Economic governance: strengthening of economic and budgetary surveillance of Member States experiencing or threatened with serious difficulties with respect to their financial stability in the euro area. 'Two pack'

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OPINION OF THE EUROPEAN CENTRAL BANK on strengthened economic governance of the euro area (Two pack).

On 21 December 2011, the ECB received a request from the Council of the European Union for an opinion on :

- a <u>proposal for a regulation</u> of the European Parliament and of the Council on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area;
- a **proposal for a regulation** of the European Parliament and of the Council on the strengthening of economic and budgetary surveillance of Member States experiencing or threatened with serious difficulties with respect to their financial stability in the euro area.

The ECB welcomes the proposed regulations and recommends **some amendments** aimed at: (a) further strengthening the budgetary discipline of the euro area Member States; and; (b) further enhancing the surveillance of the euro area Member States experiencing or threatened with serious difficulties with respect to their financial stability, irrespective of whether they receive financial assistance or may need to receive such assistance.

The ECB sees the proposed regulations as **compatible with and complementary to the new Treaty on Stability, Coordination and Governance in the Economic and Monetary Union** ('TSCG') as agreed at the European Council meeting of 30 January 2012. Finally, a condition for progressing with the above mentioned quantum leap is that Member States timely and vigorously implement their obligations under the TSCG, and the proposed regulations when adopted.

Proposed regulation on strengthening surveillance procedures: overall, the proposed regulation is welcome, as it gives an explicit basis to the practice of stronger monitoring of Member States experiencing financial market tensions or receiving financial assistance. The involvement of the ECB and European Supervisory Authorities is also welcome. Nevertheless, the ECB has several observations:

- The ECB welcomes the fact that even if a Member State is not receiving any kind of financial support, the Commission may decide to subject it to enhanced surveillance if it is experiencing severe financial difficulties. In addition, providing examples of what could constitute a serious difficulty would facilitate the understanding of the proposed regulation, contrary to developing an exhaustive definition, which would not be prudent.
- As the sources of difficulties of the Member States under enhanced surveillance might easily encompass or generate systemic risks, action in this field could benefit from the involvement of the European Systemic Risk Board (ESRB). It would therefore be useful to inform the ESRB, where relevant, about the results of the enhanced surveillance.

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- Another crucial feature of the proposed regulation is that the Council may recommend that a Member State under enhanced surveillance seeks financial assistance and prepares a macroeconomic adjustment programme if it is found that more measures are needed and the Member State's financial situation has significant adverse effects on financial stability in the euro area as a whole. This is an important provision as it strongly encourages a Member State to ask for financial assistance and to avoid unnecessary delays where this could have detrimental consequences for financial stability in the euro area as a whole. This provision could be reinforced by obliging the Council ('the Council shall') to make a recommendation of this kind.
- Member States should be encouraged not to avoid a more ambitious adjustment programme by applying for precautionary assistance instead of direct financial assistance.
- The ECB notes that obligations of the euro area Member States wishing to obtain financial assistance should entail more than just information sharing. Indeed such Member States should discuss the possibilities available under existing Union or euro area financial instruments and the facilities of international financial institutions and lenders. The proposed strengthened surveillance procedure could be further reinforced in several ways.
- The continuous monitoring by the Commission of the eligibility criteria laid down in Union and intergovernmental financial assistance instruments should also apply to Member States that have been granted access to financial assistance on a precautionary basis, even if this assistance is not linked to the adoption of new policy measures. In any case, if a Member State judges it necessary to request precautionary financial assistance, a closer monitoring seems justified.
- The ECB recommends keeping open the possibility of assessing the sustainability of government debt also with regard to Member States under a precautionary programme.
- It is important to also empower the Council to initiate and pursue the enhanced surveillance procedures by requesting the Commission to initiate enhanced surveillance, request additional information on the situation of financial institutions, perform additional stress tests or request additional action.
- The proposed regulation requires a Member State subject to an adjustment programme experiencing insufficient administrative capacity or significant problems in the implementation of the programme to seek technical assistance from the Commission.
- In addition, the setting up of a permanent resident advisor in the Member State concerned, who would advise the authorities of this Member State on the implementation of the adjustment programme and coordinate with the Union institutions and Member States involved in the technical assistance would be useful.