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From:	General Secretariat of the Council
To:	Permanent Representatives Committee/Council
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Subject:	Recommendation for a COUNCIL RECOMMENDATION on the 2019 National Reform Programme of Poland and delivering a Council opinion on the 2019 Convergence Programme of Poland

Delegations will find attached the above mentioned draft Council Recommendation, as revised and agreed by various Council committees, based on the Commission Proposal COM(2019) 521 final.

COUNCIL RECOMMENDATION

of …

on the 2019 National Reform Programme of Poland and delivering a Council opinion on the 2019 Convergence Programme of Poland

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 9(2) 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,

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,

[1] OJ L 209, 2.8.1997, p. 1.

Whereas:

(1) On 21 November 2018, the Commission adopted the Annual Growth Survey, marking the start of the 2019 European Semester for economic policy coordination. It took due account of the European Pillar of Social Rights, proclaimed by the European Parliament, the Council and the Commission on 17 November 2017. The priorities of the Annual Growth Survey were endorsed by the European Council on 21 March 2019. On 21 November 2018, on the basis of Regulation (EU) No 1176/2011 of the European Parliament and of the Council[2], the Commission also adopted the Alert Mechanism Report, in which it did not identify Poland as one of the Member States for which an in-depth review would be carried out.

(2) The 2019 country report for Poland was published on 27 February 2019. It assessed Poland's progress in addressing the country-specific recommendations adopted by the Council on 13 July 2018[3], the follow-up given to the country-specific recommendations adopted in previous years and Poland's progress towards its national Europe 2020 targets.

(3) Poland submitted its 2019 National Reform Programme on 26 April 2019 and its 2019 Convergence Programme on 29 April 2019. In order to take account of their interlinkages, the two programmes have been assessed at the same time.

[2] 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 (OJ L 306, 23.11.2011, p. 25).

[3] OJ C 320, 10.9.2018, p. 88.

(4) Relevant country-specific recommendations have been addressed in the programming of the European Structural and Investment Funds ('ESI Funds') for the 2014-2020 period. As provided for 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 that provision in guidelines on the application of the measures linking the effectiveness of the ESI Funds to sound economic governance.

(5) Poland is currently in the preventive arm of the Stability and Growth Pact. In its 2019 Convergence Programme, the government plans a slight deterioration of the headline balance from a deficit of 0,4 % of gross domestic product (GDP) in 2018 to 0,6 % of GDP in 2022, with a deficit of 1,7 % of GDP in 2019 and a surplus of 0,2 % of GDP in 2020. The recalculated structural balance, at a deficit of 1,1 % of GDP, will come close to the medium-term budgetary objective, set at a structural deficit of 1,0 % of GDP, in 2022. According to the 2019 Convergence Programme, the general government debt-to-GDP ratio is expected to decrease from 48,9 % of GDP in 2018 to 40,6 % by 2022. The macroeconomic scenario underpinning those budgetary projections is plausible. At the same time, the operational details of some of the measures needed to support the planned deficit targets from 2020 onwards have not been sufficiently specified.

[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).

(6) The 2019 Convergence Programme indicates that Poland implemented drought-related compensatory measures and that their budgetary impact in 2018 was significant. The Convergence Programme provides adequate evidence of the scope and nature of these additional budgetary costs. The specific treatment of drought-related expenditure could be considered in application of the 'unusual event clause'. According to the Commission, the related eligible additional expenditure in 2018 amounted to 0,07 % of GDP. The provisions set out in Articles 9(1) and 10(3) of Regulation (EC) No 1466/97 cater for this additional expenditure, in that the exceptionality of the drought is considered an unusual event, its impact on Poland's public finances is significant and sustainability would not be compromised by allowing for a temporary deviation from the adjustment path towards the medium-term budgetary objective. Therefore, the required adjustment towards the medium-term budgetary objective for 2018 has been reduced to take into account these additional costs.

