BRIEFING
EU Legislation in Progress

European Parliament

New economic governance rules

OVERVIEW

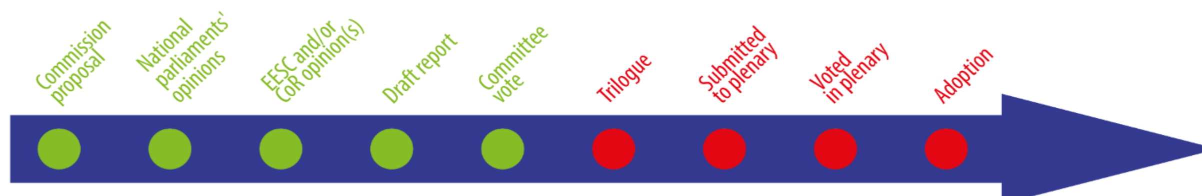
On 26 April 2023, the European Commission published a package of three proposals to revise the EU's economic governance framework: a regulation to replace the current preventive arm of the stability and growth pact (SGP), an amending Council regulation on the corrective arm of the SGP, and an amending Council directive to strengthen the role of independent fiscal institutions. The main proposal on the preventive arm is to be adopted through the ordinary legislative procedure with the European Parliament and the Council as co-legislators.

The reform proposals would see the Commission bilaterally negotiating a fiscal-structural plan with Member States, with a minimum 4-year horizon; possible extension of the fiscal adjustment path to seven years would provide an incentive to include investment and reform commitments. Greater political buy-in and better Member State ownership of the medium-term plan is also envisaged. Both reference values – the 3 % deficit-to-GDP and 60 % debt-to-GDP ratios – would remain unchanged, the proposal introduces three additional safeguards: two numerical requirements over the agreed plan's horizon and a minimum fiscal adjustment of 0.5 % of GDP per annum if a country is expected to be above the 3 % deficit ratio threshold in an excessive deficit procedure.

Both the European Parliament and the Council have adopted their mandates on the preventive arm of the SGP, paving the way to interinstitutional negotiations, which started in January 2024. These might revolve around three main topics: safeguards, the role of independent fiscal institutions, and transitory provisions.

(A) Proposal for a regulation on the effective coordination of economic policies and multilateral budgetary surveillance and repealing Council Regulation (EC) No 1466/97; (B) Proposal for a Council regulation amending Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure; (C) Proposal for a Council directive amending Directive 2011/85/EU on requirements for budgetary frameworks of the Member States

Committee responsible:	Economic and Monetary Affairs (ECON)	(A) COM(2023) 240; (B) COM(2023) 241; (C) COM(2023) 242; 26.4.2023 2023/0138(COD); 2023/0137(CNS); 2023/0136(NLE)
Rapporteurs:	Esther de Lange (EPP, Netherlands); Margarida Marques (S&D, Portugal)	
Shadow rapporteurs:	Billy Kelleher (Renew, Ireland), Philippe Lamberts (Greens/EFA, Belgium), Antonio Maria Rinaldi (ID, Italy), Johan Van Overtveldt (ECR, Belgium) José Gusmão (The Left, Portugal)	
Next steps expected:	Conclusion of trilogue negotiations	



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Introduction

On 26 April 2023, the European Commission put forward three legislative proposals to reorganise the EU's economic governance framework. Besides regulations to replace and amend the current preventive arm as well as to amend the corrective arm of the stability and growth pact (SGP) respectively, the Commission proposes also to amend a directive to strengthening the role of independent fiscal institutions (IFIs). Thus, the new economic governance rules consists of three interconnected proposals:

- a proposal to replace the regulation on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies (1466/977/EC). This regulation establishes the European Semester and the preventive arm of the SGP). The legal basis for the new proposal replacing the current preventive arm of the SGP is Article 121(6) of the Treaty on the Functioning of the European Union (TFEU), which allows the adoption of detailed rules for the multilateral surveillance procedure by means of the ordinary legislative procedure;[1]
- a proposal for a Council regulation, amending the regulation on speeding up and clarifying the implementation of the excessive deficit (1467/97/EC). This regulation establishes the corrective arm of the SGP;
- a proposal for a Council directive, amending the Directive on Requirements for Budgetary Frameworks of the Member States (2011/85/EU). This directive lays down detailed budgetary rules for Member States to ensure compliance with fiscal rules.

The legal basis for the two amending proposals for the corrective arm and the directive on budgetary rules for Member States is Article 126(14) TFEU, which sets out provisions relating to the implementation of the excessive deficit procedure annexed to the Treaties. The Council adopts such provisions for detailed rules and definitions on the basis of a Commission proposal and after consulting the European Parliament.

Context

With the Treaty of Maastricht of 1992, the EU established the architecture of the economic and monetary union (EMU) and paved the way for the introduction of the euro to pursue its shared economic objectives. The EU's economic governance framework, built and developed over the past 20 years, was established in three stages: (i) the Treaty on European Union (TEU – Maastricht Treaty), (ii) the 1997 stability and growth pact, and in reaction to the euro crisis, (iii) the 2013 Intergovernmental Treaty on Stability, Coordination and Governance in the economic and monetary union (TSCG), also known as the fiscal compact, complemented the economic governance framework. The EU coordinates economic policies through this system of institutions and procedures, to achieve EU objectives in the economic field. The framework comprises an elaborate system of policy coordination and surveillance of Member States' economic policies. It relies on the principles of monitoring, prevention and the correction of imbalances that could pose risks for Member States' economies.

In October 2021, the European Commission relaunched the public debate on the review of the EU's economic governance framework with a communication and a public consultation, feeding into a publication of a communication on orientations for a reform of the EU economic governance framework in November 2022.

