The preamble to the Treaty on European Union defines the general guiding objectives of economic policy as the “convergence of their economies” and the “economic and social progress for their peoples, taking into account the principle of sustainable development”. The fundamental problem with the economic governance framework is that it is not designed to manage these goals, but primarily to avoid excessive budget deficits (and – since the Six Pack – macroeconomic imbalances), as if with medium term balanced budgets these goals would be achieved automatically (despite decentralised economic). That this is not the case was shown by the dynamics following the economic crisis in 2008. This threatens to manifest itself again in the economic crisis triggered by CoViD-19.

Europe needs a new economic governance reform tailored to modern economic conditions that puts the sustainable development of prosperity and well-being at the centre. Over the last 30 years, unemployment and global warming have become pressing structural problems. And when we talk about price stability today, it is much more about fighting deflation than inflation. All in all, the right framework must now be set, based on the Sustainable Development Goals (SDGs) and the work of the OECD and scientists such as Joseph Stiglitz, which led to Council conclusions for an “Economy of Wellbeing” at the European level. With the “Green Deal” initiative, the current EU Commission is already moving in the right direction, especially with its new four-dimensional approach, which is similar to our proposal for a new magic polygon of well-being oriented economic policy. Now it is important to align this approach even more coherently with the key objectives, to make it more concrete and actually relevant as a steering mechanism – especially in the country-specific phase of the European Semester.

Budgetary policy will continue to play a central role in this process. But it will no longer be reduced to the avoidance of “excessive” deficits, but as an essential instrument of a balanced, well-being oriented economic policy in general and of economic cycle management in particular. Rules that give priority status to the maintenance of a certain deficit value are counterproductive in this context and should be replaced by a guideline – only indicative, but all the clearer – for structural revenue and expenditure trends. This requires a treaty reform, which should also be used to give the EU Parliament, or some form of euro area parliament, formal co-decision powers, to regulate the Eurogroup and to eliminate unilateral economic policy definitions (including 119, 123, 125 and 126 TFEU). The current crisis in particular shows us once again how dangerous inflexible regulations are. Rather than cementing a particular policy, the EU treaties must provide rules that allow for a democratic debate on the best solution at the cutting edge.

The minimum requirements for a reform are:

1. Assets and liabilities should be treated symmetrically – for example, by means of a golden investment rule whereby the permissible limits for new debt (debt accumulation) are only controlled minus the net public investment (asset accumulation).

2. The existing elements of flexibility should be applied more generously in practice so that debt reduction is not at the expense of other important goals – such as full employment or climate protection. This must also apply to countries in an excessive deficit procedure.

3. At the European level, more resources must be made available to contribute to effective fiscal and economic governance (as is currently the case with the newly created Recovery and Resilience Facility).

4. Cooperation between Member States on common objectives should be strengthened, whether in the narrower sense of fiscal policy (a fiscal stimulus that is appropriate to the economic situation), ecological investments or to ensure appropriate taxation of transnational companies;
or in a broader sense to increase prosperity and well-being in a sustainable manner.

5. **Decisions** need to be taken more democratically and transparently, to make it more likely taking into account the interests of the majority:

   - All areas of European economic policy (including the individual phases of the European Semester) should be co-decided by either the European Parliament or a form of euro area parliament.

   - The Eurogroup should become more transparent, firstly by publishing the positions of the national ministers and secondly by publishing at least part of the preparatory work by the so-called Euro Working Group.

   - The economic governance of the euro area should place particular importance on the ex-ante involvement of social partners. A form of macroeconomic dialogue for the euro area and the general strengthening of social dialogue are therefore needed. In addition, civil society groups in general – for example in the form of the European Economic and Social Committee – are to be involved more closely.
The evaluation should be used for a reform into a more active, cost-effective, coordinated and democratic economic governance framework. The growing awareness of the need to make green and social investments, to focus economic policy on prosperity and well-being, to increase democratic legitimacy of European decisions on the fiscal policies of the Member States and, finally, the public debate launched by the Commission itself, gives rise to hopes that the debate will not be decided once again behind closed doors of the Eurogroup.

