EUROPEAN CENTRAL BANK

EUROSYSTEM

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KEY ELEMENTS OF THE ECB OPINION ON ECONOMIC GOVERNANCE REFORM

The European Commission's proposals contribute to an important broadening and strengthening of the EU's economic and budgetary surveillance. But for the euro area, a more ambitious governance structure must be foreseen, to ensure the smooth functioning of Economic and Monetary Union. The Governing Council of the European Central Bank (ECB) calls upon the European Parliament and Council to strengthen the proposals along the following lines.

1. **Greater automaticity in all surveillance procedures, including the new macroeconomic surveillance framework.** When Member States do not comply with recommendations to adjust their policies, this should lead to the consequences foreseen in the preventive and corrective procedures, and the Council of the European Union ("the Council") should have less room for halting or suspending procedures against the Member States. A simple way of achieving this would be a formal declaration by the Council, or at least the Eurogroup, committing itself to voting, as a rule, in favour of the continuation of procedures where recommended or proposed by the European Commission. Thus, the Council would voluntarily constrain its discretion and would need to justify instances in which it did not follow its own rule. Also, broader use of reverse majority voting should be considered.

2. **Setting strict deadlines to avoid lengthy procedures and deleting "escape clauses".** Not allowing the Council or the Commission to (i) extend the deadline for correcting an excessive deficit during a severe economic downturn of a general nature, or (ii) reduce or cancel financial sanctions either on grounds of exceptional economic circumstances or following a request by the Member State concerned, would enhance automaticity.

3. **The new macroeconomic surveillance framework should have a clear focus** on euro area countries with large current account deficits, significant competitiveness losses and high levels of public and private debt, as well as any other vulnerability threatening Economic and Monetary Union.

4. **Introduction of political and reputational measures fostering early compliance with the surveillance framework.** This includes increased reporting obligations for Member States and the submission of reports by the Council to the European Council in the event of non-compliance with Council recommendations, as well as the possibility of the European Commission conducting missions to Member States, in liaison with the ECB for euro area and ERM II countries if the ECB deems it appropriate.

5. **Earlier and more gradual application of financial sanctions within the macroeconomic surveillance framework** to provide clear incentives for appropriate macroeconomic policies. The excessive imbalance procedure should oblige Member States to lodge an interest-bearing deposit following the first instance of non-compliance and should sanction them with a fine in case of repeated non-compliance. The proceeds from any financial sanctions imposed on euro area countries as part of budgetary and macroeconomic surveillance should be assigned to the future European Stability Mechanism.

6. **Ambitious benchmarks when establishing the existence of an excessive deficit.** The scope for considering any "relevant factors" when establishing the existence of an excessive deficit – whether on the basis of the deficit criterion or on the basis of the debt criterion – should be clearly reduced, notably when these are factors that could be regarded as mitigating the Member State's failure to comply with these criteria. As regards the deficit criterion, such factors should be taken into account only if the deficit ratio of the country concerned is close to the 3% of GDP reference value and deviates from this value only temporarily (irrespective of whether the country's debt ratio is above or below the 60% reference value). And as regards the debt criterion, such factors should be considered only if a government debt ratio in excess of 60% of GDP is projected to decline. Also, the backward-looking numerical benchmark used to assess whether a debt ratio above 60% of GDP is sufficiently diminishing should be applied without delay.

7. **Ambitious requirements as regards the adjustment path towards a country's medium-term budgetary objective.** Under the revised budgetary surveillance procedure, the question of whether sufficient progress is being made towards a country's medium-term budgetary objective should be evaluated on the basis of an overall assessment using the structural balance as the point of reference, including analysis of expenditure net of discretionary revenue measures. In this context, the annual improvement in the structural balance should be significantly higher than 0.5% of GDP where a country's government debt exceeds the reference value of 60% of GDP or there are fiscal sustainability risks.

8. **Guaranteeing the quality and independence of fiscal and economic analysis**, which requires the establishment of an advisory body at the EU level comprising persons of recognised competence. That body would provide ex post assessment of the conduct of budgetary and macroeconomic surveillance by the Council and the Commission.

9. **A commitment by the Member States to swiftly implement strong national budgetary frameworks** in order to facilitate compliance with their obligations under the Stability and Growth Pact. This would require that the proposed fiscal frameworks directive be transposed into national law as faithfully as possible, and no later than end-2012. The Eurogroup could issue a formal statement to that effect. Also, the directive has to establish clear consequences in the event that national authorities do not comply with their budgetary obligations. For euro area countries, a new directive chapter is required in order to make independent national fiscal policy institutions

mandatory. The measures in the directive should not prevent Member States from developing stronger frameworks. The EU should consider obliging Member States to adopt clear borrowing frameworks.

10. **Improvements to the quality of annual and quarterly statistics in the general government accounts, in terms of both timeliness and reliability**, by supporting the implementation under the fiscal frameworks directive of public accounting systems established on an accrual basis that are linked to ESA 95-based national accounts. Weaknesses in the collection and reporting of data have to be addressed immediately.

The EU should also consider reversing the changes to the Stability and Growth Pact of 2005 which allowed Member States greater leeway under the Pact.

Finally, while none of the amendments proposed by the ECB requires changes to the Treaties, the EU should, at some point in time, consider reforming them to further strengthen economic governance.

The ECB's Opinion is available in full in English on the ECB's website. It will also be published **in all other EU languages on the ECB's website and in the Official Journal of the European Union** in due course.