

The New Architecture of the EU Economic Governance: Meandering through an English style park or a classic French garden?

By Nicolas de Sadeleer



The financial crises and the turmoil in sovereign debt markets have clearly highlighted challenges in the EU's economic governance. The principal weakness of the Economic and Monetary Union (EMU) is that, on one hand, the Euro monetary competence is centralized at EU level whilst, on the other, the economic policy is left decentralized. That being said, with the aim of strengthening the economic pillar of the EMU, the EU has implemented various mechanisms in incremental stages. These mechanisms are intended to bring significant changes to the economic governance of the EU.

Due to the accumulation of structural deficits by certain Member States, bail-outs of debt-ridden banks and fiscal stimulus plans intended to re-launch growth, budget deficits started rapidly expanding after 2009. Accordingly, the financial crisis of 2008 was followed by a substantial fiscal crisis which compromised the financial stability of the Eurozone as a whole. After summarising the succession of mechanisms that have improved since 2011 fiscal and macroeconomic discipline, we shall highlight how this flurry of treaties and secondary legal acts is impinging on the principle of institutional balance.¹

The Architecture of the New Economic Governance

1. Financial surveillance

At the first stage, in an attempt to remedy inadequacies within the organisation of the prudential oversight system for financial

establishments which the 2008 crisis had laid bare, it first adopted in 2011 a European System of Financial Supervisors (ESFS) which comprised three sector authorities (banks, insurance and pension companies, and markets and financial services) as well as a European Systemic Risk Board (ESRB). That said, fiscal and macro-control issues were not left aside.

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2. Fiscal and macro-economic surveillance

At the second stage, taking account of the recommendations made by the Task Force on Economic Governance in the EU, the European Parliament and the Council of the European Union adopted six legislative measures (5 Regulations and a Directive) during the autumn of 2011 (the ‘six-pack’) intended to remedy deficiencies in the 1997 Stability and Growth Pact (SGP), in particular by reinforcing and expanding the range of preventive and corrective mechanisms. Four acts deal with fiscal issues whereas the two others aim at detecting and addressing emerging macroeconomic imbalances with the EU and the Euro area. Given that this part of the edifice was far from being complete, the European Parliament and the Council adopted on May 21st 2013 two additional Regulations, known as the ‘two-pack.’ The 2011 ‘six-pack’ and the 2013 ‘two-pack’ represent hitherto the most drastic reinforcement of economic governance since the launch of the EMU in 1997. The modifications brought to the SGP by these different acts reflect a significant shift towards greater focus on debt and fiscal sustainability, with a view to reinforcing compliance and ensuring that national fiscal frameworks reflect the EU's fiscal rules. The key changes can be summarized as follows:

(a) The criterion of public debt (the ratio of the difference between public debt and the 60% debt-to-GDP threshold must fall by 5% annually) is henceforth better reflected in the budgetary surveillance mechanism.

(b) The introduction of a new mechanism for macroeconomic surveillance is broadening the EU fiscal surveillance.

(c) According to a common budgetary timeline, Member States have to make public their national medium-term fiscal plan and seek the opinion of the European Commission. Member States are called on to adopt their budget by

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(d) A reinforced *ex-ante* coordination, called the ‘European Semester,’ allows a simultaneous assessment of both fiscal discipline (stability and convergence programmes), macroeconomic stability and structural reforms (NPR) fostering growth and employment.

(e) The Eurozone countries that are subject to excessive public deficits (EDP) have to submit an “economic partnership programme” whereas Member States in serious financial difficulties have to replace their economic partnership programme by an economic adjustment programme.

(f) Moreover, to increase the effectiveness of the SGP, a wider range of sanctions and measures are provided for in both the preventive and the corrective arms of the SGP. The financial sanctions range from interest-bearing deposits to fines. For Euro area countries, the Commission will be able to enforce more strongly than before the Council’s recommendations by proposing sanctions at an earlier stage. What is more, the introduction of a reverse majority rule for the adoption of enforcement measures is likely to reinforce the effectiveness of the sanctions.

