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NOTE

From:	General Secretariat of the Council
To:	Permanent Representatives Committee (Part 2) / Council
Subject:	2018 European Semester Process: How to implement structural reforms

Delegations will find attached the letter by the President of the EFC to the President of the Ecofin Council setting out some important questions for the European Semester as discussed by the EFC and the EPC. In annex, delegations will find the reports from the EPC and the EFC Alternates which contain a number of wider recommendations for further smooth running of the European Semester.



ECONOMIC AND FINANCIAL COMMITTEE

THE PRESIDENT

Brussels, 25 September
ecfin.cef.cpe(2018)5500779

Mr Hartwig Löger
President of the Ecofin Council
General Secretariat of the Council of the EU
Rue de la Loi 175
1048 Brussels

2018 European Semester Process: How to implement structural reforms

Dear Mr. President,

The 2018 European Semester progressed well. More and better bilateral information flows between the Commission and Member States, and the high quality Commission documentation, helped. Nonetheless, in view of our discussion at the Ecofin next week I would briefly like to outline two areas for improvement.

The first aspect is less on procedure, more on results. The real success of the Semester will only be measured through implemented reforms, and in this respect, we cannot call the Semester a real success. The degree of implementation of CSRs varies widely across countries and policy areas.

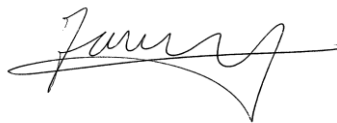
Why, for example, is progress on improving the Business Environment or competition policy patchy? Or why are some Member States implementing the reforms asked of through the recommendations whilst others progress slowly? In the context of ongoing discussions on a range of proposals from the Commission aimed at promoting and financing structural reforms, one needs to get to the bottom of how national level reform implementation could and should improve, particularly in the current good times when the necessity is not felt that much while possibilities are clearly there.

Secondly, while the bilateral policy dialogue between the Commission and national governments has improved, the lack of time allocated to the final important stage, discussion in Council committees after publication of the Country Specific Recommendations (CSRs) proposals,

continues to hinder multilateral involvement, and ultimately common ownership. Looking forward to 2019, this timing may well be even more of a concern if the CSR proposals come after the European Parliament elections and an early June European Council impinges from either side on the time available for discussions in the Council and the committees. For these discussions to take place in an environment conducive to generating a better common understanding of reform priorities, it is essential we give Member States time at home to develop a common understanding on the proposals themselves. It is therefore important that either the Commission publish the proposed recommendations well ahead of the European elections or the timelines and working methods for dealing with this in the Council need to be reviewed.

Aside from the issues I draw to your attention, in annex please find the reports from the EPC and the EFC Alternates that contain a number of wider recommendations for the further smooth running of the Semester.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Hans Vijlbrief', with a long horizontal flourish extending to the right.

Hans Vijlbrief

**ECONOMIC POLICY COMMITTEE****Note from the EPC on the 2018 European semester process**

- Lessons learned and ways forward -

The 2018 European Semester progressed well. The more frequent information flow between Commission and Member States, and the high quality Commission documentation, further contributed in this regard. However, there is still scope for improving some aspects especially as concerns the final stages of the Semester, given the uneven implementation of CSRs registered so far. This report provides a short set of recommendations for further improvements in 2019.

1) Timing constraints in 2019:

While the policy dialogue is facilitated by consultation of Member States and the publication of Country Reports well ahead of the CSR proposals, the Semester process is constrained by a lack of time allocated to the final, most important stage, discussion in Council and its committees after publication of the CSR proposals. This aspect is instrumental in generating multilateral involvement, and ultimately in improving common ownership. Looking forward to 2019, timing may well be even more of a concern if the CSR proposals are to be adopted after the European Parliament elections and an early June European Council impinge from either side on the time available for the committee work. The EPC would like to stress the importance of the Commission publishing the proposed recommendations as early as possible in order that Member States can undertake the necessary consultations and engage in necessary dialogue with the Commission.

2) Future Governance

Discussions are ongoing on a range of proposals from the Commission on aspects related to the EU budget and the Commission proposal for a Reform Support Programme. The current proposal could have important implications for the European Semester, and the EPC wishes to reiterate the need to ensure that any Reform Delivery Tool be firmly embedded within the European Semester, should not duplicate, but complement Semester arrangements, and must not compromise the strong multilateral aspects of the Semester.

3) Focused CSRs based on a common understanding of priorities.

Members appreciated the high quality of the Commission documentation throughout the Semester. This coupled with a partnership approach that allowed the sharing of the main elements of the Country Reports in advance of publication and more frequent bilateral contacts established a stronger common consensus on country specific challenges.

There was broad agreement that the CSRs focus on the right policy challenges and priorities. Consequently there were fewer comments on the draft CSRs themselves. The agreed changes mostly aimed at clarifying expected policy responses and at ensuring that reforms can gather support within the Member State, be implemented within a 12-18 month timeframe and be consistent across Member States. Coherence with the Euro Area Recommendations could be further improved.

