THE EVOLUTION OF THE EU ECONOMIC GOVERNANCE SINCE THE TREATY OF MAASTRICHT: AN UNFINISHED TASK

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ABSTRACT

This paper reviews the evolution of the Economic and Monetary Union from its inception in 1992 with the Treaty of Maastricht to the most recent reforms adopted in 2013 to respond to the eurocrisis. The paper describes the evolution of the four pillars of economic governance: the surveillance and the correction of fiscal imbalances between the Member States which are mainly based on the revised Stability and Growth Pact, the surveillance and the correction of macroeconomic imbalances between the Member States, the coordination of national economic and social policies which are now based on the Europe 2020 Strategy for Growth and Jobs, and the financial solidarity between Member States which is currently mainly based on the European Stability Mechanism. The paper also deals with the institutional implications of EMU evolution with the emergence of an institutional landscape for the euro area. Finally, the paper analyses the implications for the transformation of EU law in terms of sources of law with extensive use of international treaties, recommendations and sui generis contracts between the EU and its Member States, in terms of enforcement mechanisms relying on self-enforcement and peer pressure, and in terms of a regulatory model. The paper concludes with grim perspectives that the recent reforms may not be sufficient to make the euro sustainable.

Keywords: Economic and Monetary Union; economic governance; eurocrisis; European Stability Mechanism; Fiscal Compact; Stability and Growth Pact

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§1. INTRODUCTION

When the Economic and Monetary Union (EMU) was established in Maastricht, the authors of the Treaty made two fundamental choices. First, they decided that the euro would be the currency of the Union and all EU Member States should adopt it when their macroeconomic conditions enable them to do so. Second, they decided to centralize the monetary policy but to leave the economic policy decentralized.[1] This fundamental imbalance, which was criticized by some, was the only feasible political option at the time, as most Member States were not willing to transfer their economic policies to the EU.

However, due to the cross-countries externalities caused by a common currency, this imbalance entailed the risk of unsustainable fiscal and economic policies in some Member States, and in the long run, the installation of a transfer Union. To prevent such risk and guarantee a Union of stability and responsibility, the authors of the Treaty established a governance model based on three main characteristics:[2] (i) first, the coordination of the economic policy, to be regarded as a matter of common concern between Member States, with soft law instruments in order to achieve economic convergence (Article 121 TFEU); (ii) second, the prohibition of financial solidarity among Member States (Article 125 TFEU, the no-bailout clause) except in very exceptional circumstances beyond the control of the States (Article 122 TFEU) and the prohibition of monetary financing by the ECB and national central banks (Article 123 TFEU) in order to give sufficient incentives to Member States to maintain sustainable fiscal policies, and to markets to discriminate between countries according to their financial risks; (iii) third, limits to government deficit and debt with sanctions decided by the Council in order to force sustainable fiscal policies (Article 126 TFEU). In practice, the coordination of economic policy was based on the Lisbon Strategy and the Open Method of Coordination and the surveillance of fiscal policies was based on the Stability and Growth Pact. In brief, the governance model chosen for economic policy was based on rules and markets, not on discretion and solidarity.

The evolution in the EU over the last decade questions those two main choices made 20 years ago. The eurocrisis, which started in 2010 with the virtual bankruptcy of Greece, was a consequence of the systemic failure of the governance model chosen to deal with the

1 The Maastricht negotiations were based on the Report on economic and monetary union in the European Community, prepared by the Committee chaired by J. Delors and presented in April 1989. On the background to the negotiations, see K. Dyson and K. Featherstone, *The Road to Maastricht: Negotiating economic and monetary union* (Oxford University Press, Oxford 1999).

2 On the economic governance decided in Maastricht and complemented with the Stability and Growth Pact, see J. Pipkörn, 'Legal arrangements in the Treaty of Maastricht for the effectiveness of the economic and monetary union', 31 *CMLRev.* (1994), p. 263, as well as M.J. Herdegen, 'Price stability and budgetary restraints in the Economic and Monetary Union: The law as guardian of economic wisdom', 35 *CMLRev.* (1998), p. 9–32; J.V. Louis, 'A Legal and Institutional Approach for building a Monetary Union', 35 *CMLRev.* (1998), p. 33–76; H.J. Hahn, 'The stability pact for European Monetary Union: Compliance with deficit limit as a constant legal duty', 35 *CMLRev.* (1998), p. 77–100.

imbalance between monetary and economic policy. Experience shows that such a model was based on wrong assumptions.[3] First, the coordination of economic policies did not lead to convergence between Member States (on the contrary, the first decade of the euro led to more macroeconomic divergences between countries) because soft law is too soft to force a state to change its policies. Second, the prohibition of solidarity did not lead to different risk premiums according to national public finances (on the contrary, the spreads on government bonds nearly disappear between the countries of the euro area). This is because financial markets were imperfect and the prohibition was not credible given the massive spillover effects a bankruptcy of one country has on the other members of the currency zone. Third, the fiscal surveillance did not lead to reduction of government debts and deficit below EU limits because the sanctions were decided by political institutions and not independent courts. In brief, the recent eurocrisis shows that governance through market discipline and rules applied by political entities does not work.

Hence, this crisis calls for a fundamental revision of the economic governance. The most radical option would have been to integrate economic policy at EU level, as was done for monetary policy 20 years ago. This was not politically feasible as it implied a political integration that Member States were still not ready to accept. The alternative was to build on the existing governance model and improve it. This option was followed by the recent reforms which took place in several steps decided by the European Council with hesitation and sometimes reluctance under the heavy pressure of financial markets (see Table 1 inserted at the end of this contribution).[4]

In 2010, the Council adopted a Regulation establishing the European Financial Stabilisation Mechanism (EFSM) and the Member States of the eurozone established the European Financial Stability Facility (EFSF), two instruments for financial assistance. Then, based on the conclusions of a high-level task force set up by the European Council at the beginning of the crisis,[5] the Council and the European Parliament adopted the six-pack in 2011,[6] a set of five regulations and one directive, to strengthen fiscal and macroeconomic surveillance. In 2012, the Member States of the euro area concluded the Treaty establishing the European Stability Mechanism (TESM), a permanent financial instrument to replace the temporary EFSF and EFSM. That same year, 25 Member States concluded the Treaty on Stability, Coordination and Governance in the EMU (TSCG) to again strengthen fiscal surveillance. In 2013, the Council and the European Parliament

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[3] J.V. Louis, 'Guest editorial: The no-bail out clause and rescue package', 47 *CMLRev.* (2010), p. 971–986.

[4] D. Adamski, 'National Power Games and Structural Failures in the European Macroeconomic Governance', 49 *CMLRev.* (2012), p. 1319–1364; N. de Sadeleer, 'The New Architecture of the European Economic Governance: A Leviathan or a Flat-Footed Colossus?', 19 *MJ* (2012), p. 354–382.

[5] This task-force was composed of the finance ministers of the Member States, the Commissioner for economic and monetary affairs and the ECB President and chaired by the European Council President Van Rompuy: Final Report of 21 October 2010 by Task Force on Economic Governance, doc. 15 302/10 which was endorsed by the European Council of October 2010.

[6] The six-pack was published in OJ [2011] L 306. Most of its provisions entered into force on 13 December 2011.

adopted the two-pack, a set of two regulations, which apply only to the Member States whose currency is the euro, to further strengthen fiscal surveillance and incorporate some provisions of the TSCG into the EU legal framework.[7] Reforms will continue.[8] In particular, there are now proposals to develop more binding legal instruments for the coordination of economic policies.

This flood of legal instruments substantially improves the economic governance. Regarding the coordination of economic policy, there was little direct change as coordination continues to be based on soft law instruments and the Open Method of Coordination, but the other reforms of governance indirectly impact the coordination and economic convergence. Solidarity is where the most radical changes took place, as financial assistance can now be provided upon conditions (to ensure that Member States run sustainable fiscal policies and that the EMU does not become a transfer Union). Regarding fiscal surveillance, the rules have been made smarter and the sanctions more automatic. Moreover, a new pillar of the surveillance of macroeconomic imbalances has also been set up.[9]

While they strengthen integration, the recent reforms also increase the substantive and institutional differentiation between the countries which are part of the euro area and those which are outside.[10] Such differentiation is based on an extensive interpretation of the new legal basis introduced by the Lisbon Treaty, in particular, Article 136 TFEU.[11] This increased differentiation, combined with the recent understanding of the political consequences of a common currency, casts doubt on the first fundamental choice made in Maastricht, id est, the euro must be the currency of all the Member States. Already at that time, two Member States, the United Kingdom and Denmark, opted out of the euro. Now, voices are advocating to build a 'two-speed Europe', of which one could be based on the common currency.[12]

7 The two-pack was published in OJ [2013] L140. Most of its provisions entered into force on 30 May 2013. See European Commission, 'The Two-Pack on economic governance: Establishing an EU framework for dealing with threats to financial stability in euro area member states', *European Economy: Occasional Paper* 147 (2013).