(g) Last but not least, the requirements applicable to the national fiscal frameworks of Member States were harmonized.

With a view to fostering the implementation of the SGP and reinforcing the ‘six-pack,’ the majority of the Member States – with the exception of the UK and Czechia – adopted a Treaty on Stability, Coordination and Governance in the Economic and Monetary union (Fiscal Compact), which entered into force on the 1st of January 2013. This compact constitutes a self-standing legal framework which is super-imposed on EU law, whilst borrowing various techniques from EU law.

Thanks to the sheer breadth of this part of the reform, the Commission and the Council are now able to scrutinise the Member States’ public finances and economies much more carefully and pre-emptively than before.

3. Financial Solidarity

At the third stage, treaties concluded between the Eurozone countries have been setting up financial facilities such as the European Financial Stability Facility (EFSF) and the European Financial Stabilisation Mechanism (EFSM). Since January 2013, the European Stability Mechanism (ESM), a new inter-governmental agreement concluded by the 18 Member States of the Eurozone is replacing both the EFSM and the EFSF. In contrast to the other funds, the ESM is a permanent international financial institution with a lending capacity of 500 billion EUR. Its purpose is to mobilise funding and provide stability support under strict conditionality, appropriate to the financial assistance instrument

chosen, to the benefit of ESM Members which are experiencing, or are threatened by, severe financial problems. The ESM Treaty has been challenged before the German Constitutional Court as well as before the Irish Supreme Court. Regarding the Irish case, the full Court of Justice of the EU ruled on the validity of the European Council Decision on the 27th November 2012. The German Court dismissed the application on the 18th March 2014.

All in all, the ‘six-pack,’ the ‘two-pack,’ as well as the Fiscal Compact, are intended to reinforce fiscal and macroeconomic discipline whereas the ESM, replacing the EFSF, provides for a permanent crisis resolution framework.

2010 Task Force on Economic Governance Proposals	Implementation
Enhancing fiscal discipline	Euro Plus Pact, six-pack, two-pack, Fiscal Compact
Broadening multilateral surveillance	Regulations 1174 and 1176/2011 on macroeconomic surveillance and directive 2011/85
Policy coordination	European Semester
Crisis management	EFSF, EFSM, ESM
Reinforcement of economic governance	Euro Plus Pact, six-pack, Fiscal Compact

4. Economic Coordination

At the fourth stage, several soft law mechanisms have been adopted with a view to remedying the weaknesses within the coordination of economic policies. Firstly, by replacing the Lisbon Strategy, the 2020 Strategy adopted by the European Council in 2010 is principally aimed at enhancing competitiveness. Secondly, the Eurozone countries as well as 6 other Member States that do not use the Euro as their currency adopted in March 2011 the Euro Plus Pact. Thirdly, the Compact for Growth and Jobs, that was agreed at the European Council in June 2012, aimed at relaunching growth, investment and employment. Under this compact, EU member states committed to tackling unemployment and addressing the social consequences of the crisis effectively.

5. Byzantine Structure

Needless to say, one has the impression of meandering through an English style park rather than a classic French garden. Indeed, one can only be struck by the heterogeneous nature of the texts setting out the new structure of governance, which is based on provisions forming part of international law (EFSF, ESM and Fiscal Compact), EU treaty law (Articles 121, 126 and 136 TFEU) EU secondary law (the ‘six-pack’ and the ‘two-pack’), and soft law (2020 Strategy and Euro Plus Pact).

What is more, these measures seek to proliferate the regimes of preventive control and sanctions (notices, reports, warnings, deposits, fines, etc.). In addition to its Byzantine structure, the new governance also involves an accumulation of coordination and evaluation procedures (the 'European Semester,' the Euro Plus Pact and the 2020 Strategy), with all of the problems of scheduling and overlap which this entails for a public service which is operating under budgetary constraints.