Existing situation

In setting out the general principles of the EU's purpose, the TEU, the basis of EU law, was the first step towards EMU, introducing a set of convergence criteria to enable Member States to work towards an EMU. Protocol No 12 TEU specifies that a Member State's public finance deficit should

not exceed 3 %, and its debt level not exceed 60 % of its gross domestic product (GDP). These rules are commonly known as the 'Maastricht criteria' (for public finances). To avoid excessive public spending, the Maastricht Treaty sets out the procedure to identify and correct situations of excessive deficit – the excessive deficit procedure (EDP) – which focuses on special ongoing disciplinary scrutiny of countries' budgetary decisions.

In 1997, the Commission proposed the nascent SGP, designed to ensure sustainable public finances. In addition to the main corrective element – the EDP – the SGP added a preventive element to the fiscal framework, for Member States not subject to the EDP. Key to this preventive arm are the country-specific medium-term objectives (MTO), i.e. a structurally balanced budget or, in other words, the general government budget position, net of one-off and other temporary measures. Subsequently, the SGP has been reformed in three steps. First, the intention in 2005 was to make the indicator less rigid and sensitive to the cyclical position of an economy over the business cycle. In 2011, a second reform package was introduced, the 'six-pack' reform, including legislation correcting macroeconomic imbalances (macroeconomic imbalance procedure – MIP), such as a large current account deficit or a real estate bubble. Two years later, two more regulations (the 'two-pack') were adopted, applying to euro-area countries. These reforms placed greater emphasis on debt and expenditure control.[2] As part of the SGP's preventive arm, the European Semester allowed the Commission to closely monitor and coordinate national fiscal, economic and employment policies to avoid significant policy errors that could harm the EU economy. Lastly, the third reform in 2015 reinterpreted how the Commission would consider public investments, structural reforms and cyclical conditions when assessing Member States' fiscal positions.

Despite these reforms, national compliance with the EU fiscal framework has been uneven. The European Fiscal Board, an independent advisory body within the European Commission, found that numerical compliance with the fiscal rules stood at 54 %.[3] In an assessment of the EU fiscal rules, the Board concluded that while the above reforms provided more flexibility, they also made the rules more complex, opaque and less predictable, thus undermining Member States' compliance with the rules.[4] In response, the European Commission launched a review of the economic governance framework in February 2020, and updated it in October 2021 after the significant upheaval of COVID-19. During the pandemic, from March 2020, the European Commission and the Council activated the general escape clause, allowing Member States to undertake budgetary measures in exceptional circumstances. The clause has been extended to 2023, in light of the conflict in Ukraine, and is set to be de-activated as of 2024. With the European elections set for June 2024, time is tight to find a compromise based on the Commission proposal and adopt a new legislative backbone for the EU fiscal rules.

Preparation of the proposal

The proposals were drafted against the backdrop of a comprehensive debate and reflection upon the EU's fiscal rules. Various EU institutions, academia and think tanks have contributed to the discussion, outlining their ideas for a better governance framework,[5] while in-depth discussions took place at several levels within the Council (ECOFIN), such as the Eurogroup, the Economic and Financial Committee and the Economic Policy Committee. In parallel, the Commission launched an online consultation, responses to which ultimately fed into a communication on orientations for a reform of the EU economic governance framework, adopted by the European Commission in November 2022.[6] This orientation laid the groundwork for the underlying proposals on reforming the EU fiscal framework.

The changes the proposal would bring

The kernel of the proposed framework follows the aforementioned orientations outlined in November 2022. Debt sustainability would be ensured through stricter fiscal monitoring by the Commission, based on a country-specific fiscal adjustment path anchored to a debt sustainability analysis (DSA) framework – an analytical tool to assess fiscal risks and project macroeconomic

variables under different assumptions.[7] The Commission would negotiate bilaterally with Member States on a medium-term fiscal-structural plan, resembling the practice used under the Recovery and Resilience Facility (RRF), with a minimum four-year horizon. An incentive to include investment and reform commitments is given through a possible extension of the fiscal adjustment path to seven years. According to the Commission, the individual design of fiscal structural plans will provide greater Member State ownership of the plan. Additionally, a higher degree of political buy-in is envisaged through an expansion of the role of IFIs, national official bodies with mandates to oversee different aspects of fiscal policy. Importantly, both reference values – of a 3 % deficit ratio (government deficit to gross domestic product, GDP) and a 60 % debt ratio (government debt to GDP) – would remain unchanged.

In addition to the orientations, the proposal introduces three additional safeguards not presented by the Commission: two numerical requirements over the agreed plan's horizon and a minimum fiscal adjustment of 0.5 % of GDP per annum if a country is expected to be above the 3 % deficit ratio threshold in an excessive deficit procedure (EDP).

1. The centrepieces are the **national medium-term fiscal-structural plans** that would give Member States more leeway to set their country-specific fiscal trajectories, thus seeking to improve public finances over the medium term while protecting public investment. The basis for setting up the multi-year net expenditure path is a single operational indicator, namely nationally financed **net expenditure**,[8] defined as public expenditure net of discretionary revenue measures and excluding interest as well as cyclical unemployment expenditure (allowing automatic stabilisers to work).
2. The Commission would issue a **technical trajectory**, a benchmark fiscal adjustment path that ensures a plausible reduction of debt, for Member States with a deficit ratio exceeding the 3 % threshold or a debt ratio exceeding 60 %, with the aim of ensuring that: (i) the debt ratio follows a plausibly downward path, (ii) the deficit ratio remains or returns below the 3 % threshold, and (iii) expenditure growth remains below medium-term GDP growth. Furthermore, within the plan's timeframe, the Member States would have to ensure: (iv) that the debt ratio at the end of the plan is lower than at the beginning and (v) the fiscal effort is not back-loaded.

