

The European Stability Mechanism: Main Features, Instruments and Accountability

This document presents the main features of the European Stability Mechanism (ESM), including governance, capital structure and funding sources, main lending instruments, as well as its oversight and accountability framework. It also reviews recent proposals and contributions on the possible evolution of the ESM. This note is regularly updated.



The European Stability Mechanism ([ESM](#)) was set up in October 2012, following an *ad hoc* Intergovernmental Treaty ([TESM](#)) signed on 2 February 2012 by the governments of the Euro Area Member States (EAMS).

The ESM provides loans to Euro Area Member States facing financial difficulties, conditionally on the implementation of policy measures. It borrows money on financial markets, and the borrowed money is guaranteed by 704.8 billion Euros (its capital, as authorised by the Members).

Over the years, the ESM has provided financial assistance to Greece, Cyprus and Spain, and has contributed to the definition of both conditionality and the financial conditions on loans. Since its establishment, the legitimacy of the ESM has been debated in two aspects:

- its compatibility with Article 125 of the Treaty on the Functioning of the EU and
- its transparency and accountability at the EU level.

Against the backdrop of the evolution of the economic governance in the Economic and Monetary Union, including the Banking Union, many proposals have been made on the possible future role of the ESM, including the Commission proposal of December 2017 for its evolution into a European Monetary Fund and inclusion into the EU legal framework. More recently, the Eurogroup has decided to propose amendments to the ESM Treaty that the European Council has broadly accepted. The final decision on these amendments is expected by December 2019.

Box 1: Relevant EU and national case law

[Pringle case, ECJ, 27/11/2012](#)

The European Court of Justice (ECJ) ruled that the ESM is compatible with the Treaty on the Functioning of the EU ([TFEU](#)), including the 'no bail out' clause of Article 125: "(...) Article 125 TFEU does not prohibit the granting of financial assistance by one or more Member States to a Member State which remains responsible for its commitments to its creditors, provided that the conditions attached to such assistance are such as to prompt that Member State to implement a sound budgetary policy".

[German constitutional court ruling on 18/03/2014](#)

The German Federal Constitutional Court ruled, "Despite the liabilities assumed, the budgetary autonomy of the German Bundestag is sufficiently safeguarded. However, arrangements under budgetary law must be made to ensure that possible capital calls pursuant to the ESM Treaty can be met fully and in time within the agreed-upon upper limits".



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1. Overview

The ESM was established under public international law by the Treaty establishing the European Stability Mechanism (TESM).¹ An initial version of the ESMT, signed on [11 July 2011](#), never entered into force, being superseded by the one signed in 2012. The ESM replaced the initial rescue fund for the euro area, the European Financial Stability Facility (EFSF) set in May 2010, which had provided loans to Ireland, Portugal and Greece. Today, the EFSF (which no longer can make new loans) and the ESM are separate legal entities, but they share staff, facilities and operations². In May 2010, in parallel to the EFSF, the Council had established the European Financial Stabilisation Mechanism (EFSM)³ by means of [Regulation 407/2010](#)⁴. All these instruments constitutes the safety net created during the crisis to finance Member States (MS) in difficulties and to support financial stability⁵. The main objective of the ESM is to provide stability support to EAMS that are experiencing or are threatened by severe financial difficulties, if indispensable to safeguard the financial stability of the euro area as a whole and of its Member States.

In line with the legal framework (the TESM, the revised Article 136 TFEU and the ruling of the European Court of Justice), ESM financial assistance is strictly conditional on the implementation of policy measures. Such measures are specified in a Memorandum of Understanding (MoU)⁶ negotiated by the European Commission on behalf of the ESM, the European Central Bank (ECB), the International Monetary Fund (IMF) (where applicable) and the beneficiary Member State. The lending instrument and the attached conditions are approved by the ESM Board of Governors, which is composed of the Euro Area Finance Ministers.

There are currently no MSs under ESM financial assistance, after Greece successfully exited its programme in August 2018. Nevertheless, all those Member States that benefitted from financial assistance during the crisis are subject to the so-called “post-programme surveillance”, which aims to measure a beneficiary’s capacity to repay outstanding loans⁷.

The reform of the ESM is part of the agenda on deepening the Economic and Monetary Union. In December 2017, the European Commission presented a [proposal for a Council Regulation](#) on the establishment of the European Monetary Fund, aimed at integrating the ESM into the EU legal framework⁸. The [14 December 2018 Euro Summit](#) took some decisions on the reform of the ESM, notably regarding the precautionary instruments; making the ESM the backstop to the Single Resolution Fund (SRF) and improving the framework for assessing debt sustainability. The [June 2019 Euro Summit](#) took note of the progress reached by the Eurogroup, and expects the work to be finalised by December 2019, in order to start the procedure to ratify the agreed changes to the TESM *via* an intergovernmental agreement (Section 7 provides additional information).

¹ The [Treaty on the Functioning of the European Union](#) has been amended to allow for the establishment of the ESM. The following text was inserted under Article 136, para. 3: “*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.*”

² The ESM has its headquarter in Luxembourg and has around 190 [staff members](#).

³ The EFSM mirrors the “[Balance of payment assistance](#)” (BoP) instrument, which is available for non-euro area MS only. Both EFSM and BoP are based on the Union budget. They allow granting loans or credit lines to a MS facing difficulties. The EFSM Regulation mandates the [Commission to borrow](#) in financial markets on behalf of the Union under an implicit EU budget guarantee, with a ceiling of up to 60 billion euro. Activation of the EFSM requires a macroeconomic adjustment programme, incorporating strict conditionality, agreed with the Commission in liaison with the ECB. The EFSM has been used for Portugal and Ireland and for short-term bridge financing to Greece in 2015.

⁴ Amended by Council Regulation 2015/1360 of 4 August 2015.

⁵ Contrary to its predecessor, the EFSF, the debt issued by the ESM does not affect Member States debt levels (ESM debt is not rerouted to Member States’ debt), as decided by Eurostat (see [note](#) of 12 April 2012).

⁶ The revised ESMT will foresee that a Letter of Intent replaces the MoU in cases of precautionary conditioned credit lines.

⁷ Post-programme surveillance is foreseen by Art. 14 of the [Regulation \(EU\) N°472/2013 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](#), which reads “*a Member State shall be under post-programme surveillance as long as a minimum of 75 % of the financial assistance received from one or several other Member States, the EFSM, the ESM or the EFSF has not been repaid*”.

⁸ In June 2019, the Commission published its [Communication](#) on “*Deepening Europe’s Economic Monetary Union: Taking stock four years after the Five Presidents’ report*”, where it states that: “*The ongoing revision of the Treaty establishing the European Stability Mechanism, as an intermediate solution, is meant to further strengthen crisis prevention and resolution in the euro area. It should neither duplicate tasks with EU institutions nor add to the complexity of the economic surveillance framework,*”

2. Governance

The ESM is governed by the Board of Governors (BoG), composed of the 19 Euro Area finance ministers. The BoG decides either to be chaired by the President of the [Eurogroup](#) or elect a Chairperson from among its members (for two years, renewable).⁹

All major decisions within the BoG are taken by unanimity¹⁰, including capital increases, granting of financial assistance and approval of MoUs. The European Commission, the ECB and the President of the Eurogroup may participate in the meetings of the BoG as observers¹¹, while others, including representatives of institutions or organisations, can be invited by the BoG to attend meetings as observers on an *ad hoc* basis. The voting rights of each ESM Member in the BoG are equal to the number of shares allocated to it in the capital stock of the ESM (see Annex 1).

The Board of Directors (BoD) is the executive body of the ESM, composed of 19 Directors appointed by the Governors, from among people of high competence in economic and financial matters. Today it is chaired by Klaus Regling, who was appointed as the Managing Director of the ESM for a first term of 5 years in 2012, and [reappointed](#) for another 5-year term until October 2022.¹² The Managing Director is the legal representative of the ESM and its top executive. The [Management Board](#), composed of additional six members, conducts the ongoing business of the ESM and is responsible for organising, appointing and dismissing staff. The BoD is assisted by two internal committees: the Risk Committee, which evaluates and monitors the ESM risk strategy and its implementation, and the Budget Review and Compensation Committee that mostly deals with staff issues and remuneration. Other Committees assist the BoD in decisions relating to recapitalisation of financial institutions (the Banking Committee), corporate affairs (Corporate Projects Committee) and business continuity (Incident Management Team), among others.

