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The new European fiscal framework: how to harmonise rules and discretion

A contribution to the Commission Review of the EU Economic Governance Framework[1]

by

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Since its establishment in 2001, Astrid Foundation (www.astrid.eu) has devoted a significant part of its research programme to the analysis of the European economic institutions and policies, including the reform of the Stability and Growth Pact. This last topic has been specifically addressed by two papers. The first paper, reproduced below, is authored by Giuliano Amato, Franco Bassanini, Marcello Messori and Gian Luigi Tosato. The second paper (On Reforming the EU Fiscal Framework) *is authored by Massimo Bordignon and Giuseppe Pisauro.*

1. Introduction

In response to the pandemic shock, the European institutions followed a new approach in terms of economic policy, i.e. a new 'policy mix' (cf. Barsch *et al.*, 2020).

The European Central Bank (ECB) ceased to be the only player on the scene, even if it significantly strengthened its expansionary monetary policy, and specifically its securities purchase programmes. The ECB's increased purchases of euro area's government securities in the secondary segments of financial markets – along with the substantial suspension of the 'Stability and Growth Pact' (by means of the 'general escape clause') and the implementation of the 'Temporary Framework' – have allowed the member states with low fiscal capacity to implement expansionary national policies. Thus, ECB made possible the huge increase of national public expenditures required to handle the economic

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and social emergency due to the pandemic shock. However, the main novelty of the new policy mix in the European Union (EU) has been the launch of centralised fiscal initiatives such as the SURE, designed to countering the short-term impact of the pandemic crisis on the labour market, and the Next Generation – EU (NGEU). The latter is implementing a temporary and partial but crucial centralisation of the EU's fiscal policy mainly through its most important programme, the Recovery and Resilience Facility (RRF).

The success of the RRF requires each of the EU's member states to implement its national Recovery and Resilience Plan (RRP), examined by the Commission and approved by the EU Council. Let us recall that the national RRPs are centred on three pillars: (a) 'green' transition, (b) digital transformation, and (c) social inclusion. Pillar (a) and pillar (b) should absorb – respectively – at least 37% and 20% of the total European resources allocated to each country by means of the RRF; pillar (c) should not meet a minimum threshold, even if the expected impact of (a) and (b) on the labour market and income distribution is dramatic and makes a serious reform of welfare state and education/formation of human resources unavoidable. It follows that the three pillars together stake a claim on more than 2/3 of the RRF's total resources (cf. Buti, 2021; Messori, 2021).

We have recalled these well-known aspects to justify our thesis based on two points: (a) the features and achievements of the RRF and national RRPs matter a lot for an effective definition of the new EU economic governance and – specifically – of the new European fiscal rules; (b) an appropriate design of the latter rules would, in turn, strongly increase the probability of a successful implementation of the RRF and its possible evolution towards a permanent central fiscal capacity.

Let us elaborate on points (a) and (b). The European reaction to the pandemic crisis is showing that a centralised fiscal instrument makes crucial benefits. NGEU is conceived as a temporary and exceptional initiative. However, the EU requires the strengthening of crisis management tools, a further development of its comparative advantages ('green' economy, welfare state, regulation) that could strengthen the European role in the world, the production of common public goods and externalities, and incentives to ease the convergence between its member states (*see* Buti and Messori, 2021b). These objectives cannot be pursued by overburdening the ECB's functions; they require, instead, the creation of a permanent fiscal capacity at the EU level.

A necessary condition to gradually build this centralised and permanent capacity is the successful implementation of RRF, notably by the biggest beneficiaries. This condition cannot be met in the next quarters of 2022 due the 2026 horizon of the RRF; hence, it

cannot directly support the reform of the EU fiscal rules. However, this reform should be connected and compliant with such a positive perspective, in a double sense. First, the reform of fiscal rules can draw inspiration from the NGEU's methodology and can bet on its success. Secondly, it could help the RRF's successful implementation, thus transforming the bet in a reasonable investment on the future.

