European Commission
Economic and Financial Affairs

Six-pack? Two-pack? Fiscal compact? A short guide to the new EU fiscal governance

Economic and fiscal governance in the EU and the euro area has been fundamentally strengthened in the recent months. And the work is ongoing. Please find below an explanation of the main building blocks.

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What are the main features of the "six-pack" and the Treaty on Stability, Coordination and Governance (TSCG)?

SIX-PACK

- Entered into force on 13 December 2011;
- Five Regulations and one Directive (that is why it is called six-pack);
- EU secondary law;
- Applies to 27 MS with some specific rules for "euro-area Member States", especially regarding financial sanctions;
- The six-pack does not only cover fiscal surveillance, but also macroeconomic surveillance under the new Macroeconomic Imbalance Procedure.
- In the fiscal field, the six-pack strengthens the Stability and Growth Pact (SGP). According to the SGP Member States' budgetary balance shall converge towards the country-specific medium-term objective (MTO) - so-called preventive arm - and the general government deficit must not exceed 3% of GDP and public debt must not exceed 60% of GDP (or at least diminish sufficiently towards the 60% threshold). The six-pack reinforces both the preventive and the corrective arm of the Pact, i.e. the Excessive Deficit Procedure (EDP), which applies to Member States that have breached either the deficit or the debt criterion.
    - The six-pack ensures stricter application of the fiscal rules by defining quantitatively what a "significant deviation" from the MTO or the adjustment path towards it means in the context of the preventive arm.
    - Moreover, the six-pack operationalizes the debt criterion, so that an EDP may also be launched on the basis of a debt ratio above 60% of GDP which would not diminish towards the Treaty reference value at a satisfactory pace (and not only on the basis of a deficit above 3% of GDP, which has been the case so far).
    - Financial sanctions for "euro-area Member States" are imposed in a gradual way, from the preventive arm to the latest stages of the EDP, and may eventually reach 0.5% of GDP. The six-pack introduces reverse qualified majority voting (RQMV) for most sanctions, therefore increasing their likelihood for "euro-area Member States". (RQMV implies that a recommendation or a proposal of the Commission is considered adopted in the Council unless a qualified majority of Member States votes against it.)

TREATY ON STABILITY, COORDINATION AND GOVERNANCE (TSCG)

- Entry into force following ratification by at least twelve "euro-area Member States";
- Intergovernmental agreement (not EU law);
- Signed by 25 EU Member States (all but UK and Czech Republic); TSCG will only be binding for all "euro-area Member States", while other contracting parties will be bound once they adopt the euro or earlier if they wish (they are allowed to choose provisions they wish to comply with).
- The fiscal part of the TSCG is referred to as "Fiscal Compact".

- Requires contracting parties to respect/ensure convergence towards the country-specific medium-term objective (MTO), as defined in the SGP, with a lower limit of a structural deficit (cyclical effects and one-off measures are not taken into account) of 0.5% of GDP; (1.0% of GDP for Member States with a debt ratio significantly below 60% of GDP). Correction mechanisms should ensure automatic action to be undertaken in case of deviation from the MTO or the adjustment path towards it, with escape clauses for exceptional circumstances. Compliance with the rule should be monitored by independent institutions.
- These budget rules shall be implemented in national law through provisions of "binding force and permanent character, preferably constitutional".
- European Court of Justice (CoJ) may impose financial sanction (0.1% of GDP) if a country does not properly implement the new budget rules in national law and fails to comply with a CoJ ruling that requires it to do so. In the case of "euro-area Member States", sanctions would be channelled to the ESM, in the case of "non-euro-area Member States", the money would be attributed to the EU budget.
- Compliance with the rule implementing the MTO in national law will also be monitored at the national level by independent institutions.
- Other provisions aim at reinforcing the implementation of the Stability and Growth Pact: re-statement of the debt rule set up by the six-pack, behavioural commitment reproducing RQMV among "euro-area Member States" when the Commission considers that an excessive deficit exists (formal modification of the voting rules would require a Treaty change).
- Finally, the TSCG sets stones for a reinforced surveillance and coordination of economic policies, with ex ante coordination of debt issuance plans among Contracting Parties and economic partnership programmes for Member States in EDP, which detail the structural reforms needed for an effective and durable correction of their excessive deficit.
- TSCG also includes a part on economic governance in the euro area, e. g.: Euro Summits at least twice a year; reinforced economic cooperation.

Does the Fiscal Compact succeed the six-pack or does it run alongside it?

The Fiscal Compact, which is the fiscal part of the Treaty on Stability, Coordination and Governance (TSCG) - once it enters into force - and the six-pack will run in parallel. On the one hand, a couple of provisions included in the TSCG are mirroring concepts existing in the Stability and Growth Pact as reformed by the six-pack: medium-term objectives (MTOs), significant deviation, exceptional circumstances.