(7) On 13 July 2018, the Council recommended Poland to ensure that the nominal growth rate of net primary government expenditure[5] does not exceed 4,2 % in 2019, corresponding to an annual structural adjustment of 0,6 % of GDP. Based on the Commission 2019 spring forecast, there is a risk of a significant deviation from that recommended adjustment in 2019.

(8) In 2020, in view of Poland's projected output gap of 2,0 % of GDP, the nominal growth rate of net primary government expenditure should not exceed 4,4 %, in line with the structural adjustment of 0,6 % of GDP stemming from the commonly agreed adjustment matrix of requirements under the Stability and Growth Pact. Based on the Commission 2019 spring forecast under unchanged policies, there is a risk of a significant deviation from that requirement in 2020. Overall, the Council is of the opinion that the necessary measures should be taken as of 2019 to comply with the provisions of the Stability and Growth Pact.

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[5] Net primary government expenditure comprises total government expenditure excluding interest expenditure, expenditure on Union programmes fully matched by Union funds revenue and non-discretionary changes in unemployment benefit expenditure. Nationally financed gross fixed capital formation is smoothed over a four-year period. Discretionary revenue measures or revenue increases mandated by law are factored in. One-off measures on both the revenue and expenditure sides are netted out.

(9) Poland achieved significant progress in increasing tax compliance. At the same time, the country enjoyed strong economic growth, the labour market was buoyant and the share of labour contracts being subject to social security contributions has been gradually increasing. All those factors contributed to an increase in public revenue. A part of the increased revenue is of cyclical nature and may fade when the macroeconomic environment worsens. At the same time, over recent years, public spending increased as a share of GDP. Several new categories of expenditure are of a permanent nature and may not be easy to change in the near future. Moreover, going forward Poland's public finances will face pressures for higher spending, in particular due to population ageing. These factors amplify the need for new tools to strengthen expenditure management, including a regular assessment of the effectiveness and efficiency of spending. While in 2018 Poland continued to work to improve the budgetary system, the overall reform is complex and will be applied in stages over several years. Whereas overall the fiscal framework is strong and independent institutions cover some of the functions typically fulfilled by fiscal councils, Poland remains the only Member State without an independent fiscal council. While Poland made no progress in limiting the extensive use of reduced value added tax rates, the government launched a reform which has the potential to make the rates less complex and less error-prone.

(10) Until 2017, the average age of retirement was increasing, reflecting past reforms such as the withdrawal of early retirement options and a gradual increase of the statutory retirement age. In 2018, the average retirement age decreased both for men and for women, reflecting lowering of the statutory retirement age in late 2017. A continued increase in the effective retirement age is crucial for labour market participation and thus economic growth, given the decline in the working age population. It is also crucial to ensure the adequacy of future pensions, prevent poverty at old age and hence also to improve the fiscal sustainability of the pension system. The lowering of the statutory retirement age to 60 for women and to 65 for men in autumn 2017 will have a significant negative impact on future pension benefit levels and introduces a significant gap between men and women in this regard. Existing preferential pension schemes imply fiscal costs and reduce the mobility of workers between sectors. The special social insurance system for farmers, subsidised at a cost of around 0,8 % of GDP, is hampering labour mobility and contributing to hidden unemployment in agriculture.

(11) The favourable macroeconomic environment has helped the strong performance of the Polish labour market in recent years. Employment rates have continued to increase, while the unemployment rates, after several years of decline, stabilised at a historical low of below 4 % in 2018. However, the participation of some groups in the labour force, especially the low-skilled, persons with disabilities and their carers and older people, has remained low in comparison to other Member States. The Polish social benefit system provides insufficient incentives to take up work. The child benefit has reduced poverty and inequality, but it has had a negative effect on the participation of parents, mostly women, in the labour market due to its size and design. The enrolment rate for children under the age of three in formal childcare remains among the lowest in the Union. In addition, long-term care is mostly provided by family members without almost any institutional support, which prevents carers from working. The lowered statutory retirement age has encouraged some older workers to exit the labour force. Migration from non-Union countries has been helping to meet the increase in demand for labour, but there are signs that a continued inflow of migrant workers may be difficult to achieve.