The BoD ensures that the ESM is run in accordance with the TESM and the governance rules by-laws adopted by the BoG, and takes decisions as provided for in the TESM (such as the approval of loan disbursements) or which are delegated to it by the BoG. The BoD takes decisions according to qualified majority, while for decisions delegated by the BoG the voting method is the same as the one adopted by the BoG. The voting rights of each ESM Member are the same as in the BoG.

In addition to its management bodies, the ESM has three bodies for audit oversight. More specifically:

- [Board of Auditors](#)

The [Board of Auditors](#) is an independent oversight body of the ESM. It is composed of five members appointed by the BoG, in charge of auditing the regularity, compliance, performance, and risk management of the ESM. The Board also monitors the ESM internal and external audit processes and their results, and publishes [annual reports](#) that are sent to various authorities, including the European Parliament.

- [Internal Audit](#)

This is an independent and objective assurance function, reporting directly to the ESM Managing Director. The [Internal Audit](#) brings a systematic and disciplined approach to evaluating and improving the ESM's risk management, internal control and governance processes, thereby increasing ESM efficiency. The Internal Audit follows the Institute of Internal Auditors Code of Ethics and the International Standards for the Professional Practice of Internal Auditing.

⁹ The current Chair of the ESM BoG is Mário Centeno, elected on 4 December 2017 (effective from 13 January 2018). He succeeds Jeroen Dijsselbloem, who chaired the Eurogroup since 5 November 2012.

¹⁰ The TESM also includes an emergency voting procedure, whereby financial assistance can be granted if supported by a qualified majority of 85 % of the votes, which confers upon Germany, France and Italy a veto right.

¹¹ Following the pending review, Member States that participate alongside the ESM in facilities backstopping the SRF will also participate as observers in meetings where such issues are discussed.

¹² "The Managing Director shall be appointed by the Board of Governors from among candidates having the nationality of an ESM Member, relevant international experience and a high level of competence in economic and financial matters. (...) He or she may be reappointed once." (Article 7 TESM). He also serves as CEO of the EFSF. The mandate of ESM Managing Director is being expanded and clarified in the pending ESMT review.

- External audit

The [external audit](#) of ESM accounts is conducted by independent auditors approved by the BoG and is responsible for certifying the annual financial statements. The auditors are chosen among firms subject to public supervision. The external auditor examines the ESM Financial Statements in accordance with generally accepted auditing standards and has the power to examine all books and accounts of the ESM and obtain all information about its transactions. The audit findings in relation to the ESM Financial Statements are reflected in the external auditor's report on the Financial Statements, contained in the ESM Annual Report¹³.

3. Capital and Funding

The ESM has a subscribed authorised capital totalling 704.8 billion euro, of which 80.5 billion has been paid-in. The financial contribution of each ESM Member is based on the capital key of the ECB, which reflects the respective country's share in the total population and gross domestic product of the Euro Area (see Annex 1), and Members receive ESM shares corresponding to their subscribed capital. The ESM lending capacity is capped at €500 billion. The part of the ESM capital that is subscribed but not paid is 'callable' at any time, in case of need (i.e. the ESM Members commit to provide the corresponding funding at short notice).

Table 1: ESM capital

Capital	EUR bn
Subscribed capital	€704.8bn
Paid-in capital	€80.5 bn
Committed callable capital	€624.3bn
Maximum lending capacity	€500 bn
Remaining lending capacity (August 2019): 82%	€410.1bn

Source: <https://www.esm.europa.eu/>, August 2019

The ESM paid-in capital is managed "prudently and conservatively"¹⁴. The specific Investment Management Committee works together with the BoD to implement the [ESM Guidelines on Investment Policy](#). When a Member State adopts the Euro, it must become a member of the ESM (no 'opt-out' clause) and thus subscribe ESM shares. In cases of [enlargement](#) - which happened twice since the establishment of the ESM, with the entry of Latvia and Lithuania¹⁵ - the contribution keys of ESM Members change mechanically.

The ESM issues bills and bonds on the market¹⁶, with maturities from 1 month to 45 years. Issues may be made via syndications, auctions, private placements and taps of existing lines. The ESM can also [borrow](#) from ESM members, financial institutions or other third parties. The ESM's [funding strategy](#) follows policies similar to those of a debt management agency at national or international level, and ESM bonds are considered of high quality. Thanks to its good rating, the ESM enjoys good financing conditions¹⁷. Its creditor status is preferred, second to the IMF only. Funds raised are pooled and not earmarked for a specific country. Annex 2 to this note presents some information on ESM's investors, by geographical origin and institutional sector.

¹³ "The BoG shall make the annual report accessible to the national parliaments and supreme audit institutions of the ESM Members and to the European Court of Auditors" (Article 30, para. 5 TESM). The ESM published its latest [Annual Report](#) 2018 in June 2019.

¹⁴ See ESM <https://www.esm.europa.eu/about-us/how-we-work>.

¹⁵ The initial subscribed capital of €700 billion has increased since the accession of Latvia in March 2014 and Lithuania in February 2015. Paid-in capital has been increased by €0.5 bn and committed callable capital has been increased by €4.25 bn.

¹⁶ On 26 September 2019, the ESM [announced](#) that it has decided to begin using Luxembourgish law instead of English law as the governing law for all its new euro-denominated bonds and bills.

¹⁷ The ESM current external rating is AAA (Fitch) or Aa1 (Moody's). Although the ESM has a negative leverage (i.e. its capital base is larger than its lending capacity), its rating is sensitive to rating changes of its larger Members, because not all the capital is paid-in. In case of downgrading of an ESM Member, rating agencies may assess that the risk of non-payment of the callable capital of that Member is higher. For updated information, see "[ESM/EFSF Investors' presentation](#)".

4. Financial Assistance

4.1 ESM Financial assistance toolkit

The ESM may provide support only on the basis of strict conditionality. *“If the ESM Member is assessed as eligible, the BoG shall entrust the European Commission – in liaison with the ECB and, wherever possible, together with the IMF – with the task of negotiating, with the ESM Member concerned, a Memorandum of Understanding (MoU) detailing the conditionality attached to the financial assistance facility. The content of the MoU shall reflect the severity of the weaknesses to be addressed and the financial assistance instrument chosen”* (Article 13 TESM in its current wording; this provision is being amended, namely to avoid the obligation to draft an MoU for the precautionary conditioned credit lines).

In accordance with Article 7 of EU Regulation [472/2013](#)¹⁸, the European Commission signs the MoU on behalf of the ESM¹⁹, observing Article 152 of the TFEU (“role of social partners”) and taking into account Article 28 of the [Charter of Fundamental Rights of the European Union](#) (“right of collective bargaining and action”). Six different financial instruments are available in the [ESM toolbox](#). Most of them are clearly crisis management tools, to be used as last resort instruments when the situation of a Member State or its financial sector is already quite deteriorated; only one – the precautionary financial assistance – has a preventive nature. Two instruments target specifically the financial sector, namely the financial assistance for recapitalisation of financial institutions (‘indirect recapitalisation’) and the “direct recapitalisation instrument” (DRI). Conditionality varies with the nature of the instrument: it is typically less strict in the case of precautionary assistance. The precautionary financial assistance, part of the ESM toolbox, is being reviewed. Only two of the instruments have been used so far: the stability support loan and the ‘indirect recapitalisation’ instrument.

- [Stability support loan](#)

Such loan is granted by the ESM to the requesting ESM Member – that has significant financing needs and, to a large extent, has lost access to market financing – as part of a macro-economic adjustment programme. Such support loan has been granted to [Cyprus](#) in 2013 and [Greece](#) in 2015.