   For Member States with a deficit ratio below 3 % and a debt ratio below 60 %, the Commission would provide **technical information** to enable the deficit ratio to remain below 3 % in the medium term.
3. The **fiscal adjustment period** set out in the fiscal-structural plans covers at least four years. It can be extended, against reform and investment commitments that fulfil specific criteria (e.g. EU priorities or country-specific recommendations), to a maximum of seven years.
4. Member States would present **annual progress reports**, while national IFIs would be given a more prominent role in ex-ante assessment and ex-post surveillance of national fiscal-structural plans.
5. Two clauses would allow a Member State to deviate from its net expenditure path in **exceptional circumstances**, a severe economic downturn clause and an individual country-specific clause, codifying the process of the general escape clause in the current SGP.
6. The European Parliament's involvement in the fiscal framework would be limited to an economic dialogue to discuss the policy guidance to Member States and scrutinising the results of the surveillance process.

Replacing the preventive arm of the SGP

To reorganise the current fiscal governance framework, the Commission proposes to establish a new document: **medium-term fiscal-structural plans**. These plans are the cornerstone of this proposal

and would encompass country-specific fiscal trajectories, Member States' structural reform and investment commitments and would serve as basis for the Commission's monitoring. The underlying indicator for setting up the fiscal trajectories is a single operational indicator: **net primary expenditures**, or in other words, all public expenditure elements under direct government control, thus net of discretionary revenue measures and excluding interest, as well as cyclical unemployment expenditure (allowing automatic stabilisers to work). Plans would be for a minimum of **four years**, with the option for an extension to **seven years** against reform and investment commitments.

Before a Member State submits its fiscal-structural plans, a non-public technical dialogue between a Member State and the Commission would ensure that the plan fulfils certain criteria, in particular containing a net-expenditure trajectory covering at least four years and possible Member State action to address country specific recommendations (Annex II). The Commission would provide guidance by putting forward a **technical trajectory** for Member States with a deficit ratio exceeding the 3 % threshold or a debt ratio exceeding 60 %, based on the following characteristics: (Annex I):[9]

i. The debt ratio follows a plausibly downward path; this plausibility is assessed on the basis of two conditions: (a) if the debt ratio is declining in a deterministic projection[10] and (b) if there is a sufficiently high (low) probability that the debt ratio will not decline (increase) according to a stochastic analysis – a tool to account for uncertain macroeconomic conditions in the analysis of public debt dynamics;

ii. The deficit ratio remains or returns below the 3 % threshold under unchanged policies over a period of 10 years after the adjustment period;

iii. The fiscal effort is not back-loaded, meaning that the adjustment effort is not postponed to the final years of the adjustment period;

iv. The growth of net primary expenditure remains below medium-term GDP growth; and

v. The debt ratio at the end of the plan's horizon is lower than at the beginning.

For Member States with a deficit ratio below 3 % and a debt ratio below 60 %, the Commission would provide **technical information** to enable the deficit ratio to remain below 3 % in the medium term.

Once a Member State submits a medium-term fiscal-structural plan as part of the European Semester cycle, the **European Commission would assess** the plan according to criteria defined in Annex II, including for instance the proposed fiscal adjustment path. The adjustment period may be **extended** by a maximum of three years. For such extension, **reform and investment commitments** would need to follow certain criteria, such as supporting growth and fiscal sustainability, addressing country-specific recommendations, as well as that public investment is increasing. In particular, the set of reform and investment commitments needs to significantly contribute (Annex VII) to at least one of the common EU priorities (Annex VI), which could provide an incentive for closer macroeconomic policy coordination through the fiscal framework. As a subsequent step, the Council would adopt the plan or recommend that the Member State resubmit a modified plan. Member States themselves would be able to request to resubmit fiscal-structural plans, by a new government for instance.

Annual progress reports would be submitted by Member States, as part of the European Semester cycle, for the Commission to monitor progress in the implementation of the fiscal structural plans (Annex III).[11] A **control account** (Annex IV) for each Member State would record actual net expenditure over the plan's horizon, to allow a comparison of the cumulative balance against the committed adjustment path.

Two clauses would allow a Member State to deviate from its net expenditure path in **exceptional circumstances** for a specified, limited period. A severe economic downturn clause would apply to either the euro area or the EU as a whole. While a country-specific clause would allow an individual

Member State to deviate from the net expenditure path outlined in the fiscal-structural plan in exceptional circumstances outside the control of the Member State.

Lastly, it is worth noting that the Commission's proposals do not consider a role for the European Parliament in the multilateral monitoring process, although the Commission should keep Parliament informed. At the same time, the Commission proposes to use delegated acts for several elements included in Annexes II to VII, which would allow the Commission to adapt the criteria over time, while affording the European Parliament a veto right for potential changes.[12]

Amending the corrective arm of the SGP

The corrective arm of the SGP, meant to deter and correct excessive government deficits, relates to the numerical reference values, the 3 % deficit ratio and the 60 % debt ratio, both of which would remain unchanged. However, a transgression of those reference values would not immediately trigger the corrective arm, i.e. lead to an EDP. The 'deficit-based EDP' would remain unchanged. For Member States breaching the 60 % debt ratio, compliance with its net expenditure path committed in the fiscal-structural plan is sufficient to avoid an EDP. However, for Member States that face substantial public debt challenges, established according to the Debt Sustainability Monitor, and deviate from the net expenditure path, a debt-based EDP would be opened by default. Once a Member State is in an EDP and exceeds the 3 % deficit ratio threshold, a **corrective net expenditure path** is implemented. For the years when the deficit ratio exceeds the 3 % threshold, the net expenditure path set by the national fiscal-structural plan would be adjusted by 0.5 % of GDP.

