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Recommendation for a

COUNCIL RECOMMENDATION

on the 2019 National Reform Programme of the Netherlands and delivering a Council opinion on the 2019 Stability Programme of the Netherlands

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Articles 121(2) and 148(4) thereof,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies[1], and in particular Article 5(2) thereof,

Having regard to Regulation (EU) No 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances[2], and in particular Article 6(1) thereof,

Having regard to the recommendation of the European Commission,

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,

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, the Commission also adopted the Alert Mechanism Report, in which it identified the Netherlands as one of the Member States for which an in-depth review would be carried out. On the same date, the Commission also adopted a recommendation for a Council recommendation on the economic policy of the euro area, which was endorsed by the European Council on 21 March 2019. On 9 April 2019, the Council adopted the

[1] OJ L 209, 2.8.1997, p. 1.
[2] OJ L 306, 23.11.2011, p. 25.

recommendation on the economic policy of the euro area ('Recommendation for the euro area').

(2) As a Member State whose currency is the euro and in view of the close interlinkages between the economies in the economic and monetary union, The Netherlands should ensure the full and timely implementation of the Recommendation for the euro area, as reflected in recommendations (1) and (3) below. In particular, investment measures and measures supporting wage growth will help address the first euro area recommendation as regards euro area rebalancing, tax measures will help address the second euro area recommendation as regards fight against aggressive tax planning, and reducing the debt bias for households will help address the fourth euro area recommendation as regards reducing the debt bias in taxation.

(3) The 2019 country report for the Netherlands[3] was published on 27 February 2019. It assessed the Netherlands's progress in addressing the country-specific recommendations adopted by the Council on 13 July 2018, the follow-up given to the recommendations adopted in previous years and the Netherlands's progress towards its national Europe 2020 targets. It also included an in-depth review under Article 5 of Regulation (EU) No 1176/2011, the results of which were also published on 27 February 2019[4]. The Commission's analysis led it to conclude that the Netherlands is experiencing macroeconomic imbalances. In particular, the high stock of private debt and the large current account surplus constitute sources of imbalances, with cross-border relevance. Supported by economic growth, the private debt-to-GDP ratio has continued its downward trend both for corporate and households debts, although it is still elevated. Nevertheless, nominal household debt is slowly increasing on the back of rising house prices.

(4) On 29 April 2019, the Netherlands submitted its 2019 National Reform Programme and its 2019 Stability Programme. In order to take account of their interlinkages, the two programmes have been assessed at the same time.

(5) 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[5], 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[6.]

(6) The Netherlands is currently in the preventive arm of the Stability and Growth Pact. In its 2019 Stability Programme, the government plans a decrease in the general government surplus from 1.5% of GDP in 2018 to 0.0% of GDP in 2022. Based on the

[3] SWD(2019) 1018 final.

[4] COM(2019) 150 final.

[5] 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] COM(2014) 494 final.

recalculated structural balance[7], the medium-term budgetary objective — a structural deficit of 0.5% of GDP — continues to be overachieved throughout the programme period. According to the 2019 Stability Programme, the government debt-to-GDP ratio is projected to fall from 52.4% of GDP in 2018 to 44.6% of GDP in 2022. The macroeconomic scenario underpinning those budgetary projections is plausible. Based on the Commission 2019 spring forecast, the structural balance is projected to decline from a surplus of 0.8% of GDP in 2018 to 0.7% of GDP in 2019 and 0.2% of GDP in 2020, above the medium-term budgetary objective. General government debt is forecast to remain on a firm downward path. Overall, the Council is of the opinion that the Netherlands is projected to comply with the provisions of the Stability and Growth Pact in 2019 and 2020. At the same time, while respecting the medium-term budgetary objective, it would be important to use fiscal and structural policies to support an upward trend in investment.

(7) With respect to fiscal sustainability, the projected increase in public expenditure on long term care points to medium risks in long-term sustainability. In 2015 the government moved a large part of the long-term care system to the municipal domain to improve its efficiency and lower public expenditures. The impact of this reform on fiscal sustainability needs to be monitored.

(8) As of November 2018, the funds of the Deposit Guarantee Fund, an independent legal entity, have been moved from a segregated account in the Dutch central bank to an account with the Treasury. The Dutch Deposit Guarantee Fund was being built up gradually and had so far accumulated around EUR 1 billion, with an additional EUR 4 billion to be paid by banks by 2024, which should have been invested in a diversified portfolio of low-risk assets in line with the Deposit Guarantee Scheme Directive. The transfer of the account of the fund reduces the gross debt level, but has no effect on the public deficit. Following this transfer, the Treasury will be able to use the funds for the financing of government expenditures, but will have to make the funds available in case there is a need to make pay-outs to depositors or finance interventions in accordance with its legal mandate, which may have an impact on financial stability.

