Questions and Answers on the Economic Governance Review

Brussels, 2 May 2024

Entry into force of the new economic governance framework fit for the future

1. What are the main objectives of the new economic governance framework?

The main objectives of the new economic governance framework are to strengthen debt sustainability and promote sustainable and inclusive growth in all Member States through growth-enhancing reforms and priority investments. The framework will help make the EU more competitive and better prepared for future challenges by supporting progress towards a green, digital, inclusive and resilient economy, also bolstering Europe’s security capacity.

The reforms seek to ensure that the framework is simpler, more transparent and effective, with greater national ownership and better enforcement. They take into account the need to reduce increased public debt levels, including as a result of the COVID-19 pandemic, in a realistic, gradual and sustained manner. The new framework also builds on the lessons learned from the EU policy response to the financial crisis where a lack of investment hampered a swift economic recovery.

2. How do the reforms ensure that EU fiscal rules are fit for the challenges ahead?

The new economic governance framework has been designed to help tackle both existing and new challenges. It recognises that both prudent fiscal strategies as well as investments and reforms that enhance sustainable growth are not only indispensable, but also mutually reinforcing.

The revised EU economic governance framework will contribute to making Europe more resilient, by enabling strategic investment and reforms, and by reducing high public debt ratios in a realistic, gradual and sustained manner.

3. What are the main changes in the new economic governance framework?

The new economic governance framework aims to strengthen public debt sustainability, taking into account the need to reduce much-increased public debt levels, and enhance sustainable and inclusive growth through investment and reforms in a way that preserves national ownership. The framework will be simpler and take into account Member States’ different fiscal challenges.

The central elements of the new framework are:

- **Stronger national ownership with national medium-term fiscal-structural plans** that bring together fiscal, reform and investment policies of each Member State, within a common EU framework. These reforms and investments should help build the green, digital and resilient economy of the future and make the EU more competitive.

- **Simpler and more transparent rules, with fiscal adjustment paths** formulated in terms of multi-year expenditure targets which ensure that public debt diminishes or stays at prudent levels and that deficits stay below 3% of GDP.

- More gradual fiscal adjustment paths if underpinned by credible reform and investment commitments that foster sustainable and inclusive growth in line with EU priorities.

- **Enhanced enforcement and common safeguards** as a counterpart to the greater leeway for Member States to set their fiscal adjustment paths.

- New EU-wide minimum standards for independence and technical capacity and tasks for national Independent Fiscal Institutions as well as a comply-or-explain principle for national authorities regarding recommendations by those institutions.

4. When will the new framework into force?

The European Parliament and the Council formally adopted the legislation in April 2024. The new
framework entered into force on 30 April 2024.

5. **How will the new framework contribute to adequate levels of public investment to secure common EU priorities?**

The main objective of the new framework is to promote sustainable and inclusive economic growth and to ensure that public debt levels remain sustainable. It recognises that, in addition to fiscal consolidation, reforms and investment are crucial to promote growth and reduce debt, and that they are needed to address common challenges, in particular the green and digital transition, social and economic resilience, energy security and the build-up of defence capabilities.

The new framework encourages the implementation of investment and reforms in a number of ways:

- **Member States will have more realistic adjustment requirements** compared to the old framework:
  - **Member States with low fiscal challenges** (in general meaning debt below 60% of GDP and deficit below 3% of GDP) will be able to spend more than under the old framework if they so wish.
  - **Member States facing fiscal challenges** will have to ensure that their debt is put on a downward path or stays at prudent levels and/or that their deficit is brought or remain below 3%. However, they will have the option to do this in a more gradual way if they commit to implementing certain investment and reform measures that address common EU priorities and that address country-specific recommendations issued in the context of the European Semester. In that case, the adjustment period (i.e. the timeframe within which, through a combination of fiscal adjustments, reforms and investments, a Member State’s debt level is put on a sustainable downward path) can be extended from four to up to seven years. The new framework also strengthens the enforcement regime to ensure these commitments are delivered by the Member States.

- The new framework introduces a **single operational indicator**, namely the growth rate of net expenditure, for assessing Member States’ compliance with the new rules. This indicator is not affected by fluctuations in revenues and unemployment expenditure that are due to economic circumstances.
  - That is to say, if tax revenues are lower due to slower economic growth, Member States do not need to cut expenditure to compensate for the lower revenues. Similarly, if unemployment rises and expenditure on unemployment benefits increases, Member States will not have to spend less on other policies. This means that Member States will be able to better support their economies during more difficult economic periods.
  - At the same time, when revenues increase quickly thanks to strong economic growth or windfalls, Member States will have to use those revenues to build up fiscal buffers for later. cannot use these temporary revenues to deliver an adjustment nor finance any permanent measures.
  - The single indicator is defined as government expenditure net of new revenue measures, such as new taxation measures. This means that Member States can choose to spend more than the expenditure ceiling if this additional spending is financed by new revenue measures. The system therefore does not limit Member States' ability to increase public spending where they so choose, so long as the increase in public spending is properly financed.

