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Next steps towards a deep and genuine Economic and Monetary Union: Early co-ordination and contractual arrangements

Ex-ante coordination

What is ex-ante coordination?

Ex-ante coordination implies that plans for the most important economic policy reforms are assessed and discussed at EU level before final decisions are taken at the national level. In this process, the Commission and Council of Ministers can suggest changes to the plans.

Why is the Commission suggesting this?

Major economic reforms in one Member State can cause economic spillover effects on other Member States. Such spillover effects are all the more relevant in an Economic and Monetary Union, as the crisis has underlined. Major economic reforms can produce economic spillover effects on other Member States via trade and competitiveness and via financial markets.

Trade and competitiveness: Product, services and labour market reforms as well as certain tax reforms, might affect employment and growth in the Member State implementing the reforms, and might therefore impact demand for products and services from other Member States. Reforms might also impact positively or negatively on the reforming Member State's price and non-price competitiveness.

Financial markets: reforms that strengthen a Member State's adjustment capacity (labour, product or services market reforms), reforms that strengthen its long-term fiscal sustainability (e.g. reforms of pension and health systems) and reforms that improve its financial sector governance benefit the Member State implementing the reforms. They increase the Member State's ability to withstand external shocks and limit the risk of an increase in interest rates on government bonds. But the absence of such reforms, or weaknesses in their design and implementation, could risk an increase in interest rates, which may spread to other Member States, as shown during the crisis.

Are there any other reasons for ex-ante coordination?

Ex-ante coordination also gives Member States the possibility to learn from each other's economic policies. Benchmarking, mutual learning and the exchange of best practices across the Member States can be beneficial, as already demonstrated in the work of many Committees of the Council of Ministers.

Is this a completely new idea?

The concept of ex-ante coordination of plans for major economic policy reforms was introduced by the Treaty on Stability, Coordination and Governance (TSCG) in the Economic and Monetary Union. Article 11 of the Treaty includes a commitment to discuss ex-ante and, where appropriate, coordinate all plans for major economic policy reforms. According to the Treaty, it would be incorporated into the legal framework of the European Union within maximum five years from the date it actually enters into force. A commitment to discuss major reform plans with potential spillover effects was also underlined in the 2012 Country-Specific Recommendations for the euro area.

Which reforms would be covered by ex-ante coordination?

It would include important reforms in the areas of competitiveness, employment, market functioning, tax systems, financial stability and fiscal sustainability.

Which Member States would ex ante coordination apply to?

While there are potential spillovers between all EU Member States, such effects are magnified in the euro area because of the stronger interdependence between euro area countries. In this regard, the Commission is considering proposing a binding framework for the ex-ante coordination of major economic reform plans of the euro area countries. At the same time, ways should be found to involve other Member States. Member States in a macro-economic adjustment programme would be exempt from the reporting requirements and discussions in the context of ex-ante coordination, as they are already subject to strict reporting requirements and monitoring in the context of their programme, but they may be able to participate on a voluntary basis.

Should the ex-ante exercise focus on large countries, as they cause the biggest spillovers?

The crisis has underlined that economic spillovers can also be caused by smaller countries. All countries – no matter how large or small – should be able to learn from each other and encourage one another to carry out the necessary economic reforms in the interest of stimulating growth, competitiveness and job creation.

What would the ex-ante coordination process look like?

A Member State would provide information on a major economic reform plan in its National Reform Programme (on economic policies for the coming year) or at another time during the year. The Commission would assess the plan and deliver an opinion on it. The Commission's assessment would cover the extent to which the reform tackles the specific policy challenges and how it would improve competitiveness and adjustment capacity. The Commission's assessment would pay particular attention to the impact the reform would have on the functioning of the euro area and possible spillover effects on other Member States. These plans will then be discussed by the Council of Ministers and the Eurogroup. The Commission and the Council can suggest modifications to the national reform plan where they could be justified by the expected effects on other Member States and the functioning of the Economic and Monetary Union.

What if a Member State does not take on board the suggestions of the Commission or the Eurogroup/Council in the context of ex-ante coordination?

The Member State concerned remains fully responsible for the final decision on the reform. The Commission opinions and the outcomes of discussions in the Council of Ministers or the Eurogroup could be taken into account as part of the assessment in the European Semester. Country-Specific Recommendations could be addressed to the Member State in this context.

Will the ex-ante process not become a heavy burden on the Member States?

No. The process will only cover the most important plans for economic policy reforms; these will be limited in number. Where possible, existing reporting, such as through the National Reform Programme, should be used to provide the necessary information.

A Convergence and Competitiveness Instrument (CCI)

What is the purpose of the Convergence and Competitiveness Instrument?

By combining "contractual arrangements" with a solidarity mechanism for national structural reforms, the Convergence and Competitiveness Instrument (CCI) aims to help Member States facing difficulties undertake reforms that are necessary for growth and competitiveness and which contribute to the well-functioning of the Economic and Monetary Union. This would allow Member States under stress to complete the reforms sooner than they would be able to on their own, and contribute to the cost of addressing any potential negative impact of the reforms. This strengthens the social dimension of the Economic and Monetary Union.

