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COMMISSION STAFF WORKING DOCUMENT

Analysis of the draft budgetary plans of Spain

Accompanying the document

COMMISSION OPINION

on the draft budgetary plan of Spain

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COMMISSION STAFF WORKING DOCUMENT

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COMMISSION OPINION

on the draft budgetary plan of Spain

1. INTRODUCTION

Spain submitted its Draft Budgetary Plan (DBP) for 2017 on 15 October 2016 in compliance with Regulation (EU) No 473/2013 of the Two-Pack. Given the caretaker nature of the government in place on 15 October 2016 and in the absence of a budget proposal, the budgetary projections for 2017 in the DBP reflect projections on the basis of unchanged policies. Spain is currently subject to the corrective arm of the Stability and Growth Pact (SGP). The Council opened the Excessive Deficit Procedure (EDP) for Spain on 27 April 2009.[1]

On 12 July 2016, the Council decided that Spain had not taken effective action in compliance with the Council's recommendations. On 8 August 2016 Spain was given notice to put an end to the excessive deficit situation by 2018 by reducing the general government deficit to 4.6% of GDP in 2016, to 3.1% of GDP in 2017 and 2.2% of GDP in 2018. Based on the updated Commission 2016 spring forecast underpinning the Council decision, this was considered consistent with a deterioration of the structural balance by 0.4 pp in 2016 and improvements by 0.5 pp in both 2017 and 2018. The Council also decided that Spain should use all windfall gains to accelerate deficit and debt reduction, and should adopt and fully implement consolidation measures for the amount of 0.5% of GDP in both 2017 and 2018, in addition to the savings included in the updated Commission 2016 spring forecast.

Section 2 of this document presents the macroeconomic outlook underlying the DBP and provides an assessment based on the Commission 2016 autumn forecast. Section 3 presents the recent and planned fiscal developments, according to the DBP, including an analysis of risks to their achievement based on that forecast. In particular, it also includes an assessment of the measures underpinning the DBP. Section 4 assesses the recent and planned fiscal developments in 2016-2017 (also taking into account the risks to their achievement) against the obligations stemming from the SGP. Section 5 provides an analysis of action taken in response to the specific Council requirements to strengthen Spain's fiscal framework and its

[1] An overview of Spain's EDP history can be found at: http://ec.europa.eu/economy_finance/economic_governance/sgp/deficit/countries/spain_en.htm

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public procurement policy framework in accordance with Article 1(5) and (6) of the above-mentioned Council decision to give notice. Section 6 provides a summary.

2. MACROECONOMIC DEVELOPMENTS UNDERLYING THE DRAFT BUDGETARY PLAN

The macroeconomic forecast underpinning the DBP assumes annual real GDP growth to reach 2.9% in 2016, fully based on domestic demand growth, with private consumption accelerating and investment only decelerating slightly, compared to 2015. This is broadly similar to the forecast underlying the 2016 Stability Programme, which was based on annual real GDP growth of 2.7%. Imports are forecast to grow by 7.0% and 6.7% in 2016 and 2017, respectively, significantly faster than exports, which are set to grow by 5.4% and 5.7% in 2016 and 2017, respectively. This implies that net exports are expected to continue to detract from annual GDP growth in both years.

The Commission 2016 autumn forecast projects GDP growth of 3.2% in 2016, with growth relying less on domestic demand than projected in the DBP. While the forecast for private consumption is similar in 2016 in both the DBP and the Commission forecast, the DBP assumes more buoyant investment than the Commission forecast, which is also reflected in significantly higher imports growth. The latter explains why the contribution of net trade to GDP growth is negative by -0.3 pp in 2016 according to the DBP, whereas it is positive by 0.2 pp in the Commission forecast, despite broadly similar external assumptions.

Both the DBP and the Commission have a GDP growth forecast of 2.3% in 2017, but still with different growth composition. Both private consumption and investment are expected to grow faster in the DBP than in the Commission forecast. At the same time, although the Commission projects lower export growth in 2017, it also expects significantly lower import growth, leading to a positive contribution of net exports, compared to a negative contribution projected in the DBP.

The 2016 growth forecast in the DBP is based on outcome data showing real GDP growth of 3.4% in the first half of 2016 compared to the first half of 2015. To reach a 2.9% annual growth rate for the year as a whole, the DBP implicitly assumes a more marked deceleration of growth in the second half compared to the Commission forecast. This should create a less positive carry-over into 2017. Yet, annual growth rates in 2017 are similar, which implies that the DBP assumes quarterly growth rates in 2017 to be higher than in the Commission forecast.

Overall, the macroeconomic projections underlying the DBP are cautious in 2016 and plausible in 2017 with regard to annual GDP growth.

Box 1: The macro economic forecast underpinning the budget in Spain

The macroeconomic forecasts underpinning the 2017 DBP have been endorsed by Spain's independent fiscal institution –*Autoridad Independiente de Responsabilidad Fiscal* (AIReF)–

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in a report published on 7 October 2016. While deeming the forecast macroeconomic scenario as "probable" and "balanced", AIReF flagged both upside and downside risks, including lower interest rates and oil prices on the one hand and lower global growth on the other. There is also uncertainty regarding the impact of future fiscal policy decisions. In a report issued on 6 October 2016, it considers it likely that Spain will achieve the nominal deficit target of 4.6% of GDP.

Table 1. Comparison of macroeconomic developments and forecasts

	2015	2016			2017		
	COM	SP	DBP	COM	SP	DBP	COM
Real GDP (% change)	3.2	2.7	2.9	3.2	2.4	2.3	2.3
Private consumption (% change)	2.9	3.2	3.3	3.2	2.6	2.6	2.1
Gross fixed capital formation (% change)	6.0	5.6	5.4	4.2	4.6	4.2	3.6
Exports of goods and services (% change)	4.9	5.3	5.4	6.1	5.7	5.7	4.5
Imports of goods and services (% change)	5.6	7.0	7.0	5.8	6.7	6.7	4.3
Contributions to real GDP growth:							
- Final domestic demand	3.2	3.1	3.2	2.9	2.6	2.5	2.1
- Change in inventories	0.1	0.0	0.0	0.1	0.0	0.0	0.0
- Net exports	-0.1	-0.4	-0.3	0.2	-0.2	-0.2	0.2
Output gap[1]	-4.0	-1.7	-1.5	-1.5	-0.3	0.2	0.0
Employment (% change)	2.5	2.7	2.7	2.9	2.4	2.2	2.1
Unemployment rate (%)	22.1	19.9	19.7	19.7	17.9	17.8	18.0
Labour productivity (% change)	0.2	0.0	0.2	0.4	0.0	0.1	0.2
HICP inflation (%)	-0.6		-0.2	-0.4		1.3	1.6
GDP deflator (% change)	0.5	0.9	0.7	0.7	1.2	1.4	1.2
Comp. of employees (per head, % change)	0.4	0.8	0.8	1.2	1.3	1.2	1.2
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	2.0	2.4	2.3	2.6	2.2	2.1	2.4

Note:

[1]In percent of potential GDP, with potential GDP growth recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

Source:

Stability Programme 2016 (SP); Draft Budgetary Plan for 2017 (DBP); Commission 2016 autumn forecast (COM); Commission calculations

3. RECENT AND PLANNED FISCAL DEVELOPMENTS

3.1. Deficit developments

Driven by the cyclical improvement of the economy and continued fall in interest expenditure, the DBP expects the general government headline deficit to shrink from 5.1% of GDP in 2015 to 4.6% of GDP in 2016, in line with the headline deficit target required by the Council. The headline deficit projection is 1 pp higher compared to the 2016 Stability Programme, despite both the upward revision in underlying real GDP growth in the DBP and

additional consolidation measures having been taken in the course of 2016 (see Section 3.3). This revision mainly stems from the revenue side, whose ratio-to-GDP is expected to narrow by 0.8 pp to 37.8% in the DBP compared with a stable ratio at 38.2% of GDP in the Stability Programme. On the expenditure side, the ratio-to-GDP is projected to narrow by 1.4 pp and reach 42.4%, slightly less than the 1.5 pp decrease to 41.8% expected in the 2016 Stability Programme.[2]

The Commission 2016 autumn forecast also projects a headline deficit of 4.6% of GDP in 2016 with only very slightly higher revenue and expenditure ratios.

