

## APPENDIX 3

# SUMMARIES OF THE CONTENTS OF KEY MEMORANDA OF UNDERSTANDING FOR GREECE, IRELAND, PORTUGAL AND ROMANIA

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## Greece

**European Commission Directorate-General for economic and financial affairs (2010): The economic adjustment programme for Greece, *European economy occasional papers no. 61*, Brussels, European Commission, May 26**

(Note: The paper above includes as Attachment 1 the May 3 2010 Memorandum of Economic and Financial policies).

Between 2000 and 2009 Greece closed the income gap with the rest of the EU from 25% to 10%. The paper argues that Greece’s strong growth performance (4% compared to 2% in the euro area) was unsustainable because it was based on a domestic demand boom especially in consumption and housing investment. Real wage rises and rapid credit growth (following financial sector liberalisation and low real interest rates after adoption of the euro) fuelled the boom. An overvalued exchange rate sucked in imports and led to serious balance of payments imbalance. In 2008 the current account deficit was 14% (Occasional papers 61, p3-4).

Unit labour costs rose relative to those in north Europe which the paper assumes affected the current account deficit, yet later on the paper admits that Greece’s main service exports are not price elastic and wages are a small proportion of total price (Occasional papers 61). The authors also accept that their competitiveness estimates are subject to several sources of error (Occasional papers 61, p5).

The government sector grew from 44% to 50% of GDP – similar to some northern countries. But without stating evidence the paper assumes this was “crowding out private sector resources and therefore weakening economic performance” (Occasional papers 61, p3-4).

Nevertheless this story about declining competitiveness and crowding out by the public sector is the justification offered for the assault on the size and scope of the public sector that is core to the economic adjustment programme summarised below.

It should be noted that the measures in the programme are the same as those later adopted by Portugal (see summary in this appendix) , from public administration and health service cuts to consumer tax rises, local authority reorganisation, liberalisation of the energy markets and legal changes to collective bargaining rights.

## *Programme objective*

In the short term the programme aims to cut governments financing needs and “reassure markets on the determination of the authorities to do whatever it takes to secure medium and long-term fiscal sustainability”. The focus is on expenditure cuts in a ratio of 2:1 with tax raising measures. The medium term objective is to “improve competitiveness and alter the economy’s structure towards a more investment –and export-led growth model”. Illustrating troika priorities, “an overarching objective is to durably restore Greece’s credibility for private investors” (Occasional papers 61, p10 paras 9-11).

The authorities believe the “fiscal adjustment is fairly distributed across society and protects the most vulnerable”. They argue the programme has “taken into account the social dimension” (Occasional papers 61, p28 para 41). There are some measures such as moderating the impact of public wage cuts on the lowest paid, but whatever measures there are to protect the most vulnerable in specific policies, the overwhelming loss of GDP (planned to be €1 in €5 and in fact worse in out-turn), impoverishes the already poor and vulnerable.

## *Financial sector viability*

Private debt was not a serious element of the crisis in Greece although bad debt did rise in the aftermath of the 2008 crash. But the size of Greek public debt (which rose from an already high 90% or more, to over 100%) meant some financial speculators decided post 2008 crash that Greece was a default risk and would lend only at rates above 6%. Banks were affected through their holdings of Greek government debt – both directly and due to withdrawals by foreign investors. Greek banks lost access to capital markets and needed capital injections from the Greek government and ECB. European institutions were also concerned about risk of contagion in south-east Europe due to Greek parent banks in Balkan countries. Banking supervision is strengthened and the adjustment programme provides for higher capital buffers for banks, but liquidity remains tight and therefore lending to small businesses is weak (Occasional papers 61, p7-8, 21).

## *Fiscal consolidation*

The scale of adjustment required by the programme is enormous. To achieve the Eurozone fiscal compact rules the government has to get the fiscal deficit from 14% of GDP to 3% (originally by 2014). In fact to stabilise government debt the troika want Greece to run a primary a fiscal surplus to compensate for headwinds of Eurozone austerity, interest on debt repayments, negative Greek GDP “growth”, falling tax revenue and rising social security payments. To get an 11 point reduction in the deficit requires an 18% cut in GDP. The targets were raised following revision of Greek data in April 2010 and deeper recession (Occasional papers 61, p13, paras 16-18). To get debt down, Greece will have to run a primary surplus (raise more than it spends) after the end of the three year programme. The authorities have committed to running a “sizeable” surplus of 5% of GDP through to 2020 (Occasional papers 61, p30, para 46).