Until effective action is taken, Member States in an EDP would face fines up to 0.05 % of GDP to be paid every six months, up to cumulative fines of 0.5 % of GDP. Thus, the upper limit would be lowered and the imposed sanctions more granular.

Amending the budgetary rules for Member States

The amending directive would strengthen the role of the IFIs, which are national institutions monitoring the implementation of national fiscal frameworks. This would include preparing or endorsing budgetary forecasts, assessing sustainability analyses and the impact of policies, and ex-post evaluation of forecasts and fiscal plans. Furthermore, provisions in the directive seek to ensure operational independence, necessary resources and access to relevant information.[13] A central element of the directive focuses on improving the quality and harmonisation of public sector accounting and, in particular, including assessments of risks deriving from climate change and the impact of climate policies on public finances.

ECB and advisory committees

The European Central Bank was requested to provide a mandatory opinion on the three legislative proposals. On 5 July 2023, the ECB transmitted its opinion, adopted by the Governing Council. Several of the ECB's recommendations aim at providing more detailed information on core parts of the proposals. In particular, on specifying information covered in the proposal's annexes:

- the medium-term fiscal-structural plan (e.g. higher level of detail on the requirements for the reforms and investment commitments);
- the control account (e.g. detailed specification of the functioning and key parameters of the control account, and introducing a threshold for deviations of actual net expenditures from the net expenditure path, which would trigger a requirement for the Commission to prepare a report to launch an excessive deficit procedure);
- the methodology for the assessment of plausibility (further elaboration on key parameters and assumptions underlying the methodology); and

- the assessment framework for reform and investment commitments (e.g. further safeguards to ensure an increase in investment for critical policy priorities such as the green and digital transitions).

In addition, the ECB recommends specifying parts of the 'net expenditure' definition, for instance whether the net expenditure path would be in nominal or real terms, how to calculate discretionary revenue measures and cyclical elements of unemployment benefit expenditure.

The European Economic and Social Committee (EESC) was consulted on the proposal and, in August 2023, issued an opinion, focusing in particular on public investment. The EESC calls for public investment to be treated separately when deciding whether any excessive deficit procedure should be opened. The EESC also suggests amendments to some safeguards, taking into account that public investment as a share of GDP should remain higher during the adjustment period compared to the start of the fiscal-structural plan. In cases where a Member State is subject to the deficit adjustment benchmark of 0.5 % of GDP, it should be allowed to exclude growth- or resilience-enhancing public investments from its deficit.

National parliaments

Three national parliaments submitted reasoned opinions. In a resolution, the Czech Senate recommends involving the Czech Parliament in preparing the medium-term fiscal-structural plan to a similar extent as it is currently involved in the reform and convergence programmes. The Irish Houses of Oireachtas provided a 'political contribution', including several recommendations on a transparent calculation of debt sustainability, supporting the concept of a fiscal 'golden rule' and an enhanced role for IFIs. The German Bundestag adopted an opinion, amending the Directive on Requirements for Budgetary Frameworks of the Member States. In particular, the Bundestag highlights concerns regarding the European Public Sector Accounting Standards (EPSAS), and raises doubts over the sense and purpose of those standards. The Federal Council points out that regulation of public accounting must take into account the principle of budget autonomy and thus the principles of proportionality and subsidiarity must be observed. The Dutch Senate placed a parliamentary scrutiny reservation on the proposal through a letter to the Minister of Finance.

Stakeholder views[14]

While positive assessments have been made regarding the medium-term fiscal adjustment paths, grounded on a comprehensive analysis of debt sustainability risks and the simpler operational target of net primary expenditure, in the debate leading up to the proposal, concerns were raised regarding the European Commission's role, in particular its discretion[15] in setting a reference path[16] and the underlying DSA,[17] as well as the scope and incentive for Member States to include necessary reform and investment.[18] To increase political ownership at national level, the Commission proposals may be regarded as a shift from a one-size fits all approach backed by a detailed rule-based system, to a country-specific fiscal path system. The development of those national fiscal paths evoke analogies with the national recovery and resilience plans under the RRF.

While IFIs currently fulfil an important role in the EU's fiscal governance framework at national level, the Commission's proposal would assign a more prominent role to IFIs. As highlighted by the Network of IFIs, this would require adequate minimum standards in terms of resources, access to information and their legal basis, to ensure independence.[19] A potential review of the mandate of the European Fiscal Board, an independent advisory body within the European Commission, is only hinted at in the explanatory memorandum to the preventive arm proposal.

Legislative process

Both the European Parliament and the Council and have adopted their mandates on the preventive arm of the SGP, and interinstitutional negotiations started in January 2024.

European Parliament

In Parliament, the package of three proposals was referred to the Economic and Monetary Affairs Committee (ECON). Esther De Lange (EPP, the Netherlands) and Margarida Marques (S&D, Portugal) were appointed co-rapporteurs and delivered the final reports on 11 December 2023. For the proposal replacing the current preventive arm of the SGP, the committee adopted its report under the ordinary legislative procedure (with Parliament as co-legislator) while being consulted on the other two proposals, adopting reports accordingly on the corrective arm and national IFIs. The report proposes the following changes.

It would amend the definition of '**net expenditure**', netting out expenditure on EU programmes fully matched by EU funds revenue or national expenditure co-financing EU programmes now capped at 0.25 % of GDP; excluding costs related to RRF loans.