In this last regard, it is important that the new fiscal rules take into account the process of "vertical coordination" between the centralised fiscal policy and the national ones.[2] Until the central fiscal capacity is temporary, the financial accommodation of the 'green' and digital transitions should be ensured by leaving a fiscal space at national level. This means that, at this stage, national policies must largely finance the 'green' and digital public investments, the implementation of the related reforms, the expenditures for an appropriate adaptation of human resources to these processes (made more difficult by the aging population), and the absorption of the consequent social impact. The gradual stabilisation of a central fiscal capacity should go hand in hand with the progressive sharing of fiscal sovereignty, that can shift a part of the financial burden from national policies to the centralised fiscal policy, and with a credible enforcement of the new fiscal rules.

In the following, we specify our suggested methodological approach for the definition of the new EU's fiscal rules.[3] This approach makes it crucial to combine a few simple but clear-cut fiscal rules, a room for institutional discretion, a new 'golden rule', and an accountable framework to sanction member states infringing these shared rules. The implication is that, **as in the original European Treaties and without introducing any change to them,** the adjustment paths become more important than the single specific fiscal rule. Our conclusion is that this approach would produce positive consequences going beyond the definition of new fiscal rules.

[2] The concept of 'vertical coordination' between a European fiscal policy and national fiscal policies has been elaborated by Buti and Messori (2021a). Maduro *et al.* (2021) has later made use of an analogous concept.

[3] The recent debate on the revision of the European economic governance and, specifically, of the centralised fiscal rules now include many papers. Our proposal does not fully share previous analyses. However, it has been influenced by Blanchard *et al.* (2020), and Martin *et al.* (2021).

2. *A methodological approach: from the NGEU to the reform of the Stability and Growth Pact*

Three aspects can illustrate why the methodological features of RRF and RRPs matter a lot for an effective definition of the new European fiscal rules.

Being at the core of the RRPs, the projects relating to the 'green' and digital transitions and to social inclusion had to overcome a careful check by the Commission along the various criteria specified in the RRF guidelines. An analogous check also applied to all the other projects included in the RRPs. The implementation of these projects should follow processes able to meet partial targets and milestones, defined in terms of inputs and outcomes, at pre-determined dates. Moreover, each of these projects should be completed at the planned expiry time and at the planned costs. In few words, the design and execution of the RRPs are submitted to a careful screening by the Commission and to an approval by the EU Council (and, possibly, the European Council). This full-access screening is leading to a new bilateral relation between the Commission and each of the EU's member states; and, in its turn, this relation is based on clear-cut criteria but leaves also room for specific agreements.

Thus, our first statement (in the following**, Thesis 1**) **is:**
In the revision and implementation of the new European fiscal rules, it would be useful to attribute a crucial role to a bilateral relation of each member state with the Commission, modelled on the bilateral relation experienced in the execution of NGEU.

Let us re-examine this bilateral relation between the Commission and each of the EU member states in the light of game theory. The partial and temporary centralisation of EU fiscal policy, triggered by the RRF, leaves the 'first move' to the European institutions in order to set the framework and the general rules and to fix the maximum amount of EU's financial resources allocated to each country. However, the second and crucial move is in the hands of the member states, which decide how to utilise (in full or in part) the allocated resources and detail the utilisation in a plan. This plan (that is, the final draft of each RRP) is subject to the constraints put by the European framework and general rules; however, it is country specific. As a final move, the Commission will assess if the national initiatives, specified in the RRP, are compliant with the general framework; and, in the affirmative (completed by the approval of the EU Council), the Commission monitors their implementation (*see* European Commission, 2020).

Thus, our second statement Thesis 2) is:

The ‘RRF methodology’ could be utilized to define national ‘Fiscal and Structural Plans’ (FSPs) aimed at making government budgets compliant with the new fiscal framework.

