



**Contributions from the Sherpas  
of the Member States to  
the Five Presidents' Report**

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**IRELAND**

First Contribution

**Response by Ireland to Questions in the Analytical Note *Preparing for Next Steps on Better Economic Governance in the Euro Area***

**Question 1: How can we ensure sound fiscal and economic positions in all euro area Member States?**

**Answer:** European economic governance must support policies which promote growth and employment in Europe, which are key to fiscal sustainability. The two important post-crisis reform pillars, namely the new Economic Governance framework (including the Macroeconomic Imbalance Procedure) and Banking Union, represent a significant advance in strengthening the EMU. However, there can be no complacency. The new rules are largely untested, particularly in more benign economic conditions. Moreover, time is proving that the necessary focus on fiscal discipline in itself has not yet delivered the return to growth at the levels which we need with economic output remaining below potential.

Ireland supports the rules and feels that all Member States should respect them. The key issue is that they are credible and seen to be enforced equitably, with Member States being treated fairly irrespective of size. Enforcement must be robust and consistent, but a strictly mechanical implementation of the rules can lead to perverse outcomes that can be counter-productive for Member States and collectively, and this only serves to undermine the rules. This points to a need for some margin of interpretation and for any issues of methodology to be addressed rapidly.

**Question 2: How could a better implementation and enforcement of the economic and fiscal governance framework be ensured?**

**Answer:** See 1 above.

**Question 3: Is the current governance framework – if fully implemented – sufficient to make the euro area shock-resilient and prosperous in the long run?**

**Answer:** While structures and procedures have been reformed on foot of the crisis, challenges remain. It is clear that we have not yet succeeded in establishing a fully flexible, streamlined and growth-stimulating single currency area. However, work has to continue on fully implementing the current framework, rather than engaging in the design of new structures. In parallel, the Single Market needs to be completed to enable to the removal of barriers to labour and product mobility.

There needs to be more focus on the aggregate economic and fiscal position of the euro area as a whole. In particular, during the worst of the crisis, while certain countries were running very large deficits and did not have fiscal space to stimulate growth, other countries which were in a better fiscal position could have been encouraged to allow a degree of fiscal expansion to enhance growth across the euro area as a whole. The MIP needs to be implemented in a way which recognises that excessive current account surpluses and deficits both need to be tackled.

The 2015 AGS appears to address this with a more nuanced approach to fiscal responsibility i.e. providing for surplus countries with fiscal space to seek to boost demand while deficit countries should continue with fiscal consolidation. The January guidance provided by the Commission on the implementation of the SGP also aims to encourage a more growth-friendly fiscal stance within the EU and recent developments outside the governance framework to tackle under-investment are also to be welcomed (including progress towards the establishment of the EFSI).

**Question 4: To what extent can the framework of EMU mainly rely on strong rules and to what extent are strong common institutions also required?**

**Answer:** A rules-based framework is crucial but, as previously indicated, the rules must be reasonable and workable. The focus for the foreseeable future – certainly

during the current terms of the Institutions – must be on the effective and intelligent implementation of the major reforms agreed in recent years.

We accept that there is substantial central bank, academic and other expert analysis to the effect that the EMU is a sub-optimal currency union, and requires further institutional integration. Debate concerning the ultimate logic of EMU often raises issues such as common institutions e.g. the appointment of a euro area Finance Minister and the creation of a euro area fiscal capacity. However, political and public openness to such projects simply does not exist at this time, in our view. They would also involve substantial Treaty change, which would be hugely challenging at the current juncture. Ireland would therefore be opposed at this time to placing the possibility of Treaty change on the table.

**Question 5: What instruments are needed in situations in which national policies continue – despite surveillance under the governance framework – to go harmfully astray?**

**Answer:** See answer to Q1 above.

The current governance regime, including the corrective arms of the SGP and the MIP, has been strengthened by the semi-automaticity of the procedures and the creation of independent fiscal councils. What is now required is the full, fair and effective implementation of the existing rules. Any perception that the application of the rules are not uniformly applied would fatally weaken their effectiveness.

**Question 6: Has the fiscal-financial nexus been sufficiently dealt with in order to prevent the repetition of negative feedback loops between banks and sovereign debt?**

**Answer:** Significant progress has been made in trying to break the link between the sovereign and the banking sector with the introduction of the Single Supervisory Mechanism, the Bank Recovery and Resolution Directive, and the Single Resolution

Mechanism Regulation with the associated Intergovernmental agreement. However, work remains to be done on the completion of the Banking Union.

In an ideal world, the Single Resolution Fund (SRF) would have been fully mutualised from the outset so that the collective funds raised across the Banking Union would have been available to any institution which, after going through the due process of bail-in, required additional monies from the SRF.

Therefore, a key issue which has yet to be satisfactorily resolved is that of bridge financing. This is an important issue because there is, of course, potential for a call upon the SRF in its early years, during a time when it is likely that insufficient funds will be available to meet resolution needs. Depending on how this is addressed, there is a possibility of weakening even further the sovereign banking link. However there is also the risk of reinforcing it if a particular direction is taken. We note that the TFCA recently prepared a paper setting out various options for a bridging mechanism.