- [Primary market support facility](#)

The ESM may engage in primary market purchase of bonds and other securities issued by Member States at market price to allow them to restore their relationship with the investment community and therefore to reduce the risk of a failed auction. This instrument can complement the regular loan or a precautionary programme. The purchase is limited to 50% of the final issued amount. Such instrument was designed to be used primarily towards the end of an adjustment programme, to facilitate a country’s return to the market.

- [Secondary market support facility](#)

This facility aims at supporting the functioning of regular government debt markets when lacking market liquidity threatens the financial stability in the context of a loan, either with a macroeconomic adjustment programme or without it, if the Member’s financial and economic situation is sound. If the Member State is not under a programme, specific conditionality applies.

- [Financial assistance for recapitalisation of financial institutions \(‘indirect recapitalisation’\)](#)

Such instrument is to be used where the roots of the crisis are located in the financial sector and not directly related to fiscal or structural policies. The policy conditions in the MoU focus only on the ESM Member’s financial sector. Such financial assistance instrument was used for [Spain](#) in 2012, when the ESM provided a total amount of €41.3 billion.

¹⁸ Regulation 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.

¹⁹ The [revised ESMT](#) foresees that the Managing Director will also sign the MoU with the Commission (article 13/4 of the revised ESMT).

- **Direct recapitalisation instrument (DRI)**

DRI is an [instrument](#) introduced in December 2014. DRI may be used to directly recapitalise financial institutions, as a last resort instrument when all other instruments, including bail-in as mandated by the Bank Recovery and Resolution Directive (BRRD), have been applied and after the Single Resolution Fund (SRF) has been used. In order to preserve ESM's lending capacity for other instruments, the total amount of ESM resources available for this instrument was limited to €60 billion. DRI will, however, be replaced by an ESM credit line to be used as a [common backstop to the Single Resolution Fund](#) (see Box 2, Section 7 and Annex 5).

- **ESM precautionary financial assistance**

Such financial assistance takes the form of a credit line to support sound policies and prevent crises. It allows ESM Members to secure ESM assistance before they face major difficulties when raising funds in the capital markets. The granting of such precautionary credit line is not conditional to the launch of a full macro-adjustment programme, but to a lighter set of conditions enshrined in a MoU agreed with the Commission. There are [two types of credit lines](#): the Precautionary Conditioned Credit Line (for Member States that comply with specific eligibility criteria, including compliance with the Stability and Growth Pact) and the Enhanced Conditions Credit Line (for Member States that do not comply with the eligibility criteria for the Precautionary Conditioned Credit Line).

Box 2: The ESM and the Banking Union

Currently, the ESM may provide funding to failing financial institutions either indirectly - via the indirect recapitalisation instrument - or directly - via the Direct Recapitalisation Instrument (DRI). As such, ESM money can be used in banking resolution only in compliance with the “burden sharing cascade”, as defined in the BRRD and SRM regulations. Any capital needs should be met with (sequentially):

- Private sources (current/new shareholders, bail-in of junior and senior creditors - up to 8 % of total liabilities);
- Once 8% of the total liabilities have been “bailed-in”, the SRF can contribute under strict conditions. Its intervention is capped at 5 % of total liabilities;
- If the bank remains undercapitalised, but its continuation is imperative to safeguard financial stability, public funding can be used in “extraordinary circumstances”, provided that the 5% referred to above has been reached and all unsecured, non-preferred liabilities other than eligible deposits have been written down or converted in full. Funding can either come from national budgets (that may be financed, if needed, by an ESM loan - ESM ‘indirect recapitalisation’) or from the ESM directly (DRI).
- To be eligible for the implementation of the DRI, the ESM Member State should be unable to provide financial assistance to the beneficiary institution without very serious effects on its own fiscal sustainability. The beneficiary institution should be failing or likely to fail (the DRI is excluded for precautionary recapitalisation) and must be of systemic relevance and supervised by the ECB. It should also be unable to obtain sufficient capital from private sources (including bail-in).

The Direct Recapitalisation Instrument will be replaced by the ESM backstopping the Single Resolution Fund (SRF), as decided at the [14 December 2018 Euro Summit](#). The Eurogroup worked on a common backstop for the Single Resolution Fund for some time, as part of its work on completing the Banking Union. The main elements of such new ESM function were outlined in the Eurogroup President’s [letter](#) to the the President of the European Council of June 2018. The [4 December 2018 Eurogroup](#) agreed on [terms of reference](#) detailing the main elements of the SRF backstop. The [14 December 2018 Euro Summit](#) endorsed the terms of reference and mandated Eurogroup to finalise the necessary ESM Treaty amendments by June 2019. Leaders also agreed that the backstop can be anticipated “*provided sufficient progress has been made in risk reduction, to be assessed in 2020.*”. The [June 2019 Eurogroup](#) agreed on a revised draft ESM Treaty detailing the terms under which the ESM may provide a backstop to the SRB. Article 18A (and 37(4) referring to submissions to the European Court of Justice) and [Annex IV](#) of the draft revised ESM Treaty further detail the terms of ESM granting loans to backstop the SRF. In particular, the revised ESM Treaty foresees the ESM backstop being available only insofar the current resolution framework (notably, the bail in cascading referred to above) remains in place (Section 7 and Annex 5 to this note provides details on the proposed changes to the TESM).

For further information on the Single Resolution Fund common backstop see [EGOV paper](#) on “Completing the Banking Union”, Section 7 of the [EGOV Briefing](#) prepared ahead of the 22 July 2019 hearing of Elke König, Chair of the Single Resolution Board and EGOV specific briefing on the [ESMT 2019 amendments](#).

Following work on deepening the EMU, the [December 2018 Euro Summit](#) endorsed the Eurogroup proposals to increase the effectiveness of ESM precautionary instruments, detailed in the [draft revised text of the TESM](#) agreed by the Eurogroup on 14 June 2019. The new features of the ESM precautionary financial assistance aim at “*enhancing their effectiveness while ensuring the appropriate level of conditionality*”²⁰. Currently, Article 14 of the ESMT does not draw substantial differences between the two precautionary instruments (i.e. the precautionary conditioned credit line and the enhanced conditions credit line). An [ESM Guideline](#) provides additional details, namely defining the conditions upon which a Member State may have access to one or the other instrument²¹. Article 14 is being extensively revised. Please see separate [EGOV briefing](#) for further details.

²⁰ See Eurogroup PRES [letter](#) of 25 June 2018 to the President of the European Council.

²¹ Access to a precautionary conditional credit line is reserved for Member States where the economic and financial situation is still fundamentally sound. Access to the enhanced conditions credit line is open for an ESM member that does not fully comply with the criteria for accessing the precautionary conditional credit line, but whose general economic and financial situation remains sound. Annex III added to the revised ESMT uses a slightly different wording to characterise the situation of a Member State having access to the precautionary conditioned credit line (“fundamentally strong”). The Guideline will be amended following the revision of the ESMT.

4.2 Collective Action Clauses

In accordance with the Article 12 of TESM, all the securities issued by Euro Area Member States, with maturity above one year and issued after 1 January 2013, must include [Collective Action Clauses](#) (CACs). CACs ensure that the impact of changes to the terms of payment is identical among all the bondholders, once they are decided by qualified majority²². Changes could take the form of a standstill, extension of maturity, interest-rate cut and/or haircut. The [14 December 2018 Euro Summit](#) further decided, as part of the agenda on deepening the Economic and Monetary Union, to introduce single limb CACs²³ by 2022. Single limb CACs facilitate amending the conditions of bonds issued across bond classes, thus facilitating debt restructuring.

A proposal for an amended Recital 12 of the ESMT refers to ESM facilitating the dialogue between the ESM member requesting financial assistance and its creditors, on an “*voluntary, informal, non-binding, temporary and confidential basis*”. The reference to “private sector involvement” currently contained in Recital 12 is now in Recital 12B, slightly amended²⁴. The 2011 version of the ESM Treaty foresaw in Article 12 (2) the need for an effective contribute of the private sector to debt sustainability of an assisted Member State. For further details, see separate [EGOV briefing](#).