The pandemic emergency caused an exceptional situation beyond the control of national policymakers, so that it became possible to approve a temporary initiative such as the NGEU in the legal framework of the existing European Treaties. Therefore, the Commission – on behalf of the EU – was entitled to transfer grants and loans to EU’s member states, according to redistributive criteria, on a one-shot basis; moreover, it was authorized to finance these transfers through the issuance of European securities. It follows that the European financing can be defined as an exceptional and temporary fund devoted to support national expenditures in specific fields (the ‘components’, grouping different but homogeneous projects which are part of the RRP). In this perspective, Tosato (2021a) states that the current European Treaties allow the European institutions to activate European funds in case of ‘exceptional events’. As a consequence, it is compliant with the Treaties to attribute the discretionary management of these funds to the Commission (on behalf of the EU).

‘Exceptional events beyond the control of national policymakers’ are bound to hit the EU in the years after 2026. According to the European Commission’s objectives, tackling climate change requires that EU reach carbon neutrality by 2050; and achieving digital transformation is the unfailing condition to catch-up the USA and China, thus avoiding the marginalisation of the European economy in international markets. These two transitions ask for the implementation of a massive production restructuring and radical changes in labour skills and in consumption models. Both transitions (and the related need to implement a social capital formation and welfare reform) are conceived as the effective exit from the pandemic emergency and, thus, offer an economic and legal justification to the NGEU. However, it would be unrealistic to conceive that these transitions can be achieved by the end of NGEU. Hence, ecological sustainability (and, perhaps, even the technological catch-up) promises to open a long-term emergency phase in the EU. According to Tosato (2021a), this emergency allows the activation of long-term European funds without changing the Treaties.

Thus, our third statement (Thesis 3) is:
The new fiscal rules should take into account the need of recurrent European funds, and they could therefore confer to the Commission the power of managing these funds and to monitor their utilization.

Theses (1) – (3) have, at least, two general implications. Theses (1) and (2) imply that the new fiscal rules should be based on a general framework compatible with country-specific FSPs and, if needed by disequilibria in the government balance sheets, on gradual adjustment processes. Theses (3) and (2) imply that the new fiscal rules should conceive the transitions, opened but not achieved by the RRF (typically the 'green' transition and part of the digital transformation), as events that are beyond the control of national policymakers and require specific long-term funds at the EU level.

3. A few clear-cut rules

The two implications, set at the end of the previous section, lead to the following features of the new Stability and Growth Pact (SGP), to be conceived throughout national FSPs:

(i) The quantitative and qualitative thresholds, specified in the original European Treaty (Public Deficit/GDP ≤ 3% in normal circumstances, and the convergence to a Public Debt/GDP ≤ 60% at an appropriate pace), are sufficient to build a simple framework of general rules.

(ii) Each member state should commit to manage its public finances compliant with this framework in a shifting long-term horizon (ten years), thus determining a country-specific FSP to be rolled-over and to be assessed and monitored by the Commission (and approved by the EU Council) every year; in this perspective, the new fiscal rules should determine a revision of the European Semester and should specify the role played by the European Parliament and, where needed, by the European Council in the new setting (*see also below*, point iv).

(iii) In case an EU's member state reported significant disequilibria in one or two of the traditional fiscal parameters (*see* point (i)), its FSP should include a detailed long-term adjustment process aimed at gradually converging towards these parameters; the related corrections in the public deficit and/or debt should be agreed with the European Commission, should be approved by the EU Council, and should be compatible with a sustainable path of national growth; once agreed and approved, these same corrections will become compulsory, given that they are rolled-over and can be revised on a yearly basis (under the new European Semester).

(iv) The revised European Semester should merge the current RRPs, Stability programmes and National Reform programmes into a single document (the above mentioned FSPs), to handle and – if needed – to adjust the budget (*see*

points ii and iii, *respectively*); hence, the new European Semester would become the central coordination tool in the EU.

(v) The previous points (i) – (iv) imply that the new SGP should be composed by the two traditional (quantitative and qualitative) thresholds and by the related national FSPs, that include – if needed – the agreed country-specific long-term adjustment processes; in normal circumstances (*to be specified below*, *see* Section 4), each member state is constrained to meet the requirements of this new SGP under penalty of the obligation to accept and comply with the binding corrections unilaterally imposed by the European institutions for the incoming years.

