastern *Länder*. Although a reform of the municipal real estate tax (*Grundsteuer*) was part of the coalition agreement and announced in the 2014 and 2015 National Reform Programmes, no concrete action has been taken so far. Instead of focussing more on less distortive recurrent property taxes, the trend towards increasing real estate transfer taxes has continued. The local trade tax (*Gewerbesteuer*) has not been reviewed. Inefficiencies arise due to the inclusion of non-profit elements in the tax base. The administrative burden of taxation for companies and the cost of tax collection remain comparatively high in Germany, while electronic filing is less used in personal and corporate income tax than on average in the EU. The ongoing review of fiscal relations between the federation, *Länder* and municipalities provides the opportunity to strengthen the framework for sustainable fiscal policies, including ensuring adequate public investment at all levels of government. The review is also an opportunity to improve the allocation of revenue and expenditure competences as well as the efficiency of the horizontal fiscal equalisation system and of tax administration.

(10) No measures have been specified to increase incentives for later retirement, which appear indispensable in view of the projected strong decline in Germany's working-age population and a possible shortage of skilled workers in the medium term. The tax wedge for workers earning between 50 % and 67 % of the average wage has remained largely unchanged since 2001 and remains among the highest in the EU. The recent reforms to social insurance systems are likely to involve a further rise in contribution rates and increase the tax wedge further. This would have potentially negative effects on labour market participation and disposable income. The impact of fiscal drag is currently mitigated by low inflation. However, with dynamic wage growth and somewhat higher inflation rates in the coming years, fiscal drag could lead to significant non-discretionary tax increases. These could, in turn, also affect disposable income. Limited progress has been made in improving the educational achievement of disadvantaged people. Young people with a migrant background are twice as likely to leave school early. Fiscal disincentives are likely to be an important factor in discouraging second earners from taking up a job or working longer hours. This contributes to the low proportion of women working full-time and one of the lowest number of hours worked on average by women in the EU. The exemption of mini-jobs from personal income tax and in many cases from all employee social

contributions also discourages workers from moving into jobs with earnings above the mini-job threshold of EUR 450 per month.

(11) Policy action to stimulate competition in the services sectors, especially in professional services, has been limited. Labour productivity growth rates in professional services in Germany have been negative or close to zero for more than a decade. Germany is also among the EU Member States where regulation is least conducive to competition in the professional services sector. The restrictions include professional qualifications requirements, legal form and shareholding requirements. On the latter, limited changes are under way in some *Länder*, but there is still no broad review of such restrictions. Germany is participating in the mutual evaluation exercise provided for in the Directive amending the Professional Qualifications Directive but has not yet taken any measures as a result of this review. The competitive situation in the German railway markets has not significantly improved since last year. In particular, in the long-distance rail passenger segment, the difficult competitive environment is discouraging for new entrants. Track access charges for long-distance passenger transport are among the highest in the EU. The market share of new entrants in the long-distance rail passenger market remains below 1 % and is falling.

(12) In the context of the European Semester, the Commission has carried out a comprehensive analysis of Germany's economic policy and published it in the 2015 country report. It has also assessed the Stability Programme and the National Reform Programme and the follow-up given to the recommendations addressed to Germany in previous years. It has taken into account not only their relevance for sustainable fiscal and socioeconomic policy in Germany but also their compliance with EU rules and guidance, given the need to strengthen the overall economic governance of the European Union by providing EU-level input into future national decisions. The recommendations under the European Semester are reflected in recommendations 1 to 3 below.

(13) In the light of this assessment, the Council has examined Germany's Stability Programme, and is of the opinion[10] that Germany complies with the Stability and Growth Pact.

(14) 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. Its recommendations under Article 6 of Regulation (EU) No 1176/2011 are reflected in recommendations 1 to 3 below.

(15) In the context of the European Semester the Commission has also carried out an analysis of the economic policy of the euro area as a whole. On the basis of this analysis, the Council has issued specific recommendations for the Member States whose currency is the euro. Germany should also ensure the full and timely implementation of these recommendations,

HEREBY RECOMMENDS that Germany take action in 2015 and 2016 to:

1. Further increase public investment in infrastructure, education and research, including by using the available fiscal space. To foster private investment, take measures to improve the efficiency of the tax system, in particular by reviewing the local trade tax and corporate taxation and by modernising the tax administration. Use

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

the ongoing review to improve the design of fiscal relations between the federation, *Länder* and municipalities, particularly with a view to ensuring adequate public investment at all levels of government.

2. Increase incentives for later retirement. Take measures to reduce high labour taxes and social security contributions, especially for low-wage earners, and address the impact of fiscal drag. Revise the fiscal treatment of mini-jobs to facilitate the transition to other forms of employment.

3. Take more ambitious measures to stimulate competition in the services sector, in particular in professional services, by eliminating unjustified restrictions such as legal form and shareholding requirements and fixed tariffs. To this end, conclude the ongoing domestic review of these barriers and take follow-up measures. Remove the remaining barriers to competition in the railway markets, notably in long-distance rail passenger transport.

Done at Brussels,

For the Council
The President