4.3 Design and monitoring of conditionality

The design and monitoring of the policy conditions attached to the financial assistance are in principle performed by the Commission, in liaison with the ECB, and wherever possible, the IMF. Despite being outside EU legal framework, the ESM is referred to in Regulation [472/2013](#), which establishes the modalities of the financial assistance to EAMS. The Regulation refers to the ESM in various provisions, notably as a lender, and the ESM is not given any specific mandate or task in financial assistance design or monitoring. Nevertheless, Article 7(12)3rd subparagraph of Regulation 472/2013, and recitals 12 and 18, allow one to infer that the ESM is deeply involved in setting the policy conditions attached to the financial assistance.

In 2016, the ESM BoG initiated an evaluation process of the stability support programmes, to carefully examine the financial support provided in past programmes and to draw lessons, with the aim of increasing their future efficiency and effectiveness. Ms G. Tumpel-Gugerell was appointed as the high-level independent evaluator of the past EFSF and ESM financial assistance programmes and the [report](#) was presented in June 2017 (See Box 3).

Notwithstanding not having a formal role in programme design and implementation, in April 2018 the Commission and the ESM defined in a [Memorandum of Understanding](#) the terms of ESM involvement. The Memorandum is a non-legally binding document, but frames the cooperation between ESM and the Commission in respect, *inter alia*, of ESM's participation in missions and the preparation of Debt Sustainability Analyses²⁵.

In November 2018, the European Commission and the ESM set a [Joint position](#) on future cooperation between the two institutions. The joint position reflects the agreement between the Commission and the ESM on their respective roles in the crisis management framework, as an interim solution pending ESM incorporation in the EU framework. The Joint position builds on and further specifies the MoU previously

²² CACs also deal with a number of procedural aspects that would render the change to the terms and conditions of the bonds possible, namely, relevant majorities, *quorum* and calling of meetings. See the dedicated [web page](#) of the Economic and Financial Committee for detail. See also “[Euro CAC and the existing rules on sovereign debt restructuring in the Euro area: An appraisal four years after the Greek debt swap](#)”.

²³ Single limb CACs allow altering the conditions of various issuances of debt instruments with a single vote across all affected securities. Additional wording is being introduced on the ESMT to address this point (see article 12, point 4).

²⁴ Recital 12 currently reads: “*In accordance with IMF practice, in exceptional cases an adequate and proportionate form of private sector involvement shall be considered in cases where stability support is provided accompanied by conditionality in the form of a macro-economic adjustment programme.*” The amended Recital 12B reads: “*In exceptional cases an adequate and proportionate form of private sector involvement, in accordance with IMF practice, shall be considered in cases where stability support is provided accompanied by conditionality in the form of a macro-economic adjustment programme.*”.

²⁵ DSAs have been a particular focus in the discussions regarding the EMU deepening. The [December 2018 Eurogroup report to Leaders](#) refers to DSA, stating, “*There is broad support for the need to improve the existing framework for promoting debt sustainability in the euro area.*” For further reading on DSAs, please see this [EGOV note](#).

agreed²⁶; it addresses ongoing cooperation and cooperation in the context of designing, implementing and monitoring financial assistance. The Joint position foresees an additional mutual agreement on transparency and accountability, still to be prepared (Annex 3 provides details of both the MoU and the Joint position).

The draft revised ESMT strengthens the role of ESM by allowing it to “*follow and assess the macroeconomic and financial situation of its Members including the sustainability of their public debt and carry out analysis of relevant information and data.*” (Article 3(1)), in order to be able to perform the above-mentioned functions. The draft revised text further specifies the terms of cooperation between the ESM and the Commission, in both the conditionality design and compliance monitoring (see separate [EGOV briefing](#) addressing these issues).

Box 3: Independent evaluation report of ESM financial assistance (June 2017)

At its annual meeting in 2016, the ESM agreed to start an evaluation process of former stability support programmes to carefully examine the financial support provided in past programmes and to draw lessons from them with the aim of increasing the efficiency and effectiveness in the future. In September 2016, Ms G. Tumpel-Gugerell was appointed as the high-level independent evaluator of the past EFSF and ESM financial assistance programmes. In June 2017, she presented an [evaluation report](#), focused on EFSF and ESM financial assistance programmes for Ireland, Portugal, Greece, Spain and Cyprus. She made six recommendations to the ESM BoG:

- 1) the ESM should focus on programme credibility and support ownership;
- 2) programme design should have clear objectives and priorities;
- 3) the programmes should address financial sector issues upfront, but associated disbursements should be phased, based on progress;
- 4) the Board should further refine and develop the ESM governance framework;
- 5) the ESM should enhance programme transparency and evaluability;
- 6) ESM Members may clarify the ESM’s role in euro area institutional development.

The BoG committed to ensure that the report’s findings and recommendations are appropriately followed up to improve future programmes.

5. Lending Activities

The ESM has provided financial support to Spain (for the recapitalisation of its banking system), Cyprus and Greece. All three programmes have ended (Spanish in December 2013), Cypriot in March 2016 and Greek in August 2018), but the three countries still have to repay their loans - the average maturity of ESM loans is much longer (from 12 to 43 years) than the length of the programme, which usually expands over 3 years. The ESM lending activities are summarised in Table 2 below.

The EFSF and ESM [lending rates](#) fully cover their funding and operational costs. The ESM and EFSF have used different funding and lending approaches over time. Over the 4th quarter 2018, the ESM average lending rate was 0.83 %, while EFSF’s was 1.49 %.

²⁶ The MoU mentions that the parties will inform each other in advance of publishing press releases related to their specific competences (post programme missions or Early Warning exercises) and training, which is not reflected in the Joint Position. The Joint position further details the respective roles of Commission and the ESM when analysing requests for access to the ESM precautionary credit lines, building on the principles already established in the MoU.

Table 2: EFSF and ESM lending

Assistance	Start Date	End date	Amount		
			Agreed	Disbursed	Repaid
Ireland (EFSF)	Dec 2010	Dec 2013	€17.7bn	€17.7bn	-
Portugal (EFSF)	June 2011	May 2014	€26bn	€26bn	-
Spanish banking sector (ESM)	Nov 2012	Dec 2013	€41.3bn	€41.3bn	€17.6 bn
Cyprus (ESM)	Apr 2013	Mar 2016	€9 bn	€ 6.3 bn	-
Greece (ESM)	Aug 2015	Aug 2018	€86 bn	€ 61.9 bn	€ 2 bn

Source: [ESM Financial Assistance](#), August 2019

The ESM pricing policy is set out in a [guideline](#), based on article 20 of the TESM. The guideline states that the ESM member receiving financial assistance will pay a Commitment Fee, a Service Fee to cover ESM overheads (operational costs), a Margin (that varies depending on the financing instrument), Issuance costs and other costs and expenses (incurred by the ESM), as well as a penalty interest for overdue amounts. In accordance with the guideline, the ESM retains any capital gains (profit) which is realised under the primary and secondary market support facilities. There are specific provisions in relation to the direct recapitalisation instrument. The guideline also details the interests' calculation methodology.

The ESM has established an [Early Warning System](#) to detect loan repayment risks and allow for corrective actions, in line with article 13/6 of the TESM. The objective is to determine a country's ability to repay its loans. This work requires an assessment of the country's short-term liquidity, market access, and the medium- to long-term sustainability of public debt. It takes into account and complements the fiscal and debt sustainability analysis that the Commission and the ECB perform during and after a programme. To that end, the ESM takes part to missions to the Member States receiving financial assistance carried out by the Commission, together with the ECB and the IMF. Nevertheless, former programme countries are under the ESM Early Warning System until they repay the full amount of their ESM loan, and therefore the ESM monitoring outlives the post-programme monitoring by the European Commission in the context of the EFSM, which expires when the country reimburses 75% of its financial assistance.

6. ESM Accountability and Oversight

Being outside the EU Treaties, the ESM is not subject to the provisions relating to EU institutions, bodies or agencies (e.g. the Commission, the ECB, the European Investment Bank, the European Banking Authority), including provisions on control and oversight (e.g. the [Access to Documents Regulation](#), European Ombudsman, Court of Auditors²⁷, Anti-Fraud Office, European Data Protection Supervisor, the EU Staff Regulations). However, the signatory Member States agreed to submit disputes relating to the interpretation and application of the TESM to the European Court of Justice²⁸.