For 2017, the DBP only provides projections on the basis of unchanged policies, showing a general government deficit of 3.6% of GDP. Such a deficit reduction in 2017 is underpinned by an expenditure decrease from 42.4% of GDP to 41.3% of GDP. About half of the reduction in the expenditure ratio reflects the expected fall in unemployment benefits and interest expenditure, and the fact that pensions expenditure is expected to grow more slowly than nominal GDP. Growth in compensation of employees is expected to be held back in 2017 by the fact that 2016 was the last year when compensation for forgone Christmas bonuses was paid out. Intermediate consumption in the DBP is assumed to exhibit zero growth in 2017, leading to a fall in its share of GDP by 0.2% of GDP, partly reflecting measures already in place at regional and local levels. The revenue ratio is forecast to decrease by 0.1 pp, reflecting the expectation that social contributions will not keep pace with nominal GDP growth, as employment growth decelerates to 2.2% amid continued wage restraint.

The Commission 2016 autumn forecast projects a general government deficit of 3.8% of GDP in 2017, 0.2 pp higher than the DBP, reflecting a more prudent view of expenditure developments, in particular at the regional level, on account of lower expected savings than in the DBP from measures on healthcare, and at central government level, as – on the basis of current information – it does not project the savings from the 2016 expenditure cuts (*acuerdos de no disponibilidad*) to remain in place in 2017.

Total interest payments by the general government have continued to decrease as a share of GDP, as euro area sovereign bond yields remain at historically low levels, with 10 year rates in Spain currently standing at 1.18%.[3] Based on the information included in the DBP, interest expenditure in Spain is expected to fall from 3.1% of GDP in 2015 to 2.8% of GDP in 2016, and is projected to decrease further next year to 2.7% of GDP. This compares to the 3.5% of GDP recorded in 2014, when interest expenditure peaked. The interest expenditure forecast in the DBP is broadly in line with the Commission forecast.

On the basis of the DBP, the recalculated structural deficit is expected to widen by 0.8 pp to reach 3.6% of GDP in 2016, about 0.9 pp higher than in the 2016 Stability Programme.[4] In

[2] A direct comparison between revenue and expenditure ratios-to-GDP between the Stability Programme and the DBP or Commission 2016 autumn forecast is complicated by revisions in historical data for government revenue and expenditure as well as nominal GDP, published in September 2016. The effect of these revisions on the general government headline deficit for 2015 was relatively small, with the headline deficit remaining at 5.1% of GDP. However, both the revenue and expenditure ratios-to-GDP increased by 0.4 pp as a result of these revisions. The deficit ratios of 2013 and 2014 were also revised and now stand at 7.0% and 6.0%, respectively, 0.1 pp higher in both years.

[3] 10-year bond yields as of 31 October 2016. Source: Bloomberg.

[4] Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission using the commonly agreed methodology.

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2017, the DBP forecasts the recalculated structural deficit in Spain to worsen by 0.1 pp to 3.7% of GDP, about 1.2 pp higher than in the 2016 Stability Programme. The Commission 2016 autumn forecast estimates the structural deficit to widen by about 1.0 pp to reach 3.8% of GDP in 2016, and then to remain broadly stable in 2017.

Some differences in the appraisal of one-offs, in particular in 2016, contribute to the different estimates of the change of the structural balance. In particular, the DBP only refers to one-offs related to the support to the financial sector, which adds 0.2% of GDP to the deficit in 2016, whereas the Commission 2016 autumn forecast factors in a neutral budgetary impact from one-offs in 2016, due to the fact that the Royal Decree Law on Corporate Income Tax (CIT) instalment payments approved by the parliament on 20 October is considered to lead to a positive one-off budgetary impact on revenue amounting to 0.8% of GDP, thereby more than compensating for the 0.6% of GDP negative one-off budgetary impact in 2016 of the expiry of the previous advanced payment regime at the end of 2015.

Table 2. Composition of the budgetary adjustment

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(% of GDP)	2015	2016			2017			Change: 2015-2017
	COM	SP	DBP	COM	SP	DBP	COM	DBP
Revenue	**38.6**	**38.2**	***37.8***	**38.0**	**38.3**	***37.7***	**37.8**	**-1.0**
of which:								
- Taxes on production and imports	11.9	12.0	*11.8*	11.8	11.9	*11.8*	11.8	-0.1
- Current taxes on income, wealth, etc.	10.1	9.8	*9.6*	9.6	10.1	*9.6*	9.5	-0.5
- Capital taxes	0.6	0.6	*0.6*	0.6	0.6	*0.6*	0.6	0.0
- Social contributions	12.3	12.2	*12.2*	12.2	12.1	*12.1*	12.1	-0.2
- Other (residual)	3.7	3.6	*3.6*	3.7	3.6	*3.6*	3.7	-0.2
Expenditure	**43.8**	**41.8**	**42.4**	**42.6**	**41.2**	**41.3**	**41.6**	**-2.5**
of which:								
- Primary expenditure	40.7	39.0	39.7	39.8	38.5	38.6	39.0	-2.0
of which:								
Compensation of employees	11.1	10.9	11.0	10.9	10.8	10.6	10.7	-0.4
Intermediate consumption	5.3	4.9	5.1	5.1	4.8	4.9	5.0	-0.4
Social payments	18.5	18.0	18.3	18.1	17.7	18.0	17.8	-0.5
Subsidies	1.2	1.1	1.1	1.1	1.1	1.1	1.1	-0.1
Gross fixed capital formation	2.5	2.0	2.1	2.1	2.1	2.1	2.2	-0.4
Other (residual)	2.1	2.1	2.1	2.3	2.0	1.9	2.2	-0.1
- Interest expenditure	3.1	2.9	2.8	2.8	2.7	2.7	2.6	-0.4
General government balance (GGB)	**-5.1**	**-3.6**	**-4.6**	**-4.6**	**-2.9**	**-3.6**	**-3.8**	**1.5**
Primary balance	**-2.0**	**-0.8**	**-1.8**	**-1.8**	**-0.2**	**-1.0**	**-1.1**	**1.0**
One-off and other temporary measures	-0.2	0.0	-0.2	0.0	-0.2	0.0	0.0	0.2
GGB excl. one-offs	**-4.9**	**-3.6**	**-4.4**	**-4.6**	**-2.7**	**-3.6**	**-3.8**	**1.3**
Output gap[1]	-4.0	-1.7	-1.5	-1.5	-0.3	0.2	0.0	4.1
Cyclically-adjusted balance[1]	-3.0	-2.7	-3.8	-3.8	-2.7	-3.7	-3.8	-0.7
Structural balance (SB)[2]	**-2.8**	**-2.7**	**-3.6**	**-3.8**	**-2.5**	**-3.7**	**-3.8**	**-0.9**
Structural primary balance[2]	0.3	0.2	-0.8	-1.0	0.2	-1.1	-1.2	-1.3

Notes:

[1]Output gap (in % of potential GDP) and cyclically-adjusted balance according to the DBP/programme as recalculated by Commission on the basis of the DBP/programme scenario using the commonly agreed methodology.