- The new framework **protects national expenditure on programmes co-financed by the EU** by excluding such expenditure from the main indicator of fiscal monitoring.
  - This means that national expenditure on investment projects co-financed by the EU can be increased without affecting compliance with the EU fiscal rules.
  - Conversely, Member States will no longer have an incentive to reduce expenditure on such investment projects to achieve their fiscal targets.

6. **How will the new framework ensure sustainable and sound public finances? What safeguards are contained in the new rules to ensure sustainable debt reduction?**

The new framework introduces risk-based surveillance which differentiates between Member States based on their individual fiscal situations. This approach will adhere to a transparent common EU framework underpinned by safeguards to ensure that debt is put on a downward path (the debt sustainability safeguard) or to provide a resilience margin below the Treaty deficit reference value of 3% of GDP in order to create fiscal buffers (the deficit resilience safeguard).

**For Member States with a government deficit above 3% of GDP or public debt above 60%**
of GDP, the Commission will issue a country-specific "reference trajectory". This trajectory will provide guidance to Member States to prepare their plans, and will ensure that debt is put on a plausibly downward path or stays at prudent levels.

**For Member States with a government deficit below 3% of GDP and public debt below 60% of GDP**, the Commission will provide **technical information** to ensure that the deficit is maintained below the 3% of GDP reference value over the medium term. This will be done at the request of the Member State.

7. **Will the 3% of GDP deficit threshold and the 60% of GDP debt threshold be maintained under the new framework?**

The Treaty reference values of 3% of GDP for the deficit and 60% of GDP for public debt will **remain unchanged**.

If the planned or observed deficit exceeds the 3% of GDP reference value, it will trigger the preparation of a Commission report based on Article 126(3) of the Treaty and an Opinion by the Economic and Financial Committee based on Article 126(4) of the Treaty.

Moreover, the new framework aims to ensure a realistic, gradual and sustained debt reduction path when debt is above the 60% of GDP reference value, and at the same time ensure that the framework is credible and conducive to sustainable growth.

8. **Will the excessive deficit procedure change under the new framework?**

The **excessive deficit procedure (EDP)** for **government deficit breaches of the 3% of GDP reference value** remains unchanged. As previously announced, the Commission will propose to the Council to open deficit-based excessive deficit procedures in spring this year. As a first step, in the context of the European Semester Spring Package scheduled for 19 June 2024, the Commission will prepare a 126(3) report for these Member States.

The excessive deficit procedure for **public debt breaches of the 60% of GDP reference value** is strengthened in terms of activation and abrogation. It will focus on departures by Member States with public debt above 60% of GDP from the net expenditure path that the Member State has committed to and which was endorsed by the Council under the preventive arm of the Stability and Growth Pact. When the balance of the control account exceeds certain numerical thresholds and the Member State’s debt is above 60% of GDP, the Commission must prepare a report under Article 126(3) TFEU to assess whether a debt-based EDP should be opened, unless the budgetary position is close to balance or in surplus. Substantial public debt challenges would be a key relevant factor in such a report.

9. **How will the Commission’s reference trajectories take account of Member States’ public debt challenges? When will the Commission publish these?**

For Member States with public debt above the 60% of GDP reference value or a government deficit above the 3% of GDP reference value, the Commission will issue reference trajectories for the net expenditure path. This reference trajectory will cover the default adjustment period of four years of the national medium-term fiscal-structural plan, and its possible extension by a maximum of three years. Its purpose is to provide guidance to Member States when they design their net expenditure path that will be included in their medium-term fiscal-structural plan.

The reference trajectory will be differentiated for each Member State and will take into account its public debt challenges. In particular, it will ensure that:

- the **public debt ratio** is put on a plausibly downward path or stays at prudent levels;
- the **government deficit** is brought and maintained below the 3% of GDP reference value;
- the projected **public debt ratio** decreases by a minimum annual average, in line with the debt sustainability safeguard;
- convergence towards a **common resilience margin** relative to the deficit reference value of 3% of GDP is achieved;
- a **minimum fiscal adjustment** of 0.5% of GDP per year as a benchmark will have to be implemented so long as the deficit remains above 3% of GDP;
- the **fiscal effort** over the horizon of the plan is linear and at least proportional to the total effort over the entire adjustment period.

For Member States with both a government deficit below the 3% of GDP reference value and public debt below the 60% of GDP reference value, the Commission will provide technical information on
the structural primary balance necessary to ensure that the government deficit is maintained below
the 3% of GDP reference value. This will be done at the request of the Member State.

10. Will the general escape clause be maintained under the new framework?

The general escape clause will be maintained under the new framework and activated in case of a
severe economic downturn in the EU and/or the euro area.