²⁷ In [November 2012](#), H. Noack, the member of the ESM Board of Auditors appointed by the European Court of Auditors, commented that "However, I consider it part of my duties to keep my colleagues informed about matters which seem relevant. I consider myself bound to keep the European Parliament informed about these matters, and I will also make myself available to interested members of the national authorities of states belonging to the European currency union, as long as this is compatible with my duties as a member of the Board." Likewise, the then [President of the ECA](#), in a hearing organised by the Committee on Budgetary Control, commented on the availability of ECA for expanding its oversight mandate to the stability mechanisms, although acknowledging that the "public external audit arrangements of the ESM are largely promising" and that the ECA would, in any case, monitor the COM in providing financial assistance. In a presentation in October 2014, the [ESM](#) put forward arguments why oversight by the ECA was not necessary.

²⁸ The Treaty allows Member States to agree beforehand that a certain matter related to the subject matter of the treaties is subject to the ECJ (article [273 of the TFUE](#)). As such, EAMs agreed that disputes concerning the TESM arising among the Member States or between the Member States and the ESM would be subject to the ECJ. Article 37 of the TESM details the procedures to be followed, in particular prior discussions and decisions at the level of the BoD and BoG, which, in case of disagreement, can then be submitted to the ECJ.

The ESM is not accountable to the European Parliament (EP)²⁹ either. The Ministers of Finance, composing the ESM BoG, are accountable to their national parliaments. Nevertheless, the EP may invite the President of the Eurogroup to attend an Economic Dialogue in its capacity as President of the Eurogroup, in accordance to Regulation 472/2013, which confers responsibilities to the EP and ECON in overseeing financial assistance granted (See Box 4).

Box 5: European Parliament's role under Regulation 472/2013

- ECON is informed of the measures adopted by the MS in the context of enhanced surveillance and of the quarterly assessment on achieved progress and possible further measures;
- ECON is informed of recommendations to be issued by Council following the Commission's assessment that further measures are necessary; ECON may offer the opportunity to the MS concerned and to the Commission to participate in an exchange of views;
- ECON may invite the Commission, the ECB and the IMF to an economic dialogue in the course of an enhanced surveillance and in the context of a macroeconomic adjustment programme;
- The Chair and Vice Chairs of ECON are informed orally of the progress made in preparation of a draft macroeconomic adjustment programme and of the Commission's monitoring conclusions;
- In the context of post-programme surveillance, ECON is informed of the outcomes of post programme monitoring every six months and may offer the MS concerned an exchange of views;
- EP may invite Commission and ECB representatives to a dialogue on application of the Regulation;
- As the co-legislator, the EP receives reports and proposals on amendments of this Regulation.

Box 4: EP report on the on the role and operations of the Troika

On the ESM, the [report](#) reads (points 104-108) "the EP:

- *Emphasises that the creation of the EFSF and the ESM outside the institutions of the Union represents a **setback in the development of the Union**, essentially at the expense of Parliament, the Court of Auditors and the Court of Justice;*
- *Demands that the **ESM be integrated in the Union's legal framework** and evolve towards a Community-based mechanism, as provided for in the ESM Treaty; demands that it be made accountable to the European Parliament and the European Council, including with respect to decisions to grant financial assistance as well as decisions to grant new loan tranches; acknowledges that as long as Member States make direct contributions from their national budget to the ESM, they should approve financial assistance; calls for the ESM to be further developed, with adequate lending and borrowing capacities, and for the establishment of a dialogue between the ESM board and the European social partners and the integration of the ESM into the EU budget; calls on the members of the ESM, until the above becomes reality, to abstain from the unanimity requirement in the short run in order to allow standard decisions to be taken by a qualified majority rather than by unanimity, and to allow for precautionary assistance to be given;*
- *Asks the Council and the Eurogroup to respect the commitment made by the President of the European Council to negotiate an interinstitutional arrangement with the European Parliament in order to establish an appropriate interim mechanism for **increasing the accountability** of the ESM; calls also in that context for greater transparency in the proceedings of the ESM Governing Council;*

Underlines that the ECJ 'Pringle' case-law and jurisprudence opens up the possibility of bringing the ESM within the Community framework, with a constant Treaty on the basis of Article 352 TFEU; calls, therefore, on the Commission to put forward, by the end of 2014, a legislative proposal with that objective."

In February 2014, the EP adopted a [report](#) on the on the role and operations of the Troika (ECB, Commission and IMF) with regard to the euro area programme countries. The objective of the report was to evaluate the functioning of the Troika in the then ongoing programme countries. It covered the scrutiny of several elements, including the legal base, the mandate and the structure of the Troika; the decision making

²⁹ In its publication on "[ESM: Governance, Transparency and accountability](#)" of October 2018, the ESM claims that it is accountable to the EP (see page 11).

process, the democratic legitimacy, the “theoretical” basis for decisions, as well as the consequences of the Troika work (See Box 5).

Following a letter by the then Greek Prime Minister³⁰, the EP decided to strengthen its efforts to ensure a stronger parliamentary scrutiny of financial assistance programmes. Then the EP established a dedicated [Financial Assistance Working Group \(FAWG\)](#) in 2016.

[Transparency International EU](#) issued in November 2016 a report on [ESM transparency and accountability](#). It recommended increasing ESM transparency, accountability and integrity and made specific proposals. In a [later report](#), dated February 2019, Transparency International addressed the Eurogroup, including its links to the ESM. It recommended to reinforce Eurogroup transparency, accountability and integrity, in particular by applying “*EU transparency acquis*” to the work of the Eurogroup, even when it meets as ESM BoG³¹, by strengthening the accountability of the President of the Eurogroup before the European Parliament, and by establishing a Eurogroup full-time Presidency.

Actually, the ESM’s Managing Director has made himself available for hearings in the EP³². This practice has yet not been formalised, but the Managing Director has expressed his favour for a Memorandum of Cooperation between the ESM and the EP to formalise such hearings (see Box 6). The draft revised ESMT makes a reference to the “current dialogue” between ESM Managing Director and Parliament in recital 7.

Box 6: Extract from K. Regling’s [speech](#) of 29 January 2019

“... let me say a few words about the often-heard criticism that there is a democratic deficit or accountability deficit at the ESM, because the ESM is intergovernmentally organised. The ESM Treaty is an international treaty. The EU Treaty does not mention the ESM.

In the long-term, I am in favour of integrating the ESM into the EU Treaty. I would advocate that the ESM be introduced into the EU Treaty in the same way as the European Investment Bank (EIB). The EIB is an institution with its own capital and a Board of Governors in which the shareholders are represented. The Member States would have the final decision and the involvement of the Bundestag and the other parliaments would be respected.

The ESM recognises the central role of the European Parliament in the public debate on the currency area. That is why I speak voluntarily in the European Parliament, whenever I am invited there for an informal dialogue. I think it is very important to inform the European Parliament about our activities and to discuss them. However, for legal reasons, the ESM cannot enter into an inter-institutional agreement with the European Parliament comparable to the inter-institutional agreements between the European Parliament, the Council and the European Commission.

The reason is that the ESM is legally outside the institutional framework of the EU. The founding document of the ESM was signed by the euro countries and ratified in their parliaments. The Board of Governors, the highest decision-making body of the ESM, consists of the 19 finance ministers of the euro countries. These ministers are accountable to their national parliaments. That is good because the risks of ESM lending ultimately lie with the budgets of the member states. Thus, I do not see a democratic or accountability deficit at the ESM.

We can certainly further develop our relationship with the European Parliament. The possibility of a Memorandum of Cooperation, as currently discussed in the ECON Committee, seems to be a good option.”