8 Communication from the Commission of 28 November 2012, A blueprint for a deep and genuine economic and monetary union, COM(2012) 777; Report of 5 December 2012 by H. Van Rompuy, J.M. Barroso, M. Draghi and J.-C. Juncker, 'Towards a Genuine Economic and Monetary Union', submitted at the European Council of December 2012, SN 4577/12.

9 The euro-crisis also led to a fundamental overhaul of the EU regulation of the financial sector. In 2010, three authorities were established for micro-prudential oversight: the European Banking Authority (EBA), the European Securities and Markets Authority (ESMA) and the European Insurance and Occupational Pension Authority (EIOPA) as well as one Board for macro-prudential oversight: the European Systemic Risk Board (ESRB): see [2010] OJ L 331. In 2013, a Single Supervisory Mechanism was established at the ECB.

10 For an analysis of the integration and the differentiation in the EMU, see F. Snyder, 'EMU – Integration and differentiation: Metaphor for European Union', in P. Craig and G. de Burca (eds.), *The Evolution of EU Law* (2nd ed., Oxford University Press, Oxford 2011), p. 687–716.

11 On the EMU amendments introduced by the Lisbon Treaty, see Final Report of 21 October 2002 of the Working Group on Economic Governance; R. Smits, 'The European Constitution and EMU: an appraisal', 42 *CMLRev.* (2005), p. 425–468.

12 J.C. Piris, *The Future of Europe: Towards a Two-speed EU?* (Cambridge University Press, Cambridge 2012).

Thus today, economic governance is based on four pillars (see Table 2 at the end of this contribution), each with its own objectives and methods, with strong differentiation between the countries which are in the eurozone and those which are outside. The first pillar establishes fiscal rules and surveillance according to a 'UN regime'.[13] The second pillar sets up a macroeconomic surveillance, also according to a 'UN regime'. The third pillar establishes coordination of economic and social policies according to a 'hyper-OECD regime'. The fourth pillar organizes financial solidarity among Member States according to an 'IMF regime'. Those four pillars are based on nearly 20 legal instruments with different legal natures, as some are within the EU legal framework and others are outside that framework.[14] This contribution describes and identifies the main trends in the evolution of the four economic governance pillars, and then conjectures their impact on the transformation of EU law on the basis of the questions raised by the editors of this anniversary issue.

§2. FIRST PILLAR: FISCAL SURVEILLANCE

The first pillar of economic governance aims to control, and if necessary correct, the fiscal imbalances of the Member States. It is made of a triptych: budgetary rules, an annual surveillance procedure and correction mechanisms at the EU and national levels.

Originally, this pillar was based on the TFEU and the Stability and Growth Pact made of two Council Regulations and one European Council Resolution.[15] In 2005, after its violation by France and Germany, the pact was reformed to make its rules smarter and its procedures more flexible.[16] In 2011, after the eurocrisis, the pact was reformed again to make the procedure more stringent and the sanctions more automatic.[17] It was

13 According to the metaphors made by Y. Bertoncini, 'Zone euro et démocratie(s): Un débat en trompe l'œil', *Notre Europe Policy Paper* 94 (2013).

14 See the list of legal sources annexed to this contribution.

15 Regulation 1466/97 of the Council of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies, Regulation 1467/97 of the Council of 7 July 1997 on speeding up and clarifying the implementation of the excessive deficit procedure, adopted on the basis of Article 121(6) TFEU and Resolution of the European Council of 17 June 1997 on the Stability and Growth Pact, [1997] OJ C 236/1. A. Brunila, M. Buti and D. Franco (eds.), *The Stability and Growth Pact: The Architecture of Fiscal Policy in EMU* (Palgrave Macmillan, Basingstoke 2001).

16 Regulation 1055/2005 of the Council of 27 June 2005 and Regulation 1056/2005 of the Council of 27 June 2005, adopted on the basis of Article 121(6) TFEU. Those regulations have been adopted on the basis of the Report of the Ecofin Council 'Improving the implementation of the Stability and Growth Pact' endorsed by the European Council of March 2005. On the context and the content of the review, see F. Amtenbrink and J. de Haan, 'Economic Governance in the European Union: Fiscal discipline versus flexibility', 40 *CMLRev.* (2003), p. 1075–1106; J.V. Louis, 'The Review of the Stability and Growth Pact', 43 *CMLRev.* (2006), p. 85–106.

17 Regulation 1175/2011 of the European Parliament and of the Council of 16 November 2011 and Regulation 1177/2011 of the Council of 16 November 2011, adopted on the basis of Article 121(6) TFEU.

also complemented by a Directive on national fiscal frameworks.[18] For the eurozone Members, the pact was also complemented by one regulation adopted in 2011 to increase the possibilities of sanction[19] and by another regulation adopted in 2013 to enhance the Commission and Council's oversight over national public finances.[20] In 2012, 25 Member States concluded the Treaty on Stability, Coordination and Governance in the EMU (TSCG), an international treaty outside the legal framework of the EU to again reinforce fiscal surveillance.[21] An international treaty was necessary because some Member States, notably Germany, favoured a treaty to strengthen fiscal surveillance but the United Kingdom made the revision of EU treaties conditional upon requirements which were not acceptable to other Member States.[22]

A. FISCAL RULES

Since the beginning of the EMU in 1992, the TFEU has imposed two simple limits on national public finances.[23] The first limit requires that Member States maintain their effective deficits below 3% of GDP, unless either the ratio declined substantially and continuously and reached a level that comes close to 3%, or, alternatively, the excess over 3% is only exceptional and temporary and the ratio remains close to 3%. The second limit requires that Member States maintain their debts below 60% of GDP, unless the ratio is sufficiently diminishing and approaching 60% at a satisfactory pace. However, as events showed, those rules were too simple and too narrowly focused.

In 2003, the two largest eurozone countries, France and Germany, violated the deficit rule and managed to convince a blocking minority within the Council to reject the sanctions proposed by the Commission. They argued that the deficit rule was so

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18 Directive 2011/85 of the Council of 8 November 2011 on requirements for budgetary frameworks of the Member States, adopted on the basis of Article 126(14) TFEU.

19 Regulation 1173/2011 of the European Parliament and of the Council of 16 November 2011 on the effective enforcement of budgetary surveillance in the euro area, adopted on the basis of Article 136 TFEU in combination with Article 121(6) TFEU.

20 Regulation 473/2013 of the European Parliament and of the Council of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area, adopted on the basis of Article 136 TFEU in combination with Article 121(6) TFEU.

21 The TSCG was concluded on 2 March 2012 and entered into force on 1 January 2013. On this treaty, see House of Commons European Scrutiny Committee, *Treaty on Stability, Coordination and Governance: impact on the Eurozone and the rule of law,* HC 1817, 2012; P. Craig, 'The Stability, Coordination and Governance Treaty: Principle, Politics and Pragmatism', 37 *European Law Review* (2012), p. 231–248; S. Peers, 'The Stability Treaty: Permanent Austerity or Gesture Politics', *Eur. Const. L. Rev.* (2012), p. 404–441.

22 See B. de Witte, 'Treaty Games – Law as Instrument and as Constraint in the Euro Crisis Policy', in F. Allen, E. Carletti, S. Simonelli (eds.), *Governance for the Eurozone: Integration or Disintegration* (European University Institute, Florence 2012), p. 144–154.

