

## Working group VI « Economic governance »

### Paper from the Commission

#### **Subject : Current set up for Economic policy coordination**

The following explains the main rules and instruments of the current set up for economic policy co-ordination. Beyond those, there are several other instruments for co-ordination in specific policy areas. Depending on the instruments and the policy areas co-ordination take different forms, from strict rules to be respected to benchmarking and exchange of practices.

At the end of the note, section 3 present briefly economic policy co-ordination improvements under way within the current Treaty framework and section 4 presents the ideas put forward by the Commission in its Communication to the Convention.

#### **1. Policy responsibilities**

The principle in EMU is a single monetary policy under the responsibility of one single authority and national economic policies but with some common rules and co-ordinated (Article 99)

**Monetary Policy:** is the responsibility of the European Central Bank (Article 105). *“The primary objective of the ESCB shall be to maintain price stability. Without prejudice to the objective of price stability, the ESCB shall support the general economic policies in the Community with a view to contributing to the achievement of the objectives of the Community as laid down in Article 2”.*

The President of the Council and a member of the Commission may participate in meetings of the Governing Council of the ECB. The President of the ECB shall be invited to participate in Council meetings when discussing matters related to the objectives and tasks of the ECB. The ECB shall present an annual report to the European Parliament, the Council and the Commission. The President of the ECB and members of the Executive Board may, at the request of the European Parliament or on their own initiative, be heard by the competent committees of the Parliament.

**Exchange rate policy:** Shared responsibility of Council, ECB, Commission (Article 111).

**Economic policies:** responsibility of Member States but Article 98: *“Member States shall conduct their economic policies with a view to contributing to the achievement of the objectives of the Community as defined in Article 2, and in the context of the broad guidelines referred to in Article 99(2)....”* and Article 99: *“Member States shall regard their economic policies as a matter of common concern and shall co-ordinate them within the Council....”*. The main instruments for the co-ordination of economic policies are: Broad Economic Policy Guidelines (BEPG), Stability and Growth Pact, Employment Guidelines, Cardiff process and Cologne process. Beyond these main instruments, other ways of policy co-ordination (open method of co-ordination, benchmarking, scoreboards) have been developed in specific policy areas.

## **2. Main instruments for economic policy co-ordination**

**Broad Economic Policy Guidelines (BEPG)** (Article 99). Are the central and overarching instrument for the co-ordination of the economic policies of the Member States and of the Community. They are usually presented by the Commission in April and adopted by the Council in June. In terms of substance, one can refer to 2002 BEPGs as illustration. This year's guidelines were presented around 8 policies: ensure growth and stability-oriented macroeconomic policies, improve the quality and sustainability of public finances, invigorate labour markets, re-ignite structural reform in product markets, promote the efficiency and integration of the EU financial services market, encourage entrepreneurship, foster the knowledge-based economy and enhance environmental sustainability. The BEPGs put forward an integrated view and define the main objectives and orientations for economic policy, both for the EU and for each Member State. The Council decides by qualified majority on the basis of a Commission recommendation and following European Council conclusions.

The European Parliament is not formally involved (the Council informs the Parliament of its decision). However, the Commission has several discussions with the Parliament in the process of elaboration of the BEPGs. The Parliament produces a report at its own initiative.

In case economic policies of a Member State are not consistent with the BEPGs or risk jeopardising the proper functioning of EMU, the Council may, by qualified majority on the basis of a Commission recommendation, make the necessary recommendations to the Member State concerned. This is what happened for Ireland in 2001.

**Stability and Growth Pact (SGP)**, based on Articles 104 and 99 and subsequent European Council Resolution (13.12.97) and Council Regulation 1466/97. SGP is a key instrument for the co-ordination and surveillance of budgetary policies. It defines a medium term objective of close to balance or in surplus. Member States present every year (between mid-October and 1<sup>st</sup> of December) stability (or convergence for the non euro area members) programmes with the budgetary policy strategy for the coming years and with respect to the long term sustainability of public finances.

The Council, on the basis of a Commission recommendation, gives an opinion on the programmes. This opinion assesses whether the programme is appropriate to reach the objective of the SGP, whether it favours economic policy co-ordination and whether economic policies contained in the programme are consistent with the BEPGs.