Because Greece is in the Eurozone, the full weight of adjustment falls on domestic wages and prices – there is no scope for some adjustment through lowering the exchange rate to make imports dearer and exports cheaper and so improve the trade balance. Fiscal consolidation is front-loaded: 8% cuts in GDP in 2010 and the programme MOU states that “difficult measures will be legislated up front”. These include cuts in nominal wages and pensions (given inflation, real cuts are bigger than nominal cuts) and increases in VAT and excise taxes, which hit the poor hardest. Positively, tax administration and tax evasion are to be tackled and income tax made more progressive (Occasional papers 61, p14-15).

Since the wage cuts are in public administration and services, the poor, especially women and children, will also be hit by loss of services at the same time as their incomes are hit.

The paper states that the “public sector (is) responsible for many of Greece’s woes” (Occasional papers 61, p20). The public sector wage bill increased by close to 100% from 2000-2008 while GDP increased by 74%, although the skill mix developments over the period are not stated. Initial public sector wage cuts were about 14.5%, with pension cuts in addition, although the lowest paid public sector workers were given a flat rate compensation for some of the cut in wage and pensions. Private sector wages were not cut (Occasional papers 61, p15 and p16 Box 5, p21). The authors state that firms did not think wages were too high, that it was unlikely to make much difference to competitiveness as oligopoly firms would pass on wage rises as price rises, but it would make income distribution more unequal.

Public pensions were frozen or cut and retirement age was raised to 65 with more increases to come. Women’s pension age was increased immediately. Pension accrual rates are reduced and penalties introduced for early retirement. Pensions are increased in line with prices, rather than wages. While many of the pension changes seem to be driven primarily by fears of the costs of an ageing population, there are also changes to disability pensions (Occasional papers 61, p80).

### **Growth strategy**

Growth was expected to be negative throughout the three year programme. Future growth is believed to be liberated through structural reform in the labour and product markets – flexibilisation and liberalisation respectively. The aspiration for growth later ignores Keynes caution that “in the long run we are all dead”. The structural reforms also imply strong interference in internal democratic arrangements.

Labour market changes focus on containing wage rise pressure by decentralising wage bargaining and preventing the extension of collective agreements. Cuts in public sector wages also are expected to put downward pressure on private sector wages. Below minimum wages are introduced in the belief this will open the labour market to the young and long-term unemployed though there is no discussion of the risks of substitution of one group of workers for another. Overtime pay is reduced. It is made easier to sack workers and to offer part-time and temporary work and severance pay is to be reduced. The “social safety net” was reviewed with the aim of being “better targeted” by 2011 (Occasional papers 61, pp22, 48, 79, 80).

The authorities had aspirations to “forging consensus on policies to overcome the crisis and to inviting representatives of businesses and labour to sign a social pact”... (Occasional papers 61, p28, para 41). In letters to the troika on 15 February 2012<sup>1</sup>, the Panhellenic Socialist Movement and New Democracy agreed to support the whole reform programme. The Panhellenic Socialist Movement argued the reforms must be accompanied by positive education and training measures. They also appealed for a strong social protection net to avoid “extreme marginalisation” from the impact of lower minimum wages. In the same letter they also argued for new green growth funding sources and a stronger fight against tax evasion and tax havens.

Product market reforms focus on competition, especially by implementing European Directives on energy, rail and services (Occasional papers 61, p22). Privatisation of state assets is also on the agenda. Competition may lower tariffs and product prices, but may not. No protection for poorer consumers is mentioned.

Local government was cut both in the number of local administrations and “elected/appointed officials” (Occasional papers 61, p48 para 22).

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<sup>1</sup> The letters are attached to the Memorandum of Understanding between the European Community acting on behalf of the Euro area member states and the Hellenic Republic, 2012, March.

## ***Memorandum of Understanding between the European Community acting on behalf of the euro area member states and the Hellenic Republic, 2012***

This MOU agreed debt exchange with private creditors because it was clear that Greek sovereign debt (now over 180%) could not be reduced to the target of 120% of GDP by 2020 despite the scale and depth of the austerity programme. The nominal debt value was reduced by 53.5% in March 2012.