Which reforms are covered by the instrument?

The structural reforms to be covered would relate to the Country-Specific Recommendations and should contribute to the well-functioning of EMU as a whole. These are reforms that, for instance, address competitiveness and improve the functioning of labour and product markets. Depending on the specific reforms proposed by the Member State in its contractual arrangement, funding could, for example, support the modernisation of vocational training systems, increase the effectiveness of active labour market policies or strengthen lifelong learning schemes.

Which Member States are covered by the instrument?

The Commission puts forward two options for determining which countries would be covered by the CCI. The first would be to cover all euro area Member States (except those under a macroeconomic adjustment programme). The second would also allow Member States that are not part of the euro area to participate in the CCI, in particular those Member States preparing to join the euro.

When would the instrument be triggered?

The Commission suggests three options: First, it could be voluntary; that is, a Member State could ask for the CCI to be triggered. Second, it could be triggered when a Member State enters the Macroeconomic Imbalances Procedure. Or third, it could be triggered when countries fall under the Excessive Imbalance Procedure. Here, the Corrective Action Plan that Member States draw up under this procedure could replace the contractual arrangement.

Why the increased focus on the euro area?

The interdependence of Member States participating in a single currency increases the importance of sound budgetary and economic policies. Given the high interdependence within the euro area, Member States have an interest in the ambitious and proactive implementation of structural reforms to remove key weaknesses in their economies. On the one hand, the implementation of structural reforms strengthens the economies of the Member States concerned and may have potentially significant spillover effects from one Member State to another. On the other hand, slow or no implementation of important structural reforms exacerbates problems of competitiveness and hampers the adjustment capacity of Member States. Also, convergence towards high levels of adjustment capacity and competitiveness would better protect countries against the impact of economic downturns and avoid the development of harmful macroeconomic imbalances.

How would the contractual arrangement be drawn up?

Each Member State concerned would present a plan for a set of concrete reforms that address their respective Country-Specific Recommendations. These are approved by the Council of Ministers in the context of the European Semester, with corresponding timelines, and should be included in a contractual arrangement. The Member States' plans would be assessed by the Commission, notably on the selection of the proposed measures and the extent to which they address the economic weaknesses which are taken up in the relevant Country-Specific Recommendations. This assessment would particularly focus on the expected impact of the measures and their effectiveness in addressing the specific policy challenge at hand, potential spillover effects on other Member States, as well as the feasibility of implementation, also in the light of the proposed timelines.

Assessing spillover effects does not imply that reforms in one country should not be undertaken because of lack of reforms in other countries. The assessment of the expected impact of the measures would include, where relevant, the impact on the sustainability of public finances and their social impact. On the basis of its assessment, the Commission would embark on negotiations with the Member State concerned and subsequently formulate a proposal to the Council for approving the contractual arrangement. The Council would discuss and endorse the Commission proposal (possibly with amendments), approving the specific actions covered and the agreed deadlines for taking them. Should the Member State and the Commission fail to reach an agreement, or should the Council of Ministers disagree with the arrangement, there would be no contractual arrangement and, subsequently, no financial support.

Who benefits from the financial incentives?

Only those Member States that contribute to the instrument and sign a contract for reform should be able to benefit from it. The financial incentive would support the implementation of the reforms which are covered in the contractual arrangement.

What if a Member State does not respect its contractual arrangement?

Financial support would be conditional on the full and timely implementation of the reforms set out in the arrangement. If, through annual reporting, the Commission considers that a Member State has not fully complied with the arrangement, it can issue a warning, following which financial support could be suspended or, where necessary, recovered. The same would apply if the Commission finds that a Member State has gone back on previously implemented reforms or decides to implement further measures that go against the objectives of the agreed reforms.

How much money are we talking about?

The Commission is of the view that the financing of the instrument could remain limited initially, but could increase over the medium term, provided that it can prove to be effective in promoting the implementation of key structural reforms.

Where will the money come from?

The Commission proposes a new financial instrument as part of the EU budget. Contributions should be included in the EU budget as external assigned revenues. Being financed through assigned revenues, the instrument would not be placed under the ceilings set in the seven- year EU budget (the Multiannual Financial Framework).

In setting up the system for financing the financial solidarity pillar, one possibility is for an instrument to be financed by commitments from each Member State, and could be linked to Gross National Income (GNI). Alternatively, new and specific financing resources could be set up for this instrument.

Are these concrete legislative proposals from the Commission?

No. These are communications with ideas and options from the Commission to feed into the ongoing debate on a deep and genuine Economic and Monetary Union. The Commission is now inviting input from Member States, national and European parliaments and stakeholders. On that basis, it is the Commission's intention to come up with proposals in the course of 2013.

For more information:

IP/13/248

Commission sets out next steps towards a deep and genuine Economic and Monetary Union

Communications on the ex-ante coordination of plans for major economic policy reforms and on the introduction of a Convergence and Competitiveness Instrument

Blueprint for a Deep and Genuine Economic and Monetary Union