Some Members also stressed that a direct mandate for Commission officials to agree on amendments without a need to refer back to the Core Group would facilitate the work in the committees.

4) Streamlined CSRs but a step too far?

The number of CSRs was further reduced in an effort to streamline and focus on priorities. This should allow for better peer review and peer pressure, but comes at the cost of sometimes bundling a wide range of reforms into one recommendation or of a more constrained range of issues covered. This goes somewhat against the role of the European Semester as an over-arching economic policy guidance tool setting out reform priorities across the full spectrum of economic policy that can act as the guidance framework for, amongst others, ESIF policy documents and any proposed Reform Delivery Tool.

In a number of cases, reform challenges have been dropped from the CSRs that were assessed as only partially addressed at best. This should not lead to a false impression of implementation or impede the multi-annual assessment of CSR implementation. Decisions to drop reform challenges from the CSRs without full implementation are rarely explained within the recitals. In future years, and where relevant, the text should contain an explanation on why a CSR has been dropped.

Furthermore, some thematic policy priorities have been downplayed or are now completely absent from the text. This is particularly relevant for economic aspects of the energy sector, which moved to the Energy Union governance arrangements, but it is also relevant for single market issues and climate change and the functioning of the economy. In certain cases Member States would have welcomed that parallel governance processes of relevance are mentioned in the recital, so that the CSRs remain the main, all-encompassing, reference point for country-specific economic policy actions.

Many members welcomed that the CSRs are often general in nature, rarely directing attention to specific economic sectors. However, in some cases Member States wished to add specific sectors in the respective recitals, as this is helpful for the domestic audience. The EPC felt the Commission could be supportive in the cases where greater reform ambition is conveyed by Member States, also as a means to enhance national ownership.

5) "Catch-all" Recitals

Further consistency work would help ensure the length of the recitals is more consistent across the Member State texts. The recitals have become a "catch all" to explain the CSRs, report on progress, and in some cases address wider structural reform challenges not covered in the CSRs as a consequence of the streamlining. Some Members felt that they are often a selective and in other cases too extensive summary of issues raised in the Commission's Country Report.

The time devoted to discussing amendments to recitals in the EPC compromises its ability to discuss the policy priorities of the CSRs themselves. Some Members therefore suggested *that the Commission considers sharing the recitals* in advance of publication providing the possibility to iron out factual or technical issues, so that the discussion at the EPC can focus on substantive policy issues. This would strengthen dialogue with the Commission and assist Member States in stakeholder discussion at the national level. Short of this, bilateral contacts could be used in the brief window between publication of the draft CSRs and the first committee meeting as an opportunity to discuss the recitals and clarify a range of drafting issues to be presented to the EPC, without this process impeding the multilateral review of the CSRs and also allow EPC to focus on more substantive discussions.

Specific policy issues that require further reflection:

This set of CSRs contains fewer references to wage setting. Some Members stressed the need to ensure that wages appropriately reflect country-specific economic conditions in both economic up and downturns, while respecting the role of the social partners. Indeed, while wage rigidities may be less visible in an economic upswing, their negative impact may become extremely costly in case the economic cycle turns.

Some Members pointed to the need to avoid issues that they considered to be of a largely political nature. In a limited number of cases the language accompanying the recommendation proposals for a Member State stepped beyond pure structural economic reform issues into broader politics and political economy considerations.

In general, the integration of the European Pillar of Social Rights in the CSR proposals has been done in a manner that allows the focus to remain on structural reform priorities.

The timely production of the Ageing Report allowed for more pertinent and convincing explanation of the need to reform pensions, health and long-term care systems, leading in some cases to specific CSRs.

Whilst there were no CSRs covering the issue of Aggressive Tax Planning, there were recitals on this sensitive issue for seven Member States. Some Members regretted the Commission line not to discuss compromise language to these recitals in the EPC. Some reiterated their disagreement with the coverage of Aggressive Tax Planning in the Semester, considering that it belonged in specialized international and EU fora, while others in general supported the coverage of the topic.

In the context of the solid and lasting economic expansion, several members pointed to the need to differentiate more consistently between cyclical and structural effects in the adjustment of imbalances. The LIME working group has invited the Commission to prepare a short paper on this specific issue.

**ECONOMIC AND FINANCIAL COMMITTEE**

CHAIR OF THE EFC-ALTERNATES

18 September 2018

ecfin.cef.cpe(2018) 5316128

Report by the Chair of the Alternates to the EFC*European Semester 2018 – Lessons learnt and suggestions for the next round*

On 13 September 2018 the Alternates discussed the 2018 cycle of the European Semester and reflected on the lessons learned and possible improvements for the next round of the Semester.

