

## Revisiting the fiscal rules – a priority By Alain Grandjean

The rescue plans carried out by European states in response to the health crisis have resulted in a sharp increase in public debt. A nagging question arises: will the "COVID debts" have to be repaid and if so, by whom and how? This major question, which is currently occupying a large part of the public debate<sup>1</sup>, must be seen in a broader context: that of the reform of the rules of European economic governance. Indeed, for decades the budgetary rules defined in the Stability and Growth Pact (see annex) have been one of the main compasses of European economic policies. Their reform was already on the European agenda for 2020 because they have proved to be manifestly inadequate to the current challenges. It is in the name of these rules that European countries have imposed austerity on themselves over the last decade, that public services are being cut back, and that public investments, particularly those for the ecological transition, are always put off. The purpose of this article is to reframe the debate as a whole and to put into perspective the main priorities for accelerating the ecological transition.

### **The short-term priority: recovery plans**

As soon as it was agreed in the first quarter of 2020 that the European leaders were going to discuss a recovery plan, the priority was clearly the content: which sectors to help? What conditions to put in place vis-à-vis private actors, since it was public money? We took part in this debate and made concrete proposals<sup>2</sup>.

Today, the short-term priority is to press for the recovery plans to be effective, as far as possible carried out in the sectors of the future (compatible with a carbon-neutral trajectory), and, for the sectors of the past, for public aid to be eco-conditioned.

### **Second priority: ensure that the reform of European economic governance promotes rather than hinders ecological transition.**

The second priority is to prepare the exit from the Covid crisis or more precisely the exit from the period of budgetary exceptions that we are currently going through and which allows the States to face the crisis "whatever the cost". Indeed, the rescue and recovery plans led by the European States have been made possible by the suspension of the budgetary rules of the Stability and Growth Pact. While the Commission announces that this

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<sup>1</sup> An initial response was suggested in France almost a year ago now: that central banks cancel the public debt they hold. In my view, this option is one of the possible responses - even if it is widely criticised - and in any case it has the merit of allowing a discussion on a fundamental issue, that of monetary creation and its use in times of underemployment. To find out more: *La monnaie Ecologique* (Alain Grandjean and Nicolas Dufrêne, Editions Odile Jacob 2020); *Des annulations de dette publique par la BCE: lançons le débat!* (Laurence Scialom and Baptiste Bridonneau - Terra Nova - Apr. 2020) ; *Cancellation of public debt: the tone is rising among economists* (Le Monde Dec. 2020) ; *Cancellation of public debt: the bone of contention of heterodox economists* (Mediapart, Jan. 2021)

<sup>2</sup> See [Le débat européen sur le fonds de relance : des enjeux vitaux](#)

suspension will not end before 2022, while the IMF<sup>3</sup> and the OECD<sup>4</sup> insist on the importance of budgetary mobilisation, and while even in Germany, the flagship country of budgetary orthodoxy, the debate on the constitutional ceiling on public debt has been launched<sup>5</sup>, France seems to be going against the tide. Already, the French budget minister<sup>6</sup> or the governor of the Bank of France<sup>7</sup> are laying the ground: that "whatever it costs" will not last, and the debt will have to be repaid. They are therefore anticipating a situation of reduced spending or increased taxes.

It is essential to put forward a serious alternative to this option, initially in terms of fiscal governance. The question to be asked is indeed that of replacing the rules of the Stability and Growth Pact with rules that promote, as a priority, a socially just ecological transition.

This question is independent at first glance of the level of public debt, which, at this stage, remains sustainable: European leaders, including the President of the European Central Bank, manage to reassure the markets as shown by the interest rates on sovereign debt<sup>8</sup>. Even if no one knows how long this period of euphoria will last, a European agreement must be found, within a relatively short timeframe (of the order of a few months) on budgetary rules replacing those that have become inapplicable.

**The questions to be asked with a view to reforming the European budgetary rules are as follows.**

***With regard to the objectives:***

How to ensure that the European budgetary rules:

- clearly promote the ecological transition and the resilience of our countries to ecological crises (notably through the financing of adequate public investment programmes)?
- are designed with the logic of complementarity and coordination with monetary and prudential policies in order to direct public and private flows as well as possible towards transition projects and to accompany the transformation of the sectors of the fossil economy?
- enable all risks (health, ecological, economic and financial) to be addressed and no longer focus solely on the question of the sustainability of public debt, which is only one risk among others and not the most important one?
- are adapted to a situation of radical uncertainty, which requires the application of the precautionary principle<sup>9</sup>?

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<sup>3</sup> [State support is crucial as countries embark race to vaccinate](#) - IMF (Jan 2021)

<sup>4</sup> [OECD warns governments to rethink constraints on public spending](#), Financial Times article (4/01/2021) based on an interview with Laurence Boone, OECD Chief Economist.