In case the budgetary situation of a Member State deviates significantly from the budget target or from the trend leading to reaching or maintaining a close to balance or in surplus budget balance, the Council may, by qualified majority on the basis of a Commission recommendation, make the necessary recommendations to the Member State concerned (known as “early warning”). This is what the Commission recommended to the Council this year for Portugal and Germany. The Council did not address recommendations to these two countries since they took firm commitments in order to stick to the targets.

In case of deficits going over 3% of GDP, the excessive deficit procedure comes into play. Council decides by qualified majority on the basis of a Commission recommendation. The aim is to help the Member State concerned to take the necessary corrective measures. In case the Member State would not take corrective measures the pressure would increase up to the application of sanctions.

**Employment Guidelines (EG)**, also known as “Luxembourg process”. Based on Article 128. Are the instrument to develop a co-ordinated strategy for employment and particularly for promoting a skilled, trained and adaptable workforce and labour markets responsive to economic change with a view to achieving objectives as defined in Article 2. According to Article 128, the Employment guidelines shall be consistent with the Broad Economic Policy Guidelines.

The Council adopts EG every year, by qualified majority, based on a Commission proposal), following European Council conclusions, and after consulting the European Parliament, the Economic and Social Committee, the Committee of Regions and the Employment Committee.

**Cardiff process.** Based on European Council conclusions (Cardiff, June 1998). Aims at improving the functioning of product and capital markets through an open method of policy co-ordination. Based on Member States reporting and Commission assessment, the Council reaches conclusions. This is an important input for BEPGs content on product and capital markets as well as for the target actions of the Internal Market Strategy.

**Macroeconomic dialogue (or Cologne process).** Based on the European Council Resolution on the European employment pact, June 1999. The aim is to establish a regular dialogue (twice a year, before adoption of the BEPGs and after Autumn forecast) between the relevant policy actors for fiscal policy, monetary policy and wage developments in order to bring about strong growth in employment while maintaining price stability. It takes place in the framework of the Ecofin Council, with participation of Ecofin and Labour and Social Affairs Ministers, the Commission, the European Central Bank and the social partners. The macroeconomic dialogue is a confidence-building and confidential exchange of ideas.

**Spring European Council on economic and social questions.** The first one took place in Lisbon in March 2000. This annual Spring European Council takes a guiding and co-ordinating role to ensure overall coherence with and monitoring of progress towards the EU strategic goal as defined in Lisbon (*“to become 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”*) and complemented in Stockholm and Göteborg Councils (2001) adding the environmental and sustainable development dimension.

The Commission presents a Synthesis Report, as a basis for the Spring European Council discussion.

### **3. Improvements within the current Treaty framework**

The Lisbon European Council clearly stated that no new policy co-ordination processes were needed, beyond the ones presented above in this note, provided they are simplified and better co-ordinated. To this aim, the Commission is working on streamlining and better synchronisation of these processes.

A number of improvements have been or are being made to strengthening economic policy co-ordination, which do not require changes in the legal acts. They concern: better euro-area statistics,

systematic analysis of the Euro area's policy mix, increase focus on implementation, systematic examination of sustainability and quality of public finances.

Furthermore, the Commission intends to propose common standards for the conduct of economic policies, as stated in the Barcelona European Council conclusions. The objective would be to clarify the respective roles of economic policies in preserving macroeconomic stability, raising the growth potential and coping with shocks affecting either the area as a whole or individual Member States. Recognising the need to strengthen economic policy co-ordination in the euro area, the so-called Eurogroup was established by the Luxembourg European Council (December 1997). It was set up as an informal body to allow euro area participating Member States to discuss issues of common euro-area interest. Participants are Ministers of the euro area members, Commission and the ECB. The Eurogroup has well served its purpose, but its functioning needs to be reviewed in the light of increased need for policy co-ordination in the euro area.