**Consensus: better EU fiscal rules needed**

There are many good reasons for a renewed reform of the European fiscal rules – especially in times of crisis when interest rates are historically low. There seems to be a consensus to reduce large number of detailed rules existing side by side with even more detailed exceptions and made more responsive to the economic cycle and simplified. There is also broad agreement on strengthening the European level and paying particular attention to public investment, after reaching historic lows in the last decade: Since 2012, net public investment in the euro area as a whole was negative in sum, i.e. the accumulation of public sector assets came to a standstill. However, not only climate targets require significantly higher investments.

It should be noted that the establishment of the euro area was accompanied by a loss of national scope for economic policy-making. Fiscal policy became the central instrument of European policy that remained at the national level. Based on the notion that the economy would function better the more the state was pushed back, fiscal policy was reduced to avoid excessive deficits. The crucial questions of how euro member states could counteract an economic crisis, how they could coordinate their budgetary policies to achieve the highest possible and convergent levels of prosperity and well-being, or how parliaments could exercise their basic democratic rights, were not on the agenda at the time. However, today it is clear that these issues are central to any form of economic governance.

What are the problems with this type of budgetary policy?

This setting led to the expected problems. First, unexpected economic downturns also lead to unintended short-term overshooting of the fiscal rule limits. The expenditure cuts that are often decided as a result then further weaken the economy and place an additional burden on public budgets due to the lack of public revenues and higher costs for unemployment. The most striking older example was Germany from 2001 onwards, whose government at the time (together with that of France) subsequently pushed through a well-founded, albeit complex reform of EU fiscal rules. More recent examples were the southern member states after the "Great Recession", which – after a fundamentally sensible initial reaction applying national economic stimulus packages with the active support of the EU Commission – were forced by fiscal rules, discretionary troika decisions and unbridled financial markets to adopt a harsh austerity course – with fatal economic and social consequences.

Second, general fiscal pressures tend to lead to a decline in the expenditure that is most easily postponed or cut in the short term: public investment. However, these are particularly relevant to the economy as a whole and create lasting assets that contribute significantly to collective prosperity and well-being. The climate crisis and the gradual reorientation of policy in this regard are directly related to this: Social goals go far beyond economic growth and fiscal policy must do more than prevent excessive deficits.

But instead of correcting these mistakes, the fiscal rules were actually tightened with the Six and the Two Pack. There was a gradual shift away from this policy from summer 2013 onwards due to the obviously negative effects of austerity, which was reinforced by the more flexible handling of EU fiscal rules from January 2015 onwards. But this new pragmatism is not enough. Fiscal governance remains misguided, although temporarily masked by the simultaneous onset of the economic upswing, which nevertheless brought deficits and debt ratios down. However, with the economic crisis triggered by CoViD-19, the fundamental problem is now
becoming urgent again. A rapid return to growth is not to be expected – and this threatens a new wave of austerity policy as soon as application of the exemption clause is terminated. Instead of a “return” to the previous rules, a reversal in the form of an improved economic governance framework is necessary.

1. How can the framework be improved to ensure sustainable public finances in all Member States and to help eliminate existing macroeconomic imbalances and avoid new ones arising?

The so-called sustainability of public finances is a shortened target that needs to be expanded. In general, the task of public finances is to ensure stable government activity geared to sustainable prosperity and well-being for all citizens, and in particular to stabilise economic activity, especially employment and investment. The necessary financing must be ensured, usually through sufficient revenues. Herein lies the first problem of economic governance, because it focuses too much on the balance, but largely omits the very decisive taxation options. This applies in particular to safeguarding the tax base for profit- and asset-based taxes and curbing international tax competition, especially competition by unfair means.

The avoidance of excessive deficits as a contribution to the availability of cheap financing on the capital markets makes sense as one objective among many, but it is not an absolute priority standing in isolation from current economic, social and environmental challenges. Not only does it lose sight of other aspects of stable and stabilising government activity, but also of the fact that negative feed-back effects (such as a decline in employment and demand due to expenditure cuts) can paradoxically jeopardise the objective even if it is apparently combated with particular vigour.