(vi) To meet the costs of the public investments jointly assessed as necessary to handle the transition processes and other essential needs determined by events not manageable by national policymakers, European funds should be activated; therefore, each member state could implement its sustainable growth path (*see* point (iii)) under the new processes and, in the meantime, it could adjust its balance sheet in the long term, in compliance with the agreement reached with the European Commission.

(vii) Given the current European programmes, we already suggested that the implementation of the 'green' transition should be considered as an 'exceptional event beyond the control of national policymakers' that will last well beyond the end of the RRF (and the same should possibly apply to the digital transformation); hence, the related public investments approved by the European Commission in each country, should be subtracted from the national deficit and debt by means of an appropriate European fund (*see also*: Darvas and Wolff, 2021).

(viii) This specific 'golden rule', which should apply to all the exceptional events requiring a large amount of public investment and producing positive externalities (not fully internalized at the national level), could lead to the centralized financial coverage of European public goods under the ex-ante and ex-post control of the Commission and the approval of the EU Council.

(ix) Given that 'green' and digital investments have strong impacts on the restructuring of the national production systems and on the related composition of the labour demand, it could be appropriate to extend the European financial coverage to the public expenditures required to adapt the training and skills of human resources to these transformations.

(x) However, these expenditures, listed as current ones in the European accounting framework, leave room to distortionary opportunistic behaviours by national policymakers; hence, it would be convenient to apply to these expenditures the new 'golden rule' only within the limits of a fixed percentage of the original public investment (for instance, the 'green' one). The experience of RRPs' adoption (notably the assessment for the compliance with the 37% and 20% thresholds for the green and digital expenses, and the application of the *Do-No-Significant-Harm* condition) shows that the Commission has the tools to prevent 'green washing'.

It is important to emphasise that points (i) – (v) and the consequent abolition of some of the current fiscal rules (for instance the yearly reduction of 1/20th of the difference between the current Public Debt/GDP ratio and the target of 60%) **do not require changes to the European Treaties.** As illustrated in Tosato (2021b),[4] they can be enacted by a unanimous vote of the EU Council on the Commission's proposals. The same applies to points (vi) – (x). Hence, our suggested new SGP and the complementary activation of the European funds are compliant with the current legal framework. Let us also stress that points (i) – (x) implicitly refer to a number of questions raised by the Commission in launching the public consultation. In the following sections, we will try to make these links more explicit.

4. A simplification of the fiscal rules

Point (i) suggests going back to the basics of the European Treaties in order to drastically simplify the current and unmanageable fiscal rules.

The EU's fiscal rules have become too complex through time (*see also*: Giavazzi *et al.*, 2021). To overcome the pro-cyclicality of the original ill-founded thresholds (3% for the Public Deficit/GDP, and 60% for the Public Debt/GDP), they have been based on unobservable quantitative indicators such as the output gap, the structural deficit, and the Medium-Term Objective (MTO). Moreover, the restrictive changes introduced by the Six Pack, the Two Pack and the so-called Fiscal Compact in the years 2011-2013 have strengthened the frictions between the application of these rules and the implementation of sustainable national fiscal policies.

[4] This paper offers the general legal bases for our analysis and proposals.

The pandemic break is taking these problems to an end. The structural equilibrium in the government balance sheets (Public Deficit/GDP ≤ 0.5% if Public Debt/GDP > 60%), the reduction pace of the public debt exceeding the 60% relative to GDP (as recalled, 1/20 per year), and the increases in public expenditures restricted to the growth rate of the potential output are not conceivable in the post-pandemic world (even more so if we consider the need to massively finance the two major transitions).

