# The EU's economic policy architecture after the ratification of the Fiscal Treaty

**Jørgen Mortensen is an Associate Senior Research Fellow at the Centre for European Policy Studies (CEPS), Brussels and is a Fellow at CASE - Centre for Social and Economic Research, Warsaw**

Despite the resistance by some member states, the EC in 1990 started the process which would lead to the adoption of EMU. A Conference of the Representatives of the Governments of the Member States (the EC term for the inter-governmental conference) convened in Rome on 15 December 1990 to adopt by common accord the amendments to be made to the Treaty establishing the European Economic Community with a view to the achievement of political union and with a view to the final stages of economic and monetary union. The final negotiations took place in Maastricht on 7 February 1992, giving rise to the creation of the European Central Bank and Treaty changes concerning also Justice and Home Affairs and external policy.

With the ultimate limit for passing to Stage 3 (1 January 1999) approaching, some member states became increasingly concerned with the possibility of irresponsible budgetary behaviour by governments once admitted in the EMU club. The need for establishing rules of the game once inside the EMU was recognised by the Madrid European Council in December 1995 and reiterated in Florence six months later. An agreement on the main features was reached in Dublin in December 1996 and final agreement on the text was reached on 7 July 1997 (see annex).

Broadly speaking, the SGP stipulates the need for observing the Maastricht criteria even after EMU membership and provides somewhat specific guidelines for the process of deciding whether an EMU member country runs an excessive deficit. The SGP, however, goes considerably beyond the Maastricht Treaty by giving the Council the competence to impose sanctions if a participating member state fails to take the necessary steps the bring an excessive deficit to an end. Whenever the Council decides to impose sanctions it is 'urged' always to require a non-interest bearing deposit in accordance with Article 104(11). It is again 'urged' to convert a deposit into a fine after two years unless the excessive deficit has, in the view of the Council, been corrected.

However, an institutional crisis in the European Union emerged in 2004 as the result of the ECOFIN Council's failure to 'jump the obstacle' and take sanctions against France and Germany in accordance with the Excessive Deficit Procedure provided for in the Maastricht Treaty's article 104, the associated protocol and the Stability and Growth Pact.

The crisis can be seen as a symptom of a latent and lasting conflict between two equally valid features of the construction of the Union:

1. The need to ensure a high degree of consistency, notably in the medium and long run, between monetary and budgetary policy; and
2. The principle of 'subsidiarity' which can be taken as the theological argument for assigning the full competence in the field of fiscal affairs and social policy to the national (or regional) governments.

The need to ensure consistency between budgetary and monetary policy can, from the point of view of economic analysis, be based on the argument that in the long run monetary and budgetary policy cannot be considered to be completely independent policy instruments. There can be little doubt that a prospective building up of public debt in proportion to GDP in the long run will put enormous pressure on monetary policy and make it increasingly costly for the economy to keep inflation under control. The monetary authorities' concern with respect to the long-term sustainability of budget balances of EU member states is therefore legitimate. Clearly this potential conflict was 'forgotten' in the 1990s and the early years of 2000 but came out of hiding with the financial and economic crisis of 2007 and onwards.

Under strong influence of the emerging public debt crisis, the European Council meeting on December 9, 2011 discussed the incorporation of aspects of a reinforced Stability and Growth Pact[1] into the EU Treaties. Only the United Kingdom was openly opposed to the proposal, but this veto effectively blocked the incorporation of the reinforced SGP rules into the EU Treaties, as unanimous support from all Member States is required to bring about treaty change[2].

This gave rise to the adoption on 2 March 2012, by 25 member states (in addition to the UK, the Czech Republic opted out) of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union. As a sufficiently large

(12) number of partners had ratified it, the Fiscal Stability Treaty, in fact, came into force in January 2013.