23 Article 126(2) TFEU and Article 1 Protocol No. 12 on the excessive deficit procedure.

simple that it was stupid (as the previous Commission President Prodi put it) because it did not sufficiently take into account the specific situation of each country, nor the economic cycle. That led to the first reform of the Stability and Growth Pact Regulation introducing a new and smarter fiscal rule to ensure the sustainability of public finances, the country-specific Medium Term Objective (MTO). This is a target for the structural deficit (id est, the effective deficit corrected for the effects of the economic cycle as well as the one-off and temporary fiscal measures) in the medium term (id est, 3 years), which is determined for each Member State according to its explicit and implicit government debt. In 2005, the revised Stability and Growth Pact provides that the MTO should be comprised of between –1% of GDP and balance or surplus.[24] In 2012, the TSCG went further and provided that the MTO cannot go below –0.5% of GDP (unless the ratio of government debt is below 60% of GDP and the risks in terms of long-term sustainability of public finances are low).[25]

Successive reforms also introduced an adjustment path when a Member State is violating fiscal rules. On the one hand, if a Member State has not reached its MTO, it must reduce its structural deficit by at least 0.5% of GDP per year (or more if the Member State has a government debt above 60% of GDP or presents pronounced risks of overall debt sustainability).[26] There is an escape clause in the case of an unusual event outside the control of the Member State which has a major impact on the financial position of the general government or in periods of severe economic downturn for the euro area or the Union as a whole.[27] On the other hand, if a Member State has not reached the debt ceiling, it must reduce the difference between the actual debt level and the authorized 60% of GDP threshold at an average rate of one twentieth per year as a benchmark.[28]

Finally, the recent reforms have increased the national ownership of the rules. The six-pack provides that each Member State should have, in national law, numerical fiscal rules which effectively promote compliance with EU government deficit and debt limits.[29] The TSCG goes further by imposing on the Contracting Parties the transposition into national law of the MTO rule and its adjustment path through provisions of binding force and permanent character, preferably constitutional, or otherwise guaranteed to be fully respected throughout the national budgetary processes.[30]

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24 Article 2a(2) of Regulation 1466/97 amended. The methodology to calculate the MTO is explained in the Specifications of the Council of 3 September 2012 on the implementation of the Stability and Growth Pact and Guidelines on the format and content of Stability and Convergence Programmes. Also European Commission, *Vade mecum on the Stability and Growth Pact*, European Economy: Occasional Paper 151 (2013).

25 Article 3(1b) and (1d) TSCG.

26 Article 5(1) Regulation 1466/97 amended.

27 Article 5(1) *in fine* Regulation 1467/97 amended and Article 3(1c) and (3b) TSCG.

28 Article 2(1a) Regulation 1467/97 amended and Article 4 TSCG.

29 Articles 5 to 7 of the Directive 2011/85. These provisions do not apply to the UK.

30 Article 3(2) TSCG. See F. Fabbrini, 'The Fiscal Compact, The "Golden Rule" and the Paradox of European Federalism', 36 *Boston College International and Comparative Law Review* (2013), p. 1.

B. ANNUAL SURVEILLANCE PROCEDURE

Since the beginning of the EMU, the TFEU and then the Stability and Growth Pact have organized an annual multilateral surveillance procedure. Each year, each Member State submits a stability (if their currency is the euro) or a convergence (if their currency is not the euro) programme describing the expected evolution of its public finances.[31] After examination, the Commission proposes country-specific budgetary recommendations, which are adopted by the Council by qualified majority.

Initially, those Council recommendations were fully applied by the Member States because they were afraid they would not be admitted to the eurozone if their public finances were not compliant with EU fiscal limits. After the accession to the monetary zone, the effectiveness of surveillance weakened substantially, as the Member States did not fear exclusion from the euro area. To regain effectiveness, the procedure was reformed, especially for the eurozone countries, in three ways. First, the powers of the Commission were enhanced. The Lisbon Treaty made it possible for the Commission to address warnings directly to Member States[32] and, then, the six-pack introduced a 'comply or explain' rule where the Council should follow Commission proposals as a rule, or explain its position publicly.[33] Second, the effects of recommendations were strengthened. The six-pack introduced the possibility of sanctions (an interest-bearing deposit of 0.2% of GDP) when preventive budgetary recommendations are not applied by the eurozone countries.[34] Third, the timespan of EU oversight over national fiscal policies was extended. The two-pack imposed on eurozone countries the submission of draft budgetary plans each year in October, and gave the Commission the right to comment on, or in case of serious non-compliance with EU fiscal rules, to request a revision of those plans.[35]

C. CORRECTIVE MECHANISMS

If, despite the annual surveillance, a Member State does not comply with fiscal rules, EU law foresees corrective mechanisms at the EU level (the excessive deficit procedure), and at the national level.

31 Article 4 Regulation 1466/97 amended and the Code of Conduct of 3 September 2012 on the Specifications on the implementation of the Stability and Growth Pact and Guidelines on the format and content of stability and convergence programmes.

32 Article 121(4) TFEU.

33 Articles 2-ab(2) and 6(2) Regulation 1466/97 amended.

34 Article 4 Regulation 1173/2011.

35 Article 7 Regulation 473/2013 and Section II of the Specifications of 1 July 2013 on the implementation of the Two Pack and Guidelines on the format and content of draft budgetary plans, economic partnership programmes and debt issuance reports.

1. *At the EU level: the excessive deficit procedure*

When the EMU was created, the TFEU and then the Stability and Growth Pact established an EU corrective procedure with extensive oversight from the Commission and Council when a Member State violates fiscal rules. The Commission proposes the opening of the procedure, and a decision is made by the Council by qualified majority.[36] The Council also adopts a budgetary recommendation setting a date for correction (id est, when government effective deficit should be below 3%) and a correction path. If the Member State concerned does not comply with the corrective recommendations, the Commission proposes, and the Council decides on, the stepping up of the procedure which may end up with the imposition of sanctions (from more transparency, to limiting EIB intervention, to a non-interest bearing deposit, to a fine of 0.5% GDP).

Although the excessive deficit procedure was quickly applied after the introduction of the euro, the original procedure was prone to political bargaining. In 2003, the Commission proposed to step up the excessive deficit procedure against France and Germany, but was not followed by the Council due to intense lobbying by both countries. Instead, the Council relaxed the budgetary recommendations addressed to France and Germany.[37] The Commission sought the annulment of the Council actions at the Court of Justice, but partly lost the case.[38] As already explained, this case triggered the first reform of the Stability and Growth Pact in 2005 with, among others, the introduction of a stricter timeline for the different steps of the EDP.

In 2010, the euro crisis showed that the excessive deficit procedure had not been effective in preventing some Member States from running unsustainable fiscal policies. This led to additional reforms of the excessive deficit procedure in the same three ways as for the preventive arm of the Stability and Growth Pact. First, the powers of the Commission were enhanced. The six-pack imposed the 'comply or explain' rule for the proposals made by the Commission during the excessive deficit procedure.[39] It also provided that the newly created financial sanctions must be decided by the Council by reverse qualified majority. Then, the TSCG foresaw that the existing sanctions of the TFEU must also be decided by reverse qualified majority.[40] Second, the effects of corrective recommendations were strengthened. The six-pack introduced additional and earlier sanctions in case of non-compliance by the eurozone countries.[41] Third, the EU oversight has been reinforced. The TSCG and the two-pack imposed on eurozone countries are subject to an excessive

36 Article 126(6) and 126(13) TFEU. Article 139(4b) TFEU provides that when the EDP is decided against a eurozone country, only the other eurozone countries may vote.

37 The meeting is summarized in the Press Release of the Council meeting of 25 November 2003.

38 Case C-27/04 *Commission v. Council* [2004] ECR I-6649.

39 Article 2a(1) Regulation 1467/97 amended.

40 Article 7 TSCG which provides that the Contracting Parties commit to support the Commission proposal unless a qualified majority is opposed.