(9) Dutch households combine large illiquid assets in housing and pensions with high household debt. Long balance sheets make households vulnerable to financial and economic shocks. High household debt is explained by generous tax relief on mortgage interest payments, but also by a lack of a well-functioning middle segment on the rental market and high compulsory pension savings. A key challenge in addressing high household indebtedness lies in the housing market, where the rigidities and distortive incentives that have built up over decades shape the patterns of housing financing and sectoral savings. Since 2012, a series of measures has been implemented that partly addresses this. The announced acceleration of the reduction in mortgage interest tax deductibility has been put into law and will start in 2020. Despite this, the tax relief on mortgage payments remains generous and continues to result in a substantial debt bias for households. At the same time, the private rental market, as the only non-subsidised segment, remains underdeveloped accounting for 13% of total dwellings. The lack of a well-functioning middle segment on the rental market encourages households to buy rather than rent, leading to high debt-to-income ratios and financial vulnerability

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

(10) While the pension system performs well on pension adequacy and fiscal sustainability, it has drawbacks in terms of intergenerational fairness, transparency of pension rights and flexibility. Moreover, occupational pension contributions are high and fluctuate depending on how pension funds perform. As such it may affect household spending in a pro-cyclical way. A reform of the pension system could, over the life cycle, lead to lower compulsory pension contributions and more stable consumption (or 'consumption smoothing'). The government has the intention to substantially reform the second pension pillar in order to improve coverage and create a more transparent, more flexible and actuarially fairer system. A simultaneous reform of housing market institutions and the pension system has the potential to shorten household balance sheets, and make the household sector less vulnerable to financial and economic shocks with beneficial effects for macro-economic resilience and economic growth.

(11) Despite low unemployment, high job vacancy rates and growing shortage of workers, nominal wage growth has remained moderate so far (1.1% in 2017and 2.4% in 2018). Wages in collective agreements increased on average by 2.1% in 2018, while public wages increased at a faster rate (by 3% in the second half of 2018). Furthermore, wage agreements were reached leading to a nominal increase of 7% in 2 years for all civil servants in central government. Additional funding has been provided to increase the salaries of primary school teachers. In addition, the government adopted several fiscal measures which reduce the tax burden on labour and aim to increase the net disposable household income of those who work. Further boosting disposable household income by strengthening the conditions that support wage growth and reforming the second pillar of the pension system to make it more transparent, inter-generationally fairer and more resilient to shocks would support domestic demand and help to rebalance the euro area.

(12) The fight against aggressive tax planning is essential to make tax systems more efficient and fair as acknowledged in the 2019 euro area recommendation. Spillover effects of taxpayers' aggressive tax planning strategies between Member States call for a coordinated action of national policies to complement EU legislation. The Netherlands has taken measures against aggressive tax planning, but the high level of dividend, royalty and interest payments made via the Netherlands suggests that the country's tax rules are used by companies that engage in aggressive tax planning. A large proportion of the foreign direct investment stock is held by 'special purpose entities'. The absence of withholding taxes on outbound (i.e. from EU residents to third country residents) royalties and interest payments may lead to those payments escaping tax altogether, if they are also not subject to tax in the recipient jurisdiction. The announcement of the reform agenda on taxation, including withholding taxes on royalty, and interest payments in case of abuse or payments to low-tax jurisdictions, is a positive step to decrease aggressive tax planning and should be monitored closely.

(13) Growth in employment in recent years has mainly been due to temporary employment and self-employment, although job growth for employees with permanent contracts has recently outpaced job growth for temporary employment. Nevertheless, the share of flexible employment remains high and represents a substantial share of the labour market. The high percentage of temporary contracts and the rapid increase in self-employment without employees is observed in great differences in applicable labour regulations, labour protection, and in the differences in tax and social security legislation. A package of measures was adopted by the government (draft bill labour market in balance, *'Wet Arbeidsmarkt in Balans'*) to make it easier to hire permanent employees and make flexible contracts less flexible. Once adopted by Parliament, the

implementation of these measures (which should enter into force in 2020) should be closely monitored. Moreover, measures have been announced to ease the obligation of employers to continue to pay salaries for two years in case of illness. However, no other concrete measures have been adopted so far. Therefore, some of these institutional factors still create financial incentives for employees to start working as self-employed or favour the use the status of self-employed without employees. The self-employed are more often under-insured against disability, unemployment and old age, which could affect the sustainability of the social security system in the long run. In addition, the enforcement of measures to tackle bogus self-employment has been suspended until 2020.