The clause allows Member States to undertake measures to deal adequately with a crisis, while
departing from the budgetary requirements that would normally apply under the EU fiscal
framework.

The general escape clause will also be strengthened with the Council now deciding whether to
activate or prolong the application of the clause and setting related time limits, based on a proposal
from the Commission.

11. How will the medium-term plans work in practice?

New medium-term fiscal structural plans are at the centre of the new framework. Member States will
design and present plans setting out their fiscal targets, priority reforms and investments, and
measures to address any possible macroeconomic imbalances during a fiscal adjustment period. The
'adjustment period' refers to the timeframe within which, through a combination of fiscal
adjustments, reforms and investments, a Member State's debt level is put on a sustainable
downward path and the deficit is brought down to or remains below the reference value.

These plans will then be assessed by the Commission and endorsed by the Council, based on
common EU criteria.

Integrating fiscal, reform and investment objectives into a single medium-term plan will help to
create a coherent and streamlined process. It will strengthen national ownership by providing
Member States with greater leeway in setting their own fiscal adjustment paths and reform and
investment commitments. Member States will present annual progress reports to facilitate more
effective monitoring and enforcement of the implementation of these commitments.

12. How will the medium-term fiscal-structural plans be agreed and can they be rejected?
What will the Council's role be in this process?

Before the submission of the plan, there will be an in-depth technical dialogue with the Commission.
The Commission will also put forward for Member States with government debt exceeding 60 % of
GDP or the deficit exceeding 3 % of GDP a reference multiannual adjustment path in terms of net
primary expenditure .

Once the plan is submitted, the Commission will assess it on the basis of common, transparent
methodologies. The Commission will retain the possibility of seeking additional information or
requesting a revised plan. After the Commission has assessed the medium-term plan, the Council
can either endorse it or recommend that the Member State resubmit the plan.

Once the plan has been endorsed by the Council, it should be respected for annual national budgets
for the whole period covered by the plan, which is four or five years depending on the length of the
national legislature. The plan can only be revised if there are objective circumstances preventing its
implementation, or in the case of a newly appointed government.

13. What are the changes to the Macroeconomic Imbalance Procedure?

The new approach to the implementation of the Macroeconomic Imbalances Procedure (MIP) under
the new economic governance framework did not require any legislative changes. It seeks to foster a
MIP with a stronger forward-looking approach.

A first objective is to classify imbalances in a more dynamic way. In practice, this means that
more focus will be placed on whether risks appear to be decreasing or increasing, and on the policies
that are needed to remedy imbalances, when deciding if imbalances exist and when assessing
whether imbalances have been corrected.

The second objective is to reinforce the preventive role of the MIP. In practice, both the first
screening for imbalances in the Alert Mechanism Report (AMR) and the assessment of whether
imbalances exist in the In-Depth Reviews (IDRs) will be made more forward-looking to detect and
address emerging imbalances early on. The AMR may propose more IDRs to be carried out than what
has been the case in recent years, if the first screening provided by the AMR suggests that risks of
imbalances may exist.
There will be a **strengthened dialogue between the Commission and Member States on macroeconomic challenges**. This dialogue will aim to foster greater national ownership through a better common understanding between Members States and the Commission of the challenges identified under the MIP and the policies needed to address them. That should lead to a firm commitment from Member States to include the measures to prevent or correct imbalances in their medium-term fiscal-structural plan. At the same time, enforcement is being stepped up as no implementation of those measures in the plans could lead to escalation of the procedure, namely the opening of the excessive imbalance procedure.

Finally, the new framework seeks to give **more visibility to the EU and euro area dimensions of imbalances**. A first visible change is the inclusion of the readings for the EU and the euro area for all MIP scoreboard indicators. Stronger EU and euro area dimensions of imbalances will highlight vulnerabilities affecting the EU and the euro area as a whole, and the respective contribution of the various Members States to those issues.

**14. How does post-programme surveillance change under the new framework?**

The economic governance review found that while the framework for post-programme surveillance generally worked well, the application should be more focussed and streamlined. In particular, post-programme surveillance should focus on the following objectives:

- Assessing the repayment capacity of Member States through considering the economic, fiscal and financial situation;
- Monitoring the implementation of unfinished reforms that begun under the adjustment programme; and
- Assessing whether corrective measures are needed in the context of concerns for repayment capacity or continued market access.

In light of these objectives, the intensity of post-programme surveillance should evolve over time and with the assessment of risks:

- Initial years of surveillance would be more intense, notably to monitor the implementation of unfinished reforms agreed within the adjustment programme, with the intensity decreasing once reforms are implemented.
- In 'normal' times, post-programme surveillance would focus on assessing repayment capacity and could be streamlined where repayment risks are assessed to be low, also through a better integration with other surveillance tools.
- In case the economic, fiscal or financial situation were to deteriorate, post-programme surveillance would again increase in intensity and assess whether corrective measures were needed.