Reference trajectory (initially 'technical' trajectory): for Member States with debt above the 60 % debt threshold or deficit above 3 %, the Commission would propose a reference trajectory in a report to Parliament and Council, to serve as the basis for the bilateral dialogue between the Member States and the Commission in setting the fiscal adjustment path. In a previous draft report, this sequence was reversed, allowing Member States to propose a reference trajectory first, but this has been deleted in the final report. The debt safeguard included in the fiscal trajectory has been amended (see safeguards below).

The **fiscal-structural plans** have been amended in the following areas:

- Annex V, which defined the methodology for assessing the plausibility of fiscal-structural plans has been incorporated into Article 8;
- Annex VI on common priorities of the EU has been incorporated into Article 12, laying down requirements for the fiscal structural plans to explain how such priorities will be addressed;
- While the Commission assessment of the plan must take into account the updated debt safeguard, such an exercise would no longer include an examination against the excessive deficit procedure; the European Fiscal Board and national IFIs must evaluate the Commission assessment;
- To extend the fiscal adjustment period, several requirements must be fulfilled. One requirement that would ensure nationally financed public investment levels in the fiscal structural plan over the extended adjustment period would be higher than in the shorter period of the initial plan, has been deleted;
- A revised fiscal structural plan, submitted for instance by a new government in a Member State, should include similarly ambitious reform and investment plans compared to the original plan.

Debt sustainability analysis: by means of a delegated act, the Commission should adopt a common methodology (akin to the commonly agreed method of the output gap) for their DSA. This methodology would identify relevant factors such as future growth, inflation and interest rates, liquidity and climate risks, and the growth impact of committed reforms and investments.

Updated **safeguards**:

- **debt safeguard** – instead of a lower public debt ratio at the end of the planning horizon compared to the year before the start of the technical trajectory, the report proposes the stabilisation of the public debt ratio over the adjustment period. For Member States with debt ratios above 90 % of GDP, an annual fiscal consolidation of 1 percentage point of GDP on average over the projection period (i.e. the adjustment period plus 10 years) is required. Member States with debt ratios between 60 % and 90 % of GDP, fiscal consolidation of 0.5 percentage points is required;

- **net expenditure growth** – the safeguard to limit net expenditure growth to below medium-term GDP growth is deleted in the report;
- **no-backloading safeguard** – this point has been kept unchanged.

Control account: the report proposes a 1 % of GDP threshold at which a Member State is considered not to be in compliance with its net expenditure path. However, this would only apply for years of positive GDP growth. For certain strategic investments, an exception allows for exceeding this threshold if investments address common EU priorities for a period of up to five years.

European Fiscal Board: the report would permanently establish an advisory European Fiscal Board, whose mandate is currently temporary, as an independent expert group to advise on the EU's economic policy coordination. IFIs would provide their opinion on a fiscal structural plan of its Member State.

European Parliament's role: several amendments would strengthen the provisions aimed at keeping Parliament better informed, mainly by means of the existing economic dialogue and a new dedicated 'medium-term fiscal-structural plan dialogue'.

- A new 'medium-term fiscal-structural plan dialogue' would be introduced, whereby the Commission appears before the competent European Parliament committee on request, to discuss the content, submission, assessment and monitoring of its medium-term fiscal-structural plans. Parliament can also invite other presidents from the Council, the European Council or the Eurogroup for discussions.
- The existing economic dialogue, in the report referred to as 'European Semester Dialogue', would be enhanced, with additional reporting requirements by the Commission, the Council and (annually) the Eurogroup.
- Parliament would be able to invite representatives from Member States if, for instance, the Council recommended using the Commission's reference trajectory (as opposed to the Member States' reference trajectory), if a Member State submitted a revised fiscal structural plan, or if the Council recommended a shorter adjustment period.
- Additional information would be provided to Parliament: transmission of fiscal-structural plans, minutes and underlying documents of technical dialogues, including proposed reference trajectories (in such a way as to allow replicability), net expenditure paths, debt sustainability assessments and progress reports on reform and investment commitments.

To facilitate Parliament's scrutiny, the report proposes establishing a **scoreboard**, based on a delegated act, to monitor progress on implementing the medium-term fiscal-structural plans.

In addition, the text corroborates provisions that require Member States to consult their national parliaments and civil society when drawing up their fiscal-structural plans.

Excessive imbalance procedure: should the Council decide against opening an excessive imbalance procedure, the report proposes that the Council would issue a public statement explaining its position.

Annexes: several annexes have been added to the legislative text, while the conferral to adopt delegated acts to amend Annexes II to VII has been deleted. The conferral of the two added delegated acts on the DSA methodology and the scoreboard have been limited to five years.

- Annex I, which set criteria for the technical trajectory, has been deleted and its content incorporated mainly into Articles 5, 6 and 7;
- Annex IV defining the functioning of the Control Account has been deleted and incorporated into Article 21 (Monitoring of the Commission);

- Annex V, laying down the methodology to assess the debt sustainability, has been deleted and incorporated into Article 8;
- Annex VI on common priorities of the EU has been incorporated in Article 12 laying down requirements for the fiscal structural plans.

The Committee on Employment and Social Affairs provided an opinion (rapporteur: Gabriele Bischoff, S&D, Germany) on the preventive arm of the SGP, based on its areas of competence (e.g. European pillar of social rights in the context of the European Semester). The Budgets Committee provided an opinion (rapporteur: Jan Van Overtveldt, ECR, Belgium) on the corrective arm of the SGP. The ECON committee decision to enter into interinstitutional negotiations was confirmed by plenary on 17 January 2024.