Assessment of progress in 2018

The track record on the implementation of the Country-Specific Recommendations is not very strong and is not improving over time. National ownership of the reforms is seen as a crucial element to improve implementation. A precondition for generating ownership is good communication to national audiences on why reforms are needed.

The Alternates welcomed the continued improvement of public finances. Only one Member State is subject to the corrective arm of the Pact, down from twenty-three in 2011. In the preventive arm, about half of the Member States were at or above their Medium-Term Budgetary Objectives (MTOs) in 2017. Many are expected to remain above their MTOs over 2018-2019 based on the Commission spring 2018 forecast, and do not have country specific recommendations on fiscal policy.

At the same time, several countries are far from their MTOs and are at risk of not making sufficient efforts in 2018 and 2019 based on the Commission spring 2018 forecast¹. In some cases fiscal policies are projected by the Commission to be expansionary. These countries need to take the necessary measures in line with the Stability and Growth Pact (SGP). There was a broad recognition that the positive cyclical conditions call for rebuilding fiscal buffers, in particular in countries where debt ratios are high, while continuing to strengthen the growth potential of our economies. Some Alternates underlined that debt reduction should be a priority in these Member States, while others noted the need to use fiscal space, where it exists, to continue to strengthen the economic growth potential.

Formulation of CSRs and recitals

Overall, the Alternates expressed broad support for the Commission's proposals for Council country-specific recommendations under the European Semester process:

- The Alternates welcomed the increased transparency of the fiscal CSRs this year, compared to the previous exercise. In particular, Alternates welcomed the return to numerical targets for the forthcoming year in the CSRs for countries which are not close to their MTOs.

¹ The Commission forecast uses a no-policy change assumption for 2019.

- One suggestion for improvement was for the Commission to explain better in the recitals why CSRs have been dropped, in particular in cases where CSRs have not been followed-up and where cross-country consistency would not justify dropping the CSR.
- The Alternates also broadly supported the recommendations aiming at tackling the remaining weaknesses in the financial sector.
- The Alternates recognised the importance of consistency and equal treatment in the CSRs. However, some underlined the need to take into account national specificities in the CSRs to ensure their relevance for the national debate.
- Finally, some Alternates repeated that the design and implementation of reforms takes time and invited the Commission to reinforce the multi-annual approach to the CSRs.

Semester process

Overall, there was broad agreement that the CSR discussions in the Alternates had been very smooth, also thanks to the constructive and cooperative approach between the Commission and the Members:

- There was agreement that this year's more horizontal approach to the CSR discussions had been efficient and had helped structure the Alternates' debate. This practice could be further improved in 2019.
- Both the Commission and the Alternates agreed that the April discussion on financial sector challenges, based on the Country Reports, had been helpful to prepare the subsequent CSR discussion. Having more preparatory horizontal discussions on selected themes could be envisaged in 2019 to prepare the CSR discussions.
- The Alternates intend to discuss during the second half of 2018 a number of outstanding methodological issues where views currently diverge. This can facilitate the CSR drafting exercise which will follow in 2019.
- The importance of a continued exchange of information and dialogue between the Commission and the Member States was stressed. Members agreed that the DG ECFIN country desks already play a crucial role in the process and expressed a wish to reinforce this further.

Alternates also discussed the frequency of the Commission's forecast as they are the basis for fiscal surveillance. The Commission explained that it had returned to a normal forecast cycle with two fully-fledged forecasts (in spring and in autumn) and two interim forecasts (in winter and in summer). While most agreed that two forecasts were sufficient, some noted that with the disappearance of the fully-fledged winter forecast, the Ministries of Finance lost an important reference point to justify to their IFIs the macro-economic assumptions used in the Stability Programmes, while another deemed two forecasts sufficient.

The EFC is invited to reflect how the Alternates can best prepare the EFC and ECOFIN discussions on the fiscal and financial CSRs, in order further to enhance the quality and depth of the multilateral dialogue at that level.

Over the years the European Semester has gained in importance as the overarching economic policy coordination process, especially for Euro area members. In that respect, early discussions on common challenges referred to in the Euro area recommendations, to feed into the preparation of Country-Specific Recommendations were deemed important. The analysis and in particular the Country-Specific Recommendations which are put forward under the European Semester also contribute to the priority-setting in other EU policies such as the European Structural and Investment Funds. Furthermore, the proposed Reform Delivery Tool would relate financial support for structural reforms to the challenges identified in the European Semester, including in the Country-Specific Recommendations.

It is therefore crucial to reserve sufficient time for the multilateral discussion of the CSR proposals in the Council and its committees, in order to ensure high quality and shared ownership. Looking forward to 2019, should the Commission's next CSR proposals be adopted only after the European Parliament elections, as was done in 2014, and taking into account an early European Council meeting in June, only 2½ working days would remain between the adoption of the CSR proposals and the EFC meeting, putting at risk any meaningful discussion of the recommendations.

Yours sincerely,



Marketta Henriksson