### ***Eurogroup statement on Greece of 27 November 2012<sup>2</sup>***

In a Eurogroup statement on Greece of 27 November 2012, the Eurogroup praised Greece for its additional implementation mechanisms to safeguard fiscal consolidation and privatisation. "Greece will transfer all privatisation revenues, the targeted primary surpluses as well as the 30% of the excess primary surplus" to its debt servicing account. Much of Greece's effort is still going to pay external creditors rather than rebuild its economy.

Yet the Eurogroup noted that the November 2012 outlook was worse compared to March 2012 when Greece's second economic adjustment programme concluded. Target dates to achieve primary surplus have been moved from 2012 to 2014 and interest rates and fees charged on troika loans have been reduced.

## **Ireland**

In a press release of November 28 2010<sup>3</sup> the European Commission and IMF praised the Irish economic adjustment programme as a "roadmap for sound public finances" and stated that it made "due regard for Ireland's strong system of social protection". The summary below indicates the strong focus of the programme on expenditure cuts compared to revenue rises and the "liberalisation" of labour markets and services.

### ***Memorandum of economic and financial policies May 11 2010***

#### ***Objective***

Export-led growth and improved current account balance following "ambitious fiscal consolidation" and "fundamental downsizing and re-organisation of the banking sector". The Memorandum anticipates downside risks of falling domestic demand and low inflation keeping the real value of debt high. The MOU also acknowledges that "profit repatriation by multinationals and large interest payments to foreign holders of Irish debt are expected to limit improvement in the programme period" (three years)." (MOU 2010, May 11 paras 3-5).

#### ***Financial sector viability***

In late 2009, the government boosted bank capital and established the National Asset Management Agency (NAMA) to take on bad debt in banks and property development; it also committed to introducing structural reforms to stabilise the financial sector including enhanced supervision, deleveraging (reducing the ratio of debt to assets), holding higher levels of capital (which reduces capacity to create credit lending) and taking two large banks into public ownership (MOU 2010, May 11 paras 6-12).

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<sup>2</sup> Eurogroup statement on Greece of 27 November 2012 get access address

<sup>3</sup> European Commission (2010) *Commission and IMF issue joint statement on Ireland*, November 28, accessed at [http://ec.europa.eu/economy\\_finance/articles/eu\\_economic\\_situation](http://ec.europa.eu/economy_finance/articles/eu_economic_situation)

The Irish government committed also to: making it easier to go personally bankrupt, providing means tested support for mortgage holders in difficulties; strengthening credit unions (community based lenders) and ensuring the flow of credit to small businesses ((MOU 2010, May 11 paras 16-20).

It should be noted that “capital injections in the banks have placed a heavy burden on public finances” (MOU 2010, May 11 para 7).

### ***Fiscal consolidation***

In November 2010 the Irish government published a “National Recovery Plan 2011-2014” which formed the basis of the 2011 budget. Over three years, it aimed to make cuts of €15b, equivalent to 9% of GDP, merely to stabilise the deficit. These cuts were front-loaded, with €6b of measures in the first year (MOU 2010, May 11 paras 21-22).

There was much more emphasis on expenditure cuts than revenue rises and cuts were proposed for capital (infrastructure) and current spending. The latter included cuts to public sector workforces (which the government aimed to achieve without compulsory redundancies) and therefore services, and also public service pensions. Cuts to “social transfers” (cash benefits to qualifying individuals and households) were focused on those of working age and on universal benefits, such as child benefit.

The net effect of this approach is to refocus the ambition of social security to a safety net “protecting the socially vulnerable” (MOU 2010, May 11 para 22). There is no ambition to prevent or remediate poverty.

Revenue raising ambition was weaker than expenditure cuts, amounting to €2b a year from 2011. The main focus was to increase the tax take from families on modest incomes (“ordinary incomes”) through a reduction of 10% in income tax bands (which lowers the income threshold at which any tax rate is payable) and in tax credits (income supplements for low paid workers) and a reduction in pension tax relief (MOU 2010, May 11 para 23).

New service charges planned for 2012 onwards included property taxes, water charges (for the first time) and increased fees for higher education (the latter while ensuring “lower-income groups remain supported”) (MOU 2010, May 11 para 24).