Council

On 20 December 2023, the Council reached a political agreement on the economic governance proposal. The Council's negotiating mandates for the preventive arm, as well as the political agreements on the corrective arm and on the budgetary framework, were formally endorsed by ambassadors on 21 December 2023.

Interinstitutional negotiations between the co-legislators on the preventive arm proposal might revolve around three main areas of contention.

Safeguards. The **debt safeguard** is mostly aligned between Council and Parliament. Member States with a high debt level (above 90 % of GDP) have to decrease their debt-to-GDP ratio by 1 percentage point, while Member States with medium debt levels (between 60 and 90 % of GDP) need to reduce the debt ratio by 0.5 percentage points. However, while Parliament would see this adjustment over a projection period, meaning the adjustment period plus 10 years, the Council defines the adjustment period as length of the structural fiscal plan, covering four to seven years. An additional difference between the two positions is that the Council would have the debt reduction assessed only after a Member State has reduced its deficit below the 3 % threshold.

This is in contrast to a new '**deficit resilience safeguard**' the Council agreed on, thereby diverging from Parliament's report, which would require Member States to continue reducing their 3 % deficit by half, through a safety margin of 1.5 % of GDP. If a Member State's fiscal plan – and thus the fiscal trajectory – is four years, the annual adjustment to the structural primary balance would be 0.4 % of GDP. For Member States with an extended plan, the deficit adjustment would be 0.25 % of GDP.

IFIs. In the Commission proposal, national IFIs were a crucial element to monitor compliance and thus increase national ownership of fiscal plans. However, despite featuring significantly throughout Parliament's report, IFIs' role would be cut significantly according to the Council mandate.

Transitory provisions. The Council mandate adds transitory provisions – for instance to take into account RRF loans and co-financed EU funds in the coming years – that apply to safeguards in the preventive arm. In the corrective arm (where Parliament is only consulted), once a country is in an excessive deficit procedure and required to adjust its annual (primary) structural deficit by 0.5 % of GDP, interest payments are excluded from this adjustment until 2027. Beyond 2027, the corrective net expenditure path would need to be adjusted by 0.5 % of GDP including interest expenditures.

The regulation on the corrective arm and the directive on requirements for Member States' budgetary frameworks require the European Parliament to be consulted.

EUROPEAN PARLIAMENT SUPPORTING ANALYSIS

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OTHER SOURCES

European Parliament, Economic governance: requirements for budgetary frameworks of the Member States, Legislative Observatory (OEIL).

European Parliament, Effective coordination of economic policies and multilateral budgetary surveillance, Legislative Observatory (OEIL).

European Parliament, Excessive deficit procedure: speeding up and clarifying the implementation, Legislative Observatory (OEIL).

ENDNOTES

1. The legislative procedure is important to consider in the negotiations, as the ordinary legislative procedure puts the Parliament and the Council on an equal footing. The Parliament votes by a simple majority (first reading) and the Council by a qualified majority.
2. The second set of reforms of the SGP changed the EDP procedure. Instead of approving a proposal for sanctions by qualified majority voting, the Council was deemed to agree with the Commission unless a qualified majority of its members objected.
3. This aggregate figure masks large differences across Member States. For instance, Luxembourg, Estonia, Finland and Ireland complied with the fiscal rules in more than two out of three years. On the other hand, Portugal, Greece, Italy and France complied in fewer than one out of three years. See S. Santacroce and M. Larch, Tracking compliance with EU fiscal rules: A new database of the Secretariat of the European Fiscal Board, VoxEU, September 2020.
4. In this assessment, the EFB advocates for a reformed stability and growth pact that would be based on one single target (sustainable public debt), one single instrument (controlling net expenditure growth), and one general escape clause. See European Fiscal Board, Assessment of EU fiscal rules with a focus on the six and two-pack regulations, September 2019.
5. For a detailed literature review on reform proposals, see Report on Public Finances in EMU 2021, Institutional Paper 181, European Commission, July 2022, pp. 33-44.
6. For a concise description of the Commission's orientations for a reformed economic governance framework see A. D'Alfonso et al., Economic and Budgetary Outlook for the European Union 2023 (Chapter 7), EPRS, European Parliament, February 2023.
7. The methodological backbone of the Commission's proposal is the DSA framework, which determines the technical trajectory and in turn serves as a benchmark for Member States' multi-year fiscal adjustment paths. Many international organisations and financial institutions, including the International Monetary Fund (IMF) and the World Bank, use debt sustainability analyses in their surveillance procedures. In the EU context, under the Treaty establishing the European Stability Mechanism, consideration of financial assistance to euro area Member States requires, inter alia, a debt sustainability assessment by the European Commission (in liaison with the European Central Bank, and possibly also the IMF) (see Article 13, paragraph 1(b), Treaty establishing the European Stability Mechanism). The DSA framework requires an estimate of unobservable variables such as potential output to project future debt developments. While the assumptions and estimates of the underlying model would be made public by the Commission, a projection of a rising debt ratio, or even a declaration of unsustainable debt, could create a self-fulfilling prophecy if this leads to rising financing costs and, consequently, increases debt. See P. Sigl-Glöckner., On shrinking the public balance sheet and the use of debt sustainability analyses, statement at a hearing of the European Parliament's Committee on Economic and Monetary Affairs, December 2022.
8. According to Annex II, point (a), expenditure on EU programmes fully matched by EU funds would also be taken out of the single operational indicator.
9. Compared with the Commission's orientation, the current proposal does not distinguish between Member States with a substantial/moderate/low public debt challenge when calculating the technical trajectory (as opposed to 'reference adjustment path' in the orientation). It does, however, consider Member States' debt challenge from the debt sustainability monitor – in the assessment of the plausibility of the projected debt ratio, in the assessment of investment and reform commitments, as well as when opening an excessive deficit procedure.
10. Whether or not public debt ratio is declining, or stays at prudent levels, is estimated in the Commission's medium-term public debt projection framework described in the Debt Sustainability Monitor 2022.