Although the last governance reform took this analysis partially into account by including macroeconomic imbalances in the framework, the way in which these are dealt with has not proved to be effective. Their definition remains unclear and in practice – above all in the scoreboard – their application is one-sidedly fixed on the empirically questionable concept of price competitiveness – and thus a permanent weakening of aggregate wage and therefore demand trends in the monetary union as a whole. The fact that the procedure for avoiding and correcting macroeconomic imbalances in its current form has not been able to develop any great relevance for steering the economy is therefore not simply negative.

In order to improve the economic governance framework in the future, the focus must be placed on general guiding objectives. In particular, the objectives “convergence of their economies” and “economic and social progress for their peoples, taking into account the principle of sustainable development”, as stated in the preamble to the European Treaties, should be mentioned. The work on the “Wellbeing Economy”, the SDGs or that of Joseph Stiglitz and others (most recently within the OECD) can be used as a starting point for practical implementation as well as the current flagship initiative “Green Deal”. In particular, the four new dimensions of an “Economy that Works for People and the Planet”, which are broadly in line with our proposal for a new magic polygon of well-being oriented economic policy, is already moving in the right direction.

![Magic polygon](quellen-AK)
The important thing is now to align this approach even more closely with the key objectives, to make it more specific and actually relevant within the economic governance framework – especially in the country-specific phase of the European Semester.

Fiscal policy will continue to play a central role in this process. However, it must no longer be reduced to the avoidance of “excessive” deficits, but rather as an essential instrument of a balanced, well-being oriented economic policy in general and of economic cycle management and a high level of investment in particular.

Institutional changes are also required along these guidelines for content orientation. In future, all economic policy decisions – for example in the context of the European Semester – should no longer be possible without parliaments at the European and national levels. Fiscal councils should be merged with the productivity boards and developed into councils for the sustainable development of prosperity and well-being, with their members nominated not by governments but by parliaments and civil society, especially the social partners. These changes would not make the process any easier, but more transparent and legitimate – and therefore probably more effective.

2. How to ensure responsible fiscal policies that safeguard long-term sustainability, while allowing for short-term stabilisation?

As stated in the answer to the previous question, the contribution of fiscal policy to long-term sustainability is much broader than compliance with certain values for the debt level or the balance of public finances. In light of the ever more pressing issue of the Earth overheating and employment prospects for all, a sufficient level of investment or a growing public capital stock is at least as important a criterion. The fact that fiscal sustainability is mainly measured by the reference value for gross debt of 60 % of GDP is a largely arbitrary and overly restrictive benchmark that needs to be changed or at least widened and weakened. It was a cardinal error of the last governance reform that this reference value was actually revalued with the so-called 1/20 rule.

The question is also misleading because it suggests a trade-off between sustainability and stabilisation. However, sustainable public finances cannot exist without economic stability. The latter must therefore be given priority. As within the EMU monetary and exchange rate policy is not available at the national level for macroeconomic management, fiscal policy is an especially important tool to foster economic stabilisation. Making the fiscal policy guidelines more flexible in line with the economic situation in 2015 was a first step in the right direction, although it has not been enough.

The best solution would be to expand the scope of national fiscal policy and to limit it only by a single clear benchmark for structural expenditure developments, depending on long-term average real economic growth plus the ECB’s target inflation rate, adjusted for discretionary revenue decisions and net investment (golden rule for public investment). This benchmark should be defended strongly in the public debate with good arguments, but should not be enshrined in law, because this would counteract an honest and qualified debate, as recent years have shown impressively. Planned shortfalls are also a problem for the sustainable development of prosperity and well-being and should be addressed as well as overruns. In view of the pressure to maintain strict fiscal rules, the proposal by the Institute for Macroeconomics and Business Cycle Research (IMK), which stipulates mandatory compliance with the ceiling for government expenditure growth above a gross debt level of 90% of GDP, could be taken up as a compromise. In this sense, the economic governance framework reform must be on the agenda in the context of the planned debate on the “future of the EU”, without discarding treaty changes. However, in the short term we need to move closer to our proposed benchmark solution. Here, too, a step in the right direction has already been taken with the stronger focus on the expenditure rule at the end of 2018. Further steps should include the following measures:

• A better accounting of public investment, by including only the depreciations (instead of only averaging the nationally financed investments over four years).