In its [resolution](#) on the Establishment of the European Monetary Fund adopted in March 2019, the EP “*proposes the establishment of a protocol for an interim Memorandum of Cooperation (MoC) between the ESM and Parliament, with immediate effect, to improve interinstitutional dialogue and enhance the ESM’s transparency and accountability, specifying the rights of Parliament and its Members as regards questions put to*

³⁰ On 19 August 2015, Mr. Tsipras, then Greek Prime Minister sent a letter to the President of the European Parliament requesting the Parliament stronger involvement in the regular review process in implementing the adjustment programme.

³¹ See the Transparency International EU paper on “[Vanishing act: the Eurogroup accountability](#)”, p. 14 and 18 (“*In the context of financial assistance/ macroeconomic adjustment programmes in particular, the Eurogroup gained substantial new powers. In its incarnation as the Board of Governors of the ESM, the Eurogroup is no longer merely an informal body but takes, under a different legal framework, formal decisions with far-reaching consequences for entire countries.*”).

³² On 16 May 2013, K. Regling has also attended, upon invitation, the Conference of Presidents of the EP. He then took part in workshops and hearings organised by the EP (e.g. on 25 May 2016, on [15 January 2014](#), on [24 September 2013](#)).

the reformed ESM, regular hearings, nomination rights and appropriate budgetary control rights; recalls its request for an interinstitutional arrangement for economic governance; stresses that the Managing Director of the reformed ESM should be elected by and report to the European Parliament, following a proposal by the Council; urges that gender balance be ensured in the composition of the reformed ESM governing bodies; (point 17). Box 7 presents a possible content of such an agreement - in light of existing agreements among European institutions³³ - if the EP wishes to further advance discussions.

Box 7: Possible content of an agreement between the EP and ESM

In the case the EP and the ESM would decide to start negotiations on the co-operation agreement between them and bearing in mind current practice of cooperation agreements among institutions, and in full respect of the respective competences, the agreement could cover issues^(a) such as the following:

- Reporting on activities, namely, providing a broad overview of the work carried out and oral presentation of activities, on an annual basis^(b);
- Exchange of information^(c) and ESM presence in Parliament (either ordinary hearings or *ad hoc*, specific appearances^(d)) and answering to questions within the ESM scope of activities^(e);
- Access to information^(f), including confidential information and adequate procedures to handling confidential information, provided either orally or in written format, as well as procedures and mechanisms to handle breaches to the obligation of confidentiality^(g);
- Further cooperation arrangements, namely in the context of EP Inquiry Committees^(h).

^(a) The agreement could also cover provisions of administrative or procedural nature, such as date of application, modifications and revisions, etc.

^(b) See Point 1 of the agreement between the EP and the SRB as well as in Point 1 of the agreement between the EP and the ECB. The provisions cover extensively the content of the annual report to be presented at the EP, as well as the delay in which it is to be sent to Parliament and an obligation of disclosing the report.

^(c) The main objective of the MoU between the SRB and the ECB referred to is, indeed, the exchange of information between the two institutions for adequate performance of their respective responsibilities and avoidance of duplicative burdens on institutions.

^(d) The EP agreement with the SRB has a detailed explanation of the modalities, calendar and confidentiality requirements for such hearings in point 2. See also, in a similar vein, Point 2 of the Agreement between EP and the ECB.

^(e) The Agreement of EP with the SRB covers this aspect in point 3; likewise, the agreement with the ECB covers this matter in point 3.

^(f) Access to information is covered in point 4 of the Agreement between EP and the SRB.

^(g) Recital N of the Interinstitutional Agreement between the EP and the ECB invites the EP to establish an adequate framework to follow up on any case of breach of confidentiality by its Members or staff. Likewise, recital N of the Interinstitutional Agreement between the EP and the SRB also calls for mechanism.

^(h) Point III of the Agreement between EP and the SRB, as well as Point III of the Agreement with the ECB.

7. Suggestions on possible evolution of the ESM as part of the debate on EMU governance

The on-going debate on possible new roles for the ESM has recently intensified. With no remaining on-going financing programme, the ESM appears to be in a less active phase than at the peak of the crisis³⁴.

³³ The following agreements could be considered as examples: [Interinstitutional Agreement](#) between the European Parliament and the European Central Bank on the practical modalities of the exercise of democratic accountability and oversight over the exercise of the tasks conferred on the ECB within the framework of the Single Supervisory Mechanism; [Interinstitutional Agreement](#) between the European Parliament and the Single Resolution Board on the practical modalities of the exercise of democratic accountability and oversight over the exercise of the tasks conferred on the Single Resolution Board within the framework of the Single Resolution Mechanism; [Memorandum of Understanding](#) on the working relations between the European Commission and the European Stability Mechanism; the [Memorandum of Understanding](#) between the Single Resolution Board and the European Central Bank in respect of cooperation and information exchange. The legal framework, scope and objectives of these agreements are very different: the first two have a clear legal basis in Union legislation, the two MoUs formalise agreements reached between the institutions subject to *bona fide* execution, but not legally binding. It is worth mentioning that [Regulation \(EU\) No 468/2014](#) of the European Central Bank on the framework for cooperation within the Single Supervisory Mechanism refers to the Interinstitutional Agreement between the EP and the ECB in the introduction.

³⁴ E.g. ESM staff produces [Working papers](#) and [Discussion](#) papers on many topical issues.

- Already in 2015, the [Five Presidents' Report](#) had proposed the integration of the ESM in the EU law framework by 2025. The Commission followed up with the publication of the Reflection Papers on the [Deepening of the Economic and Monetary Union](#) (in May 2017) and the [Future of EU Finances](#) (in June 2017).
- The EP provided its opinion through various contributions, including its resolution of February 2014 on the Troika (see Box 5), as well those of 16 February 2017 on: i) budgetary capacity for the euro area ([2015/2344\(INI\)](#)); ii) possible evolutions of and adjustments to the current institutional set-up of the European Union ([2014/2248\(INI\)](#)) and iii) improving the functioning of the European Union building on the potential of the Lisbon Treaty ([2014/2249\(INI\)](#)). More specifically, in its [resolution](#) on “Budgetary capacity for the euro area”, the EP stressed the need for the European Monetary Fund to be equipped with adequate lending and borrowing capacities and a clearly defined mandate: “...*The ESM, while fulfilling its ongoing tasks, should be further developed and turned into a European Monetary Fund (EMF) with adequate lending and borrowing capacities and a clearly defined mandate, to absorb asymmetric and symmetric shocks.*”
- In December 2017, the Commission set out a [Roadmap for deepening the Economic and Monetary Union](#), including a legal proposal for a Council Regulation establishing a European Monetary Fund (EMF) under the EU legal framework³⁵. According to the [proposed Regulation](#), the EMF would become a Union body integrated in the EU legal framework, [based on](#) Article 352 of the [TFEU](#). The proposal is subject to the consent³⁶ of the EP, which adopted an interim [resolution](#) in March 2019. In April 2018, the ECB published its [Opinion](#) on the Commission proposal: while generally supporting the proposal, the ECB required some clarification on the competences, and object the proposed name, as it would misleadingly make citizens to think that the EFM would have competences in monetary affairs. The justification (to create a “European IMF”) does not take into account the historical and global context of the IMF³⁷. Annex 4 to this note provide details.
- In an [interview](#) of April 2018 K. Regling, Managing Director of the ESM, expressed his preference for an ESM reform in line with the European Investment Bank (EIB) statute³⁸.
- At its meeting in [December 2018](#), the Eurogroup - in its inclusive format - agreed on several initiatives relating to the deepening of the EMU. Ministers did not refer to the draft Council Regulation on the EMF proposed by the Commission, but envisaged changes made through amendments to the ESM Treaty. Ministers agreed on a [Term sheet on the ESM reform](#), which referred to:
 - the [terms of reference of the common backstop to the Single Resolution Fund](#) (SRF);
 - the precautionary instruments, for which the ex ante eligibility criteria are to be made more transparent and predictable;
 - debt sustainability issues, including: the inclusion of single limb Collective Action Clauses; the possibility for the ESM to facilitate the dialogue between Member State and its private investors (in case of sovereign debt crisis and upon request by the relevant Member State); conditionality on debt sustainability (“repayment capacity”);
 - the [agreement](#)³⁹ reached by the Commission and the ESM on “future cooperation between the European Commission and the ESM”.
- At the [Euro Summit](#) of 14 December 2018, Leaders endorsed all the elements of the Eurogroup report on EMU deepening, claiming “*This comprehensive package paves the way for a significant strengthening of the EMU*”. In particular, the Euro Summit asked the Eurogroup to prepare the necessary amendments to the ESM Treaty (including the common backstop to the SRF) by June 2019.
- On 14 June 2019, the Eurogroup broadly agreed the [draft revised text of the ESM Treaty](#), including its [Annexes](#) III (on the Precautionary Conditional Credit Line) and IV (on the backstop facility to the SRF).