The provisions of the Treat may be summarised as follows:

- The budgetary position of a 'contracting party' must respect a country-specific medium-term objective as defined in the SGP with a lower limit of a 'structural deficit' of 0.5% of GDP but with the time-frame fixed with due account of country-specific sustainability risks.
- The lower limit for the structural deficit may be increased to 1% once the public debt is lower than 60% of GDP.
- The speed of reduction of the deficit is fixed at on twentieth of the gap between the actual deficit and the limit.
- In the case of failure on behalf of a contracting party to comply with the recommendation a procedure may be launched with the Court of Justice which can impose a sanction not exceeding 0.1% of its GDP.

In addition, the Stability Treaty stipulates some more formal rules of governance and also, importantly, in article 16, states that within five years at most of the entry into force, on the basis of an assessment of the experience with its implementation, the necessary steps shall be taken with the aim of incorporating the substance of the Fiscal Treaty into the legal framework of the European Union.

The only really significant innovation due to the Fiscal Treaty is the assignment to the European Court of Justice of the responsibility of deciding to sanction a member state for having an excessive deficit.

In addition, however, the Stability Treaty (in article 8) stipulates that where, on the basis of the Commission's assessments, taking account of observations from the country concerned, the latter has failed to comply with its obligations, the 'matter will be brought to the Court of Justice by one or more Contracting Parties'. And where a Contracting Party, independently of the Commission's report, considers that another Contracting Party has failed to comply with the provisions it may also bring the matter to the Court of Justice. In fact, according to article 8: where, on the basis of its own assessment or that of the European Commission, a Contracting Party considers that another Contracting Party has not taken the necessary measures to comply with the judgment of the Court of Justice, it may bring the case before the Court of Justice and request the imposition of financial sanctions following criteria established by the European Commission in the framework of Article 260 of the Treaty of the Functioning of the European Union.

The inter-governmental nature of the Stability Treaty is also made evident by the fact that the Commission, despite its important role in the preparation of reports and conclusions as regards the existence of an excessive deficit, is not as such entitled to bring a case before the Court of Justice. However, as regards the eurozone countries, article 7 stipulates an 'obligation' for the members to supporting the proposals or recommendations submitted by the European Commission where it considers that a eurozone member states is in breach of the deficit criterion in the excessive deficit procedure. This

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obligation, however, shall not apply if a qualified majority is opposed to the decision proposed or recommended.

Another issue is, however, to what extent the Stability Treaty, due to its inter-governmental nature, can be expected to entail a modification of the roles of the EU institutional pattern and, notably, the role of the European Parliament. In this respect, Article 13 of the Treaty stipulates that the European Parliament and the national Parliaments of the 'contracting parties' will together determine the organisation and promotion of a conference of representatives of the 'relevant committees of the European Parliament and representatives of the relevant committees of national Parliaments in order to discuss budgetary policies and other issues covered by this Treaty'.

What remains to be seen is, however, also the reality of legal procedures initiated when a Contracting Party actually makes use of the provisions in the Treaty and puts a case before the Court of Justice. At stake here is the interpretation by the Court of the provisions in Article 3 and, notably, how the Court will decide as regards the definition of the annual structural balance of the general government as being the 'cyclically-adjusted balance net of one-off temporary measures' and even more the definition of 'exceptional circumstances' in paragraph 3, point 'b'.

Under normal circumstances the Court cannot be expected to have the in-house expertise to arrive at an 'independent' estimate of the structural budget balance of the country concerned and must therefore, at least initially, rely on the estimates of this balance prepared by the Commission. However, the country brought before the Court, not least to avoid paying the penalty and the accompanying stigmatism, may argue that the Commission's estimates do not take full account of very 'special circumstances'.

In order to arrive at a balanced conclusion, the Court and the country concerned may therefore need to call in experts from outside and it cannot be excluded that, in the end, the Court's decision will not support the Commission's views or those of the Contracting Party having brought the case before the Court. To arrive at a purely judicial definition of a 'structural budget balance' and 'special circumstances' might thus create a rather unique precedence for a decision concerning a key economic variable, normally subject of economic cleavages and scientific and political debates but at the end normally left to the validation of economists and policy makers.