• Expansive measures to stabilise employment should not be regarded as structural expenditure.

• If fiscal rules are suspended due to a severe economic downturn for the euro area or the Union as a whole, fiscal rules should at least not take effect again until unemployment falls significantly. (This change is particularly important in view of the economic crisis triggered by CoViD-19 in order to avoid overly rapid and harsh consolidation steps from 2022 at the latest.)

• The estimation method to calculate the cyclical component should be changed to simple long-
term averages, as they, although less convincing in theory, prevent model-driven shocks and are much easier to manage and communicate.

- The multiplier effect of discretionary measures should be taken into account in the ex-ante surveillance of budgetary policies.

Aside from fiscal rules, two steps are needed to improve the stabilisation of the economy and the sustainability of national public finances: First, the scope for fiscal policy action at the European level needs to be expanded. The new Recovery and Resilience Facility is a milestone in this respect, even if the planned disbursement is too slow to quickly stabilise investment and employment. Secondly, the refinancing of public finances must be safeguarded better. It is precisely in times of crisis that the financial markets themselves enter crisis mode – and are thus clearly unsuitable for stable financing options that are particularly important at that point. Once again, the European Central Bank is acting quickly and adequately in the current crisis. In view of the loss of efficiency resulting from the ban on primary market intervention and its mandate which is generally too narrowly defined, appropriate treaty amendments would have to be sought in the medium term.

3. What is the appropriate role for the EU surveillance framework in incentivising Member States to undertake key reforms and investments needed to help tackle today and tomorrow’s economic, social, and environmental challenges while preserving safeguards against risks to debt sustainability?

The economic governance framework should above all promote an honest and well-informed discussion on the sustainable development of prosperity and well-being. The more broadly the process is organised and the more varied the interests bundled into an overall package capable of winning majority support, the more promising the process will be.

Consequently, Member States also need the material means to implement this. Fiscal rules – especially in the form of the proposed golden rule for investment – and financing possibilities are key to this; support from the EU budget is helpful.

In this regard, the current governance framework functions only to a limited extent:

- Instead of focusing on sustainable prosperity and well-being – based on a comprehensive social, ecological and economic perspective – the focus is often on economic policy that is one-sidedly geared to GDP growth, competition and austerity.

- The process is technocratic and not very participatory: Neither the European Parliament nor the national parliaments play a decisive role. Social partners and other key stakeholders are consulted at best, and divergent opinions are often not given sufficient space. The focus is on the European Commission's own analyses, which are intended to preserve the appearance of the only objectively right thing.

- In the country-specific second half of the semester, the pan-European orientation is often lost, although this is precisely what could be a particular added value of the EU Commission's country reports compared to similar analyses in the respective country itself. For example, the country analyses rarely mention what can be done in the individual Member States for a wage, investment or budget policy that is recommend for the euro area. Instead, the report is often reduced to how the individual country performs in relation to other individual states or certain standards.

- As far as material possibilities are concerned, the EU budget has been too limited and static so far to be able to set specific current priorities in motion. At the same time, the financial and economic crisis in 2008 limited national room for manoeuvre – and further restricted it by relying on market discipline plus more rigid fiscal rules. It has also failed to stimulate innovative cooperation projects – for example, that countries with current account surpluses finance productive investment projects in countries with high foreign debt (e.g. for the Green Deal).

With its assumption of office and now in the economic crisis triggered by CoViD-19, the EU Commission has taken some steps in the right direction. These steps must be intensified in the next cycle of the European Semester.13 For example, the Green Deal should be given even greater focus and the analysis should be geared more strongly to the SDGs – especially in the country-specific phase. In order to increase legitimacy, the EU Parliament should be involved in formulating the basic orientation and recommendations. ECOFIN and the Eurogroup should become more transparent, on the one hand by making the positions of the national ministers public, and on the other hand by publishing at least part of the preparatory work by the so-called Euro Working Group. In addition, civil society groups – for example in the form of the European Economic and Social Committee – are to be involved more closely.
4. How can one simplify the EU framework and improve the transparency of its implementation?