[2]Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.

Source:

Stability Programme 2016 (SP); Draft Budgetary Plan for 2017 (DBP); Commission 2016 autumn forecast (COM); Commission calculations

3.2. Debt developments

The DBP projects the debt-to-GDP ratio to remain fairly stable at the 2015 level of slightly below 100% of GDP in 2016 and 2017. This is somewhat higher than the ratios presented in the 2016 Stability Programme. Since nominal GDP is also higher in the DBP compared to the 2016 Stability Programme, it implies that absolute debt levels (in EUR) increased even more in the DBP compared to 2016 Stability Programme. The debt ratio's stable profile is the result of the debt-increasing impact of the primary deficit and interest expenditure being offset by relatively high nominal GDP growth and the planned debt-decreasing impact of a stock-flow

adjustment of 1.1% of GDP in 2016. The DBP does not provide a breakdown of the various components of the stock-flow adjustment.

Compared with the DBP, the Commission 2016 autumn forecast projects a slightly lower debt ratio in 2016, mainly reflecting higher nominal GDP growth, and a slightly higher one in 2017, reflecting a higher primary deficit and lower inflation. The Commission 2016 autumn forecast projects the debt-to-GDP ratio to reach 99.5% in 2016 and 99.9% in 2017.

Table 3. Debt developments

(% of GDP)	2015	2016			2017		
		SP	DBP	COM	SP	DBP	COM
Gross debt ratio[1]	**99.8**	**99.1**	**99.8**	**99.5**	**99.0**	**99.7**	**99.9**
Change in the ratio	-0.6	-0.6	0.0	-0.3	-0.1	-0.1	0.4
Contributions[2]:							
1. Primary balance	**2.0**	**0.8**	**1.8**	**1.8**	**0.2**	**1.0**	**1.1**
2. "Snow-ball" effect	**-0.5**	**-0.7**	**-0.6**	**-1.0**	**-0.8**	**-1.0**	**-0.7**
Of which:							
Interest expenditure	3.1	2.9	2.8	2.8	2.7	2.6	2.6
Growth effect	-3.1	-2.6	-2.8	-3.1	-2.3	-2.2	-2.2
Inflation effect	-0.5	-0.9	-0.7	-0.7	-1.2	-1.4	-1.2
3. Stock-flow adjustment	**-2.1**	**-0.7**	**-1.1**	**-1.1**	**0.5**	**0.0**	**0.0**

Notes:

[1] End of period.

[2] The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual

Source:

Stability Programme 2016 (SP); Draft Budgetary Plan for 2017 (DBP); Commission 2016 autumn forecast (COM); Commission calculations

3.3. Measures underpinning the draft budgetary plan

The DBP builds on the measures reported in the 2016 Stability Programme, and factors in the following two measures taken by the Spanish government in response to the Council decision to give notice of 8 August 2016: (i) the decision to bring forward the closing date of the 2016 fiscal year; and (ii) the Royal Decree Law 2/2016, raising the amount of CIT instalment payments. The former is a budget management strategy to help to rein in expenditure in 2016, with estimated savings amounting to EUR 1 billion (0.1% of GDP). The latter was adopted by the Spanish government, and ratified by parliament in October 2016, to offset an anticipated 0.6% of GDP shortfall in 2016 CIT revenues, resulting from the expiry on 1 January 2016 of the transitory measures governing CIT instalment payments.[5] According to the DBP, on top

[5] In Spain, the CIT is levied through three instalment payments - taking place in April, October and December of year t – and a tax settlement in July of year t+1. Over 2011-2014, Spain's Corporate Income Tax law was amended several times. Among these changes were the temporary increases in the amount of the three-yearly instalment payments, which expired on 1 January 2016, thus leading to a sharp drop in revenue from the April 2016 payment.

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of compensating the above-mentioned shortfall in CIT instalment payments, the measure is planned to have an additional 0.2% of GDP net positive impact on the 2016 headline balance, thus implying an impact of this measure in 2016 of around 0.75% of GDP. This is due to the fact that the new regulation on CIT instalment payments targets, among other things, a higher number of large companies and raises the amount of the minimum payment.[6] Like the expiry on 1 January 2016 of transitory measures governing CIT instalment payments, the Royal Decree Law 2/2016 does not introduce any changes to the overall tax burden for corporations, but only affects the timing of the tax liabilities and payments. Therefore, the DBP considers the net incremental impact of both measures to be of a temporary nature.

In addition, the 2017 DBP recalls the measures taken by the government in response to the March 2016 Commission recommendation[7], namely, the expenditure cuts (*acuerdos de no disponibilidad*) agreed at central and regional government levels, the budgetary impact of which is estimated in the DBP at EUR 2 billion and EUR 1.5 billion (1.8% and 1.3% of GDP), respectively. Moreover, the DBP updates, as necessary, the expected impact of measures pre-dating the above-mentioned Commission recommendation, such as the 2014 tax reform and the 2013 local administration reform.

In total, the DBP presents an incremental consolidation effect resulting from discretionary measures of 0.7% and 0.2% of GDP in 2016 and 2017, respectively (see Table 4).[8] In both years, the reported net effect largely stems from measures on current expenditure, as revenue-raising measures, are almost outweighed by the effects of the 2014 Personal Income Tax (PIT) and CIT reforms, even after factoring in the recently-adopted increase in CIT instalment payments. On the expenditure side, savings stem from efficiency-enhancing policies (as per the public administration reform), the continued implementation of the 2013 pension reform, various measures at regional and local level, and in 2016, from spending cuts at central government level.

Of the above-mentioned measures, the Commission 2016 autumn forecast takes into account incremental consolidation measures with a net effect of about 0.2% of GDP in 2016 and slightly below 0.2% of GDP in 2017. Differences with the government's estimate arise mostly on the expenditure side, reflecting also the use of a different expenditure baseline (higher in the DBP than in the Commission forecast).

Specifically, the Commission forecast includes a lower estimate for savings from measures taken since the adoption of the March 2016 Commission recommendation. Based on the actual response of regional governments to the Ministry of Finance's call in April 2016 for spending cuts (through *acuerdos de no disponibilidad*) the forecast expects close-to-zero-savings from this measure at this government level. At central government level, the forecast

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[6] Table A-7 summarises the changes brought about by RDL 2/ 2016.