### ***Growth strategy: market liberalisation***

Despite the negative impact on current growth, the government believes the measures will provide a basis for “medium-term growth *potential*” (MOU 2010, May 11 para 24). Therefore current pain for those more dependent on public support is for potential gain – but for whom?

The main focus is on structural reforms to increase “competitiveness” in the service sector and “efficiency” in utilities, through privatisation of state-owned assets (MOU 2010, May 11 paras 26-27).

### ***Financing for economic adjustment (the size of Ireland’s borrowing is detailed in Appendix 2)***

Despite the severe cuts, Ireland needed to borrow from the European institutions – about €80b over the three year programme, to finance its effective balance of payments deficit and to support banks’ ability to rollover their debt. Ireland intends to borrow only as needed and hopes to pay down its borrowings faster than required – tightening the fiscal squeeze (MOU 2010, May 11 paras 28-30).

## ***Programme monitoring***

Monitoring is continuous and includes performance criteria, timetables and targets legally agreed in the Technical Memorandum of Understanding and in compliance with the Eurozone Excessive Deficit Procedure (EDP). There are structural benchmarks and recommended structural policies (MOU 2010, May 11 paras 31-32 and Tables 1 and 2).

## ***Memorandum of Understanding – specific economic policy conditionality – 3 December 2010***

The structural reforms are specified in detail in this MOU, in terms of deadlines and cash expected to be saved or raised in the first period. Additional measures in the first year focus on the labour market. It includes a €1 cut in the minimum wage (later reversed) and measures to make it easier for firms to sack workers. Incentives to work rely on punitive measures such as reducing the replacement rates of various working age benefits and increasing conditionality and sanctions in activation measures for unemployed people (MOU December 2010 p5-6).

Pension measures include raising the state pension age to 66 by 2014 and 68 by 2028 (MOU December 2010 p7) and cutting the real value of state pensions by freezing its money value (MOU December 2010 p14). The government also cut the value of public service pension entitlements through a move to pensions based on career average earnings. Public sector pay was cut 10% for new entrants (MOU December 2010 p9).

Also in the first year, the government committed to opening access to the legal and medical professions and cutting drug costs in pharmacies (MOU December 2010 p8).

In summer 2012, Ireland was in a position to begin market borrowing again. The seventh review mission (July 3-12) assessed compliance with policy conditionality of the programme and an overview of “remaining challenges”. Ireland’s progress and compliance was praised. The neoliberal framework of the programme is clear. The report acknowledged weaker growth in Ireland’s trading partners and therefore very weak (and falling) Irish growth of 0.4%. There is both high unemployment (14.8%) and rising long term unemployment. Despite this, the focus of the report was on further austerity. The report recommended further cuts in “overruns” on health and welfare spending (the latter surely a consequence of weak growth and high unemployment). They approved the steps to weaken wage bargaining and strengthen competition law. Despite high unemployment, they stated that more needed to be done to eliminate “work disincentives” and “unemployment traps” and approved of the plan to decouple housing support from unemployment status, which should be “rigorously pursued”.<sup>4</sup>

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<sup>4</sup> Occasional papers Index (2012) *Economic adjustment programme for Ireland - summer 2012 review*, Occasional Papers No. 115/2012

### *Memorandum of understanding on specific economic policy conditionality 17 May 2011<sup>5</sup>*

#### **Objective**

The programme aims to reduce the budget deficit to 5.9% of GDP in 2011, 3% by 2013 and a balanced budget in the medium term. The focus is on expenditure cuts and increased competitiveness, while “minimising the impact of (fiscal) consolidation on vulnerable groups” (MOU 2011, 17 May, para 1). The domestic slack is expected to be taken up by exports (Amending Decision 2012, October 2 para 3, see below).

#### **Financial sector viability**

The aim is to stabilise the banking sector and maintain liquidity. There are commitments to reduce banks’ risk exposure by enforcing deleveraging and the holding of higher capital ratios. There are also new regulations to protect depositors and enhance banking supervision. There are new developments on indebtedness that aim to ease personal bankruptcy proceedings and to rescue viable firms (MOU 2011, 17 May, paras 2.1-2.22).

There is also privatisation of some of the business of state savings banks, e.g. insurance (Amending Decision 2012 October 2, see below).

#### **Fiscal consolidation**

Expenditure cuts aim to “eliminate services that do not represent a cost-effective use of public money” (MOU 2011, 17 May, para 1.7). There is no alternative option of retaining valued public services but providing them in a more efficient way.