41 Article 5 of Regulation 1173/2011 provides for a non-interest bearing deposit amounting to 0.2% of GDP; Article 6 Regulation 1173/2011 provides for a fine of 0.2% of GDP.

deficit procedure, the submission of an economic partnership programme describing the policy measures and structural reforms necessary to correct the excessive deficit.[42]

2. At national level: the automatic correction mechanism

Initially, EU law did not explicitly require the establishment of a national correction mechanism for the violation of EU fiscal rules. That contributed to the lack of national ownership of the EU constraints. To remedy this weakness, the six-pack required that national fiscal laws contain effective and timely monitoring of compliance with the rules based on a reliable analysis carried out by an independent body, as well as the consequences of non-compliance.[43] Going further, the TSCG required the establishment of a national correction mechanism to be triggered automatically in case of significant deviation from the MTO or the adjustment path towards it. This national correction mechanism is to be based on seven common principles adopted by the Commission[44] and included in provisions of binding force and permanent character, preferably constitutional, or otherwise guaranteed to be fully respected throughout the national budgetary processes.[45] The transposition is monitored by the Commission and is subject to the adjudication of the Court of Justice.[46]

§3. SECOND PILLAR: MACROECONOMIC SURVEILLANCE

Originally, the multilateral surveillance focused only on fiscal imbalances and not on other economic imbalances, such as a banking crisis or housing bubble, susceptible to threaten the stability of the eurozone. This weakness was repaired by the six-pack, which introduced a new pillar in the economic governance, mirroring the triptych of the first pillar, with a scoreboard of macroeconomic indicators, an annual surveillance procedure, and a correction procedure. This pillar is based on two regulations adopted in 2011 by the Council and the European Parliament, one applicable to all Member States[47] and the other applicable only to the eurozone members.[48]

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42 Article 9 Regulation 473/2013 and Article 5 TSCG; Section IV of the Specifications of 1 July 2013 on the implementation of the Two Pack and Guidelines on the format and content of draft budgetary plans, economic partnership programmes and debt issuance reports.

43 Article 6 Directive 2011/85.

44 Article 3(1e) TSCG and Communication from the Commission of 20 June 2012, Common principles on national fiscal correction mechanisms, COM(2012) 342.

45 Article 3(2) TSCG.

46 Article 8 TSCG. Note the Court of Justice does not control the correct implementation of the mechanism for the annual national budgets.

47 Regulation 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances, adopted on the basis of Article 121(6) TFEU.

48 Regulation 1174/2011 of the European Parliament and of the Council of 16 November 2011 on enforcement measures to correct excessive macroeconomic imbalances in the euro area, adopted on the basis of Article 136 TFEU in combination with Article 121(6) TFEU.

A. MACROECONOMIC SCOREBOARD

The Commission has established a scoreboard with 11 indicators of internal and external macroeconomic imbalances to facilitate early identification of Member States affected or at risk of being affected by imbalances.[49]

B. ANNUAL SURVEILLANCE PROCEDURE

Each year, the Commission screens the Member States with the scoreboard. On that basis, the Commission adopts an Alert Mechanism Report which identifies the countries which are affected or may be affected by imbalances and which need an in-depth review.[50] If after this in-depth review the Commission finds macroeconomic imbalances, it proposes country-specific recommendations, which are adopted by the Council by qualified majority.[51]

C. EU CORRECTIVE PROCEDURE: EXCESSIVE IMBALANCE PROCEDURE

If a Member State presents macroeconomic imbalances requiring a correction procedure, the Commission proposes the opening of an Excessive Imbalance Procedure which is decided by the Council by qualified majority. The Council also adopts economic recommendations to correct such imbalances.[52] In this case, the Member State concerned submits a corrective action plan and is subject to extensive oversight from the Commission and the Council.[53] If the country is part of the eurozone and does not comply with the Council's economic recommendations, the Commission proposes a financial sanction (a fine of 0.1% of GDP) which is adopted by the Council by reverse qualified majority.[54]

§4. THIRD PILLAR: SOCIO-ECONOMIC COORDINATION

The third pillar of the economic governance relates to the coordination of national economic and social policies in order, on the one hand, to prevent fiscal and macroeconomic imbalances and, on the other hand, to stimulate growth and jobs in Europe.

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49 Article 4 Regulation 1176/2011 and European Commission, 'Scoreboard for the Surveillance of Macroeconomic Imbalances', *European Economy: Occasional Papers* 92 (2012). Five indicators are external (current account balance, net international investment position, real effective exchange rate, export market shares and nominal unit labour cost) and six indicators are internal (change in deflated house prices, private sector credit flow, general government debt, unemployment rate and total financial sector liabilities).

50 Article 3 Regulation 1176/2011.

51 Articles 5–6 Regulation 1176/2011.

52 Article 7 Regulation 1176/2011.

53 Articles 8–11 Regulation 1176/2011.

54 Article 3(2a) Regulation 1174/2011.

A. TARGETS AND GUIDELINES

With the introduction of the EMU, different strategies to coordinate the national economic and employment policies have progressively been set up: coordination of economic policies with the Broad Economic Policies Guidelines in 1992, coordination of employment policies with the European Employment Strategy in 1997 (Luxembourg process),[55] coordination of structural reforms in 1998 (Cardiff process)[56] and macro-economic dialogue in 1999 (Cologne process).[57] All those coordination processes were then integrated in 2000 into one overarching Strategy decided at the Lisbon European Council, aiming at making the EU 'the most competitive and dynamic knowledge-based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion'.[58] This strategy was recast on growth and employment in 2005.[59]

In 2010, the Europe 2020 Strategy for Growth and Jobs was adopted by the European Council to succeed to the Lisbon Strategy.[60] It aims to achieve, by 2020, five headlined targets relating to employment rate, R&D investment, climate change, education and poverty reduction, which have been translated by each Member State in national targets. To achieve those objectives, the Council adopted 10 integrated policy guidelines to steer national policies, six broad economic policy guidelines (adopted on the basis of Article 121(2) TFEU) and four Employment Guidelines (adopted on the basis of Article 148(2) TFEU).[61]

In addition, two political pacts set complementary guidelines for the coordination of economic and social policies. The Euro Plus Pact, adopted by 23 Member States at the European Council of March 2011, provides for structural reforms to enhance competitiveness, employment, the sustainability of the public finances and financial stability.[62] The Compact for Growth and Jobs, adopted by all the Member States at the

55 Conclusions of the Luxembourg Extraordinary European Council on Employment of November 1997.

56 Conclusions of the Cardiff European Council of June 1998.

57 Conclusions of the Cologne European Council of June 1999.

58 Conclusions of the Lisbon European Council of March 2000, §5. On the strategy, see M.J. Rodrigues, *European Policies for a Knowledge Economy* (Edward Elgar, Cheltenham 2003).

59 Conclusions of the European Council of March 2005, based on W. Kok, *Facing the challenge: The European Strategy for Growth and Jobs, Report of the High-Level Group* (2004) and Communication from the President of the Commission of 2 February 2005, Working together for growth and jobs – A new start for the Lisbon Strategy, COM(2005) 24.

60 Conclusions of the European Council of June 2010, based on the Communication from the Commission of 3 March 2010, Europe 2020 – A strategy for smart, sustainable and inclusive growth, COM(2010) 2020.

61 Council Recommendation 2010/410 of 13 July 2010 on broad guidelines for the economic policies of the Member States and of the Union and Council Decision 2010/707 of 21 October 2010 on guidelines for the employment policies of the Member States.

62 Annex of the Conclusions of the European Council of 24–25 March 2011.

European Council of June 2012, provides for national and EU measures to stimulate growth and jobs.[63]

Finally, the TSCG provides that the Contracting Parties undertake to work jointly and take the necessary actions which are essential to the proper functioning of the euro area in pursuit of the objectives of fostering competitiveness, promoting employment, contributing further to the sustainability of public finances and reinforcing financial stability.[64]

B. ANNUAL COORDINATION

At the beginning of the EMU, each policy strategy had its own coordinating method and process which were developed organically according to practical needs. All those methods were streamlined in 2000 by the Lisbon European Council with the Open Method of Coordination comprising four steps: (i) EU guidelines with goals and a timetable; (ii) quantitative and quality indicators and benchmarks; (iii) national action plans with targets and policy reforms; and (iv) periodic monitoring, evaluation and peer review organized as a mutual learning process.[65] The coordination of the economic, employment and social policies was then explicitly referred to in the Lisbon Treaty.[66]

In 2010, the coordination was further improved with the introduction of the European semester[67] which synchronizes the fiscal surveillance (Member States' stability/convergence programmes), the macroeconomic surveillance (Commission Alert mechanism report and in-depth review) and the coordination of economic and employment policies (Member States' National reform programmes). It also places the EU surveillance and coordination during the first semester of the year before the adoption of the national budget and policies during the second semester of the year.