#### **4. Commission proposals for the Convention**

The Commission adopted on 22 May a Communication entitled "A project for the European Union", as a first contribution of the Commission to the Convention. This Communication contains a section on "reinforcing the co-ordination of economic policies" with the following proposals:

- instruments with Council involvement should be based on a Commission proposal instead of on a Commission recommendation as at present. This applies to the BEPGs and the Stability and Convergence programmes opinions and related recommendations to a Member State. At present, the Council adopts Commission recommendations by qualified majority irrespective to whether the Commission approves or not the changes made to its recommendation. In the case of a Commission proposal rather than a recommendation, the Council would continue to decide by qualified majority, but if the Commission does not agree with a change to its proposal envisaged by the Council, the latter would need to decide by unanimity on this. That would better enable the Commission to guard the consistency of the policy guidance.
- the Commission should be able to address first early-warnings directly to the Member State concerned, to better ensure objective judgement and increase the efficiency of the co-ordination.
- the institutional set up for the euro area should be reviewed to allow Community institutions to play fully their role. The role of the Eurogroup as informal body for the euro area members to discuss issues of common interest is clearly recognised. However, it would be useful to also have a formal instance for euro area decisions ("Ecofin-euro area") to allow strengthen co-ordination for the euro area to take place within the normal Community framework.

- the implication of the Parliaments should be increased. At the EU level, the European Parliament should be better involved; the nature of the European Parliament involvement should be defined according to the instrument and taking into account that economic policy co-ordination is not a legislative process. At the Member States level, national parliaments should be better involved, by their respective governments, in the discussion of the main co-ordination instruments. Between the European Parliament and national parliaments, co-operation should be intensified.
- external representation of the euro area. The euro area should have a unified representation in the economic and financial international bodies. The EU would gain in having a strong and stable voice. The euro area should eventually be represented by the Commission, in close conjunction with all bodies concerned.

**Forms of economic policy co-ordination in EMU**

	<b>POLICIES</b>	<b>FORM OF CO- ORDINATION</b>	<b>MODE OF CO- ORDINATION</b>	<b>ACTORS INVOLVED</b>	<b>PROCEDUR ES</b>
<b>SINGLE POLICY</b>	<b>Monetary policy</b>	Single policy (euro area)	Single institution	ECB	
	<b>Exchange rate</b>	Single policy (euro area)	Co-ordination in the Council	Council ECB Eurogroup Commission	
	<b>Competition policy</b>	Single policy	Implementation by the Commission	Member States Commission Council	
<b>CLOSE CO- ORDINATI ON</b>	<b>Budgetary policy (balances)</b>	<ul style="list-style-type: none"> <li>- Treaty rules</li> <li>- Commonly agreed rules and objectives</li> <li>- Information exchange</li> <li>- Peer review</li> </ul>	Co-ordination in the Council  Joint fora	Member States Commission Council Eurogroup	Excessive Deficit Procedure Stability and Growth Pact Broad Economic Policy Guidelines
	<b>Structural policies (Internal Market)</b>	<ul style="list-style-type: none"> <li>- Rules</li> <li>- Joint decisions</li> <li>- Council directives</li> <li>- Peer review</li> </ul>	Co-ordination in the Council	Member States Council Commission	
<b>LOSE CO- ORDINATI ON</b>	<b>Policy-mix</b>	<ul style="list-style-type: none"> <li>- Dialogue</li> <li>- Information exchange</li> </ul>	Joint fora	ECB Commission Council Eurogroup Social partners	

<b>Budgetary policy (quality of public finances)</b>	- Commonly agreed objectives	Co-ordination in the Council	Member States Commission Council Eurogroup	Broad Economic Policy Guidelines Stability and Growth Pact
<b>Wage developments</b>	- Dialogue - Information exchange	Joint fora	Social partners Commission Council ECB	Macroeconom ic Dialogue (Cologne process) Broad Economic Policy Guidelines
<b>Labour market policies (structural reforms)</b>	- Information exchange - Discussion of best practices - Guidelines - Peer review	Co-ordination in the Council	Member States Commission Council Social partners	Employment Guidelines (Luxembourg process) Broad Economic Policy Guidelines
<b>Product and capital market policies (structural reforms)</b>	- Information exchange - Discussion of best practices - Guidelines - Peer review	Co-ordination in the Council	Member States Commission Council	Reports on economic reform --product and capital markets-- (Cardiff process) Broad Economic Policy Guidelines
<b>External representation and communication</b>	- Agreement on a common understanding (communication only)	Joint fora	ECB Eurogroup Commission	

**Economic policy co-ordination (including dialogue with the ECB)**