**15. How will the new framework affect the European Semester?**

This new fiscal surveillance process will be embedded in the existing European Semester, which will remain the central framework for economic and employment policy coordination.

All Member States will be required to address the priorities identified in the country-specific recommendations issued in the context of the European Semester in their medium-term fiscal-structural plans. These plans will merge the current Stability and Convergence Programmes with the National Reform Programmes. They will need to take into account Member States’ recovery and resilience plans during the lifetime of the Recovery and Resilience Facility to ensure policy consistency.

Member States will report annually on progress with the implementation of these commitments and on the actions taken to address the country-specific recommendations. The Commission will monitor delivery of those national commitments closely.

**16. How will the fiscal-structural plans interact with the Recovery and Resilience Plans during the lifetime of the Recovery and Resilience Facility?**

The fiscal and structural policies put forward in the medium-term fiscal-structural plans should be consistent with Member States’ recovery and resilience plans. In particular, the structural reforms and investment envisaged in the recovery and resilience plans up to 2026 should be an integral part of the new plans.

Member States’ commitments under the recovery and resilience plans will be taken into account for extensions of the fiscal adjustment period under the first vintage of the plans.
17. **How will these changes simplify the economic governance framework?**

The new economic governance framework will simplify processes and procedures in several ways:

- **First**, **fiscal surveillance will now focus on a single operational indicator**, namely the Member State's multi-year net expenditure path, as endorsed by the Council. This path will serve as a basis for carrying out annual fiscal surveillance over the lifetime of the Member State's medium-term fiscal-structural plan. Several provisions from the previous framework, such as the debt reduction benchmark, the medium-term budgetary objective and the significant deviation procedure are repealed.

- **Second**, **annual monitoring by the Commission will be less burdensome for Member States**. Instead of proposing annual fiscal policy recommendations, the Commission will focus on Member States' compliance with the multi-year net expenditure path. Member States will need to submit annual reports focussing on implementation instead of annual Stability or Convergence Programmes and National Reform Programmes.

- **Third**, **the reform will simplify enforcement procedures**, which will mostly be triggered by deviations from the agreed net expenditure paths for "debt-based" excessive deficit procedures, with the procedure staying unchanged in case of deficits in excess of 3% of GDP.

18. **How do the reforms enhance national ownership of the economic governance framework?**

The new economic governance framework seeks to enhance national ownership by **empowering Member States to design and present their own medium-term fiscal-structural plans** setting out their fiscal targets, priority reforms and investments, and measures to address any possible macroeconomic imbalances over a minimum period of four years.

The new **risk-based surveillance framework gives Member States more flexibility** to set their adjustment paths.

It also **envisages an important role for independent fiscal institutions (IFIs)**.

- All EU Member States - not just those of the euro area - will be required to have an IFI. These institutions will have to assess, produce or endorse the macroeconomic forecasts underlying the government's annual and multiyear budgetary plans and monitor compliance with the national fiscal rules. These changes will help trigger more debates at national level on national fiscal plans resulting in a higher degree of national ownership.

- The new framework also envisages a role for IFIs in the fiscal surveillance at EU level. Eight years after the entry into force of the preventive arm Regulation, IFIs will be required to assess the macroeconomic forecasts underlying the medium-term fiscal-structural plans.

- At the request of a Member State, IFIs may also be tasked with assessing ex-post annual compliance with the expenditure path and analyse the factors that if not, what could explain any deviation.

19. **How will the new framework help citizens?**

The new economic governance framework is a means to an end. Ultimately, it seeks to support jobs, growth, investment, social fairness and macroeconomic stability, for the benefit of all EU citizens.

Facilitating reforms and investment while improving debt sustainability will ensure the EU is ready to face both existing and new challenges. These challenges include building a green, digital, inclusive and resilient economy that offers protection and opportunities for every EU citizen.

Finally, sound public finances help to keep financing costs low, facilitating private investment and consumption that helps spur growth and create jobs.

20. **What are the next steps under the new framework?**

The Commission will present the European Semester Spring 2024 Package on 19 June. As part of this package, the Commission will present reports under Article 126(3) TFEU, indicating for which Member States the Commission will propose to the Council to open deficit-based Excessive Deficit Procedures (EDPs).

It will also provide guidance to Member States on the content of their medium-term fiscal-structural plans and the annual progress reports that they will need to submit. The technical dialogues with Member States will begin after the Commission has provided these inputs.

Member States must prepare and present their medium-term plans by 20 September 2024, which
will need to be implemented as of 2025. The Commission will begin assessing the plans immediately after the submission and should publish its assessment within six weeks of receiving the plans. This deadline can be extended by a further two weeks if necessary.

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