(14) Despite a labour market that is performing well overall, fostering equal opportunities regarding employment and active inclusion remains an important challenge, in particular for people with a migrant background, for those operating at the margins of the labour market and for those who are economically inactive. In addition, there is still untapped labour potential, in particular among the high number of part-time working women.

(15) Technical and digital skills and qualified professionals are crucial for the Dutch economy's capacity to innovate and for productivity growth. This points to the need to invest more in training, including training in digital skills, and to promote flexible upskilling and reskilling opportunities. Improving society's capacity to innovate also requires investments to support education in science, technology, engineering and mathematics. Moreover, increased investment in skills, education and training is crucial to improving access to the labour market and the employability of those at the margins of the labour market, while fostering equal opportunities and active inclusion.

(16) While the research and development investment intensity for the Netherlands rose to over 2%, it is still well below the 2.5% national target and the level of top performers. In terms of productivity, the Netherlands is one of the best performing countries in many sectors. Continued productivity growth is therefore highly dependent on innovation. Additional investment in research and development, and innovation, especially in the private sector, would support this.

(17) The energy transition and the reduction of greenhouse gas emissions requires substantial investments to ensure a more sustainable and resource efficient economic development. The Netherlands is likely to overachieve its 2020 targets in the field of greenhouse gas reductions, while reaching the 2030 targets will require additional measures. The 2020 primary energy efficiency and renewable energy targets will not be reached without additional measures. The Dutch target for renewable energy by 2023 as defined by their Energy Agreement target should be within reach thanks to investments in off-shore wind farms. By the end of 2019, the Dutch government aims at adopting a National Energy and Climate Plan which will provide an overview of its investment needs until 2030 for the different dimensions of the Energy Union, including renewable energy, energy efficiency, security of supply, and climate mitigation and adaptation.

(18) Congestion remains a challenge in the Netherlands, which is a dense and well equipped country and a key player in EU logistics with the biggest EU port in Rotterdam and one of the biggest airports in Schiphol. The issue has been alleviated with additional infrastructure works but it still remains an issue with high social costs and hours wasted stuck in traffic.

(19) The programming of EU funds for the period 2021-2027 could help address some of the needs identified in the recommendations, in particular in the areas covered by Annex D to the country report[8]. This would allow the Netherlands to make the best use of those funds in respect of the identified sectors.

(20) In the context of the 2019 European Semester, the Commission has carried out a comprehensive analysis of the Netherlands's economic policy and published it in the 2019 country report. It has also assessed the 2019 Stability Programme and the 2019 National Reform Programme and the follow-up given to the recommendations addressed to the Netherlands in previous years. It has taken into account not only their relevance for sustainable fiscal and socio-economic policy in the Netherlands, but also their compliance with Union rules and guidance. This reflects the need to strengthen the Union's overall economic governance by providing Union-level input into future national decisions.

(21) In the light of this assessment, the Council has examined the 2019 Stability Programme and is of the opinion[9] that the Netherlands is expected to comply with the Stability and Growth Pact.

(22) In the light of the Commission's in-depth review and this assessment, the Council has examined the 2019 National Reform Programme and the 2019 Stability Programme. Its recommendations under Article 6 of Regulation (EU) No 1176/2011 are reflected in recommendation (1) and (3) below. Those recommendations also contribute to the implementation of the Recommendation for the euro area, in particular the first and fourth euro area recommendation. Fiscal policies referred to in recommendation (3) contribute inter-alia to addressing imbalances linked to the current account surplus.

HEREBY RECOMMENDS that the Netherlands take action in 2019 and 2020 to:

1. Reduce the debt bias for households and the distortions in the housing market, including by supporting the development of the private rental sector. Ensure that the second pillar of the pension system is more transparent, inter-generationally fairer and more resilient to shocks. Implement policies to increase household disposable income, including by strengthening the conditions that support wage growth, while respecting the role of social partners. Address features of the tax system that may facilitate aggressive tax planning, in particular by means of outbound payments, notably by implementing the announced measures.

2. Reduce the incentives for the self-employed without employees, while promoting adequate social protection for the self-employed, and tackle bogus self-employment. Strengthen comprehensive life-long learning and upgrade skills notably of those at the margins of the labour market and the inactive.

[8] SWD(2019) 1018 final.

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

3. While respecting the medium-term budgetary objective, use fiscal and structural policies to support an upward trend in investment. Focus investment-related economic policy on research and development in particular in the private sector, on renewable energy, energy efficiency and greenhouse gas emissions reduction strategies and on addressing transport bottlenecks.

Done at Brussels,

For the Council
The President