Fiscal rules offer an important starting point for simplification. As mentioned above, these should be limited to a single reference value that is used both in the corrective and the preventive arm of the SGP. Their calculation and analysis is complicated enough – although necessary to meet the specific circumstances of each case.

In terms of transparency, we identify two main deficits:
First and of particular importance, the decisions taken in the Council bodies. The positions of the national ministers must be comprehensible and the preliminary work of the working group must be published at least in part so enable a public debate at national level in advance. This is particularly true for the Euro Working Group.

Second is the selection and weighting of country-specific problems in the context of the country reports or the procedure to address macroeconomic imbalances. Based on the SDGs or a framework for assessing the sustainable development of prosperity and well-being, European problem areas should first be identified and addressed, which then need to be addressed in the country-specific phase together with country-specific challenges. Transparency is to be achieved above all through homogeneous procedures, explanation and public respectively parliamentary debate.

5. How can surveillance focus on the Member States with more pressing policy challenges and ensure quality dialogue and engagement?

No special focus on individual countries is necessary in the European Semester. What is missing is the focus on the European level as a whole and specification of national contributions if, for example, a wage or budget policy that is recommendable from a pan-European perspective is to be implemented.

6. How can the framework ensure effective enforcement? What should be the role of pecuniary sanctions, reputational costs and positive incentives?

The economic governance framework should above all promote an honest and well-informed discussion on the sustainable development of prosperity and well-being. Financial sanctions are counterproductive in this regard because they prevent an honest debate and are also unrealistic because infringements are particularly likely to occur in bad times, when nobody wants to make a financial emergency worse. The illusion of market discipline is similar: in good times, it has little disciplinary effect; in bad times, it has an additional destabilising effect.

Moreover, the years following the Great Recession showed that monetary sanctions often hit those governments that are trying to improve the situation. It is a misguided illusion to believe that states, like a neoclassical homo economicus, can be influenced through incentives or sanctions. In democracies, the sanctioning of incompetent governments is the exclusive preserve of the electorate – and the more effective this mechanism is in Europe, the greater the likelihood that European sanctions will harm the wrong people, especially newly elected governments. This may even have the effect of restoring governmental responsibility to the very parties that were responsible for any previous mistakes.

In order to make the discussion process more effective, bilateral escalations between the EU Commission and national governments should be avoided. This requires more European voices in national public debates, well-founded decisions involving parliaments and social partners or other civil society actors and the scientific community, and more debate on national policies in the Council itself. Successful policies bear fruit in the medium term and encourage further steps – no additional financial incentives are needed, but sometimes additional financing is needed.
7. Is there scope to strengthen national fiscal frameworks and improve their interaction with the EU fiscal framework?

In general, the task of public finances is to ensure stable government activity geared to sustainable prosperity and well-being for all citizens, and to stabilise economic activity, especially employment and investment. Instead of further narrowing national fiscal policy, the framework conditions at both levels should be changed to better enable these tasks to be carried out. For example, by ensuring these objectives are firmly anchored in the legal framework and in the political processes and by means of new institutions, such as councils for the sustainable development of prosperity and well-being.

These councils for the sustainable development of prosperity and well-being should replace fiscal councils and productivity boards, but they should address both issues comprehensively as an integral part of well-being oriented economic policy. At the European level, there should also be such an advisory body, whose analysis could be the conclusion of the past semester and the informal start of the new European Semester. Although the members of the Council should be academics, they should cover a wide range of subjects and be nominated by the EESC and the European Parliament.

8. How should the framework take into consideration the euro area dimension and the agenda towards deepening the Economic and Monetary Union?

