European Committee of the Regions

ECON-VII/020

149th plenary session, 27-28 April 2022

OPINION

The EU economy after COVID-19: implications for economic governance

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THE EUROPEAN COMMITTEE OF THE REGIONS

- reiterates its support for the activation of the general escape clause of the Stability and Growth Pact (SGP), for the first time in the history of the euro area; this activation has played an important role in the response to the crisis from Member States, regions, and local and regional authorities by enabling full use of public budgets to mitigate the consequences – most notably social – of the COVID-19 pandemic;
- believes that if the escape clause of the SGP were to be deactivated in the economic governance framework's current state and against the backdrop an energy crisis, geopolitical instability and the recovery from the COVID-19 pandemic, the required debt reduction would lead to a return to austerity policies, and consequently result in great economic, social and environmental costs; therefore calls for the general escape clause to remain active until a revised economic governance framework is put in place as quickly as possible;
- reiterates its position in favour of abandoning unanimous decision-making in taxation, in order to allow the European Union to take the necessary decisions by qualified majority, as in other areas of action as it allows for progress in the fight against tax abuse and information sharing between Member States. This provision continues to respect the competence at national, regional or local level for collecting taxes or setting tax rates;
- reiterates its repeatedly-expressed request for a "golden co-financing rule" which states that: public spending by Member States and local and regional authorities as part of Structural and Investment Fund co-financing in line with the respective EU co-financing limits should not be considered as national or equivalent structural expenditure as defined within the SGP; underlines that public government investments, such as the sustainable green, digital and social transition and maintaining European competitiveness are important for future generations and should therefore be treated adequately when it comes to public government investments.

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Rapporteur:

Elio DI RUPO (BE/PES), Minister-President of Wallonia

Reference document

Communication from the Commission to the European Parliament, the Council, the European Central Bank, the European Economic and Social Committee and the Committee of the Regions
The EU economy after COVID-19: implications for economic governance
COM(2021) 662 final

Opinion of the European Committee of the Regions –
The EU economy after COVID-19: implications for economic governance

I. POLICY RECOMMENDATIONS

THE EUROPEAN COMMITTEE OF THE REGIONS,

1. welcomes the European Commission's communication *The EU economy after COVID-19: implications for economic governance*, and the willingness it shows on the part of the Commission to reform the economic and budgetary rules, including taking into account the impact of the COVID-19 crisis; also welcomes the announcement to present a legislative proposal for mid-2022;

2. considers that the European economic governance reform must also take into account citizen proposals discussed in the context of the Conference on the Future of Europe;

3. recalls the findings, most notably those established by the Barometer 2020 and 2021 reports[1], which show that the multi-faceted impact of the COVID-19 crisis is asymmetric and has territorial dimensions; this impact reinforces certain pre-existing differences between regions across and within the Member States, as local and regional authorities are still at the frontline, not only to fight the pandemic and its effects, but also to implement measures to support people and companies, and to prepare for a gradual and sustainable recovery;

4. notes that throughout the EU, citizens are calling on public authorities, Member States, regions, and on local and regional authorities to help them face not only the consequences of the COVID-19 pandemic, but also the green and digital transitions called for by EU and, currently, the consequences of the war in Ukraine;

5. highlights that some Member States already had a significant investment backlog even before the COVID-19 crisis, for example in infrastructure renewal and building renovation, and that public investment has been put on hold in order to fund efforts to cope with the crisis; the longer this investment is delayed, though, the more expensive it will become;

6. notes that the EU has arrived at a critical moment, and needs to find ways and means to ensure cohesion and the prosperity of European citizens;

Response to the crisis

7. welcomes the success of the SURE programme, financed by bonds issued by the European Commission, and asks the Commission to ensure its proper follow up by submitting a White Paper, which, based on an assessment of the SURE programme, would present the policy options for a permanent European unemployment reinsurance scheme;

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1 European Committee of the Regions, EU Annual Regional and Local Barometer 2020, 12 October 2020, and EU Annual Regional and Local Barometer 2021, 12 October 2021.