[11] The Member States' annual reports would replace the three-year budget plans submitted through the stability programmes for euro-area countries or convergence programmes for non euro-area countries, as well as the national reform programmes that give an overview of the policy actions and economic reforms under way in Member States.

[12] For a detailed development of the use of delegated acts in the Commission's proposal, see: K. Hagelstam, S. De Lemos and G. Loi, Enhanced political ownership and transparency of the EU economic governance framework, Economic Governance and EMU Scrutiny Unit, Directorate-General for Internal Policies European Parliament, December 2023.

[13] An assessment of the EU IFIs describes the significant differences between IFIs across the Member States, for instance in terms of the breadth of their mandates, their resources or their visibility in public debate. This highlights that there is a heterogeneity of efforts should such minimum standards be applied according to the proposals. See L. Jankovics and M. Sherwood, Independent Fiscal Institutions in the EU Member States, European Commission, Discussion Paper 067, July 2017. It should be noted that the role of IFIs in the proposals goes beyond what the Council communicated: that the current role of IFIs should be maintained and that they should not play a role in the design phase of the national plans.

[14] This section aims to provide a flavour of the debate and is not intended to be an exhaustive account of all different views on the proposal. Additional information can be found in related publications listed under 'European Parliament supporting analysis'.

[15] See O. Blanchard, A. Sapir and J. Zettelmeyer, The European Commission's fiscal rules proposal: a bold plan with flaws that can be fixed, Bruegel Blog, November 2022.

[16] See A targeted golden rule for public investments?, Economic Governance and EMU Scrutiny Unit, Directorate-General for Internal Policies, European Parliament, 2023, argue that the bilateral negotiations (between Commission and Member States) will give the Commission room for discretion, or political leeway, for instance on the individual fiscal adjustment paths. However, this might come at a costs, as argued in A targeted golden rule for public investments? A comparative analysis of possible accounting methods in the context of the review of the Stability and Growth Pact, Economic Governance and EMU Scrutiny Unit, Directorate-General for Internal Policies, European Parliament, 2023, because the non-public, bilateral negotiations risk to be politicised, making agreements more complicated.

[17] See Debt sustainability analysis as an anchor in EU fiscal rules, Economic Governance and EMU Scrutiny Unit, Directorate-General for Internal Policies, European Parliament, March 2023, which highlights that a DSA analysis comes with several caveats, such as reliance on assumptions and estimation of unobservable elements, through its methodological focus on where public debt is penalising investments. Further, the issue of fiscal policy coordination and the euro area fiscal stance are raised, when fiscal paths derived from DSA is negotiated on a bilateral basis.

[18] See A. D'Alfonso A. et al., Economic and Budgetary Outlook for the European Union 2023 (Chapter 7), EPRS, European Parliament, February 2023, or The role of public investments in the EU economic governance framework, Economic Governance and EMU Scrutiny Unit, Directorate-General for Internal Policies, European Parliament, January 2023.

[19] For an assessment of the role of IFIs in the EU fiscal governance framework see Strengths and weaknesses of independent advisory fiscal institutions in the EU economic governance framework, Economic Governance and EMU Scrutiny Unit, Directorate-General for Internal Policies, European Parliament, May 2023.

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Third edition. The 'EU Legislation in Progress' briefings are updated at key stages throughout the legislative procedure.

Annex – Comparative tables

Table 1 – Safeguards in the new economic governance framework

Safeguard	European Commission (COM) proposal	European Parliament (EP) report	Council mandate	Comment
1) The debt ratio follows a plausible downward path	The public debt ratio is put or remains on a plausibly downward path, or stays at prudent levels.	The public debt ratio is put or remains on a plausibly downward path, **leading to sustainable debt reduction**, or stays at prudent levels.	The **technical trajectory** shall be risk-based and differentiated for each Member State, ensuring that: (a) by the end of the adjustment period, at the latest, assuming no further budgetary measures, the projected general government debt ratio is put or remains on a plausibly downward path, or stays at prudent levels below the 60 % GDP Treaty reference value over the medium-term; […)	While the COM proposal and the EP report refer to a general downward path of the debt ratio, the Council refers to the technical trajectory, i.e. covering an adjustment period of between 4 and 7 years.
2) The deficit ratio remains or returns below the 3 % threshold	The government deficit is brought and maintained below the 3 % of GDP reference value.	same	The **technical trajectory** shall be risk-based and differentiated for each Member State, ensuring that: […] (b) the projected general government deficit is brought below the 3 % of GDP reference value over the adjustment period and maintained below such reference value over the medium term assuming no further budgetary measures; […]	While the COM proposal and the EP report refer to a deficit brought and maintained at the 3 % reference value, the Council specifies a timeframe by which the deficit threshold needs to be reached (adjustment period, i.e. the plan's horizon) and maintained over the medium term.
3) Expenditure growth remains below medium-term GDP growth	National net expenditure growth remains below medium-term output growth,	deleted	deleted	