It thus comes as no surprise that competences are not clear-cut: the 2020 Strategy and the Euro Plus Pact stand astride EU and national competences, whereas the Fiscal Compact requirements reckon upon EU competences.

Last but not least, the scope of these measures varies. As shown below, some rules are applicable to the 18 States with the Euro as their common currency (Regulation (EU) No 1174/2011), whilst others apply to the whole Union (Regulations (EU) No 1173/2011 and No 1176/2011; Directive 2011/85/EU), and others still to 23 States (Europa plus Pact). This has led to a balkanisation of economic governance.

Measures	Member States
'Six-pack' regulations 1175/2011, 1176/2011 and 1177/2011	28 EU Member States
Reference values mentioned in the Protocol No 12 on EDP and Numerical Fiscal Rules (Articles 5 to 7 Directive 2011/85)	27 (all EU MSt except UK)
'Six-pack regulations' 1173/2011 and 1174/2011 and 'two-pack' regulations 472/2013 and 473/2013	18 MSt having the Euro as a currency
Fiscal Compact	25 (all EU MSt except UK, Cz, Croatia)
SEM	18 MSt having the Euro as a currency
Europa plus	23 (all EU MSt except Sw, Hu, Cz, and UK)

The Impacts of the Reforms on the Institutional Equilibrium

The institutional balance in relation to budgetary and economic matters has always been atypical. On the one hand, the coordination of economic policy has been a matter for national sovereignty, whilst on the other hand budgetary control has been based on an equilibrium which is highly skewed in favour of the Council, where a blocking minority can easily stand in the way of Commission proposals. The European Parliament has only played a secondary role in such matters. Does the reform enshrine the victory of the EU method over intergovernmentalism or the opposite?

The recourse to multilateral cooperation has proved to be necessary in order to adopt the Euro Plus Pact and to set up the EFSF, the ESM as well as the Fiscal Compact, all of which are testament to a move towards intergovernmentalism. Nonetheless, neither the Fiscal Compact nor the ESM call into question the primacy of EU law. What is more, the



crisis has enabled a gradual improvement in the efficacy of this institutional framework by reinforcing the role of the Eurogroup, the Council of the Euro area and the Commission to the detriment of intergovernmentalism. Furthermore, the adoption of the 'six-pack' and the 'two-pack' is testament to the fact that directives and regulations have not been dwarfed by these intergovernmental arrangements.

At the end of the day, apart from the European Parliament, all EU institutions appear to be much stronger given that they were granted more competences. In particular, the new powers conferred on the Commission and the Council are likely to give real teeth to economic governance in the EU. The Fiscal Compact confirms some of the surveillance mechanisms introduced by the 'six-pack' and the 'two-pack.'

Whether the balance of power has tilted in favour of one institution remains to be seen. Some institutional developments have been contradictory. Besides, the crisis has shown the extent to which informal mechanisms (the Euro Group is an informal grouping within the Council whereas the Council of the Euro area is not an EU institution in its own rights) are likely to prevail over formal mechanisms. Last, given that an *avant-garde* of countries whose currency is the Euro is likely to foster more integrated economic policies, this might be the beginning of a permanent 'two-class' EU. **EBR**

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legal information on this topic.

Reference

1. For an exhaustive analysis of the EU fiscal regulatory framework, see de Sadeleer, N., 'The New Architecture of the European Economic Governance' in Philipsen, N. and Xu, G. (eds.), *The Role of Law and Regulation in Sustaining Financial Markets* (Abingdon, Oxon and New York: Routledge, 2014); de Stree, A. (2013) 'The Evolution of the EU Economic Governance since the treaty of Maastricht: An Unfinished Task', *MJ* 20: 3, 349–351; EU Committee of the House of Lords, *Genuine EMU and the implications for the UK* (14th Febr. 2014).