On the other hand, some provisions of the TSCG are more stringent than the six-pack. For example, it says that at each stage of the Excessive Deficit Procedure (EDP) "euro-area Member States" will support the Commission's proposals or recommendations in the Council if a "euro-area Member State" is in breach of the deficit criterion, unless a qualified majority of them is against it. In practice this means that if a "euro-area Member State" breaches the deficit criterion a kind of reverse qualified majority voting (RQMV) applies to all stages of the EDP, even if not foreseen in the six-pack.

Moreover, as mentioned above, the TSCG requires Member States to enshrine the country-specific MTOs in national binding law, preferably of constitutional nature.

In addition, the TSCG reinforces economic governance (see above).

The Commission clearly supports the objective to incorporate key provisions of the TSCG in EU law as soon as possible (the TSCG mentions a 5-year horizon, but some provisions may be enshrined in secondary legislation without delay).

How does the "two-pack" fit in?

TWO-PACK

- Work in progress: Discussions between Commission, Council and Parliament are ongoing;
- Shall be agreed in summer (indicative);
- Two Regulations;
- Applicable to "euro-area Member States" only (based on Art 136 TFEU);
- Aims at further strengthening the surveillance mechanisms in the euro area;
- Regulation on monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficits in "euro-area Member States" (original Commission proposal):
    - Common budgetary rules at the national level shall be monitored by independent institutions.
    - As part of a common budgetary timeline, "euro-area Member States" shall submit their draft budgetary plan for the following year to the Commission and the Eurogroup before 15 October, along with the independent macro-economic forecast on which they are based.

  - This builds on the Stability and Growth Pact (SGP), under which Member States present the main characteristics of their medium-term public finance plans to the Commission and the Council in spring (in Stability or Convergence Programmes). The exercise in autumn introduced by the two-pack allows monitoring and sharing information on MS budgetary policies closer to their adoption. The Commission analyses if the draft budget is in line with the SGP and the recommendations from the European Semester (which the country has received in May/June).
  - If the Commission assesses that the draft budgetary plan shows serious non-compliance with the SGP, the Commission can require a revised draft budgetary plan. Otherwise it may address an opinion to the Member States concerned, which would also be discussed by the Eurogroup.
  - This Regulation therefore complements the preventive arm of the SGP, in particular, by ensuring appropriate integration of EU policy recommendations in the national budgetary preparations and increasing peer pressure in the Eurogroup.
  - The National Parliaments remain fully sovereign in voting the Budget Law. With the Regulation, they would be now equipped with an independent opinion on the budgetary plans, namely the Commission opinion.
  - For "euro-area Member States" in EDP, the Regulation introduces a system of graduated monitoring in order to secure a timely and durable correction of excessive deficits. This would in particular allow an early detection of risks that a Member State does not correct its excessive deficit by the deadline set by the Council, and permit to take action accordingly.
  - The co-legislators, together with the Commission, are aiming at incorporating elements of the TSCG in this Regulation: in particular, the requirement to set up independent institutions in charge of monitoring fiscal rules which should implement the MTO at the national level, ex ante coordination of debt issuance plans and economic partnership programmes detailing structural reforms necessary to ensure an effective and durable correction of the EDP.

- Regulation on enhanced surveillance of "euro-area Member States" experiencing or threatened with financial difficulties:
  - "Euro-area Member States" experiencing or threatened with serious difficulties will be subject to enhanced surveillance. Commission may decide this.
  - Automatic enhanced surveillance for countries receiving certain types of precautionary financial assistance (in keeping with EFSF and future ESM guidelines). The list of precautionary assistance instruments concerned will be established and maintained by the Commission.
  - Surveillance involves
    - An obligation on Member States to adopt measures to address the sources of instability.
    - Regular review missions and the provision of more detailed or disaggregated financial sector data if requested.
    - Quarterly reporting by Commission to Eurogroup Working Group.
  - Procedure for deciding and monitoring a macro-economic adjustment programme:
    - Member States facing insufficient administrative capacities must seek technical assistance from Commission (e.g. Task Force for Greece).
    - If necessary Council may decide that beneficiary Member State does not comply with policy requirements contained in the adjustment programme. As a result, the country concerned would face financial consequences with regard to the disbursements under the programme.
  - Simplification of the monitoring of programme countries: In order to avoid duplication and overburdening, the monitoring under the SGP and the implementation of the Macroeconomic Imbalance Procedure and the European Semester shall be suspended, as programme countries are per se subject to wide ranging surveillance and strict targets.
  - Post-programme surveillance: According to the draft regulation, a country shall be subject to post-programme surveillance as long as it has not repaid 75% of its debt.