Another key issue which needs to be addressed in order to sever the bank/sovereign link is to put in place a backstop to the Single Resolution Fund rather than relying on individual Member States. A commitment has been made by Member States to put a backstop in place during the SRF transitional period; however no timetable for doing so has yet been decided. An early start on this, and more importantly an early agreement, would do a lot to weaken the link even further.

We would also wish to revisit the issue of common deposit insurance.

**Question 7: How could private risk-sharing through financial markets in the euro area be enhanced to ensure a better absorption of asymmetric shocks?**

**Answer:** At this juncture it is still not fully clear what will emerge in the Commission Action Plan on Capital Markets Union scheduled for later in the year. From an Irish perspective, in addition to benefits from aggregate EU growth, CMU could serve to

significantly increase issuer and investor access to more liquid European markets. Irish businesses, in particular SMEs, are heavily reliant on bank lending and so any initiative which has the objective of reducing this reliance through growing capital markets is to be welcomed. We will, however, critically analyse CMU from the perspective of a smaller Member State.

**Question 8: To what extent is the present sharing of sovereignty adequate to meet the economic, financial and fiscal framework requirements of the common currency?**

**Answer:** See answers to questions 1, 3 and 4 above.

**Question 9: Is a further risk-sharing in the fiscal realm desirable? What would be the preconditions?**

**Answer:** See answer to question 4 above. We believe that this is not an issue for the short-to-medium term, despite its possible intellectual attractions.

Our position is that in any future proposal for further risk-sharing in the fiscal area, national competences and democratic processes would have to be respected.

Ideally, a well-designed fiscal capacity would have three features, namely it would be: economically significant, automatic, and be fiscally neutral over the long term. However, adequate consideration must be given to addressing the risk of moral hazard which would arise with the creation of any form of insurance mechanism at the central level. Any form of risk mutualisation would require strong conditionality. As taxation is at the heart of democratic legitimacy, moral hazard concerns should be not addressed by way of greater tax coordination. A mechanism which would involve the convergence of taxation systems would not be acceptable.

**Question 10: Under which conditions and in which form could a stronger common governance over structural reforms be envisaged? How could it foster real convergence?**

**Answer:** The Communication on the European Semester package published by the Commission on 26 February stated that *‘Streamlining and reinforcing of the European Semester with a view to boosting its ownership and effectiveness will be an important part of the broader discussion on the deepening of the Economic and Monetary Union’*. We agree with this approach and our position is that the existing European Semester process should be fully implemented before we embark on developing further governance mechanisms.

We fully accept that achieving real national ownership of reform commitments is challenging and difficult, as is meaningful peer review and we are open to further debate.

The consistent implementation of structural reform recommendations is important. For this to improve, Member State ownership of structural reforms is key. The new ‘streamlined’ European Semester should improve the implementation record over time. Getting real engagement by national Parliaments and social partners is highly challenging. However, further efforts need to be made by the Commission in terms of improving the transparency, clarity and organisation of the various engagements with Member States throughout the newly reorganised Semester cycle, with greater engagement at senior level. There is a risk that a lack of transparency could serve ultimately to undermine the effectiveness promised by the new Semester timeline in boosting national ownership of reforms.

As proposed in the 2015 Annual Growth Survey, the Commission should consider presenting a smaller number of CSRs for each Member State. CSRs should remain focussed only on the most pressing and important structural reforms for each Member State e.g. deficit countries need to address remaining labour market/product market rigidities – focussing on supply side reforms; surplus countries need to boost demand to improve consumption. We would be open to exploring ways in which peer involvement could be enhanced (there are some interesting models at OECD level and in the EPSCO

framework). We would also be open to discussion as to whether it is optimal for CSRs, especially those relating to medium-term structural reforms, to be framed and examined on an annual basis.

For legal, political and practical reasons we remain unconvinced by the concept of binding “contracts for competitiveness” or similar instruments. We do not see how they would necessarily in practice enhance real political engagement and commitment, while at the same time they would further narrow the space for elected national Governments and parliaments to frame economic policy and amend it as needed.

**Question 11: How can accountability and legitimacy be best achieved in a multilevel setup such as EMU?**

**Answer:** Overall, a sustained improvement in the economic performance of the EU and the euro area, involving a wide range of future-oriented and growth-friendly economic policies (trade, services, digital single market, better regulation...) as well as effective economic governance in the narrower sense, will be essential in boosting public support and legitimacy. This pattern has been observable over 30 years of Eurobarometer surveys.

In institutional terms, the role of national parliaments is central and we support measures to involve them in the European Semester process more fully. Ways to ensure the more regular attendance of Commission, ECB and other institutional representatives at national parliaments need to be considered. So too should the further enhancement of dialogue between national parliaments and the European Parliament – as envisaged in the Fiscal Stability Treaty.

It is for the European Parliament to organise itself as it sees fit, in conformity with the Treaties, but we would not object in principle to some form of heightened scrutiny of the euro area as such.



More generally, the balance between the complexity and transparency of rules need to be constantly assessed. Simplification of the rules would assist in communicating them to citizens. However, the trade-off could be the potential loss of flexibility.

**Dublin, 27 March 2015**