8. also welcomes the success of the green bonds issued under NextGenerationEU – the largest green bond issuance in the world – which contribute to financing climate investments through the Recovery and Resilience Facility (RRF);

9. reiterates its support for the activation of the general escape clause of the Stability and Growth Pact (SGP), for the first time in the history of the euro area; this activation has played an important role in the response to the crisis from Member States, regions, and local and regional authorities by enabling full use of public budgets to mitigate the consequences – most notably social – of the COVID-19 pandemic;

10. underlines that the war in Ukraine has demonstrated the importance of energy independence for the European Union and stresses that the energy transition must be accelerated; fears, however, that the classification of gas and nuclear power as sustainable energies in the Taxonomy Regulation will provide incentives that are at odds with the rapid expansion of renewable energies;

11. regrets that public debts have increased due to these measures: public debt levels rose by 13 percentage points in 2020, reaching 92% of GDP in the EU as a whole, and 100% in the euro area[2];

12. believes that if the escape clause of the SGP were to be deactivated in the economic governance framework's current state and against the backdrop an energy crisis, geopolitical instability and the recovery from the Covid-19 pandemic, the required debt reduction would lead to a return to austerity policies, and consequently result in great economic, social and environmental costs; therefore calls for the general escape clause to remain active until a revised economic governance framework is put in place as quickly as possible;

13. supports the European Fiscal Board's assessment on the need for an SGP reform to achieve public debt sustainability, with one main operational rule – a public expenditure benchmark – to target a gradual reduction of the debt ratio towards the anchor, at a pace tailored to country circumstances[3];

A revised governance framework

14. emphasises that the European economic governance framework has major effects on all levels of government, and more specifically on local and regional governments, which are responsible for almost a third of public spending and more than half of public investment in the EU as a whole, with wide variations between Member States[4];

15. reiterates that the SGP and other aspects of the current European economic governance framework have five major flaws: adverse procyclical effects, complexity, a lack of efficiency

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2 European Commission, *European Economic Forecast for Autumn 2021*, Institutional Paper 160, November 2021.

3 See the Board's Annual Report for 2021: https://bit.ly/3HqqvIQ.

4 2018 figures. Source: Eurostat, data codes: TEC00023 and TEC00022.

and effectiveness, insufficient consideration given to indicators linked to sustainable development and well-being, and finally, a lack of transparency and democratic legitimacy;

16. believes that a revised EU economic governance framework must ensure transparent policy-making by involving European and national parliaments and, depending on the internal competences of the Member States, parliamentary assemblies with legislative powers. This involvement must also include local and regional authorities, social partners, civil society, and the academic community;

17. believes that the revised framework also needs to consider the very high level of public debts, which need to be reduced gradually as they cannot be substantially reduced overnight following: the COVID-19 crisis, the cost of natural disasters and other extraordinary circumstances, the great disparities between and within Member States, the new macroeconomic deal (very low bond rates, constrained monetary policy as well as major uncertainty concerning inflation, interest rates and the labour market), the need to avoid austerity policies, and environmental, energy, technological and social priorities;

18. reiterates its position in favour of abandoning unanimous decision-making in taxation, in order to allow the European Union to take the necessary decisions by qualified majority, as in other areas of action as it allows for progress in the fight against tax abuse and information sharing between Member States. This provision continues to respect the competence at national, regional or local level for collecting taxes or setting tax rates;

19. once again insists that national, regional and local governments and the public should be able to clearly understand the rules to be applied; welcomes, in this regard, the Commission's position in support of simpler fiscal rules using observable indicators; recalls that it is of utmost importance to incorporate cyclically adjusted countercyclical stabilisation;

20. believes that a governance framework aimed at ensuring sound budgets must be based not only on wise spending but also on sound and balanced revenues; recalls that in the EU, tax avoidance and fraud deprive public budgets of several hundreds of billions of euros each year, and that the fight against tax fraud is one of the key areas in which more Europeans would like to see greater EU intervention;

21. believes that economic governance must strike a balance between indicators related to budgetary discipline, and those related to social cohesion and the provision of infrastructure and services of general economic interest to all citizens, such as public health and well-being; therefore believes that, in keeping with the macroeconomic imbalance procedure (MIP), which encompasses more varied indicators, including unemployment rates, reformed economic governance must also take into account other environmental and social goals; these concerns cannot remain of secondary importance compared to indicators linked to budgetary discipline;

22. again suggests that the MIP be extended to auxiliary indicators relating to regional disparities, and thinks that it could also take into account the progress made in the implementation of the Sustainable Development Goals (SDGs) that cover not only environmental protection but also social, economic and governance criteria, and which are supported by 193 states worldwide;

23. points out that the corrective measures taken as part of the Member States' macroeconomic imbalance procedures have different effects in different regions, and are particularly detrimental in regions with less diversified economies, such as outermost regions, who have structural and exceptional constraints identified in Article 349 TFEU. These regions are highly sensitive to exogenous shocks and contractionary economic policies have a greater impact on reducing investment and employment there;