The need to ensure a high degree of consistency between budgetary and monetary policy should, however, not be

interpreted as an argument in favour of assigning increased discretionary competences to the Council in the field of budgetary policy, at least not in the foreseeable future.

Admittedly views differ with regard to the existence or the gravity of the 'democratic deficit' within the EU's decision-making procedures. Allowing the Council to take binding decisions in fiscal affairs would be against the normal assignment of legislative powers to the elected parliament. At the level of the EU such competences should therefore only be transferred from the national parliaments to the European Parliament. While such transfers may well take place in a more distant future this is not to be counted upon as a way to ensure consistency between budgetary and monetary policy.

The Maastricht criteria, the protocol, the SGP and the Stability Treaty do not involve any transfer of discretionary competence to the Council and consequently do not run counter to normal democratic functioning of the EU institutions. From the point of view of legal status the provisions contained in these acts are equivalent to rules frequently found in federations putting a cap on allowable budget balances or obliging regional authorities to keep expenditure within the limits of available resources. The Treaty provisions, the SGP and the Stability Treaty may therefore be considered valid attempts to obtain appropriate trade-off between the need to ensure long-term consistency between budgetary and monetary policy and the respect for the principle of subsidiarity.

The entering into force of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union does not significantly modify the assessments concerning the implications of the Maastricht Treaty and the Stability and Growth Pact. It does provide a slightly modified excessive deficit procedure and in sharp contrast to the Maastricht Treaty and the SGP stipulates a direct involvement of the European Court of Justice, attempting thus to fill the judicial vacuum recognised in the cancellation by the Court of the Council decision to suspend the excessive deficit procedure as regards the French and German deficits in 2003-2004.

In addition to introducing a slightly more specific constraint on budget balances, the main purpose of this inter-governmental treaty was, in fact, to make an attempt to fill the legal void demonstrated by the excessive-deficit procedure against France and Germany. This procedure having been concluded by the cancellation by the European Court of Justice of the Council's decision to suspend the procedure, the future of the excessive-deficit procedure in fact depended upon the unlikely adoption by the Council of a Commission proposal to sanction a member state in a situation of excessive deficit.

However, the transfer to the Court of Justice of the final decision as to whether or not a Contracting Party is in fact in a situation of excessive deficit and whether it should be sanctioned by a fine leaves serious questions open: on what criteria should the Court take this decision in case there is disagreement as regards the nature of the deficit and the route to be followed towards reduction of this deficit? Given the exceptionally large number of excessive-deficit procedures now under way (twenty), it may be legitimate to apprehend with some doubts the unfolding and outcome of these procedures from 2013 to 2016 and beyond.

All-in-all, the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union does not seem to offer a definitive solution to the problem of finding the appropriate budgetary-monetary policy mix in the EMU already well identified in the Delors report in 1989, regularly emphasised ever since and now seriously aggravated due to the Crisis. Furthermore, the implementation of this Treaty may under certain circumstances contribute to an increase in the uncertainties as regards the distribution of the competences between the European Parliament and national parliaments and between the former and the Commission and the Council.

*1. As presented by the Directorate-General for Economic and Financial Affairs of the European Commission, the Stability and Growth Pact (SGP) is the concrete EU answer to concerns on the continuation of budgetary discipline in Economic and Monetary Union (EMU). Adopted in 1997 as indicated above, the SGP strengthened the Treaty provisions on fiscal discipline in EMU foreseen by articles 99 and 104, and the full provisions took effect when the euro was launched on 1 January 1999.*
*2. For more see, for example, Broin, Peadar ó: The euro crisis: The fiscal treaty – an initial analysis, Working Paper 5 of the Institute of International and European Affairs (Dublin 2012).*