There is no intention to cut overall tax take, but to re-orient it to “lower labour costs and boost competitiveness” , broaden the base by minimising allowances (e.g. deductions for health care insurance) and subsidies and make tax collection more effective (MOU 2011, 17 May, para 1.3). The major tax increases are regressive, mainly increases in VAT and excise taxes, but also property tax and application of income tax to all social transfers (MOU 2011, 17 May, paras 1.21-1.24). Otherwise a “standstill rule” prevents the government introducing any new tax raising measures (MOU 2011, 17 May, para 1.18).

Changes to civil service administration aim to cut headcount by 1% in central government and 2% in local government and to cut budgets by 15% in both government tiers. Wages are frozen in nominal terms (therefore real wage cuts) and benefits and pensions are reduced. Cuts to public sector pensions overall are planned to save €445m, but pensions below €1500 are relatively protected (MOU 2011, 17 May, paras 1.9 and 1.11).

Cuts and mergers in the regional and local tiers of government aim to save €175m, with another €110m from other public bodies, mainly by delocalisation.

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<sup>5</sup> Portugal: Memorandum of understanding on specific economic policy conditionality 17 May 2011, 2011-05-18-mou-portugal\_en.pdf, accessed at [ec.europa.eu/economy\\_finance/eu\\_borrower/mou/2011-05-18-mou-portugal\\_en.pdf](http://ec.europa.eu/economy_finance/eu_borrower/mou/2011-05-18-mou-portugal_en.pdf)

The MOU agrees to take €195m out of the schools budget, reducing the number of schools and the staff headcount. At the same time there is a commitment to improve the quality of secondary school education and vocational training partly by introducing payments-by-results contracts (MOU 2011, 17 May, paras 1.8 and 4.10).

Complete revision of Portugal's National Health Service aims to cut €550m. Changes include cuts in hospital provision, much greater user charges for medicines and transport to hospital and competition for the provision of certain services (MOU 2011, 17 May, paras 1.10 and 3.5-3.83).

Section 4 of the MOU describes labour market measures that weaken worker rights. They make it easier to dismiss workers for unsuitability, weaken seniority rules and reduce severance pay. They flexibilise working time arrangements and cut overtime pay rates and opportunities to claim overtime hours. The minimum wage is effectively frozen for three years. Collective bargaining rights are seriously weakened: extension of rights can be denied on competitiveness grounds and works councils can conclude firm level agreements without trades union input.

The neoliberal agenda is clear in the scale of privatisation of state-owned assets and in the approach to housing. Section 5 of the MOU agrees to deregulation of gas and electricity tariffs and an increase in VAT on them, which is liable to hit the budgets of poor and vulnerable people, though increased competition in the telecoms market may reduce charges. Liberalisation of transport includes raising rail ticket prices and increasing competition in airlines. Most evident in sections 5 and 6 is that the MOU is being used to enforce EU competition law. The MOU explicitly insists on the full implementation of various EU Directives in telecoms and Services as well as rail packages.

The MOU states that access to rental housing will be improved by "phasing out rent control mechanisms considering the socially vulnerable" and making it easier to evict tenants (MOU 2011, 17 May, para 6.1). Property tax changes reduce allowable income tax deductions "except for low income households".

There is no suggestion of monitoring the impact on poverty of the MOU package, nor is there any discussion of growth.

### ***Council implementing decision amending implementing Decision 2011/344/EU on granting Union assistance to Portugal<sup>6</sup>***

The decision and report published on October 2 2012 noted that Portuguese rebalancing was at a faster than expected pace. It illustrates the severity of the fiscal squeeze; the current account deficit fell from 10% to 3% in two years. Paragraphs 9-12 approve of progress in liberalising the labour market, implementing the Services Directive, enforcing competition law and deregulating planning and tourism.

Yet Portugal remains in severe recession, with contraction of 3% of GDP in 2012 and contraction expected to continue in 2013 "affected by a diminishing stimulus from external demand and the impact of further budgetary consolidation" (Amending Decision 2012 October 2, para 2) .

The perverse effects of the austerity programme are clear. There has been a significant decline in tax revenue due to falling incomes and profits and shrinking and shifting domestic demand. High unemployment is increasing social security expenditure, but staff cuts have brought in more savings than expected. The report admits that "the fiscal programme targets over 2012-2014 (are) unattainable".