[7] See March 2016 Commission recommendation regarding measures to be taken by Spain in order to ensure a timely correction of its excessive deficit, available at: http://ec.europa.eu/economy_finance/economic_governance/sgp/pdf/30_edps/other_documents/2016-03-09_es_commission_recommendation_en.pdf

[8] In view of the caretaker nature of the government until the deadline of 15 October set by the Council for the submission of the report, and consistently with the no-policy-change projections presented in the DBP for 2017, the DBP does not present any new fiscal policy measures for 2017, which would be necessary to ensure compliance with the 2017 and 2018 headline deficit and structural targets. It only highlights the continued impact of measures already adopted in 2016 or before.

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factors in a combined effect of the spending cuts and the anticipated closure of the 2016 budget of around 0.2% of GDP. This is 0.1 pp less than in the DBP, given uncertainties surrounding the realisation of the full impact of those spending cuts at central government level. Moreover, unlike the DBP, the forecast does not project these savings to remain in place in 2017, unless new spending cuts are adopted by the government for that year.

Moreover, the Commission forecast only incorporates part of the reported savings from the implementation of the existing limitations to new public sector hiring, in light of the latest developments in public sector employment, which on average increased by 1.3% year-on-year up to the third quarter of 2016. Neither does the forecast include savings at regional level from the application of the new pharmaceutical and healthcare spending rule in 2017. There is no evidence of any region having agreed explicitly to apply that rule at the cut-off date of the forecast, based on information from the available 2016 regional adjustment plans under the Regional Liquidity Fund.

On the revenue side, the Commission forecast has a more conservative estimate (relative to the DBP) of the budgetary impact of measures against tax fraud and on rebates regarding employers' social security contributions for new open-ended hiring (for 2016 only). Starting from 2016, the forecast has started to factor in the expected savings from the 2013 pension reform in the baseline calculations of social transfers other than in kind.

Lastly, the 2016 autumn forecast takes on board the expected impact of Royal Decree Law 2/2016. However, unlike the DBP, which considers this measure as temporary, but not one-off, the Commission forecast also treats the net impact of this measure as one-off (see section 3.1), in line with Commission classifications principles for one-off measures.[9]

[9] See: European Commission (2015), Report on public finances in EMU – 2015, European Economy institutional paper, N° 14, Chapter II.3. One-off measures – Classifications principles used in fiscal surveillance.

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Table 4. Main discretionary measures reported in the DBP

A. Discretionary measures taken by General Government - revenue side

Components	Budgetary impact (% GDP) (as reported by the authorities)		
	2016	**2017**	**2018**
Taxes on production and imports	0.2	0.1	na
Current taxes on income, wealth, etc.	-0.2	-0.2	na
Capital taxes	0.0	0.0	na
Social contributions	0.0	0.0	na
Property Income	0.0	0.0	na
Other	0.0	0.0	na
Total	0.0	-0.1	na

Note:
The budgetary impact in the table is the aggregated impact of measures as reported in the DBP, i.e. by the national authorities. A positive sign implies that revenue increases as a consequence of this measure.
Source: Draft Budgetary Plan for 2017

B. Discretionary measures taken by general Government- expenditure side

Components	Budgetary impact (% GDP) (as reported by the authorities)		
	2016	**2017**	**2018**
Compensation of employees	0.0	0.1	na
Intermediate consumption	0.5	0.1	na
Social payments	0.1	0.1	na
Interest Expenditure	0.0	0.0	na
Subsidies	0.0	0.0	na
Gross fixed capital formation	0.0	0.0	na
Capital transfers	0.0	0.0	na
Other	0.0	0.0	na
Total	0.7	0.3	na

Note:
The budgetary impact in the table is the aggregated impact of measures as reported in the DBP, i.e. by the national authorities. A positive sign implies that expenditure increases as a consequence of this measure.
Source: Draft Budgetary Plan for 2017

4. COMPLIANCE WITH THE PROVISIONS OF THE STABILITY AND GROWTH PACT

Spain is currently subject to the corrective arm of the SGP. Box 2 recalls the main recommendations in the area of public finances issued to Spain in the context of the European Semester and the Excessive Deficit Procedure (EDP) opened by the Council on 27 April 2009. It also recalls the provisions of the Council's decision to give notice to Spain under Article 126(9) of the Treaty, following its earlier decision under Article 126(8) of the Treaty

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that Spain had not taken effective action in compliance with the Council's recommendations of 21 June 2013.

Box 2: Council decision to give notice to Spain

On 9 March 2016, the Commission issued a recommendation according to which Spain should take measures to ensure a timely and durable correction of the excessive deficit, including by making full use as appropriate of the preventive and corrective tools set out in Spain's Stability law to control for slippages at the sub-central government level from the respective deficit, debt and expenditure rule targets.

On 12 July 2016, the Council addressed recommendations to Spain in the context of the European Semester. In particular, in the area of public finances, the Council recommended to Spain to ensure a durable correction of the excessive deficit, in accordance with the relevant decisions or recommendations under the excessive deficit procedure, by taking the necessary structural measures and by using all windfall gains for deficit and debt reduction. The Council also recommended to Spain to implement at all government levels the tools set out in the fiscal framework law and to enhance control mechanisms for public procurement and coordination of procurement policies across government levels.

On 11 July 2016, the Council adopted a Decision establishing that Spain had not taken effective action in response to the Council Recommendation of 21 June 2013.

On 8 August 2016, the Council gave notice to Spain under Article 126(9) of the Treaty to correct its excessive deficit by 2018. According to that notice, Spain shall reduce the general government deficit to 4.6 % of GDP in 2016, to 3.1 % of GDP in 2017 and to 2.2 % of GDP in 2018. This improvement in the general government deficit is consistent with a deterioration of the structural balance by 0.4 % of GDP in 2016 and a 0.5 % of GDP improvement in both 2017 and 2018, based on the updated Commission 2016 spring forecast. Spain shall also use all windfall gains to accelerate deficit and debt reduction. In addition to the savings already included in the updated Commission 2016 spring forecast, Spain shall adopt and fully implement consolidation measures for the amount of 0.5 % of GDP in both 2017 and 2018. Spain shall stand ready to adopt further measures should risks to the budgetary plans materialise. Fiscal consolidation measures shall secure a lasting improvement in the general government structural balance in a growth-friendly manner. Moreover, Spain shall adopt measures to strengthen its fiscal framework, in particular with a view to increasing the automaticity of mechanisms to prevent and correct deviations from the deficit, debt and expenditure targets and to strengthening the contribution of the Stability Law's spending rule to public finance sustainability. Furthermore, Spain shall set up a consistent framework to ensure transparency and coordination of public procurement policy across all contracting authorities and entities with a view to guaranteeing economic efficiency and a high level of competition. Such framework shall include appropriate ex-ante and ex-post control mechanisms for public procurement to ensure efficiency and legal compliance.

For 2016, the DBP plans the headline deficit to decrease from 5.1% to 4.6% of GDP, in line with the headline deficit target required by the Council. It should be noted that the target is only expected to be achieved thanks to the adoption of Royal Decree Law 2/2016 reinstating a minimum advance payment in CIT. As noted in Section 3, this measure is expected to have a

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one-off impact of EUR 8.3 billion (0.75% of GDP) in 2016, implying that the deficit would have been substantially higher had this measure not been adopted. It should be recalled that in addition to the shortfalls in corporate income taxes foreseen in July (related to the changes in corporate income tax advance payments, which have now been remedied by the Royal Decree Law), further shortfalls in income taxes have now been projected, compared to the July forecast.