Safeguard	European Commission (COM) proposal	European Parliament (EP) report	Council mandate	Comment
	on average, as a rule over the horizon			
4) The debt ratio at the end of the plan is lower than at the beginning	The public debt ratio at the end of the planning horizon is below the public debt ratio in the year before the start of the technical trajectory.	The public debt ratio **stabilises over the adjustment period and is reduced every year over the projection period on average by at least 1 percentage point of debt-to-GDP for the Member States with a debt-to-GDP ratio exceeding 90 % and at least half a percentage point for the Member States with a debt-to-GDP ratio of 60 % to 90 %.**	The **technical trajectory** shall ensure that the projected general government debt-to-GDP ratio decreases by a minimum annual average amount of: (a) 1 percentage point of GDP as long as the general government debt-to-GDP ratio exceeds 90 %; (b) 0.5 percentage point of GDP as long as the general government debt-to-GDP ratio remains between 60 % and 90 %. The average decrease shall be computed from the year before the start of the technical trajectory or the year in which the excessive deficit procedure is projected to be abrogated under Council Regulation (EC) No 1467/97, whichever occurs last, until the end of the adjustment period.	While the general definition of this safeguard is aligned between the EP report and the Council, the time spans differ: - EP report: debt ratio reduced over projection period, i.e. adjustment period plus 10 years: - Council: period over which the debt reduction is assessed (over the plan's horizon), starts only after countries have reduced their deficits below 3 % (i.e. EDP is projected to be abrogated)
5) Fiscal effort is not back-loaded	The fiscal adjustment effort over the period of the national medium-term fiscal-structural plan is at least proportional to	same	The **technical trajectory** shall be risk-based and differentiated for each Member State, ensuring that: […]	aligned

Safeguard	European Commission (COM) proposal	European Parliament (EP) report	Council mandate	Comment
	the total effort over the entire adjustment period.		(c) the fiscal adjustment effort over the period of the national medium-term fiscal-structural plan is linear as a rule and at least proportional to the total effort over the entire adjustment period; […]	
New: Debt resilience safeguard	n/a	n/a	**1. The Commission technical trajectory, referred to in Article 6, shall ensure that fiscal adjustment continues, where needed, until the Member State reaches a deficit level that provides a common resilience margin in structural terms of 1.5 % of GDP relative to the 3 % of GDP deficit Treaty reference value.** **2. The annual improvement in the structural primary balance to achieve the required margin shall be of 0.4 % of GDP, which shall be reduced to 0.25 % of GDP in case of an extension of the adjustment period in accordance with Article 13.**	This newly adopted safeguard by the Council introduces a government deficit margin. The 'debt resilience safeguard' is levering the 3 % deficit threshold through a safety margin of 1.5 %, with annual minimum adjustments of the structural primary balance between 0.25 and 0.4 % of GDP.

Table 2 – European Fiscal Board and independent fiscal institutions

Fiscal institution	COM proposal	EP report	Council mandate	Comment
European Fiscal Board (EFB)	Exploratory memorandum: The Commission will explore how to strengthen the role of the European Fiscal Board.	1. The Commission shall establish the European Fiscal Board (EFB), an independent expert group … 2. The EFB shall: (a) be independent and not seek or take instructions from the budgetary authorities of the Member States, from the Commission or from any other public or private bodies; b) have the capacity to produce opinions in a timely manner and communicate publicly; […]. 3. The EFB shall … provide advice to the European Parliament, the Council, the Commission and the Eurogroup.	1. The independent European Fiscal Board ('the Board') established by Commission Decision (EU) 2015/1937 of 21 October 2015 shall contribute in an advisory capacity … 2. In the performance of its tasks, the Board shall enjoy full independence in the discharge of its functions, performing its duties impartially and solely in the interest of the Union as a whole. It shall not seek nor take instructions from any government of a Member State, the Union's institutions or bodies or from any other public or private body. 3. [Tasks] 4.-6. [Governance structure] 7. The Board shall report once a year on its activities to the Commission, the Council and the European Parliament. All reports and advice of the Board will be made public.	'While the COM proposal mentions the EFB only in the proposal's exploratory memorandum, the EP as well as the Council give a clear, independent mandate to the EFB, including detailed tasks. In addition, the Council specifies the governance structure of the EFB.

Fiscal institution	COM proposal	EP report	Council mandate	Comment
Independent fiscal institutions (IFIs)	Each national independent fiscal institution referred to in Article 8 of Council Directive […][32] [on the national budgetary frameworks] shall provide an assessment of compliance of the budgetary outturns data reported in the progress report referred to in Article 20 with the net expenditure path. Where applicable, each national independent fiscal institution shall also analyse the factors underlying a deviation from the net expenditure path.	'1. Each national independent fiscal institution referred to in Article 8 of Council Directive […][22] [on the national budgetary frameworks] shall provide an assessment of compliance of the budgetary outturns data reported in the progress report referred to in Article 20 with the net expenditure path, including of non-quantifiable targets. Where applicable, each national independent fiscal institution shall also analyse the factors underlying a deviation from the net expenditure path. 1a. The qualitative and quantitative assessments in the opinions of the national independent fiscal institution referred to in paragraph 1 shall take into account different views and allow for the disclosure of minority and divergent positions. For that purpose, relevant stakeholders shall be regularly consulted. 1b. Opinions and assessments delivered by the independent fiscal institutions in accordance with this Regulation shall be made public.	Member States **may request** the relevant national independent fiscal institution referred to in Article 8 of Council Directive […][14] [on the national budgetary frameworks] to provide an assessment of compliance of the budgetary outturns data reported in the progress report referred to in Article 20 with the net expenditure path. Where applicable, Member States **may also request** the relevant national independent fiscal institution to also analyse the factors underlying a deviation from the net expenditure path. These analyses should be **non-binding** and additional to those provided by the Commission.	Role of IFIs weakened in Council mandate compared with the COM proposal or EP report. The COM proposal as well as the EP report would require IFIs to assess the expenditure path and underlying factors that explain any deviation. The Council would give national governments the option to 'request' such assessment, while such analysis would be non-binding.