Assurance of Compliance in the 2nd GRC Programme

I. Background

According to information from the Troika, Greece has most likely missed key programme objectives again in 2011. In particular, the budget deficit has not decreased compared to the previous year. Therefore Greece will have to significantly improve programme compliance in the future to honour its commitments to lenders. Otherwise the Eurozone will not be able to approve guarantees for GRC II.

II. Proposal for the improvement of compliance

To improve compliance in the 2nd programme, the new MoU will have to contain two innovative institutional elements on which Greece will have to commit itself. They will become further prior actions for the second programme. Only if and when they are implemented, the new programme can commence:

1. Absolute priority to debt service

Greece has to legally commit itself to giving absolute priority to future debt service. This commitment has to be legally enshrined by the Greek Parliament. State revenues are to be used first and foremost for debt service, only any remaining revenue may be used to finance primary expenditure. This will reassure public and private creditors that the Hellenic Republic will honour its comittments after PSI and will positively influence market access. *De facto* elimination of the possibility of a default would make the threat of a non-disbursement of a GRC II tranche much more credible. If a future tranche is not disbursed, Greece can not threaten its lenders with a default, but will instead have to accept further cuts in primary expenditures as the only possible consequence of any non-disbursement.

2. Transfer of national budgetary sovereignty

Budget consolidation has to be put under a strict steering and control system. Given the disappointing compliance so far, Greece has to accept shifting budgetary sovereignty to the European level for a certain period of time. A budget commissioner has to be appointed by the Eurogroup with the task of ensuring budgetary control. He must have the power a) to implement a centralized reporting and surveillance system covering all major blocks of expenditure in the Greek budget, b) to veto decisions not in line with the budgetary targets set by the Troika and c) will be tasked to ensure compliance with the above mentioned rule to prioritize debt service.

The new surveillance and institutional approach should be formulated in the MoU as follows: “In the case of non-compliance, confirmed by the ECB, IMF and EU COM, a new budget commissioner appointed by the Eurogroup would help implementing reforms. The commissioner will have broad surveillance competences over public expenditure and a veto right against budget decisions not in line with the set budgetary targets and the rule giving priority to debt service.” Greece has to ensure that the new surveillance mechanism is fully enshrined in national law, preferably through constitutional amendment.