Table 5. Compliance with the EDP recommendation

(% of GDP)	2015	2016		2017		2018	
	COM	DBP	COM	DBP	COM	DBP	COM
Headline balance							
Headline budget balance	-5.1	-4.6	-4.6	-3.6	-3.8	-	-3.2
EDP requirement on the budget balance		-4.6		-3.1		-2.2	
Fiscal effort - change in the structural balance							
Change in the structural balance[1]	-0.9	-0.7	-1.0	-0.1	0.0	-	0.0
Cumulative change[2]		-0.7	-1.0	-0.9	-1.0	-	-1.0
Required change from the EDP recommendation		-0.4		0.5		0.5	
Cumulative required change from the EDP recommendation		-0.4		0.1		0.6	
Fiscal effort - adjusted change in the structural balance							
Adjusted change in the structural balance[3]		-	-0.5	-	0.2	-	0.0
of which: *correction due to change in potential GDP estimation (α)*		-	0.0	-	0.0	-	0.0
correction due to revenue windfalls/shortfalls (β)		-	-0.6	-	-0.2	-	0.0
Cumulative adjusted change [2]		-	-0.5	-	-0.2	-	-0.2
Required change from the EDP recommendation		-0.4		0.5		0.5	
Cumulative required change from the EDP recommendation		-0.4		0.1		0.6	
Fiscal effort - calculated on the basis of measures (bottom-up approach)							
Fiscal effort (bottom-up)[4]		-	-0.1	-	0.3	-	0.0
Cumulative fiscal effort (bottom-up)[2]		-	-0.1	-	0.2	-	0.1
Requirement from the EDP recommendation		0.0		0.5		0.5	
Cumulative requirement from the EDP recommendation		0.0		0.5		1.0	

Notes

[1] Structural balance = cyclically-adjusted general government balance excluding one-off measures. Structural balance based on DBP is recalculated by the Commission on the basis of the Draft Budgetary Plant scenario using the commonly agreed methodology. Change compared to t-1.

[2] Cumulated since the first year for correction in the lastest EDP recommendation.

[3] Change in the structural balance corrected for unanticipated revenue windfalls/shortfalls and changes in potential growth compared to the scenario underpinning the EDP recommendation.

[4] The estimated budgetary impact of the additional fiscal effort delivered on the basis of the discretionary revenue measures and the expenditure developments under the control of the government between the baseline scenario underpinning the EDP recommendation and the current forecast.

Source:

Draft Budgetary Plan for 2017 (DBP); Commission 2016 autumn forecast (COM); Commission calculations.

While the Council decision to give notice under Article 126(9) of the Treaty of 8 August 2016 requires Spain to limit the deterioration of the structural balance to at most 0.4% of GDP in 2016, the Commission 2016 autumn forecast points to an expected deterioration in the structural balance of 1.0 pp, 0.6 pp above what was recommended. Taking into account the differences in one-offs, where the Commission 2016 autumn forecast considers a neutral

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impact from one-offs in 2016 whereas the DBP reports a deficit-increasing impact of 0.2% of GDP, the DBP assumes a similar structural deterioration in 2016. This larger-than-expected worsening of the structural balance appears to be driven mostly by the revenue shortfalls referred to above.

Accounting for revisions in the potential output growth estimate and unexpected revenue windfalls/shortfalls since the time of the notice, the estimated corrected change in the structural balance amounts to -0.5 pp, in 2016, 0.1 pp more negative than the requirements from the notice.[10]

The Council's decision to give notice does not require Spain to adopt any additional measures in 2016. According to a bottom-up assessment (which estimates the size of the fiscal effort for 2016 on the basis of the additional revenue measures taken and the expenditure developments under the control of the government between the EDP baseline scenario and the ad-hoc Commission forecast), Spain is expected to record a negative effort of 0.1% of GDP in 2016, thereby marginally missing the 0.0% of GDP target required by the Council decision. This results from the Commission forecast estimated change (as measured in the bottom-up method) in total nominal expenditure for 2016 being higher than the estimated change in the baseline forecast underlying the Council decision. There have been no discretionary revenue measures additional to those already included in the above-mentioned no-policy change forecast, other than Royal Decree Law 2/2016. However, as it is of a one-off nature (see section 3.3) it is thus not taken into account in the bottom-up assessment.

For 2017, the headline deficit forecast in the DBP is 0.5 pp higher than the headline deficit target of 3.1% of GDP. This reflects the fact that the DBP is on a no-policy change basis, as a result of there being only a caretaker government by the deadline of 15 October. Also, according to the Commission 2016 autumn forecast, the headline deficit target is not expected to be achieved, with a forecast headline deficit of 3.8% of GDP.

The Council decision requires Spain to achieve an improvement of the structural balance of 0.5 pp in 2017. While acknowledging the no-policy-change nature of these projections, the Commission forecast reveals that in the absence of further measures the fiscal effort would fall short of the level required by the Council in both years on any of the metrics. Specifically, the forecast projects no change in the structural deficit for 2017. Correcting for the change in the estimated potential growth between the projections underlying the Council decision and the Commission 2016 autumn forecast, as well as revenue shortfalls projected for 2017, the estimated change in the structural balance would be at 0.2 pp.

On a cumulative basis over 2016-2017, the estimated shortfall amounts to 1.1% of GDP when measured against the unadjusted change in the structural balance, and to 0.3% of GDP when adjusted for the above-mentioned elements.

The bottom-up estimate of the fiscal effort in 2017 is 0.3% of GDP. This is below the target of about 0.5% of GDP of measures deemed necessary in 2017 to reach the structural targets spelled out in the new EDP recommendation, leading to an underperformance of 0.3% of GDP in cumulative terms over 2016-2017.

[10] The difference between the uncorrected and corrected structural balance is due to the impact of revenue shortfalls compared to the scenario underlying the recommendation.

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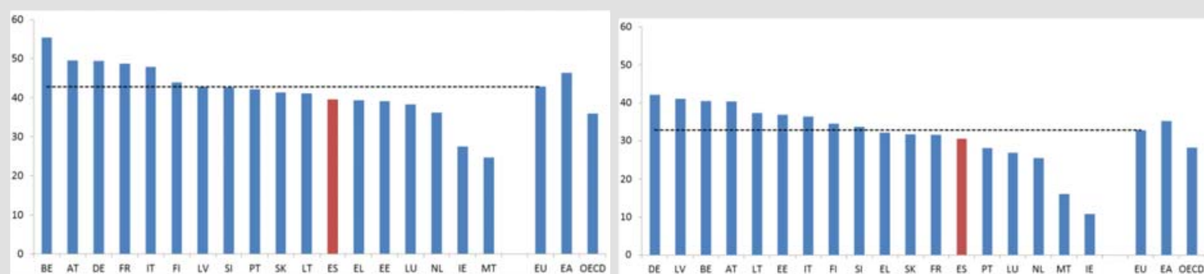
For 2018, according to the Commission 2016 autumn forecast, the headline target is not expected to be achieved, with a forecast headline deficit of 3.2% of GDP. The Council decision requires Spain to achieve an improvement of the structural balance of 0.5 pp in 2018. However, the Commission 2016 autumn forecast projects no change in the structural deficit in 2018. This is about 0.5 pp below the recommended structural effort. On a cumulative basis over 2016-2018, the estimated shortfall amounts to 1.6% of GDP when measured against the unadjusted change in the structural balance, and to 0.8% of GDP when adjusted. The bottom-up estimate of the fiscal effort in 2018 is 0.0% of GDP. This is below the target of about 0.5% of GDP of measures deemed necessary in 2018 to reach the structural targets spelled out in the notice, leading to an underperformance of 0.9% of GDP in cumulative terms over 2016-2018.