The cycle starts with the adoption by the Commission of the Annual Growth Survey which sets the priorities for the European Union to achieve growth and jobs. Then, the Council and the European Parliament hold debates on the Survey, which leads to the adoption of general orientations by the Spring European Council. In April, when it adopts its fiscal convergence/stability programme, each Member State also adopts its National Reform Programme indicating the structural reforms already done and to be undertaken in order to achieve its national Europe 2020 targets. After examination, in May the Commission proposes country-specific recommendations for each Member

63 Annex of the Conclusions of the European Council of 28–29 June 2012.

64 Article 9 TSCG referring to the policies areas defined in the Euro Plus Pact of March 2011.

65 Conclusions of the Lisbon European Council of March 2000, §37. For a critical assessment of the Open Method of Coordination, see R. Dehousse, *L'Europe sans Bruxelles: une analyse de la méthode ouverte de coordination* (L'Harmattan, Paris 2004).

66 Article 5 TFEU.

67 The European Semester is provided by Article 2-a Regulation 1466/97 amended.

State. In July, the Council adopts the recommendations, acting by qualified majority and following the 'comply or explain' principle.

The TSCG foresees further coordination methods and provides that the Contracting Parties ensure that all major economic policy reforms that they plan to undertake are discussed ex-ante and, where appropriate, coordinated among themselves.[68] The operationalization of such *ex-ante* coordination is still under discussion.[69]

§5. FOURTH PILLAR: FINANCIAL SOLIDARITY

As already explained, when the EMU was established, financial solidarity between Member States and monetary financing from central banks were prohibited except in very exceptional circumstances. However, when in spring 2010 Greece was at the verge of a bankruptcy which would have had massive effects on the other Member States, the European Council decided to provide financial assistance. In May 2010, Member States granted bilateral loans to Greece.[70] Then the Council adopted a Regulation establishing the European Financial Stabilisation Mechanism (EFSM), which is an EU instrument with a lending capacity of 60 billion EUR.[71] As this financial capacity was not enough to be credible but could not be increased because of the small size of the EU budget, Member States of the Eurozone also established, for three years, the European Financial Stability Facility (EFSF), which is an intergovernmental special-purpose vehicle with a lending capacity of 440 billion EUR.[72] In parallel, the ECB adopted the Securities Market Programme (SMP) allowing the purchase of government bonds on the secondary market with a ceiling of 209 billion EUR.[73] Unfortunately, those reforms did not succeed in ending the eurocrisis which expanded to Portugal, Ireland and then Spain, victims of the burst of their housing bubbles and the collapse of their financial systems.

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68 Article 11 TSCG.

69 See Communication from the Commission of 20 March 2013, *ex ante* coordination of plans for major economic policy reforms, COM(2013) 166.

70 Statement of 25 March 2010 of the Heads of State or Government of the euro area and Eurogroup meeting of 2 May 2010, doc. 9417/10. On the first financial assistance measures and their compatibility with EU law, see A. de Gregorio Merino, 'Legal developments in the Economic and Monetary Union during the debt crisis: The mechanism of financial assistance', 49 *CMLRev.* (2012), p. 1613–1646; J.V. Louis, 47 *CMLRev.* (2010), p. 971–986; T. Middleton, 'Not Bailing Out … Legal Aspects of the 2010 Sovereign Debt Crisis', in *A Man for All Treaties, Liber Amicorum en l'honneur de Jean-Claude Piris* (Bruxelles, Bruylant 2012), p. 421–439; M. Ruffert, 'The European Debt Crisis and European Union Law', 48 *CMLRev.* (2011), p. 1777–1806. The bilateral loans to Greece and the EFSF have been validated by the German Constitutional Court: BverfG, 7 September 2011, BvR 987/10.

71 Council Regulation 407/2010 of 11 May 2010, adopted on the basis of Article 122(2) TFEU.

72 Decision of 10 May 2010 of the Representatives of the Governments of the Euro Area Member States Meeting within the Council of the European Union establishing the European Financial Stability Facility, doc. 9610/10 and the EFSF Framework Agreement of 7 June 2010 between the participating Member States.

73 Decision 2010/281 of the European Central Bank of 14 May 2010 establishing a securities markets programme, [2010] OJ L 124/8.

In February 2012, the Member States of the euro area concluded the Treaty establishing the European Stability Mechanism (TESM), a permanent international financial institution with a lending capacity of 500 billion EUR to replace the temporary EFSF and EFSM.[74] An international treaty was necessary because EU law does not foresee a legal basis for permanent financial assistance. During the negotiations, Germany requested the revision of Article 136 TFEU to secure the legality of the TESM with regard to EU law.[75] Since then, the Court of Justice, sitting as a full Court, validated the TESM by adopting a teleological interpretation of Article 125 TFEU.[76] The Court imposed three conditions, met by the TESM, to validate an assistance mechanism: (i) the beneficiary state remains responsible for its commitments to its creditors, (ii) conditions are attached to the assistance such as to prompt that Member State to implement a sound budgetary policy and (iii) the assistance is indispensable for the safeguarding of the financial stability of the euro area as a whole. However, the euro crisis only started to calm down when the ECB announced its Outright Monetary Transaction (OMT) programme allowing unlimited purchase of state bonds with a maturity of between one and three years on the condition of the adoption of an appropriate European Financial Stability Facility/European Stability Mechanism (EFSF/ESM) programme.[77]

Thus, now there is a new fourth pillar in the economic governance, which applies when the implementation of the three other pillars do not suffice to prevent a Member State from experiencing serious financial stability difficulties.

74 The TESM was concluded on 11 July 2011 and a revised version was concluded on 2 February 2012. It entered into force on 27 September 2012. On this treaty, see: J.V. Louis, 'The Unexpected Revision of the Lisbon Treaty and the Establishment of a European Stability Mechanism', in D. Ashiagbor, N. Countouris, I. Lianos (eds.), *The European Union after the Treaty of Lisbon* (Cambridge University Press, Cambridge 2012), p. 284–319.

75 The revision, done with the simplified treaty revision procedure, added a third paragraph to Article 136 TFEU providing that: "The Member States whose currency is the euro may establish a stability mechanism to be activated if indispensable to safeguard the stability of the euro area as a whole. The granting of any required financial assistance under the mechanism will be made subject to strict conditionality": European Council Decision 2011/199 of 25 March 2011 amending Article 136 of the Treaty on the Functioning of the European Union with regard to a stability mechanism for Member States whose currency is the euro [2011] OJ L 91/1. It entered into force on 1 May 2013.

76 Case C-370/12 *Pringle v. Ireland*, Judgment of 27 November 2012, para. 136–137. The Court of Justice also decided that the revision of Article 136 TFEU was not a necessary condition for the validity of the TESM with regard to EU law. The TESM is also challenged before the German Constitutional Court. In an interim ruling, the Court allowed the German authorities to ratify the Treaty: BverfG, 12 September 2012, BVR 1390/12. The final decision is still pending.

77 Press Release of the ECB of 6 September 2012, Technical features of Outright Monetary Transactions. The validity of the OMT programme is contested before the German Constitutional Court in TESM case.

A. THE POSSIBILITIES OF ASSISTANCE

If a Member State of the Eurozone needs assistance to stabilize its financial situation,[78] it can address a request to the European Stability Mechanism which foresees several possibilities: a precautionary conditioned credit line or an enhanced conditions credit line, a loan for the specific purpose of recapitalizing the national financial institutions, a loan without specific purpose, the purchase of the Member State's bonds on the primary market, and operations on the secondary market in relation to the state's bonds.[79] Such assistance is conditioned by the adoption of a macroeconomic adjustment programme by the requesting state.

B. DECISION ON FINANCIAL ASSISTANCE AND THE MACROECONOMIC ADJUSTMENT PROGRAMME

The decision to grant assistance and the macroeconomic adjustment programme are negotiated in several steps. First, the Commission, in liaison with the ECB and where possible with the IMF (the troika), assesses the sustainability of the Member State's government debt and its actual or potential financing needs.[80] On this basis, the ESM Board of Governors (id est, the Finance Ministers of the Member States of the euro area) decides, acting by mutual agreement except in urgent cases, to grant, in principle, stability support and gives a mandate to the Commission to negotiate a Memorandum of Understanding determining the conditions for assistance.[81] Then, the state concerned and the Commission negotiate the Memorandum of Understanding and the underlying macroeconomic adjustment programme. Those provide for annual fiscal targets and measures to achieve them and take into account the recommendations addressed to the state concerned during the European Semester.[82] Then, the ESM Board of Governors, acting by mutual agreement except in urgent cases, approves the Memorandum of Understanding and the Council, acting by qualified majority of the Eurozone Members, approves the macroeconomic adjustment programme.[83] Finally, the Commission signs

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78 If a Member State which is not part of the Eurozone faces serious difficulties in their balance of current payment, it may receive assistance from a Community facility with a lending capacity of 50 billion euros (Council Regulation 332/2002 of 18 February 2002 establishing a facility providing medium-term financial assistance for Member States' balances of payments, [2002] OJ L 53/1). Such facility has been used recently for Hungary, Latvia and Romania.