Rational promotion of public investment

24. continues to believe that the European economic governance framework is partly responsible for the sharp drop in public investment that occurred following the euro area crisis because it does not sufficiently take into account the distinction between current expenditure and long-term investment expenditure; between 2009 and 2018, public investment as a whole fell in the EU by 20% (as a share of GDP); investment by local and regional authorities decreased by almost 25% and by 40% or more in some of the Member States worst affected by the crisis[5]; believes that it is imperative to avoid repeating such events in the aftermath of the COVID-19 crisis; notes that investment at local and regional level could play a decisive role in economic recovery;

25. stresses that the European Fiscal Board established that Member States with a high public investment rate tended to significantly reduce it during excessive deficit procedures (EDPs)[6], and that the Commission itself noted that the budgetary framework has not prevented a drop in investments[7];

26. emphasises that the CoR already felt in its opinion on the 2015 interpretative communication on the matter[8] that the existing flexibility for investments in the SGP was too restrictive and limited. Furthermore, it was only requested by two Member States, and even then, only resulted in minimum impact;

27. stresses that at the same time, the EU is facing immense funding needs in order to address major current challenges: 650 billion per year according to the Commission for the green and digital transitions alone[9], as well as nearly 200 billion per year for social infrastructure[10];

28. believes that in this current context of extraordinary investment needs, discouraging deficit financing for public investment (as the current financial framework does), including investment

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5 Eurostat, data code: TEC00022.

6 European Fiscal Board, Assessment of EU fiscal rules with a focus on the six and two-pack legislation, p. 76.

7 European Commission, *Economic governance review* COM(2020) 55 final of 5 February 2020..

8 CoR opinion on *Making the best use of the flexibility within the existing rules of the stability and growth pact*, COR-2015-01185, rapporteur: Olga Zrihen (BE/PES), adopted on 9 July 2015.

9 European Commission, *The EU economy after COVID-19: implications for economic governance*, COM(2021) 662 final of 19 October 2020.

10 European Commission, Commission Staff Working Document: Identifying Europe's recovery needs, SWD(2020) 98 final of 27 May 2020.

by local and regional authorities, could encourage underinvestment, to the detriment of future generations and future goals, such as the EU climate goals;

29. welcomes the fact that the Commission has finally clearly acknowledged the need for the governance framework to encourage investments, especially green, digital and resilience-enhancing public investments;

30. reiterates its repeatedly-expressed request for a 'golden co-financing rule' which states that: public spending by Member States and local and regional authorities as part of Structural and Investment Fund co-financing in line with the respective EU co-financing limits should not be considered as national or equivalent structural expenditure as defined within the SGP; underlines that public government investments, such as the sustainable green, digital and social transition and maintaining European competitiveness are important for future generations and should therefore be treated adequately when it comes to public government investments;

31. stresses that, due to the type of project supported by Structural and Investment Funds, such a 'golden' co-financing rule would automatically be particularly supportive of efforts to address current major challenges and implement European priorities. These include economic, social and territorial cohesion; strengthening resilience; implementing social, environmental and digital policies, etc. Granting them favourable treatment within the financial framework would thus strengthen the overall coherence of European policies;

32. calls on the Commission to present a white paper on an overhaul of economic governance based on the potential establishment of a golden rule in line with the respective EU co-financing limits, after it has reformulated its proposals to take account of the economic and budgetary damage caused by COVID-19. The Commission should in its assessment also consider other instruments such as an expenditure rule, which on the basis of trend economic growth and the level of debt imposes a limit on the annual growth of total government expenditure, and can serve to safeguard public trust by boosting transparency, reducing administrative burdens and striking a balance between budgetary discipline and preserving sufficient capacity for public investment;

33. recalls that this expenditure is, by definition, investment in the general European interest with a proven leverage effect in terms of sustainable growth and strengthening territorial cohesion;

34. furthermore, calls for a 'golden' green and social cohesion rule, excluding public investments in projects aimed at encouraging the transition to an environmentally, economically and socially sustainable society, as defined in the SDGs and the Green Deal, from the accounts, as these investments are recognised as essential not only with regard to the recovery following the COVID-19 crisis, but also for the prosperity and quality of life of future generations;

35. suggests that another solution could be to exempt the local and regional government sector from having to apply the Stability and Growth Pact rules. In 2019, public investment in this sector at the European Union level totalled 49.2% of total public investment[11], while the gross debt of the

