COMMISSION OF THE EUROPEAN COMMUNITIES

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EU RESTRICTED

Recommendation for a

COUNCIL DECISION

on the existence of an excessive deficit in Germany - Application of Article 104(6) of the Treaty establishing the European Community

(presented by the Commission)

EXPLANATORY MEMORANDUM

On 13 November 2002, the Commission released its Autumn economic forecast, projecting for Germany a general government deficit of 3.8% of GDP for 2002, clearly exceeding the reference value of 3% of GDP. Based on this prima facie evidence, the Commission initiated the Excessive Deficit Procedure for Germany on 19 November 2002, with the adoption of the report foreseen in Article 104.3 of the Treaty. On 18 December 2002, the Commission received the updated Stability Programme of Germany, which confirmed a government deficit figure of 3 ¾ % of GDP for 2002. The application of the excessive deficit procedure (EDP) is governed by Article 104 of the Treaty (ex 104c), Council Regulation N°1467/97 "on the speeding up and clarifying the implementation of the excessive deficit procedure", which is part of the Stability and Growth Pact. It is also affected by the political commitments enshrined in the Resolution of the Amsterdam European Council on the Stability and Growth Pact of 17 June 1997.

In an initial step of the EDP, the Commission prepared a report according to Art. 104.3 of the Treaty. That report was adopted by the Commission on 19 November. It concluded that in 2002, the general government deficit in Germany was likely to reach 3.8% of GDP, significantly exceeding the reference value of 3%. Gross government debt was projected to reach 60.9% of GDP by end-2002, also rising above the respective reference value of the Treaty (60% of GDP). The excess of the German deficit in 2002 over the reference value did not result from an unusual event outside the control of the German authorities, nor was it the result of a severe economic downturn. On developments in 2003 the report concluded that, while it was clear that the deficit would be reduced, it was not yet possible to assess whether the deficit would come to fall below the 3% of GDP reference value. Moreover, given that the debt-to-GDP ratio was projected to rise to close to 62% of GDP by the end of 2003, any slippage in budgetary execution or a deceleration in nominal GDP growth would imply an additional deterioration of the debt ratio.

Treaty Art. 104.4 states that "the Committee provided for in Article 114 (i.e. the Economic and Financial Committee) shall formulate an opinion on the report of the Commission". The Committee issued its opinion on 29 November 2002 (document EFC/ECFIN/593/02), largely subscribing to the Commission's Assessment. In particular, the EFC concluded that budgetary developments in Germany in 2002 were such that both the deficit and the debt criterion referred to in Article 104(2) were not respected. Consideration of other relevant factors supported the assessment based on these criteria. While taking note of the strong commitment by the German authorities to introduce all the necessary measures to correct the situation, the EFC, following the report by the Commission, considered that there was a risk of the general government deficit exceeding the Treaty's reference value again in 2003. The Committee also underlined that gross debt was unlikely to reverse its rising trend to comply with the Treaty's reference value of 60 percent of GDP.

The Commission, having examined the relevant factors taken into account in its report and having regard to the opinion of the EFC, is of the opinion that an excessive deficit exists in Germany. This opinion, adopted by the Commission on [8 January 2003], is herewith addressed to the Council, according to Article 104.5 of the Treaty. The Commission recommends that the Council shall decide accordingly, in conformity with Article 104.6. In addition, the Commission is submitting to the Council a recommendation for a Council recommendation to be addressed to Germany with a view to bringing an end to the situation of an excessive government deficit, according to Treaty Article 104.7.

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on the existence of an excessive deficit in Germany – Application of Article 104(6) of the Treaty establishing the European Community

THE COUNCIL OF THE EUROPEAN UNION

Having regard to the Treaty establishing the European Community, and in particular Article 104(6) thereof,

Having regard to the recommendation from the Commission under article 104(6) of the Treaty,

Having regard to the observations made by Germany,

Whereas:

(1) In stage three of Economic and Monetary Union (EMU), according to Article 104 of the Treaty Member States shall avoid excessive government deficits.

(2) The Stability and Growth Pact is based on the objective of sound government finances as a means of strengthening the conditions for price stability and for strong sustainable growth conducive to employment creation.

(3) The Amsterdam Resolution of the European Council on the Stability and Growth Pact of 17 June 1997 solemnly invites all parties, namely the Member States, the Council and the Commission to implement the Treaty and the Stability and Growth pact in a strict an timely manner.

(4) The excessive deficit procedure under article 104 provides for a decision on the existence of an excessive deficit. The Protocol on the excessive deficit procedure annexed to the Treaty sets out further provisions relating to the implementation of the excessive deficit procedure. Council Regulation (EC) 3605/93[1], as last amended by Commission Regulation (EC) 351/2002[2] lays down detailed rules and definitions for the application of the provision of the said Protocol.

(5) 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. The Commission has addressed such an opinion on Germany to the Council on 8 January 2003. According to this opinion:

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[1] OJ No L332, 31.12.1993, p.7.
[2] OJ No L 055, 26.02.2002 p. 23.

– Following the publication of its own Autumn forecast on 13 November 2002, which showed a government deficit of 3.8% of GDP in 2002 for Germany, the Commission, in accordance with Article 104(3) of the Treaty, prepared in November 2002 a report on Germany which takes account of the relevant factors;

– In accordance with Article 104(4) of the Treaty, the Economic and Financial Committee has formulated an opinion on the report of the Commission;

– Germany has submitted an updated Stability Programme in accordance with Article 3 of Council Regulation (EC) No. 1466/97, which had been adopted by the Federal government on 18 December 2002. According to the update, the government deficit in 2002 amounted to 3 ¾% of GDP.

– The Commission considers that there exists an excessive deficit in Germany;

(6) Article 104(6) of the Treaty lays down that the Council should consider any observations which the Member State concerned may wish to make before the Council decides after an overall assessment whether an excessive deficit exists;

(7) The overall assessment leads to the following conclusions: in the late 1990s, when Germany enjoyed relatively strong economic growth, progress in fiscal consolidation was limited, with the general government deficit remaining at around 1 ½% of GDP. Thus, there had been little budgetary leeway to accommodate for the effects of a cyclical slowdown or for any unexpected revenue shortfalls from a tax reform implemented in 2001. From a low of 1.4% of GDP in 2000, the deficit rose to [3.8%] of GDP in 2002, significantly exceeding the reference value of 3% in that year. While general economic conditions have weakened in Germany as elsewhere, the overrun in budgetary expenditure and the shortfall in revenue can only partially be explained by cyclical factors. Moreover, government debt is projected to rise to 60.9% of GDP by the end of 2002, a level also exceeding, albeit slightly, the respective reference value of 60% of GDP.

HAS ADOPTED THIS DECISION:

Article 1

From an overall assessment it follows that an excessive deficit exists in Germany.

Article 2

This decision is addressed to the Federal Republic of Germany.

Done at Brussels, 21 January 2003.

For the Council