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<sup>6</sup> Council of the European Union (2012) *Council implementing decision amending implementing Decision 2011/344/EU on granting Union assistance to Portugal*, 13936/12 ECOFIN 786 UEM 278, October 2

The targets are adjusted, but front-loaded to “maintain the credibility of the programme” (Amending Decision 2012 October 2, paras 3 and 4). In paragraph 5 the Amending Decision recommends focussing on cutting the public sector wage bill, cutting health spending still further, increasing the effective rate of income tax by changing the bands and increasing VAT and excise taxes. Paragraphs 6-9 of the 2011 Decision are replaced, but recommend the same type of cuts in current (especially public sector wages and pensions) and capital spending plus frontloading of the cuts in social benefits and other incomes to “secure the deficit target for 2012” (Amending Decision 2012 October 2, para 6a). The privatisation programme is expanded (Amending Decision 2012 October 2, para 7g).

Growth is mentioned only in the Amending Decision paragraph 7a: “The Portuguese Government shall explore ways to increase the weight of expenditure reduction in the overall consolidation package for 2013 in order to ensure medium term growth-friendly (fiscal) adjustment tilted to the expenditure side”. Expenditure cuts are likely to affect poor people more than tax rises; therefore even within the assumptions that the strategy is an effective one, the room for growth is being extracted from the living conditions of the poor. Since the budget consolidation is permanent, the poor are permanent losers; “unavoidable costs of adjustment” according to the Sixth Review Mission to Portugal.<sup>7</sup> Yet growth by 2014 is expected to be just 0.8% and there are “stronger headwinds”.

## Romania

### ***Memorandum of Understanding between the European Community and Romania, June 6, 2009***

The Memorandum contains an ***Annex 1 on specific economic policy criteria*** covering conditionality for disbursement of the second and subsequent loan instalments.

Romania is not a member of the Eurozone and its loan requirements from the EU, IMF and World Bank are for balance of payments assistance.

#### ***Financial viability***

Bank stress tests were already completed following the financial crash. Capital adequacy ratios are agreed to rise to 10% (from 8%). Financial supervision will be strengthened and greater monitoring of liquidity will take place, with a wider range of assets acceptable as collateral (MOU 2009, May, p4).

#### ***Fiscal consolidation***

The MOU states that procyclical fiscal policy and weak public finance management resulted in Romania’s high fiscal deficit. To reduce the fiscal deficit to 3% of GDP by 2011, in May 2009 the EU, IMF and World Bank provided Romania with medium term financial assistance of up to €5b, 12.95b and €2b respectively. (Later Eurozone economic adjustment programmes for Ireland, Greece and Portugal were funded in a ration of about 70:30 by the European institutions). The loans were conditional on expenditure cuts of more than 4% of GDP and a small effort in revenue raising of 0.25%, mainly by cutting some deductions and allowances (MOU 2009, May, p2-3). A fiscal responsibility law enforces a binding medium term budget framework.

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<sup>7</sup> Europa press release (2012) *Statement by the EC, ECB, and IMF on the Sixth Review Mission to Portugal*, Reference MOU 12/879, Brussels, November 19, accessed at [http://Europa.eu/rapid/press-release\\_MOU-12-879\\_EN.htm](http://Europa.eu/rapid/press-release_MOU-12-879_EN.htm)

The focus of expenditure cuts was on public administration wages and headcount and spending on services and public enterprises. Only one in seven public sector job-leavers were to be replaced and wages were cut by 5%. These cuts were on top of measures already taken by the Romanian government. Pay scales and bonuses were reformed to reduce and cap the share of bonuses in pay (MOU 2009, May, p2-3). There was a commitment also to produce a plan to tackle undeclared work (MOU 2009, May, p6 section 5d).

Public pensions are to be updated only by prices rather than wages and further increases in the pension age were introduced, especially for women. Contributions to pensions are increased. But there is a “view to protect vulnerable pensioners and to obtain the objective of 45% replacement ratio for retirees on average” (MOU 2009, May, p4, section 5b and p10-11 Annex).

### ***Growth strategy***

The focus is on structural reform “in line with the policy areas covered in the country specific recommendations issued by the Council in the framework of the Lisbon strategy” (MOU 2009, May, p5, section 5d).