The analysis for the EU or the euro area in particular should be the focal point and the country-specific part should be more strictly oriented towards it. This applies in particular to fiscal policy recommendations, where the sum of the country-specific recommendations should be consistent with the fiscal stimulus recommended for the euro area as a whole. A similarly concrete coordination process should be sought for the other policy areas, such as CO2 reduction targets, wage policy coordination, the reduction of the aggregate current account balance, etc.

With regard to the agenda for intensifying the EMU, lessons can be drawn from the current crisis, for example by making instruments such as the Recovery and Resilience Facility more permanent in the sense that they will be available again in similarly severe crises – with fewer political conflicts. In addition, it would be useful to create an investment stabilisation function that would provide, within the framework of the EU budget, a permanent higher level of investment to promote sustainable and convergent development of prosperity and well-being in the EU.

It is also important to strengthen the legitimacy of the decisions by involving the European Parliament or some form of euro area parliament. Since the current treaty foundations for EU economic policy (especially Art. 121 and 126 TFEU) do not explicitly provide for co-decisions by the EU Parliament, the treaties will have to be amended in order to achieve full co-decision options. Intensification must also go hand in hand with strengthening the social dimension, for example with a "Protocol for Social Progress" at the level of EU primary law. Those principles include, for example, the primacy of fundamental social rights, including trade union rights, market freedoms, strengthening of the principle of equal pay and equal working conditions for equal work in the same place, in particular in the context of effectively combating wage and social dumping and ensuring the autonomy of social partners. For a democratic economic and budgetary policy at the EU level, all neo-liberal stipulations (including 119, 126, 123 and 125 TFEU) in the Treaties must also be deleted. The current crisis has demonstrated once again how dangerous the inflexibility of these regulations is. Rather than cementing a particular policy, the EU treaties must provide rules that allow for a democratic debate on the best solution at the given time. The completion of the banking union is an important building block for a stable EMU and will help to reduce fiscal risks for Member States. However, the path towards a common deposit guarantee scheme, which in itself makes sense, requires a structural reform of the banking sector to prevent deposit guarantee instruments from being used for investment banking risks. The idea of risk weighting government bonds is also dangerous, as it could undermine the objective of safer and therefore cheaper bonds (see last paragraph of the answer to question 2). Instead, it would make sense to create a European "safe asset", which could represent a decisive step towards Europeanisation of the banking market and also represent an important instrument for common monetary policy.

9. Within the context of the European Semester, how can the SGP and the MIP interact and work better together, so as to improve economic policy coordination among Member States?

As stated before, both should be part of a broader framework focussing on sustainable development of prosperity and well-being.
Footnotes

01 The positioning is largely based on the ETUI Working Paper “Towards a progressive EMU fiscal governance” (https://www.etui.org/publications/working-papers/towards-a-progressive-emu-fiscal-governance), which was developed together with economists close to the trade unions from euro area heavyweights Germany, France, Spain and Italy as well as Greece and Ireland.

02 For example, the work of the OECD "High Level Expert Group on the Measurement of Economic Performance and Social Progress": https://www.oecd.org/statistics/measuring-economic-social-progress/


05 Cf. the options for more fiscal leeway in the ETUI Working Paper cited above (Table 1, p. 15).


11 Dullien et al. (2020): Proposals for a reform of the EU’s fiscal rules and economic governance. IMK Report 159e: https://www.imk-boeckler.de/de/faust-detail.htm?sync_id=8946


The Austrian Federal Chamber of Labour (AK) is by law representing the interests of about 3.8 million employees and consumers in Austria. It acts for the interests of its members in fields of social-, educational-, economical-, and consumer issues both on the national and on the EU-level in Brussels. Furthermore the Austrian Federal Chamber of Labour is a part of the Austrian social partnership. The Austrian Federal Chamber of Labour is registered at the EU Transparency Register under the number 23869471911-54.

The main objectives of the 1991 established AK EUROPA Office in Brussels are the representation of AK vis-à-vis the European Institutions and interest groups, the monitoring of EU policies and to transfer relevant information from Brussels to Austria, as well as to lobby the in Austria developed expertise and positions of the Austrian Federal Chamber of Labour in Brussels.