(12) Between 2015 and 2017, Poland took measures to tackle labour market segmentation by limiting the possibility to abuse temporary employment, increasing social security contributions on some non-standard labour contracts and introducing a minimum hourly wage for some of these contracts. While the share of temporary contracts has been declining since 2015, thanks to the measures taken and due to the shortages of workers, and this process accelerated during 2018, it still remains among the highest in the Union. Further legislative changes addressing this issue were not pursued as the reform of the labour code was finally not implemented. The adequacy of future pensions of workers who are self-employed and those who have certain non-standard contracts emerges as a potential issue.

(13) A quality education and training system that takes the life-long perspective, supported by sufficient investment, could be one crucial factor supporting future growth prospects in Poland. Equipping people with skills and competences that are needed to find employment in a rapidly changing labour market is of crucial importance to encourage both participation in the labour force and the innovative capacity of the economy. The rate of the participation of adults in education and training is much lower than the Union average and vocational training in enterprises is underutilised. This, combined with certain weaknesses in digital skills, as well as in literacy and numeracy skills, particularly among adults with no higher education, is hampering their employability. The insufficient quality of teacher training and some gaps in their skills are likely to have a negative impact on the quality of education. There are also weaknesses in the quality assurance system of the higher education. Despite recent reforms in vocational education and in higher education, the effective coordination of adult learning is still lacking and the impact of different policy measures on the quality of the education and training provided and the skill levels is not clear.

(14) Poland's long-term economic prospects depend on developing the economy's capacity to innovate. However, Poland still ranks low in terms of innovation, with low-tech sectors representing an important share in the country's economic structure and with important regional disparities in innovation performance. While some measures have been taken to improve science-business cooperation, a number of financial and non-financial obstacles persist. In particular, complex administrative procedures and limited skills of academics in managing joint public-private research and development (R&D) projects remain key barriers. The clusters and formalised corporate networks, especially between small and medium-sized enterprises and large firms, play a limited role in diffusing innovative solutions. The 2018 higher education reform improves some aspects of the Polish scientific landscape, but only partially addresses important issues such as the fragmentation of the research sector, researchers' wages or the internationalisation of Polish science. Gross domestic expenditure on R&D remained at about half of the Union average in 2017, with important regional disparities.

(15) Health outcomes have continued to improve but remain below the Union average with males faring worse in life expectancy than females by 7,9 years in 2017 while the gap between the highest and lowest educated Poles was 10 years in 2016. Access to and the effectiveness of the healthcare system is affected by low spending and staff shortages. The number of practising doctors and nurses relative to population size is among the lowest in the Union with quarter of the medical staff above retirement age. Unmet needs for medical services declined in 2017, but remain among the highest in the Union and the waiting times for certain procedures have increased substantially since 2010. Poland has developed maps of healthcare needs, but they have not yet become tools for supporting decisions on the purchasing of health services and investments. The healthcare system remains overly hospital-based and primary and ambulatory care remain underdeveloped. Long-term care system is weak, lacking standardised services and a coherent strategic approach. Most long-term care is provided by informal carers, often family members with little institutional support. In 2017, Poland's public healthcare expenditure totalled 4,7 % of GDP, well below the Union average of 7 % of GDP. Poland plans to gradually increase this expenditure in the coming years. However, this may be difficult to achieve, given that the recently announced plans to increase social transfers to medium- and high-income households will limit fiscal space in the future.

(16) While infrastructure in Poland has improved significantly, some sectors still exhibit important connectivity gaps. Road investments that are to be completed by 2024 according to the national road construction programme will be concentrated mainly in the eastern part of Poland, leaving some northern regions less connected. There are still important gaps in the Trans-European Transport Network Railways, and investment in rail is proceeding slower than investment in roads. The road fatality rate is still among the highest in the Union. Cities face growing mobility challenges, such as congestion and air pollution created by the increasing passenger car fleet and the large share of old cars. Greenhouse gas emissions from road transport have increased strongly over the last five years. The current incentives to use collective, low-emission and active transport modes are insufficient to tackle these challenges. Fixed internet connectivity in Poland remains one of the lowest in the Union, with ultra-fast broadband available mainly in big cities.