Reform of public administration will focus on “the respect of the *aquis communautaire*”. There will be a focus also on removing impediments to doing business and improving absorption of EU funds, especially through improving the effectiveness of the Transport Ministry.

### ***Memorandum of Understanding between the European Community and Romania, December 14, 2009: Annex: Memorandum of Understanding on specific economic policy conditionality (first supplemental Memorandum)***

This MOU *updates the specific economic policy criteria in the annex of the original Memorandum of Understanding of June 2009.*

Many of the measures are focused on improving financial management, monitoring and reporting in the public sector and by financial organisations. But unlike some other emergency assistance countries, there has been no move to ease personal insolvency or debt collecting law as it might “undermine credit discipline” (MOU 2009 December, p7, para19). Other measures re-emphasise the early implementation of actions related to the EU Services Directive, especially in rail and retail (MOU 2009 December, p9).

In terms of fiscal consolidation, this MOU requires “sufficient buffers on the expenditure side” (i.e. more cuts) to compensate for potential underperformance in tax revenues (MOU 2009 December, p1, para1).

The MOU also requires stronger monitoring of state owned enterprises and more action on government payment arrears. It reemphasises the cap on the total public sector wage bill and increasing all wages only in line with productivity “while respecting the autonomy of the social partners, national traditions and practices. Labour market reforms also re-emphasise extending the use of fixed term contracts “while ensuring this does not increase labour market segmentation”, and time off rather than increased pay to compensate for overtime hours worked (MOU 2009 December, p1, paras 3-6, p10 paras 35-38).

In addition to budget control of state hospitals, new measures include introduction of legislation to enable means-tested co-payments for access to medical services (MOU 2009 December, p4-5, paras 7, 9). Other measures that may affect lower income households more are the plans to phase out regulated energy prices for domestic consumers by 2015, with gradually increased tariffs in the meantime. There is though a commitment to “explicitly define vulnerable consumers in the electricity and gas laws and develop mechanisms to protect them” (MOU 2009 December, p7-8, paras 23-24).

## ***Memorandum of Understanding between the European Union and Romania, May 12, 2011***

This MOU contains also an *Annex 1 on Specific economic policy criteria* which largely restates the measures in the earlier MOU Annexes. The updated Annex 1 is more explicit about closing unprofitable parts of the rail network.

Although the austerity measures in 2010 cut the budget deficit from 7.3% of GDP in 2009 to 6.4% in 2010 on a cash basis, inflation rose to 8% in 2010 due to “significant hikes in indirect taxation and higher food and energy prices” (MOU 2011 May, p2, para 4). It is likely much of this inflation was policy induced by the deregulation required by the original MOU.

In May 2011 the Council of the European Union provided further “precautionary” financial assistance of €1.4b for Romania under the Balance of Payments (BoP) facility. The money is tied especially to labour and product market reforms. Additional “precautionary” IMF stand-by assistance equivalent to €3.5b was put in place. The money is “precautionary” in the sense it is activated on request by Romania because the fiscal situation has seriously deteriorated due to “factors outside the control of the authorities” (MOU 2011 May, p1, para 2). In addition to the existing €400m of development loans, the World Bank provided payments-by-results finance for implementation of social assistance and health “reforms”.

Because Romania has low “flat” income taxes, VAT is about 30% of total tax revenue and therefore pursuing VAT evasion and fraud is a key part of strategy, but nothing is said about moderating the impact of indirect tax on poorer households, or about tax fairness (MOU 2011 May, p3, para 5B).

Structural reform of the labour market is re-emphasised, but this time with a requirement for more adequate employment protection (MOU 2011 May, p4, section E).

## ***Memorandum of Understanding between the European Community and Romania, June 22, 2012: Annex: Memorandum of Understanding on specific economic policy conditionality (second supplemental Memorandum)***

Although Romania is not in the Eurozone, this MOU aimed to get down the budget deficit for 2012 to the fiscal compact criteria of 3% of GDP.

The MOU content concerns the updating of the earlier MOUs and Annexes in respect of implementation of the measures described. It also enjoins the Romanian authorities to consult with the Troika “on the adoption of policies that are not included in this Memorandum but that could have a material impact on the achievement of the programme objectives” (MOU 2012, June, p2).