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Status of Work on Reform of EU Economic Governance

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So far, the economic governance reforms have produced an agreement on the assumptions underlying the method of reinforcing budgetary and non-fiscal surveillance and on the establishment of a "European semester." An important role in this process has been played by the Task Force (on economic governance) working under Herman Van Rompuy, which has held three meetings to date. The results of the Task Force's work and the decisions of the European Council adopted on their basis will have a fundamental bearing on the political credibility of the reform.

Fiscal Surveillance. The substance of agreements that will eventually be reached concerning the strengthening of sanctions for non-compliance with budgetary discipline and the scope and triggers of the sanctions will be a measure of the member states' political will to enhance economic coordination. On this issue the member states differ. The Task Force chaired by the president of the European Council succeeded at its 12 July meeting (earlier meetings had been held on 21 May and 17 June) in obtaining a general consent to the expansion of sanctions both in the financial and non-financial dimension.

The European Commission pointed out in its communication of 30 June that, failing progress on financial consolidation, temporary imposition of interest-bearing deposits could be a possible preventive sanction (applicable to the euro-area countries). With regard to the corrective arm, the Commission proposed the establishment of a two-stage system for suspending transfers from the EU budget (applicable to the structural and agricultural funds and the fisheries fund). Step one would see the suspension of budgetary commitments in the wake of the opening of the Excessive Deficit Procedure (EDP), but no automatic suspension of payments would follow. A state's failure to take effective deficit-reducing measures would result, in stage two, in the cancellation of the commitments, i.e. the loss of payments. In the case of the funds targeted at agriculture and fisheries, the loss would concern transfers to the national budget and, under the European Commission's proposal, it would not diminish funds channelled to the end beneficiaries. This scheme is likely to meet with resistance from some states because it effectively means that the national budget would be required to make up for the lost funds. The introduction of a system of budgetary sanctions will necessitate the adoption, in the financial framework 2014–2020, of corresponding provisions in regulations on the functioning of the funds (at present only the Cohesion Fund Regulation contains a clause on the suspension of commitments to a state which fails to reduce its deficit effectively). With respect to the eurozone countries, sanctions with a similar impact are to be provided for in a regulation based on Article 136 TFEU that will be put forward by the European Commission in September.

The suspension of a member state's voting rights, as proposed by France and Germany in their common position of 21 July, is an increasingly discussed option. Yet, for such a solution to be adopted, treaty amendments would be needed, and these are unlikely in the present political conditions, so the two states propose that in the short term sanctions of this type be based on non-binding political agreement of euro-area members.

The degree of automaticity of sanctions remains a pending issue. This is about making the imposition of sanctions less dependent on decisions of the ECOFIN Council (at present it is the Council that, under Article 126 section 11, decides by a qualified majority on the launch of sanctions), so that they are less vulnerable to political influences. The adoption of this solution could also necessitate a revision of the treaty, notably of its Article on the EDP (currently, Article 126 of the TFEU).

The June European Council agreed to increase, in the process of fiscal surveillance, the significance of the public debt criterion. The European Commission proposes that states with debt levels in excess of 60% be subject to the EDP if they fail to make progress on debt reduction in line with adopted reduction benchmarks. Furthermore, the reduction of deficit below 3% would not be a sufficient condition for closing the procedure if the pace of debt reduction is unsatisfactory. The Commission also suggests that debt reviews made for surveillance purposes should take into account many factors, including implicit pension obligations (Poland's stipulation), the structure of debt, the level of private debt, or the reserves held. This approach would be conducive to a more penetrating, in-depth assessment from the perspective of debt evolution in the long term, just as it would make possible the adoption of preventive measures in response to the emergence of negative trends.

Non-fiscal Macroeconomic Surveillance. Non-fiscal macroeconomic surveillance, addressing primarily the imbalances issue, extends to all states rather than just euro-area members (which was the European Commission's original proposal), although it is to be more comprehensive in respect of the latter. The Task Force agreed that this surveillance is to consist of a preventive and a corrective arm. A pillar of the preventive arm will be a "scoreboard" of indicators, different for eurozone members and for the remaining states, to act as a warning mechanism. If the indicators reveal distressing imbalance trends, the state concerned will come under in-depth monitoring, and if major problems are identified, the Council will be free to set in motion the corrective part, one underpinned by an "excessive imbalance procedure," which provides for close surveillance (including regular reporting to the Council and to the Eurogroup). In respect of the eurozone countries, the European Commission has proposed an additional enforcement mechanism to be put into operation in the event of flagrant non-compliance by the state concerned with the recommendations. Supplementing the surveillance of (macroeconomic) imbalances and competitiveness developments will be a thematic review of structural reforms under the "Europe 2020" strategy (jointly, they will make up non-fiscal macroeconomic surveillance). Since the existing treaty framework does not permit the introduction of hard corrective mechanisms in respect of EU-wide non-fiscal surveillance, it appears that the effectiveness of this process will depend, to a greater extent than that of budgetary discipline, on the gravity of political commitments made in the European Council.

European Semester. One important result of the reform process to date is the consent (reaffirmed at the July meeting by the ECOFIN Council) to launch, as of the beginning of 2011, a "European semester"—a synchronized cycle of economic policy coordination that combines fiscal policy under the Stability and Growth Pact with "Europe 2020" strategy issues. The cycle is to commence in January with the publication by the European Commission of an assessment of the economic situation in the euro area and in the whole EU and of related challenges (Annual Growth Survey – AGS), to be followed by a debate in the Parliament and in the Council to be completed with the adoption by the European Council of strategic guidance. These decisions are to be taken into account during the preparation of the Stability/Convergence Programs (SCPs) and the National Reform Programs (NRPs) by member states. Both programs will be submitted to the European Commission in April. The SCPs are to contain, among other things, basic information on budget plans, including macroeconomic projections and revenue and expenditure forecasts for the next year (Y+1) as well as a description of the main components thereof. Upon the assessment of both programs by the Commission, the Council will issue, early in July, sets of country-specific policy guidance on the implementation of the SCP and NRP, to be taken into account at subsequent stages of national budget process. In the autumn, implementation progress of the member states is to be reviewed, including for purposes of the next AGS. At present preparations for launching the cycle are underway, with the adoption by the ECOFIN Council in July of the broad economic policy guidelines featuring as an important element.

Prospects. Economic governance decisions that the European Council will adopt in the autumn on the basis of the Task Force's report could provide a strong political mandate for further stage of this reform, i.e. for hammering out concrete legislative solutions. The adoption or the strengthening of national fiscal frameworks underpinned by budgetary rules designed, among other things, to contain the growth rate of expenditure and debt, would provide a necessary supplement to EU legislation. This approach has been promoted by Germany, France, Poland and by the European Commission.

It appears that in the ongoing debate not enough attention is given to improving the independence and quality of fiscal surveillance in the EU. This has been strongly emphasised by the ECB, which promotes the establishment of a fiscal agency to monitor the development of budget situations in the EU states. Yet chances of this idea being put into practice are small, especially as the creation of such an agency could be perceived as an attempt to sideline the European Commission and because such conclusions as have been reached in the debate to date point instead to the need to strengthen the Commission's role in the process of budgetary surveillance.