Box 3: Addressing the tax burden on labour in the euro area

The tax burden on labour in the euro area is relatively high and weighs on economic activity and employment. Against this background, the Eurogroup has expressed a commitment to reduce the tax burden on labour. On 12 September 2015, it agreed to benchmark euro area Member States' tax burden on labour against the GDP-weighted EU average, relying in the first instance on indicators measuring the tax wedge on labour for a single worker at average wage and a single worker at low wage. It also agreed to relate these numbers to the OECD average for purposes of broader comparability.

The tax wedge on labour measures the difference between the total labour costs to employ a worker and the worker's net earnings. It is made up of personal income taxes and employer and employee social security contributions. The higher the tax wedge, the higher the disincentives to take up work or hire new staff. The graphs below show the tax wedge in Spain for a single worker earning respectively the average wage and a low wage (50% of the average) compared to the EU average.

The tax burden on labour in Spain at the average wage and a low wage (2015)



Notes: Data for Latvia, Lithuania and Malta is for 2014. No recent data is available for Cyprus. EU and EA averages are GDP-weighted. The OECD average is not weighted.
Source: European Commission Tax and Benefit Indicator database based on OECD data.

Benchmarking is only the first step in the process towards firm, country-specific policy conclusions. The tax burden on labour interacts with other policy elements such as the benefit system and the wage-setting system. A good employment performance indicates that the need to reduce labour taxation may be less urgent while fiscal constraints can dictate that labour tax cuts should be fully offset by other revenue-enhancing or expenditure-reducing measures. In-depth, country-specific analysis is necessary before drawing policy conclusions.

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The 2014 PIT reform in Spain, which reduced rates across the board, went some way to reduce the tax wedge on labour. However, the tax reform, which was phased in over 2015-16, was underfunded and contributed negatively to the general government balance.

Specifically, also with a view to encouraging employment creation, the reform reduced the tax wedge by exempting income up to EUR 12 000 from personal income tax and by lowering rates. In addition, the social security contribution flat rate scheme (*tarifa plana*) of EUR 100 was replaced in March 2015 by an exemption for the first EUR 500 earned for new permanent contracts, benefiting those on lower incomes, such as young people and the low-skilled.
While across-the-board reductions in PIT may not be the most appropriate way to promote employment, to date the effects of the targeted subsidies in promoting job creation on permanent contracts remain unclear.

5. IMPLEMENTATION OF FISCAL STRUCTURAL REFORMS

5.1. Measures to strengthen Spain's fiscal framework

a) Measures taken in response to the Commission recommendation of 9 March 2016

In March 2016, when the Commission recommended to Spain to take measures to ensure a timely correction of its excessive deficit,[11] the Commission also invited the government to make full use as appropriate of the preventive and corrective tools set out in Spain's Stability Law to control for slippages at the sub-central government level from the respective deficit, debt and expenditure rule targets. In response to that recommendation, the government has taken the following actions in 2016:

- The Ministry of Finance activated for the first time some provisions in Spain's Stability Law, such as the requirement for several regional governments that missed the 2015 deficit target to adopt spending cuts to reach the 0.7% of GDP deficit target set to them for 2016.

- Secondly, the Ministry of Finance implemented preventive and corrective measures to help bring the average payment period to suppliers of regional and local governments down to 30 days.

- Thirdly, the Ministry also took initiatives aimed at improving the monitoring of public finances at sub-central level. Namely, it required several regions to comply with data provision requirements set out in the Stability Law's implementing legislation and started publishing, in April 2016, monthly data to allow the verification of compliance with the expenditure rule target at various levels of government.

- Lastly, in 2016, the government published for the first time, i) the eligibility conditions for the access by regions to the Regional Liquidity Fund, ii) the adjustment plans submitted by applicant regions and iii) periodic follow up assessments of the implementation of

[11] See http://ec.europa.eu/economy_finance/economic_governance/sgp/pdf/30_edps/other_documents/2016-03-09_es_commission_recommendation_en.pdf

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those plans, despite the fact that the publication of none of the above is mandated by domestic law.

b) Measures taken in response to the Council decision to give notice of 8 August 2016

The August 2016 decision to give notice to Spain required Spain to strengthen its fiscal framework, in particular with a view to increasing the automaticity of mechanisms to prevent and correct deviations from the deficit, debt and expenditure targets and to strengthening the contribution of the Stability Law's spending rule to public finance sustainability.

Since the August 2016 decision, the Ministry of Finance has stepped up the application of corrective measures to reduce the average payment period to suppliers of regional and local governments. Specifically, in September 2016, it withheld tax revenues earmarked for one region to pay down its commercial arrears, as the average payment period of that region kept exceeding the statutory limits.

c) Assessment of action taken in response to the Council decision to give notice of 8 August 2016

The implementation of these measures goes in the right direction, in that they strengthen incentives for public administrations to reach their deficit, expenditure rule and average payment period targets. However, as noted in section 3.3, the response of regional governments to the Ministry of Finance's call in April 2016 for spending cuts has been quite mild, judging from the actual amount of cuts (EUR 40 million)[12] adopted in 2016.

Moreover, in 2016, the monitoring of regions' budgetary developments is being hampered by the fact that revised deficit, debt and expenditure rule targets for 2016 could not be adopted by parliament.

More importantly, two requirements of the Council decision to give notice to Spain have not been followed up in Spain's report on effective action, in particular: i) the requirement to adopt measures with a view to increasing the automaticity of mechanisms to prevent and correct deviations from the deficit, debt and expenditure targets, and; ii) the requirement to strengthen the contribution of the Stability Law's spending rule to fiscal discipline, namely by means of appropriate implementing legislation to clarify its application at various government levels and to avoid interpretations of the rule that undermine its contribution to fiscal discipline.[13]

[12] See: http://www.airef.es/es/contenidos/informes/732-informe-sobre-el-cumplimiento-esperado-de-los-objetivos-de-estabilidad-presupuestaria-deuda-publica-y-regla-de-gasto-2016-de-las-aapp

[13] The absence of a detailed regulation of the spending rule in the Stability Law has allowed recently for interpretations that weaken the contribution of that rule to fiscal consolidation. For example, the maximum level of eligible expenditure in 2016 is based on the actual level of eligible spending in 2015 and not the level that would have resulted from compliance with the rule in that year. In other words, non-compliant public administrations are not required to make up for spending slippages in the year following their occurrence. See AIReF's report on the 2016-17 regional economic and financial plans at: http://www.airef.es/system/assets/archives/000/001/581/original/2016_07_15_Informe_PEF_2016-2017_final.pdf?1468573939

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5.2. Measures to strengthen public procurement

a) Measures taken in response to the Council decision to give notice of 8 August 2016

In response to the Council decision, the Spanish authorities have put forward the following measures.