79 Those possibilities are described in Articles 14 to 18 TESM and detailed in guidelines adopted by the ESM Board of Directors.

80 Article 6 Regulation 472/2013 and Article 13(1) TESM.

81 Article 13(2) TESM.

82 Article 7 Regulation 472/2013 and Article 13(3) TESM. During the negotiations, social partners and civil society are consulted and the adjustment programme fully observes Article 152 TFEU relating to wage formation and Article 28 of the Charter of Fundamental Rights of the European Union relating to collective action: Articles 7(1) and 8 Regulation 472/2013.

83 Resp. Article 5(6f) and Article 13(4) TESM and Article 7(4) Regulation 472/2013.

the Memorandum of Understanding and the ESM Board of Directors approves the financial assistance facility agreement detailing the financial aspects of the stability support.[84]

C. SURVEILLANCE OF THE IMPLEMENTATION OF THE MACROECONOMIC ADJUSTMENT PROGRAMME

The Commission (in liaison with the ECB and where appropriate with the IMF) monitors the implementation of the adjustment programme and every three months informs the Economic and Financial Committee and the Chairs and Vice-Chairs of the Committee on Economic and Monetary Affairs of the European Parliament.[85] It also examines changes to the adjustment programme made necessary by the evolution of the macroeconomic context.[86] If the Commission observes significant deviations from the adjustment programme, it proposes to establish that the state concerned does not comply with the policy requirements contained in its programme and the Council decides by qualified majority. In this case, the state concerned must, in cooperation with the troika, take measures to stabilize markets.[87]

§6. INSTITUTIONAL FRAMEWORK

The reforms of economic governance led to an adaptation of the institutions in charge of its implementation. At the national level, EU law imposes minimal quality requirements for the institutions involved in economic governance and these requirements are stricter for the Member States of the euro area. At the EU level, a new euro institutional constellation has been established: the ministerial bodies of the euro area have been substantially strengthened, new bodies have been created for the ESM and, to a lesser extent, new roles have been given to parliamentary bodies.

A. NATIONAL INSTITUTIONAL FRAMEWORK

Initially, EU requirements related to national institutions involved in economic governance were very weak. They mainly relate to the provision of statistics and were minimal, as Eurostat did not enjoy extensive investigation power, and no clear sanctions

84 Article 13(4) and (5) TESM.

85 Article 7(4) Regulation 472/2013 and Article 13(7) TESM. To reduce administrative burden and alleviate a duplication of procedures, the macroeconomic adjustment programme and its monitoring replace the other surveillance procedures of the Stability and Growth Pact and the macroeconomic imbalances regulations: Articles 10 to 13 Regulation 472/2013.

86 Article 7(5) Regulation 472/2013.

87 Article 7(7) Regulation 472/2013.

were provided in case of statistics manipulation. When the need for good national institutions was recognized, EU law increased quality requirements.

In 2009, a new regulation on national fiscal statistics was adopted and was revised in 2010 to increase the investigation power of Eurostat.[88] In 2011, the six-pack required minimum quality for the budgetary framework defined as 'the set of arrangements, procedures, rules and institutions that underlie the conduct of budgetary policies of general government'.[89] Thus, all Member States must have in place public accounting systems subject to internal control and independent audits, adopt realistic macroeconomic and budgetary forecasts and establish a credible, effective medium-term budgetary framework.[90]

In 2013, the two-pack strengthened the institutional requirements specifically for the eurozone countries. First, they must apply a common budgetary timeline with three main deadlines: adoption of a national medium-term fiscal plan in April, of a draft budget in October, and of the budget by the end of the year.[91] Second, they must establish national fiscal councils, independent from the budegtary authorities,[92] with three main tasks: producing or endorsing macroeconomic forecasts and possibly budgetary forecasts, monitoring compliance with national numerical fiscal rules, and monitoring the implementation of the national automatic correction mechanism in case of violation of the fiscal rules.[93]

B. EU INSTITUTIONAL FRAMEWORK

In 1997, an informal coordination body between the Eurozone Finance Ministers was established, the Euro Group.[94] Over time, the governmental and parliamentary bodies involved in EU economic governance, in particular at the EMU level, were stepped up.

Regarding governmental bodies, the coordination of the eurozone countries has been strengthened at three levels. At the top, a Euro Summit composed of the Heads of State or Government of the Member States whose currency is the euro and chaired for 2.5 years

88 Regulation 479/2009 amended.
89 Article 2 Directive 2011/85.
90 Articles 3, 4 and 9 Directive 2011/85.
91 Article 4 Regulation 473/2013.
92 Article 2(1a) Regulation 473/2013. The independence of independent fiscal council requires a statutory regime grounded in national law, nomination procedures based on experience and competence, and adequacy of resources and appropriate access to information, freedom to communicate publicly in a timely manner. In the context of the national data protection authority, the Court of Justice has interpreted strictly the independence requirement and decided that it was not contrary to democratic legitimacy: Case C-518/07 *Commission v. Germany* [2010] ECR I-1885, para. 30 and 46.
93 Article 5 Regulation 473/2013.
94 Point 6 of the Resolution of the European Council of 13 December 1997 on economic policy coordination in stage 3 of EMU and on Treaty Articles 109 and 109b of the EC Treaty, [1998] OJ C 35/1.

by an elected President, was established by the TSCG.[95] At the ministerial level, the Eurogroup had a more stable elected presidency for 2.5 years in 2005, was consolidated with an explicit legal basis introduced by the Lisbon Treaty in 2009,[96] and a full-time president is now envisaged.[97] At the preparatory level, the Euro Working Group, which is composed of the representatives of the Eurozone countries at the Economic and Financial Committee, is now chaired by a full-time and Brussels-based President.[98]

Some specific bodies were also established for the European Stability Mechanism. The main decisional body is the Board of Governors which adopts the most important decisions such as the granting of financial assistance. It is composed of the finance ministers of the Contracting Parties and chaired by a President elected by qualified majority of its members or by the Eurogroup President. Most of its decisions are adopted by mutual agreement.[99] However, some decisions are adopted by qualified majority, which is defined as 80% of the votes cast and weighted according to the Member State's financial contribution to the ESM.[100]

Because the recent reforms of economic governance considerably strengthened the Commission, the Council and the Eurogroup's oversight over national fiscal and socio-economic policies, it was important to increase the role of parliamentary bodies to ensure the legitimacy and the acceptability of the new rules. Thus, the four pillars of the economic governance provide for an 'economic dialogue' between, on the one hand, the relevant committees of the European Parliament and, on the other hand, the President of the Council, the Commission, the President of the European Council or the President of the Eurogroup. The dialogue may also take place between the European Parliament and the Member State concerned by a measure adopted on the basis of economic governance rules.[101] Moreover, representatives of the Commission may be invited to the national parliament of the Member State concerned.[102] Finally, the TSCG sets up a conference of representatives of the relevant committees of the European Parliament and representatives of the relevant committees of national Parliaments to discuss the coordination and surveillance of fiscal and economic policies.[103]

95 Article 12 TSCG, already foreseen by Points 1–3 of Annex I to the Euro Summit Statement of 26 October 2011: Ten measures to improve the governance of the euro area.

96 Article 137 TFEU and Protocol No. 14 on the Eurogroup.

97 Point 5 of Annex I to the Euro Summit Statement of 26 October 2011: Ten measures to improve the governance of the euro area.

98 Ibid., Points 7 and 8.

99 Article 5(6) TESM.

100 Article 4(5) to (7) and Article 5(7) TESM. As the contribution of Germany or France is above 20%, each of those states has a veto right in a vote by qualified majority.

101 For the first pillar of economic governance: Article 2-ab Regulation 1466/97 amended; Article 2-a Regulation 1467/97 amended; Article 3 Regulation 1173/2011; Article 15 Regulation 473/2013. For the second pillar: Article 14 Regulation 1176/2011. For the third pillar: Article 2-ab Regulation 1466/97 amended. For the fourth pillar: Article 3(8), Article 7(10) and (11), Article 14(3) and (5), Article 18 Regulation 472/2013.