³⁵ An EGOV paper provides a detailed [comparison between the main features of the ESM and those of the proposed EMF](#).

³⁶ Under the consent procedure, the EP cannot propose amendments, but only accept or rejects the proposed text.

³⁷ An EGOV document provides a [comparison between the ESM's and IMF's](#) main features.

³⁸ An EGOV document provides a comparison between the main features of the [ESM and the statute of the EIB](#).

³⁹ See Section 4.3 and Annex 3.

- In June 2019, the Commission published its [Communication](#) on “Deepening Europe’s Economic Monetary Union: Taking stock four years after the Five Presidents’ report”, where it recognises that there is no political will to integrate the ESM into the EU legal framework at this stage: “The ongoing revision of the Treaty establishing the European Stability Mechanism, as an intermediate solution, is meant to further strengthen crisis prevention and resolution in the euro area. It should neither duplicate tasks with EU institutions nor add to the complexity of the economic surveillance framework”. The Commission also notes that “(..) the Court of Justice has underlined the responsibility of the Commission as guardian of the Treaties for monitoring the application of the framework of the European Stability Mechanism in practice and for helping to ensure that fundamental rights of individuals are fully protected in this context”. The Commission also highlights some critical elements in the new draft provisions of the ESM Treaty. In particular, referring to Article 18A, it notes, “it is important that the responsibilities of the European Stability Mechanism are clearly defined and do not overlap or create frictions with the EU institutions and bodies that have been tasked to supervise banks or manage bank crises. Most importantly, the reform of the Treaty establishing the European Stability Mechanism must not create obstacles to future amendments of EU legislation, which would give rise to fundamental problems affecting the autonomy of the EU legal order. The EU’s banking legislation must remain open to further developments in accordance with the Community method to adjust to changing market circumstances and complete the Banking Union” (p. 10). Furthermore, in the chapter on “The way forward”, the Commission states, “In addition, a euro-area Treasury could take shape, to access financial markets on behalf of its members to fund part of their regular refinancing needs. The euro-area Treasury could bring together existing competences and services that are today scattered across different institutions and bodies, including the European Stability Mechanism, after its integration into the EU legal framework.”
- At the Euro Summit of [21 June 2019](#), leaders welcomed the progress on made in the Eurogroup on the strengthening of the Economic and Monetary Union and stated “We expect the Eurogroup to continue its work so as to allow for an agreement on the full package in December 2019”.

On the possible evolution of the ESM and its tools, the EP has published the following papers, written by external experts:

- [A European Monetary Fund](#), Charles Wyplosz, The Graduate Institute Geneva;
- [An evolutionary path towards a European Monetary Fund](#), Daniel Gros, Center for European Policy Studies;
- [An evolutionary path for a European Monetary Fund? A comparative perspective](#), Jonathan A. Rodden, Stanford University.
- [Debt Sustainability Assessments: The state of the art](#), Giancarlo Corsetti, University of Cambridge;
- [Debt Sustainability Assessments: The state of the art](#), Cinzia Alcidi Daniel Gros, CEPS

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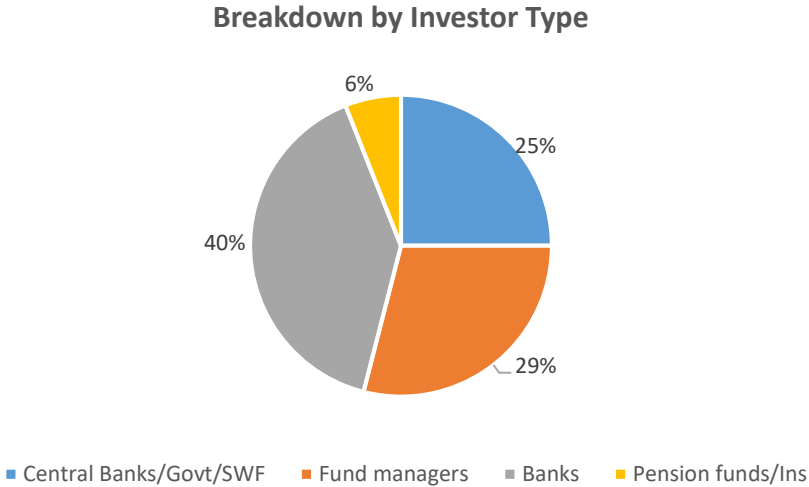
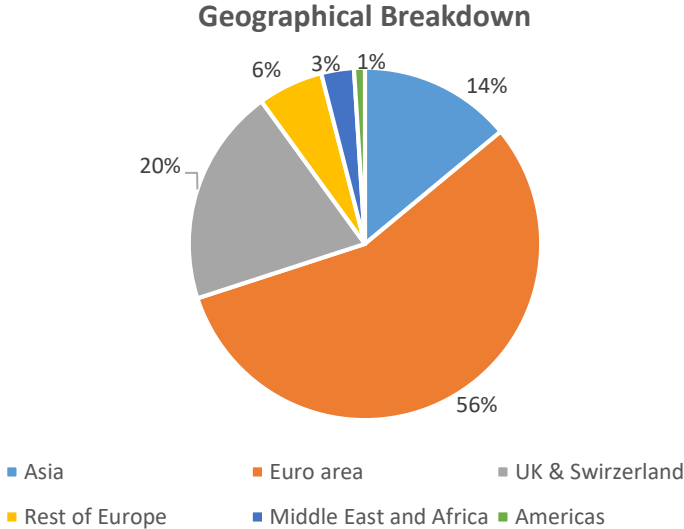
Annex 1: Capital Contribution of ESM Members

Member	ESM Key (%)	Capital Subscription (€bn)	Paid-in capital (€bn)
Austria	2.7644	19.48	2.23
Belgium	3.4534	24.34	2.78
Cyprus	0.1949	1.37	0.16
Estonia	0.1847	1.30	0.15
Finland	1.7852	12.58	1.44
France	20.2471	142.70	16.31
Germany	26.9616	190.02	21.72
Greece	2.7975	19.72	2.25
Ireland	1.5814	11.14	1.27
Italy	17.7917	125.40	14.33
Latvia	0.2746	1.93	0.22
Lithuania	0.4063	2.86	0.33
Luxembourg	0.2487	1.75	0.20
Malta	0.0726	0.51	0.06
Netherlands	5.6781	40.02	4.57
Portugal	2.4921	17.56	2.01
Slovakia	0.8184	5.77	0.66
Slovenia	0.4247	2.99	0.34
Spain	11.8227	83.33	9.52
Total	100	704.80	80.55

Source: [ESM website](#)

Note: Paid-in capital refers to the final amount once all of the five instalments have been paid.

Annex 2: Who Buys ESM Bills and Bonds (ESM Investors)



Source: [ESM investor presentation](#), p. 35, August 2019

Annex 3: Cooperation between the European Commission and the ESM

- [Memorandum of Understanding between the European Commission and the ESM \(April 2018\)](#)

After recalling the objectives leading to its signature, the [MoU](#) presents its scope and framing, as well as the general principles of cooperation. The MoU specifically mentions the possibility of ESM staff participating in missions related to economic policy coordination and budgetary monitoring, in agreement with the Member States concerned.

The MoU envisages bi-annual meetings between the ESM Managing Director and the Commissioners responsible for Financial Stability and Economic and Financial Affairs, aimed at discussing and reviewing the cooperation arrangements.