<sup>5</sup> See the FT article (2/2/21) [Europe should pay attention to Germany's debt brake debate. EU leaders will be grateful to Merkel aide who sought to lift Berlin's fiscal taboo](#). Ben Hall. (02/02/21)

<sup>6</sup> Interview of Olivier Dussopt, Minister in charge of public accounts, "2021 must be the year of exiting the "whatever it costs", Les Echos (20/01/2021)

<sup>7</sup> The Governor of the Banque de France recalls that the debt will have to be reimbursed from 2022 on BFM TV (11:12/2020)

<sup>8</sup> France borrows at negative rates (10 years). In January, it issued 50 years bonds at the rate of 0,5%.

<sup>9</sup> See <https://www.banque-france.fr/intervention/green-swan-central-banking-and-financial-stability-age-climate-change-banque-des-regle>

- promote cooperation within Europe and are acceptable in countries with a wide variety of cultures, practices and economic situations?

***With regard to the formulation:***

- Is it possible to move away from an exclusively quantitative formulation of budgetary rules?
- Can they not be reduced to indicators relating to debt, deficit, GDP, inflation?

***With regard to governance:***

- Should these new rules give the European Commission more power of interpretation? More power to the European Parliament? What place for civil society?
- How can they be made more transparent and democratic?

***In terms of method:***

- What proposals can be made and to whom to make progress on this issue?
- At what legal level must the proposals be situated in order to have an impact: reform of the European Treaties, legislative proposals (new regulation, new directive etc.), improved guidance within the current frameworks (via communications from the Commission, via the Vade Mecum)?

**Conclusion**

Making proposals to reform the European budgetary rules that have so far been a major footbrake raises many questions and will require a lot of work. This is a subject we have been following for a long time and on which we have already published proposals, either in the book "Acting without delay" or in various contributions<sup>10</sup>. One of the major problems we are facing is that, despite the vital importance of these rules, the question of their reform appears to be an abstruse, technical subject that does not mobilise public debate. One of the major challenges is therefore to convince citizens that this is a high-stakes issue and to mobilise civil society, to put pressure on the authorities in charge of the final decision.

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<sup>10</sup> See for example [Libérer l'investissement vert](#) or [Pour un nouveau pacte européen et solidaire](#)

## ANNEX - The Stability and Growth Pact: European economic governance

Launched by [a resolution of the Amsterdam European Council on 17 June 1997](#), the Stability and Growth Pact (SGP) brings together a set of European legal texts<sup>11</sup> with the aim of coordinating national budgetary policies and avoiding the emergence of excessive public deficits. It is the operational expression of the main principles of economic governance enshrined in the Treaty on the Functioning of the European Union (TFEU).

The SGP has two components.

-The preventive aspect is based on Article 121 of the TFEU, which sets out the main principles and operating methods of economic coordination<sup>12</sup>. The European semester (November to June) sets the annual calendar for this coordination.

Within this framework, each Member State must submit a national reform program and a stability program including an assessment of the past year and macroeconomic projections over 3 years. The preventive section also sets the objectives to be achieved by the Member States in terms of public deficit and debt, which are an adaptation of the rules laid down in the TFEU (the public deficit must not exceed 3% of GDP and the debt 60% of GDP<sup>13</sup>).

-The corrective arm is based on [Article 126 of the TFEU](#), which lays down the general principle that "Member States shall avoid excessive government deficits" and details the different stages of the excessive deficit procedure (EDP) and specifies in particular the methods for triggering and the amounts of financial sanctions.

The European Commission is responsible for examining the decision to launch the EDP. It sends an opinion and a proposal to the Council, which may on this basis decide that an excessive deficit exists and make recommendations to the State concerned with a view to improving its structural budget balance by at least 0.5% each year. In the absence of action by the State concerned, the Council shall initiate each of the following stages of the procedure up to sanctions. It should be noted that since 2011, the voting mechanism on financial sanctions has been by reverse majority, which means that they are deemed to be approved by the Council unless a qualified majority<sup>14</sup> overturns them.

For more information, please visit

-[The European Union Treaties](#)

-[The Stability and Growth Pact](#) on the Commission's website (history, stability programmes of the States, explanations on the preventive and corrective aspects, etc.).

-[The European Semester](#) on the European Commission site (agenda, reports submitted by the countries, reactions of the commission, etc.). See in particular [the annual draft budgets submitted by the Member States](#).

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<sup>11</sup> Notably the « six pack » in 2011 and the "Two Pack" in 2013

<sup>12</sup> See [the regulation 1466/97](#)

<sup>13</sup> The numbers are set in the Protocol n°12 of the TFEU

<sup>14</sup> Qualified majority in the Council means 15 out of 27 Member States and Member States representing 65% of the total EU population are in favour.