102 See for instance, Article 7(2) Regulation 473/2013; Article 3(8) and Article 7(11) Regulation 472/2013.

103 Article 13 TSCG.

Table 1. Evolution of the four pillars of economic governance

	First pillar Fiscal Surveillance	Second pillar Macroeconomic Surveillance	Third pillar Socio-Economic Coordination	Fourth pillar Financial Solidarity
1992	***Maastricht Treaty*** Fiscal rules and surveillance and correction procedures		***Maastricht Treaty*** Coordination of economic policies	
1997	***Stability and Growth Pact*** – Preventive phase: surveillance – Corrective phase: correction		***Amsterdam Treaty and Luxembourg process*** Coordination of employment policies	
1998			***Cardiff process:*** structural reform	
1999			***Cologne process:*** Macroeconomic dialogue	
2000			***Lisbon Strategy*** Formalization of the Open Method of Coordination	
2005	***Review of the Stability and Growth Pact*** Smarter fiscal rules and stricter correction procedures		***Lisbon Strategy*** Mid-term review	
2009	***Lisbon Treaty*** Possibility of 'enhanced cooperation' within EMU			
2010			***Europe 2020 Strategy for Jobs and Growth***	– ***Regulation EFSF*** – ***Framework Agreement EFSM***
2011	***Six-pack*** Strengthening of the surveillance and correction procedures, esp. for Eurozone Member States	***Six-pack*** Macroeconomic scoreboard, surveillance and correction procedures		
2012	***TSCG (title III)***		***TSCG (title IV)***	***Treaty ESM***
2013	***Two-pack*** Additional Commission and Council oversight			***Two-pack*** – Enhanced surveillance – Negotiation framework for conditionality

Table 2. Overview of EU economic governance pillars for Member States whose currency is the euro

	First pillar Fiscal Surveillance	Second pillar Macroeconomic Surveillance	Third pillar Socio-Economic Coordination	Fourth pillar Financial Solidarity
Rules/ targets	– Deficit: 3% GDP and MTO – Debt: 60% GDP	Scoreboard with 11 indicators and thresholds	– 5 headline targets – 10 integrated guidelines	Serious difficulties with financial stability having spillover effects
Surveillance procedure	**EU Semester** – April: National Stability Programmes and National Reform Programmes by the Member States – July: Country-specific recommendations by the Council – October: Member States Draft budgetary plans			---
Corrective mechanism	**EU Excessive deficit procedure** – Council Decision – Member State economic partnership programme – Surveillance with possibility of sanctions **National correction mechanism**	**EU Excessive imbalance procedure** – Council Decision – Member State corrective action plan – Surveillance with possibility of sanctions	---	**Enhanced surveillance** – Decision of the Commission – Recommendation of the Council **Financial assistance upon conditions** – Decision of the ESM Board of Governors and Decision of the Council – Macroeconomic adjustment programme – Surveillance by troika – Recommendation of the Council
Institutional framework	– **EU:** European Council, Council, Economic and Financial Committee, Commission Economic dialogue at the European Parliament and inter-parliamentary conference – **EMU:** Euro Summit, Eurogroup, Eurogroup Working Group – **National:** fiscal framework, incl. independent fiscal councils			
				ESM: Board of Governors, Board of Directors, Managing Director

§7. TRANSFORMATION OF EU LAW

The evolution of EU economic governance over the last 20 years has been remarkable, especially in the last three years, and will probably have broader consequences on the three issues raised by the editors of this anniversary issue: the sources of EU law, the enforcement mechanisms, and the regulatory models.

A. SOURCES OF EU LAW

To analyse the legal sources of economic governance, a distinction should be made between the acts which establish the governance and those used to implement the governance.

On the one hand, the establishment of EU economic governance is mainly based on the TFEU and regulations adopted by the Council and, since the entry into force of the Lisbon Treaty, by the Council and the European Parliament. It is also based on international treaties such as the TESM agreed by 17 Member States and the TSCG agreed by 25 Member States. The conclusion of international treaties between some Member States is allowed under EU law when the contracting parties respect their EU obligations.[104] Those treaties may even entrust tasks to the EU institutions when those tasks do not alter the essential character of the powers conferred on those institutions by EU law.[105] International treaties concluded by some Member States have advantages over EU primary law as they do require unanimity, as well as over EU secondary law as they can be negotiated quickly between the governments of contracting parties without the EU institutions and they enjoy a higher symbolic value. But they also have drawbacks: they complicate the legal landscape, they need to be ratified by the Contracting Parties which may delay their application and, more importantly, they bypass the EU decision making-process – being treaty revision or enhanced cooperation – with their inherent checks and balances protecting the interests of the Union and all its Member States, and they risk undermining the legal integrity of the EU.[106] This is the reason why the TSCG and the TESM contain consistency clauses with EU law, and the TSCG foresees

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104 B. de Witte, 'Old-fashioned flexibility: International agreements between Member States of the European Union', in G. de Búrca and J. Scott (eds.), *Constitutional Change in the EU: From Uniformity to Flexibility?* (Hart Publishing, Oxford 2000), p. 30; B. de Witte, in F. Allen, E. Carletti and S. Simonelli (eds.), *Governance for the Eurozone: Integration or Disintegration*, p. 139–160; S. Peers, 'Towards a New Form of EU Law?: The Use of EU Institutions outside the EU Legal Framework', 9 *European Constitutional Law Review* 1 (2013), p. 37–72.

105 Case C-370/12 *Pringle v. Ireland*, para. 158 citing its previous case law: Joined Cases C-181/91 and C-248/91 *European Parliament v. Council (aid to Bangladesh)* [1993] ECR I-3713, para. 20 and Case C-316/91 *European Parliament v. Council (Lomé Convention)* [1994] ECR I-653, para. 41. This position is shared by the majority of the authors, but see the critical view of P. Craig, 37 *European Law Review* (2012), p. 241.

106 P. Craig, 37 *European Law Review* (2012), p. 238 and M. Ruffert, 48 *CMLRev.* (2011), p. 1789.

its progressive integration within the EU legal framework (which already started with the two-pack).

On the other hand, the implementation of EU economic governance relies mainly on recommendations proposed by the Commission and adopted by the Council. Those recommendations do not have direct binding effect as their violation cannot lead to an infringement case before the Court of Justice. However, they have indirect binding effect as their violation may lead to an investigation by the Commission and the imposition of sanctions by the Council. As in other EU fields (such as electronic communications), the recommendations have important legal effect through ad hoc sanction procedures. Thus, economic governance recommendations have fewer binding effects than those of the hard law but more binding effects than those of the (standard) soft law. To make a parallel with the typology between hard, smart and soft power used in international relations, economic governance recommendation is smart law.

Economic governance is also implemented through *sui generis* legal instruments which tend to contractualize the relationship between the EU and its Members. Each year, Member States submit a stability/convergence programme, a national reform programme and, for the eurozone countries, a draft budgetary plan. Those are commitments taken by the Member State vis-à-vis the EU on its fiscal, economic and employment policies. Moreover, a Member State must submit and receive approval from the Council on an economic partnership programme when it is subject to an excessive deficit procedure, a corrective action plan when it is subject to an excessive imbalance procedure, and a macroeconomic adjustment programme when it receives financial assistance. In the socio-economic coordination pillar, it is now envisaged that Member States may conclude with the EU a contract of structural reforms in exchange for financial incentives.[107] In this latter case, the contractualization model will not only be based on sanctions but also on incentives. Those contracts enable a better national ownership and allow for more detail in the recommended policy reforms, but their legal nature remains very unclear.

B. ENFORCEMENT MECHANISMS

The enforcement mechanisms used by economic governance present two main differences compared with the standard enforcement based on sanctions decided by courts. The first difference is that enforcement of economic governance rules is mainly based on voluntary actions by Member States and peer pressure and, only as a last resort, on sanctions. Unfortunately, the last decade shows that such an enforcement system is not very effective. This is why the recent reforms improve national ownership by requiring a minimum quality for national fiscal institutions, the establishment of

[107] Report of 5 December 2012 by J.M. Barroso, M. Draghi and J.-C. Juncker, Towards a Genuine Economic and Monetary Union; Communication from the Commission of 20 March 2013, The introduction of a Convergence and Competitiveness Instrument, COM(2013) 165.

a national correction mechanism (in parallel to the excessive deficit procedure) and the coordination of policies during the first semester of the year before the adoption of national decisions during the second semester. Recent reforms also increase the possibilities of sanctions which may be imposed earlier in the excessive deficit procedure, and also during the annual multilateral surveillance.