- Firstly, a draft law was submitted to parliament on 13 October 2016 to reinforce the powers of the central government's advisory council on public procurement (the *Junta Consultiva del Estado*). Specifically, upon its entry into force, i) the *Junta Consultiva* will supervise the ex post controls on the procurement activities carried out by the central government's contracting authorities and ii) a coordination committee reporting to the *Junta Consultiva* will be created to promote homogeneous interpretation criteria of procurement regulations, to draw up a proposal for a nation-wide strategy for procurement supervision and to prepare a methodology for ex-post procurement controls. The committee will be composed of representatives of the central and sub-central government levels.

- Secondly, the draft law eliminates the currently unrestricted capacity of contracting authorities to use the negotiated procedure without prior publication for low-value contracts.

- Thirdly, the forthcoming adoption of a ministerial decision laying down the composition and working methods of the central government's office for evaluation (*Oficina Nacional de Evaluación*[14]*)* will finally enable it to become operational. The office is due to perform an ex-ante check of the financial sustainability of public works and services' concessions procured by the central and local governments, while regional governments can choose also to come under the scope of the office.

b) Assessment of action taken in response to the Council decision to give notice of 8 August 2016

The proposed measures go some way in improving some public procurement practices in Spain, but overall they do not address the need for a consistent framework that ensures sufficient transparency and coordination of public procurement policy across all contracting authorities and entities. Furthermore, the report does not spell out clear objectives for public procurement, specific instruments for action and a timeline for their adoption and implementation. Specifically:

- The planned measures do not decisively contribute to enhancing transparency in public procurement policy. The planned elimination of the unrestricted capacity of contracting authorities to use the negotiated procedure without prior publication for contract values below the EU thresholds goes in the right direction. However, there are no measures to limit the relatively wide use of this procedure for procurement subject to the EU Directives, where according to TED data, Spain uses this procedure twice as much as the EU average. It also remains unclear why the publication rates of public contracts at EU level, as identified in TED data, are relatively low in Spain.

[14] The office was created with Law 40/2015 of 1 October 2015.

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- Also, the proposed measures do not seem to strengthen ex-ante checks sufficiently. In particular, they do not address the shortage of staff in the relevant bodies performing ex-ante checks at the various general government levels and the independence of the relevant bodies at sub-central level. While the operationalisation of the *'Oficina Nacional de Evaluación'* goes in the right direction, it has narrow scope (since it only covers works and services' concessions, and not public contracts) and the non-binding nature of its decisions on contracting authorities does not guarantee their effective impact. This is important at regional level, since regional governments do not have the obligation to undergo the checks carried out by the office.

- While the *Junta Consultiva* will be given monitoring powers, these are related solely to ex-post checks. Moreover, the draft law does not provide details about the operational aspects of those checks. In particular, it does not specify how the *Junta Consultiva* will supervise the ex-post checks at central level and coordinate those on sub-central government procurement, nor does it specify which contracting entities and public bodies will be subject to the checks and for which type of public contracts and/or value of contracts. Moreover, the draft law does not give enforcement powers (e.g. the possibility to impose sanctions and lodge legal actions) to the *Junta Consultiva*, thus weakening its supervisory role, and does not guarantee its independence. It also does not secure sufficient resources for the bodies carrying out ex-post checks, at central and sub-central level, in view of their increased functions.

- Lastly, coordination of public procurement policy across all contracting authorities could be significantly enhanced by the setting up of an independent body in charge of ensuring efficiency and legal compliance throughout the country. More systematic and widespread use of centralised purchasing could help to increase fiscal savings. Neither of these measures is envisaged yet.

6. OVERALL CONCLUSION

Based on the Commission 2016 autumn forecast, Spain is expected to achieve a headline deficit of 4.6% of GDP in 2016, which is in line with the headline deficit target required by the Council decision to give notice of 8 August 2016, and of 3.8% of GDP in 2017, 0.7% of GDP above the headline deficit target for that year. The large gap in 2017 is due to the lack of new measures for 2017, as the DBP was prepared on the basis of unchanged policies. In 2018, under the usual no-policy-change assumption, the Commission projects a headline deficit of 3.2% of GDP, above the headline deficit target of 2.2% of GDP and the Treaty reference value of 3% of GDP.

At the same time, the Commission considers that there is a risk that the structural effort required in the notice of 8 August 2016 may not be met in 2016. In the absence of additional measures for 2017, the fiscal effort is also expected to fall short of the required effort in that year. Overall, while the measures taken by the caretaker government for 2016 have significantly increased the probability of meeting the 2016 headline deficit targets, further measures appear to be needed to fulfil the headline deficit and structural effort targets going

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forward. Until such measures have been taken, risks to the timely and durable correction of the excessive deficit by 2018 remain.[15]

The 2017 DBP reports on the measures taken or planned in response to the Council request to strengthen Spain's fiscal and public procurement policy frameworks. On the former, while the DBP provides detailed information on the implementation of the preventive and corrective mechanisms in the Stability Law throughout 2016, it does not report on plans to amend that law so as to make the implementation of those mechanisms more automatic. Furthermore, in the absence of appropriate implementing legislation, the application of the Stability Law's spending rule remains unclear and can be subject to interpretations that undermine its contribution to fiscal discipline. Regarding public procurement, the reported measures can go some way towards improving some public procurement practices in Spain, but overall they do not address the need for a consistent framework that ensures sufficient transparency and coordination of public procurement across all contracting authorities and entities. Furthermore, the report does not spell out clear objectives for public procurement, instruments for action and a timeline for their adoption and implementation.

[15] In a letter addressed to Vice-president Dombrovskis and Commissioner Moscovici dated 8 November 2016, the Spanish Minister of Economy, Industry and Competitiveness, announced that the Spanish government will submit an updated DBP within the next coming weeks. According to the letter, this updated budget would ensure compliance with the 2017 headline deficit target of 3.1% of GDP in 2017 and the structural effort requirement of 0.5% of GDP.

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Annex. EDP related tables

Table A1. Forecast of key macroeconomic and budgetary variables under the baseline scenario

		2015	2016	2017	2018
Real GDP growth	%	3.2	2.9	2.3	2.1
Nominal GDP growth	%	3.8	3.4	3.6	3.6
Potential GDP growth	%	0.0	0.4	0.7	0.9
Structural balance	% of pot. GDP	-2.7	-3.1	-3.2	-3.2
General government balance	% of GDP	-5.1	-4.6	-3.3	-2.7
Change in structural balance	% of pot. GDP	-0.9	-0.4	-0.1	0.0
p.m. Output Gap	% of pot. GDP	-4.0	-1.7	-0.2	0.9
Source: Commission Staff Working Document accompanying the Decision to give notice to Spain.					

Table A2. Forecast of key macroeconomic and budgetary variables under the EDP scenario

		2015	2016	2017	2018
Real GDP growth	%	3.2	2.9	1.7	1.5
Nominal GDP growth	%	3.8	3.4	3.1	3.0
Potential GDP growth	%	0.0	0.4	0.7	0.9
Structural balance	% of pot. GDP	-2.7	-3.1	-2.6	-2.1
General government balance	% of GDP	-5.1	-4.6	-3.1	-2.2
Change in structural balance	% of pot. GDP	-0.9	-0.4	0.5	0.5
p.m. Output Gap	% of pot. GDP	-4.0	-1.7	-0.8	-0.1
Source: Commission Staff Working Document accompanying the Decision to give notice to Spain.					