11 Source: Eurostat National Accounts.

European Union's local government sector represents only 6.0% of the European Union's gross domestic product[12] and is therefore not the cause of high public debt. Moreover, the local government sector only takes on debt for investment and not for macroeconomic stabilisation with current expenditure, and local governments are subject to internal budgetary oversight by the regional or national government. The Committee strongly urges the Commission to examine the possibility of exempting local authorities from having to apply the rules of the Stability and Growth Pact;

36. considers it necessary, in general, that the "do no harm to cohesion" principle, which is included in the Commission's Communication on the 8th Cohesion Report, be taken into account in order to ensure complementarity and synergies between cohesion policy and other EU policies, thus avoiding both hampering the process of convergence and an increase in regional disparities;

37. calls on the Commission to submit, between now and the end of 2022, a legislative proposal for a recast of the economic governance framework, based, in particular, on the implementation of these 'golden' rules combined with the expenditure rule, which can strike a balance between budgetary discipline and preserving sufficient capacity for public investment;

38. nevertheless, in order to ensure compliance of expenditure identified by the governments as falling under one of these 'golden' rules, proposes that the application of these rules be subject to strict surveillance on two levels: from the national independent fiscal councils, and the European fiscal board, which will submit public annual reports to the Council and to the European Parliament;

A substantially revised European Semester

39. stresses that economic governance, which is implemented in practice through the European Semester coordination cycle, lacks efficiency and effectiveness in terms of carrying out reforms;

40. also stresses that the scope of the reforms considered under the European Semester has never been defined in EU legal texts, particularly with regard to their relevance and their added value at EU level. This lack of definition limits potential interactions between reforms undertaken at national level and EU policies (financial legislation and programmes) and is problematic with regard to the principle of subsidiarity;

41. considers it necessary that the European Semester be – on an equal footing and in synergy with its economic and financial objectives – the framework for implementing the environmental and social cohesion requirements defined in the United Nations Sustainable Development Goals (SDGs), which the EU and the Member States have committed to achieving by 2030;

42. firmly believes that its proposed code of conduct for the involvement of local and regional authorities in the European Semester[13] is likely to rectify the Semester's lack of efficiency and

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12 Source: Eurostat National Accounts

13 CoR opinion on *Improving the governance of the European Semester: a Code of Conduct for the involvement of local and regional authorities*, COR-2016-05386, rapporteur: Rob Jonkman (NL/ECR), adopted on 11 May 2017.

effectiveness, as local and regional realities would be better taken into account, and that its implementation remains necessary, especially as the national plans in the context of the RRF are, in part, based on the country-specific recommendations of the European Semester;

43. believes that such a double reorientation of the Semester, regarding its objectives and also its operating processes, would strengthen its democratic legitimacy and that of the EU economic governance system as a whole, which is currently far too weak.

Brussels, 27 April 2022

The President
of the European Committee of the Regions

Apostolos Tzitzikostas

The Secretary-General
of the European Committee of the Regions

Petr Blížkovský

II. PROCEDURE

Title	The EU economy after COVID-19: implications for economic governance
Reference(s)	COM(2020) 55 final COM(2021) 662 final
Legal basis	Article 307(4) TFEU
Procedural basis	Rule 4(1)b)(i) and Rule 56 of the Rules of Procedure
Date of Council/EP referral/Date of Commission letter	
Date of Bureau/President's decision	
Commission responsible	Commission for Economic Policy (ECON)
Rapporteur	Elio DI RUPO (BE/PES)
Analysis	20 December 2021
Discussed in commission	25 February 2022
Date adopted by commission	25 February 2022
Result of the vote in commission (majority, unanimity)	Majority
Date adopted in plenary	27 April 2022
Previous Committee opinions	Opinion on *Making the best use of the flexibility within the existing rules of the stability and growth pact*, rapporteur: Olga Zrihen (BE/PES), adopted on 9 July 2015. Opinion on *Improving the governance of the European Semester: a Code of Conduct for the involvement of local and regional authorities*, rapporteur: Rob Jonkman (NL/ECR), adopted on 11 May 2017. Opinion on the *Proposals for reform of the Economic and Monetary Union* (December 2017), rapporteur: Christophe Rouillon (FR/PES), adopted on 5 July 2018. Opinion on the *Economic governance review*, rapporteur: Elio Di Rupo (BE/PES), adopted on 10 December 2020.
Date of subsidiarity monitoring consultation	N/A

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