European Commission - Press release

Stability and Growth Pact: Commission issues guidance to encourage structural reforms and investment

Strasbourg, 13 January 2015

The European Commission has presented today detailed new guidance on how it will apply the existing rules of the Stability and Growth Pact to strengthen the link between structural reforms, investment and fiscal responsibility in support of jobs and growth.

The guidance, which the Commission will apply as of now, has three key aims:

1. Encourage effective implementation of structural reforms;
2. Promote investment, specifically in the context of the new European Fund for Strategic Investments (EFSI) (see press release IP/15/3222);
3. Take better account of the economic cycle in individual Member States.

This guidance also serves to develop a more growth-friendly fiscal stance in the euro area.

The Communication follows the commitment President Jean-Claude Juncker made in his Political Guidelines, on the basis of which the Commission was elected by the European Parliament. Respecting the Pact, while making the best use of the flexibility which exists within its rules, was also the focus of discussions of the June 2014 European Council.

The Commission now gives Member States additional certainty on how it will apply the Pact. Equal treatment of all Member States and predictability of the rules are at the core of the Pact.

Valdis Dombrovskis, Vice-President for the Euro and Social Dialogue, said: "*The Stability and Growth Pact is the cornerstone of European economic governance. We are making sure it is applied in an intelligent, effective and credible manner. With today's guidance on the use of flexibility within the Pact, we aim to facilitate structural reforms and investment so necessary to spur growth and create more jobs in Europe. At the same time, we are making sure the commonly agreed rules are followed*."

Pierre Moscovici, Commissioner for Economic and Financial Affairs, Taxation and Customs, said: *"Fiscal responsibility is a necessary but not a sufficient condition for jobs and growth. We also need to pursue structural reforms and step up investment. The smarter application of the Stability and Growth Pact that we are announcing today will help us to make more decisive progress on all three fronts."*

1. Clarifications regarding structural reforms

The Commission will take into account the positive fiscal impact of structural reforms. This applies to different degrees both, to Member States respecting the Treaty's 3% of GDP deficit and 60% of GDP debt reference values (preventive arm of the Pact), and to those that do not (corrective arm of the Pact, in other words countries subject to an Excessive Deficit Procedure).

For Member States in the preventive arm of the Pact, the Commission will take account of the impact of reforms (the so-called "structural reform clause"), provided that they (i) are major, (ii) have verifiable long-term positive budgetary effects, including by raising potential sustainable growth, and (iii) are implemented. Reform measures adopted by the government and/or the Parliament may also qualify "ex ante" if Member States have presented a dedicated structural reform plan with well-specified measures and credible timelines for their adoption and implementation.

The Commission will assess the reforms before recommending to the Council to allow possible temporary deviations from the medium-term budgetary objective (MTO) or the fiscal adjustment path towards it. Such deviations should not exceed 0.5% of GDP. An appropriate safety margin must be preserved so that the 3% of GDP deficit reference value is respected. The MTO should be reached within four years of the clause being activated.

When opening an Excessive Deficit Procedure, the Commission may recommend a longer deadline for the correction of the excessive deficit provided that a dedicated structural reform plan as described above also exists. For countries in Excessive Deficit Procedure, which have made the required fiscal effort but need more time to reach the 3% reference value, the Commission may recommend giving a longer extension to the correction deadline provided that a dedicated structural reform plan as

described above also exists.

The Commission will closely monitor the reforms and will propose necessary action if Member States fail to implement them.

2. Clarifications regarding investment

A favourable treatment for national contributions to the EFSI

In its Investment Plan for Europe, published last November, the Commission already indicated that it would take a favourable position under the Pact towards national contributions to the EFSI, for which the Commission also adopted a legislative proposal today. The Commission now makes good on its commitment by stating that Member State contributions to the EFSI will not be counted when defining the fiscal adjustment under either the preventive or the corrective arm of the Pact. In the case that the reference value of a 3% deficit is not respected, the Commission will not launch an Excessive Deficit Procedure if it is due to the contribution, provided the deviation is small and expected to be temporary. When assessing respect of the debt criterion, contributions to the EFSI will not be taken into account.

A more accessible and clearly defined "investment clause"

The Commission has provided guidance in the past on how to consider public investments under the Pact. Today's Communication specifies and formalises this guidance (commonly referred to as the "investment clause"). It clarifies that Member States in the preventive arm of the Pact can deviate temporarily from their medium-term budget objective or from the agreed fiscal adjustment path towards it, in order to accommodate investment, under the following conditions:

1. Their GDP growth is negative or GDP remains well below its potential (resulting in an output gap greater than minus 1.5% of GDP);
2. The deviation does not lead to non-respect of the 3% deficit reference value and an appropriate safety margin is preserved;
3. Investment levels are effectively increased as a result;
4. Eligible investments are national expenditures on projects co-funded by the EU under the Structural and Cohesion policy (including projects co-funded under the Youth Employment Initiative), Trans-European Networks and the Connecting Europe Facility, as well as co-financing of projects also co-financed by the EFSI.
5. The deviation is compensated within the timeframe of the Member State's Stability or Convergence Programme (Member States' medium-term fiscal plans).

3. Clarifications regarding cyclical conditions

To better take account of the ups and downs in the economic cycle, the Commission will use as of now a matrix that specifies the appropriate fiscal adjustment expected from countries under the preventive arm of the Pact. This means that Member States will be required to make a larger fiscal effort during better times and a smaller fiscal effort during difficult economic times.

For countries which are in the corrective arm and thus subject to the Excessive Deficit Procedure, the Commission has developed a new approach to assessing the delivery of the required structural fiscal effort, which the ECOFIN Council endorsed in June 2014. This helps to disentangle as much as possible those budgetary developments that can be assumed to be under the control of the government from those linked to an unexpected fall in economic activity.

Next steps

The Commission is not proposing any changes to the existing rules. Therefore, no legislative steps are needed and the Commission will apply the new guidance immediately.

The Commission will enter into a dialogue with Member States and the Council to provide any necessary explanations ahead of forthcoming milestones, notably the presentation of the Stability/Convergence Programmes and National Reform Programmes expected in spring 2015.

The Commission will also present this Communication to the European Parliament.

In addition, the Commission will involve stakeholders at all levels to define further steps towards the deepening of the Economic and Monetary Union. The Euro Summit of 24 October invited the President of the Commission, in close cooperation with the President of the Euro Summit, the President of the Eurogroup and the President of the European Central Bank, to prepare next steps on better economic governance in the euro area. As agreed by the December European Council, a report on these matters should be presented to heads of state and government by latest June 2015. As part of its Work Programme for 2015, the Commission has committed to take further steps towards pooled sovereignty in economic governance.

For more information see:

MEMO/15/3221

The Commission Communication

Stability and Growth Pact website

IP/15/3220

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