Point 3 of the MoU addresses the working arrangements in the framework of financial assistance and post-programme surveillance. In particular, the MoU details the respective competences of the Commission and the ESM, pointing to a close cooperation between the two institutions. The MoU specifies: *“The ESM will mainly contribute in those areas where it has particular policy expertise and which relates to its responsibility of providing financial assistance”*: e.g., in the context of a debt sustainability analysis, *“the Commission prepares fiscal and macroeconomic projections and the ESM provides inputs on Member States funding plans and costs”*. When monitoring compliance with the conditionality and financial conditions of the financial assistance, the ESM takes part in joint missions. The MoU also requests bilateral exchanges of information and alerts, when the Commission or the ESM issue reports or documents related to missions.

The MoU foresees in Point 4 the operational arrangements for mutual access to information and confidentiality requirements. In Point 5, the MoU specifies on the intentions to provide joint training and to organise common events. The MoU was [signed](#) in Sofia on 27 April 2018.

- [The Joint position on “Future cooperation between the European Commission and the ESM” \(June 2018\)](#)

The [Joint position](#) builds on and further specify the MoU previously agreed; it addresses cooperation outside financial assistance and in the context of designing, implementing and monitoring financial assistance.

Cooperation outside financial assistance:

- Informal meetings to share assessments and analysis pertaining to their respective competences as well as to discuss and assess macro-financial risks;
- If appropriate, ESM staff can joint Commission missions related to economic policy coordination and fiscal monitoring (with the agreement of the concerned Member State);
- on a reciprocal basis, the Commission and the ESM will share data, analysis and assessments while respecting applicable Union law and confidentiality obligations and the ESM’s funding activities.

Cooperation in the context of designing, implementing and monitoring financial assistance:

- In assessing [eligibility for a precautionary credit line](#), the Commission will be in charge of the overall assessment of the Member State’s economic situation and policy track record in line with the applicable EU macro-economic and fiscal surveillance framework (in particular SGP and MIP) and the ESM will assess market access of the Member State concerned and the risks thereto;

- In preparing a [financial assistance decision](#):

- o Commission and ESM (and ECB) will work closely together;
- o Commission ensures consistency with the Union’s economic policy coordination framework and measures adopted in that context;
- o ESM performs its analysis and assessment from the perspective of a lender;
- o The Commission, (in liaison with the ECB,) and the ESM collaborate on the preparation of the assessments of beneficiary’s repayment capacity and [debt sustainability analysis \(DSA\)](#);
- o For the preparation of a DSA (which is mandatory in all circumstances), the Commission works mainly on the basis of its growth forecasts and estimates, and the ESM analyses mainly Member State’s funding plans and cost of funding. In case the collaboration does not yield a common view, [the Commission will make the overall assessment of the sustainability of public debt, while the ESM will assess the capacity of the Member State concerned to repay ESM loans](#);
- o The Commission and the ESM assess [financing gap and needs](#); the Commission will provide projections for the budgetary path, and the ESM will focus on medium- and long-term debt redemption;

- Assessment of financial stability risks will be done by the Commission, in liaison with the ECB; ESM will contribute from the perspective of sovereign bond markets and aspects related to sovereign financing;
- The Commission (with the ECB) and the ESM collaborate on the design and negotiation of policy conditionality, preserving Commissions' role and competences under the Treaties; ESM contributes from its perspective as a lender; the Commission and the Managing Director of the ESM will sign the MoU detailing the conditionality. The Commission in close cooperation with the ESM, will determine the goals and expected impact of reform measures in relation to the financing needs, return of the Member State to the markets and maintaining its repayment capacity.
- The Commission in close cooperation with the ESM (and in liaison with the ECB), will monitor compliance of policy conditionality during the financial assistance; tasks and responsibilities will be shared along the same lines as in financial assistance preparation;
- Article 14 of Regulation (EU) 472/2013 and the ESM Early Warning System set the framework for post programme monitoring. Post-programme surveillance missions and EWS missions are, in principle, combined.

- **Common methodological working document on Debt Sustainability Analysis**

At its meeting of 8 July 2019, the [Eurogroup](#) agreed to continue work to finalise the package related to the revision of the ESM Treaty by December. This includes *"the common methodological working document on Debt Sustainability Analysis. We invited the Commission and the ESM to start working on the latter as soon as possible. We will strive to make significant progress on these issues by November."*

Annex 4: Commission's proposal for a Council Regulation establishing the European Monetary Fund

On 6 December 2017, the Commission published its [Proposal for a Council Regulation on the establishment of the European Monetary Fund](#) as part of the Roadmap for deepening the Europe's Economic and Monetary Union. The proposed EMF *"will be established as a unique legal entity under Union law. It will succeed the European Stability Mechanism, with its current financial and institutional structures essentially preserved. This means that the European Monetary Fund will continue to provide financial stability support to Member States in need, to raise funds by issuing capital market instruments and to engage in money market transactions. The membership will not change and the participation of additional Member States will remain possible, once they adopt the euro"* (p. 5).

All its discretionary decisions will be **endorsed by the Council**, according to the Meroni doctrine⁴⁰.

In addition to the current pre-reform ESM functions, the proposed EMF will have the following **four new features**:

1. **Common backstop to the Single Resolution Fund (SRF)**, with a ceiling of EUR 60 billion, increasable, in the form of credit lines or guarantees. The backstop would be fiscally neutral over time, since any funds used would be recovered from the banking sectors in the Member States participating in the Banking Union.
2. **Management of financial assistance programmes**: a more direct EMF involvement alongside the Commission. Any reference to the involvement of the IMF is removed from the statute.
3. **Possible new financial instruments**: the EMF shall be able in the future to develop new financial instruments, e.g. a macro-economic **stabilisation function** of Member States whose currency is the euro. A stabilisation function is the possibility to rapidly activate resources in an automatic way subject to eligibility criteria defined in advance. Member States should first activate their national automatic stabilisers and discretionary fiscal policy in compliance with the Stability and Growth Pact (SGP); if not sufficient, the stabilisation function would be triggered.
4. **A fast decision-making voting procedure**, with four types of voting rules:
 - unanimity, for decisions having a major direct financial impact on Member States (e.g. decisions on the lending capacity, on capital calls not urgently needed);
 - reinforced qualified majority (85%), for decisions related to granting financial support, disbursement and the deployment of the backstop;
 - qualified majority (80%); and
 - simple majority.

In specific urgent situations, the EMF's Board of Governors (BoG) can take decisions that will be transmitted immediately to the Council, which will have 24 hours to discuss them and object, adopting another decision, or to refer the matter back to the BoG, which will respect the reasons given by the Council. A consultative role in the **appointment process of the Managing Director has been foreseen for the EP**.

The EMF will be accountable to the Council, the Commission, the EP, with the submission of an annual report, hearings, oral and written questions, confidential discussions behind closed doors, and to national parliaments that will be able to invite the Managing Director and submit oral and written questions.

The ECON co-rapporteurs (Vladimír Maňka and Pedro Silva Pereira, both S&D) have put forward their [report](#) on the Commission proposal on 22 November 2018. ECON voted the [draft report](#) in 26 February 2019 and [Plenary](#) adopted it in 14 March 2019. The final text (a) proposes to retain the name of ESM (the draft report proposed renaming the EMF as European Stability Fund, to avoid confusion with ECB monetary policy mandate), (b) calls for an interim strengthening of ESM without losing sight of its future integration in the Community method, (c) concurs with the Commission in giving the ESM a more prominent role in managing financial assistance without impinging on Commissions' responsibilities, and (d) calls on the establishment of *"a protocol for a Memorandum of Cooperation (MoC) with the European Parliament, with immediate effect, to further promote institutional dialogue and enhance the ESM's transparency, accountability and democratic legitimacy in line with the further deepening of interinstitutional cooperation on the economic governance of the euro area"*.

⁴⁰ The Meroni doctrine, which arose from Cases 9/56 and 10/56 ([Meroni v High Authority \[1957/1958\] ECR 133](#)), relates to the extent to and conditions under which EU Institutions may delegate their tasks to regulatory agencies.