Table A3. Current estimates of the macroeconomic and fiscal developments

		2015	2016	2017	2018
Real GDP growth	%	3.2	3.2	2.3	2.1
Nominal GDP growth	%	3.7	3.9	3.5	3.6
Potential GDP growth	%	0.1	0.5	0.7	0.9
Structural balance	% of pot. GDP	-0.9	-1.0	-0.1	-0.1
General government balance	% of GDP	-5.1	-4.6	-3.8	-3.2
Change in structural balance	% of pot. GDP	-2.8	-3.8	-3.8	-3.8
p.m. Output Gap	% of pot. GDP	-4.0	-1.4	0.1	1.2
Source: Commission 2016 Autumn Forecast					

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Table A4. Adjustment of apparent structural effort for the revision in potential growth - details of calculations

ES	Potential GDP growth underlying the 2016 Council decision to give notice (%)	Potential GDP growth at the time of assessment (%)	Forecast error (%)	Structural expenditure (% of potential GDP)	Correction coefficient α (% of nominal potential GDP)
	(1)	(2)	(3)=(1)-(2)	(4)	(5)=(3)*(4)/100
2016	0.4	0.6	-0.1	41.5	0.0
2017	0.7	0.7	0.0	41.5	0.0
2018	0.9	0.9	0.0	41.6	0.0

Table A5. Adjustment of apparent structural effort for the expected revenue windfalls/shortfalls - details of calculations

ES	Change in current revenues (yoy) (billions)		Discretionary current revenue measures (billions)		Nominal GDP growth assumptions (%)		Change in output gap		Current revenues in year t-1 (billions)		Revenue gap (billions)*	Nominal GDP	Correction coefficient β (% of nominal GDP)
	notice	assessment	notice	assessment	notice	assessment	notice	assessment	notice	assessment		assessment	
	(1)	(1')	(2)	(2')	(3)	(3')	(4)	(4')	(5)	(5')	(6)=[(1')-(2')-[(3')+(ε-1)*(4')/100]*(5')]-[(1)-(2)-[(3)+(ε-1)*(4)/100]*(5)]	(7)	(8)=100*(6)/(7)
2016	8.0	4.1	-8.0	0.2	3.4	3.9	-1.7	-1.5	407.0	408.8	-6.6	1118.0	-0.6
2017	12.8	23.8	5.5	-2.5	3.6	3.5	-0.2	0.0	411.1	416.8	-2.6	1157.0	-0.2
2018	15.8	16.0	0.2	0.2	3.6	3.6	0.9	1.2	434.9	429.6	-0.3	1199.1	0.0
	*revenue elasticity (ε): 1.0												

Table A6. Forecast of key variables for the computation of the fiscal effort under the baseline scenario

			2016	2017	2018
Enters top-down	α	*Structural expenditure (% of potential GDP)*	*41.08*	*41.37*	*41.39*
		Potential GDP growth (%)	*0.45*	*0.72*	*0.9*
	β	*Current revenue (national currency)*	*411.13*	*434.88*	*450.87*
		Discretionary measures wih impact on current revenue (national currency)	*-8.04*	*5.53*	*0.19*
		Nominal GDP growth (%)	*3.4*	*3.63*	*3.56*
		p.m Output gap (% of Pot. Output)	*-1.73*	*-0.23*	*0.92*
Enters bottom-up		*Discretionary measures wih impact on total revenue net of one-offs and other temporary measures (national currency)*	*-2.75*	*5.52*	*0.19*
		Total expenditure net of one-offs and other temporary measures (national currency)	*469.48*	*480.62*	*490.7*
		Interest expenditure (national currency)	*31.47*	*30.52*	*29.61*
		Total unemployment	*4542.96*	*4136.8*	*3765.64*

Source: Commission Staff Working Document accompanying the Decision to give notice to Spain.

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Table A-7. Regulation of CIT instalment payments (CIT-IP) (*)

Type of corporate income tax instalment payment		Regulation in 2014 and 2015	Regulation in 2016 before RDL 2/2016	Regulation after RDL 2/2016
a) CIT-IP as % of companies' CIT taxable income	Eligible companies	Standard regime (companies pay under this modality unless they opt for option b) or are obliged by law to apply option b)	Unchanged	Unchanged
	Amount	[Taxable income in t-1 - applicable tax credits - withholdings made on tax payer's revenues] x 18%	Unchanged	Unchanged
	Minimum instalment payment	Non applicable	Unchanged	Unchanged
b) CIT- IP as % of companies' CIT tax base	Eligible companies	Companies voluntarily adhering to this scheme	Unchanged	Unchanged
		Tax payers with turnover above EUR 6 million in the 12 months preceding the start of the fiscal year.	Unchanged	Unchanged
		Specificities for tax payers with turnover above EUR 20 million in the 12 months preceding the start of the fiscal year (see minimum instalment payment below)	Non applicable	Specificities for tax payers with turnover above EUR 10 million in the 12 months preceding the start of the fiscal year (see below)
	Amount	For companies with turnover below EUR 10 million in the previous fiscal year: CIT tax base x 5/7 x 28% – [applicable tax credits + previous instalment payments of the fiscal year + capital withholdings] For companies with turnover between EUR 10 and EUR 20 million in the previous fiscal year: CIT tax base x 15/20 x 28% – [applicable tax credits + previous instalment payments of the fiscal year + capital withholdings] For companies with turnover between EUR 20 and EUR 60 million in the previous fiscal year: CIT tax base x 17/20 x 28% – [applicable tax credits + previous instalment payments of the fiscal year + capital withholdings] For companies with turnover above EUR 60 million in the previous fiscal year: CIT tax base x 19/20 x 28% –	CIT tax base x 5/7 x 25% – [applicable tax credits + previous instalment payments of the fiscal year + capital withholdings]	For companies with turnover below EUR 10 million in the previous fiscal year: CIT tax base x 5/7 x 25% – [applicable tax credits + previous instalment payments of the fiscal year + capital withholdings] For companies with turnover above EUR 10 million in the previous fiscal year: CIT tax base x 19/20 x 25% – [applicable tax credits + previous instalment payments of the fiscal year + capital withholdings]
	Minimum instalment payment	Applicable to companies with turnover above EUR 20 million in the 12 months preceding the start of the fiscal year calculated as follows: 12% (6% in some cases) of company's profits in the first 3, 9 and 11 months of the current year, net of instalment payments made throughout the same fiscal year.	Non applicable	Applicable to companies with turnover above EUR 10 million in the 12 months preceding the start of the fiscal year as follows: 23% (25% for credit institutions and oil drilling companies) of eligible company's profits in the first 3, 9 and 11 months of the current year, net of instalment payments made throughout the same fiscal year and amounts deriving from agreements with creditors.

(*) To note that companies subject to Spain's CIT have to make three instalment payments per fiscal year. Under Article 40.2 of Spain's CIT law, the instalment payment is defined as 18% times the company's *taxable income* (cuota integra). However, companies can decide on a voluntary basis to make instalment payments under Article 40.3 of the CIT law. In this case, the instalment payment is calculated as a percentage over the company's CIT *tax base*. Nevertheless, the CIT law obliges some companies (namely, larger ones) to make their instalment payments according to Article 40.3 of the CIT law. Moreover, over 2012-2015 and in 2016 (i.e., after Royal Decree Law 2/2016), instalment payments made by those companies have been subject to floors (defined as a percentage over the company's turnover).

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