(17) The Polish economy is among the least carbon-efficient in the Union. Poor insulation of public and private buildings contributes to higher energy consumption and energy poverty. Poland also has the most air-polluted cities in the Union, especially in the southern and central regions. Investing in higher energy efficiency, in particular in the buildings sector, increasing the share of low-carbon intensive and cleaner energy production, and supporting lower emissions from transport, would reduce the dependency on fossil fuels and limit air pollution, while reducing social costs and improving the quality of life. The current legislative environment, including the gas stock-piling actthe electricity price freeze act and on-shore wind farms regulations, may hamper investments in electricity and gas markets and affect the competitiveness of Poland's energy sector and energy-intensive industries in the long term.

(18) The quality of new and revised legislation, and a stable and predictable business environment are of high importance for sustaining favourable economic conditions and supporting the increase in private investment. The unstable regulatory framework and other barriers to the expansion of firms are negatively affecting investment activity and productivity. Establishing an effective dialogue with all stakeholders would help improve the quality of legislation and — by limiting the number of revisions needed — would contribute positively to the stability of the business environment. Therefore, strengthening the role of consultations of social partners and public consultations – by ensuring a sufficient length of time for consultations, improving the uptake of the stakeholders' opinions gathered in the process, and minimising the number of laws exempted from consultations – would substantially help to minimise the administrative burden resulting from frequent changes in the law, increase investment and promote sustainable economic growth in the long term. Guaranteeing the rule of law and the independence of the judiciary are also essential in this context. It is recalled that in December 2017, the Commission presented to the Council a reasoned proposal to determine that there is a clear risk of a serious breach by Poland of the rule of law. These concerns are the subject of a judgement and on-going procedures which are pending before the Court of Justice of the European Union. Legal certainty and trust in the quality and predictability of regulatory, tax and other policies and institutions are important factors for the investment environment.

(19) The programming of Union funds for the period 2021-2027 could help address some of the gaps identified in the recommendations, in particular in the areas covered by Annex D to the 2019 country report. This would allow Poland to make the best use of those funds in respect of the identified sectors, taking into account regional disparities.

(20) In recent years, the State role strongly expanded in banking, insurance and energy sectors. Increased State ownership presents a new challenge to competition and the regulatory and governance framework. The quality of governance and the independence of regulators and supervision is therefore becoming increasingly important given potentially conflicting interests and stronger financial-sovereign links.

(21) In the light of this assessment, the Council has examined the 2019 Convergence Programme and its opinion[6] is reflected in particular in recommendation (1) below,

HEREBY RECOMMENDS that Poland take action in 2019 and 2020 to:

1. Ensure that the nominal growth rate of net primary government expenditure does not exceed 4,4 % in 2020, corresponding to an annual structural adjustment of 0,6 % of GDP. Take further steps to improve the efficiency of public spending, including by improving the budgetary system.

2. Ensure the adequacy of future pension benefits and the sustainability of the pension system by taking measures to increase the effective retirement age and by reforming the preferential pension schemes. Take steps to increase labour market participation, including by improving access to childcare and long-term care, and remove remaining obstacles to more permanent types of employment. Foster quality education and skills relevant to the labour market, especially through adult learning.

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

3. Strengthen the innovative capacity of the economy, including by supporting research institutions and their closer collaboration with business. Focus investment-related economic policy on innovation, transport, in particular on its sustainability, digital and energy infrastructure, healthcare and cleaner energy, taking into account regional disparities. Improve the regulatory environment, in particular by strengthening the role of consultations of social partners and public consultations in the legislative process.

Done at Brussels,

For the Council

The President