The second difference is that the sanctions are not decided by independent courts, but are proposed by the Commission and decided by the Council. There may be good reasons not to subject the fiscal policy to the adjudication of a court, but that leads to political bargaining as the German and French cases showed in 2003. Thus here again, the last decade shows that such enforcement is not very effective. This is why the recent reforms limit the possibilities of bargaining in order to achieve a degree of objectivity and independence expected from a court. Within the Commission, an extensive habilitation has been granted to the Commissioner for Economic and Monetary Affairs and the euro to limit pressure of the Member States on Commissioners.[108] Within the Council, most sanctions are now decided under reverse qualified majority which substantially increases the probability of adoption.[109] And the new national sanction mechanism foreseen by the TSCG is automatic and monitored by independent fiscal councils.

C. REGULATORY INNOVATION

When the EMU was established, its economic part was based on an original governance model because, on the one hand, the standard model of hard law decided by the Council and the European Parliament and controlled by the Court of Justice was not politically acceptable and, on the other hand, full sovereignty of the Member State was not any more economically sustainable given the cross-countries externalities created by the common currency. At the time, economic governance was thus based on two main pillars: multilateral surveillance of fiscal policies with peer pressure and sanction as a last resort, and coordination of economic policies based on the soft Open Method of Coordination. The last decade shows that this original regulatory model does not work: fiscal policies were, and still are, not sustainable in many Member States and convergence did not take place.

Given such failures, our political leaders could have decided not to be innovative and follow what happens in most federal states by integrating their economic policies. Instead, they continue to rely on the original model decided on in Maastricht and try to fix it by deepening and enlarging its pillars. That led to governance now based on four pillars: multilateral surveillance of fiscal policies with more possibilities of more

108 See Commission Press Release of 27 October 2011, IP/11/1284.

109 W. Van Aken and L. Artige, 'Reverse Majority Voting in Comparative Perspective: Implications for Fiscal Governance in the EU', in B. de Witte, A. Héritier and A. Trechsel (eds.), *The Euro Crisis and the State of the European Democracy* (European University Institute, Florence 2013), p. 129.

automatic sanctions, a new multilateral surveillance of macroeconomic imbalances, a coordination of economic policies which continues to be based on the soft Open Method of Coordination and financial assistance under conditions. Those pillars are implemented with recommendations (whose legal effects are situated below those of the hard law but above those of the soft law), contractual arrangements between the EU and its members, and sanctions decided in practice by the Commission.

The future will tell whether this enhanced governance will be solid enough to ensure the sustainability of national public finances and economic convergence between Member States, and ultimately the sustainability of the euro area. I have my doubts because the current reforms do not address the fundamental weakness of the EMU which is that a common currency union needs a budget and fiscal power at the level of that union.[110] But I also have concerns because the current governance suffers important legitimacy gaps[111] which may lead to a rejection of the new rules. More crucially, those gaps can stop EMU integration, although that is probably the only way forward to keep the common currency in the long run and, more generally, to keep the EU construction alive.

ANNEX: LIST OF LEGAL SOURCES THAT ESTABLISHED THE EU ECONOMIC GOVERNANCE[112]

FIRST PILLAR: FISCAL SURVEILLANCE

Stability and Growth Pact

- Regulation 1466/97 of the Council of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies, [1997] OJ L 209/1, amended by Regulation 1055/2005 of the Council of 27 June 2005, [2005] OJ L 174/1 and by Regulation 1175/2011 of the European Parliament and of the Council of 16 November 2011, [2011] OJ L 306/12.
- Regulation 1467/97 of the Council of 7 July 1997 on speeding up and clarifying the implementation of the excessive deficit procedure, [1997] OJ L 209/6, amended by Regulation 1056/2005 of the Council of 27 June 2005, [2005] OJ L 174/5 and by Regulation 1177/2011 of the Council of 16 November 2011, [2011] OJ L 306/33.

110 For a standard analysis of the conditions for sustainable currency union, see P. de Grauwe, *Economics of Monetary Union* (9th ed., Oxford University Press, Oxford 2012).

111 I. Pernice et al., ‘A democratic solution to the crisis: Reform model for a democratically based economic and financial constitution for Europe’, *WHI-Paper* 01/2012; F. Scharpf, ‘Monetary Union, Fiscal Crisis and the Preemption of Democracy’, *Max Planck Institute for Study of Societies Discussion Paper* 11/11 (2011).

112 The legal sources in italics have been adopted outside the EU legal framework.

– Specifications of 3 September 2012 on the implementation of the Stability and Growth Pact and Guidelines on the format and content of Stability and Convergence Programmes.

Complement to Stability and Growth Pact applicable to the Member States whose currency is the euro

– Regulation 1173/2011 of the European Parliament and of the Council of 16 November 2011 on the effective enforcement of budgetary surveillance in the euro area, [2011] OJ L 306/1.
– Regulation 473/2013 of the European Parliament and of the Council of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area, [2013] OJ L 140/11.
– Specifications of 1 July 2013 on the implementation of the Two Pack and Guidelines on the format and content of draft budgetary plans, economic partnership programmes and debt issuance reports.

TSCG

– *Treaty of 2 March 2012 on the Stability, Coordination and Governance in the Economic and Monetary Union (TSCG), Title III.*
– Communication of the Commission of 20 June 2012, Common principles on national fiscal correction mechanisms, COM(2012) 342.

SECOND PILLAR: MACROECONOMIC SURVEILLANCE

– Regulation 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances, [2011] OJ L 306/25.
– Regulation 1174/2011 of the European Parliament and of the Council of 16 November 2011 on enforcement measures to correct excessive macroeconomic imbalances in the euro area, [2011] OJ L 306/8.

THIRD PILLAR: ECONOMIC COORDINATION

– Conclusions of the European Council of June 2010 with the Europe 2020 Strategy for Jobs and Growth.
– Council Recommendation 2010/410 of 13 July 2010 on broad guidelines for the economic policies of the Member States and of the Union, [2010] OJ L 291/28.

- Council Decision 2010/707 of 21 October 2010 on guidelines for the employment policies of the Member States, [2010] OJ L 308/46.
- *Treaty of 2 March 2012 on the Stability, Coordination and Governance in the Economic and Monetary Union (TSCG), Title IV.*

FOURTH PILLAR: FINANCIAL SOLIDARITY

- Council Regulation 332/2002 of 18 February 2002 establishing a facility providing medium-term financial assistance for Member States' balances of payments, [2002] OJ L 53/1, as amended by Council Regulation 1360/2008 of 2 December 2008, [2008] OJ L 352/11 and by Council Regulation 431/2009 of 18 May 2009, [2009] OJ L 128/1.
- Regulation 407/2010 of the Council of 11 May 2010 establishing a European financial stabilisation mechanism (EFSM), [2010] OJ L 118/1.
- Regulation 472/2013 of the European Parliament and of the Council of 21 May 2013 on the strengthening of economic and budgetary surveillance of Member States in the euro area experiencing or threatened with serious difficulties with respect to their financial stability, [2013] OJ L 140/1.
- *Decision of 10 May 2010 of the Representatives of the Governments of the Euro Area Member States Meeting within the Council of the European Union establishing the European Financial Stability Facility (EFSF), and European Financial Stability Facility Framework Agreement of 7 June 2010 between the participating Member States and the EFSF.*
- *Treaty of 2 February 2012 establishing the European Stability Mechanism (TESM).*

INSTITUTIONAL FRAMEWORK

National Institutions

- Regulation 479/2009 of the Council of 25 May 2009 on the application of the Protocol on the excessive deficit procedure annexed to the Treaty establishing the European Community, [2009] OJ L 145/1, amended by Regulation 679/2010 of the Council of 26 July 2010, [2010] OJ L 198/1.
- Directive 2011/85 of the Council of 8 November 2011 on requirements for budgetary frameworks of the Member States, [2011] OJ L 306/41.

European Institutions

- Protocol (No. 14) on the Euro Group.
- Council Decision 2012/245 of 26 April 2012 on a revision of the Statutes of the Economic and Financial Committee, [2012] OJ L 121/22.
- *Treaty of 2 March 2012 on the Stability, Coordination and Governance in the Economic and Monetary Union (TSCG), Title V.*