On the other hand, the exit from this maze cannot be found in a more flexible implementation of the current fiscal rules. At the beginning of 2015, the Commission pursued that solution with a double unintended and distortionary result: increasing the complexity in the implementation of the already too complex fiscal rules; and incentivising (a) more public deficits in countries without fiscal capacity, and (b) a restrictive stance in the policies implemented by countries with large fiscal capacity. Points (a) and (b) highlight – if it came to – that **any suppression of centralised fiscal rules in the EU through the recourse to a permanent 'general escape clause' would be inappropriate.** This move would be equivalent to incentivising extreme opportunistic behaviours on the side of national policymakers. Moreover, the lack of a centralised fiscal rule would send wrong signals to financial markets, inducing an increase in the interest rates on public securities for the most indebted countries that could undermine the sustainability of their balance sheets. Conversely, well designed European fiscal rules would help national governments and Parliaments of highly indebted countries to pursue a gradual public debt reduction, despite the opposition of a part of the public opinion and of the political parties.

Our suggested solution is, thus, to go back to the two simple, transparent, and observable indicators included in the original Treaties: (a) Public Deficit/GDP ≤ 3% in normal circumstances, and (b) the convergence to a Public Debt/GDP ≤ 60% at an appropriate pace. We are fully aware that these indicators do not have a scientific underpinning, and that various scholars and institutions are looking to redefine the quantitative thresholds of these two indicators by only amending the Protocols annexed to the Treaties (*see for instance*: ESM, 2021). However, we maintain that these suggestions are not so important in the light of our emphasis on the country-specific fiscal plans.

Nevertheless, a return to the original fiscal rules raises the same unsolved questions that have suggested some of the negative refinements introduced since 2005. Specifically, the elimination of structural indicators and the exclusive reference to nominal variables suffer a problem of pro-cyclicality. This is one of the reasons why point (ii) (*see above*, Section 3) emphasises **the pivotal role to be played by national FSPs.** The two traditional fiscal

ratios (Public Deficit/GDP and Public Debt/GDP) should represent a target to be approximated by following country-specific paths. However, to avoid that national policymaker (especially in the most indebted countries) pursue opportunistic behaviours, it is necessary that these specific paths be bilaterally agreed with the Commission, include – if needed – gradual but adequate decreases in deficit and/or public debt, be exposed to a yearly centralised assessment, and become compulsory in normal times once the bilateral agreement is reached and approved by the EU Council.

There is a second and most important reason why the national FSPs are crucial. Effective centralised fiscal rules should take into account the situation of each member state and should support an economic and social convergence within the EU. NGEU shows that the same size does not fit all the different countries. Hence, the new fiscal rules should offer a general framework that can be efficiently met by each country. Moreover, each of the EU' member states should adjust its disequilibria and converge towards the two simple fiscal rules at its efficient pace, without giving up its objective in terms of economic and social development. For instance, it would be over-ambitious to ask to a euro area's country with a huge public debt (and a consequent high financial burden) to be immediately compliant with the 3% threshold, if there were negative conditions imposing an increase in public investments or in public current expenditures.

In principle, the bilateral agreements with the Commission should offer a protection towards negative events hitting each of the EU's countries. However, these events cannot be fully foreseen. For instance, it is difficult to perfectly anticipate the timing of a downturn in the cyclical expansion of the European economy; and it is even more difficult to forecast all the possible idiosyncratic shocks that are threatening a specific member state. This explains the emphasis on normal circumstances in point (v) (*see above*, Section 3). Once unforeseen negative events are significant and are acknowledged as such by the European institutions, countries involved are not committed to meet their previous fiscal engagements and are required to re-negotiate their specific national FSPs with the Commission as soon as possible (that is, without waiting for the incoming European semester). In addressing these events, the Commission should handle the most problematic national cases as a priority.

5. *'Golden rules', discretion, and sanctions*

The unforeseen abnormal events, recalled at the end of the previous section, should not be confused with the 'exceptional events beyond the control of national policymakers'

listed in points (vi) – (x) (*see above*, Section 3). In our perspective, the latter require the introduction of a specific '**golden rule'** and not a simple renegotiation of the country-specific plans or adjustment processes.

As indicated by the NGEU and the RRF, 'green' transition, digital transformation and other possible exceptional events require a huge amount of public investments; moreover, the implementation of these investments have dramatic effects on the obsolescence of the existing stock of capital goods and of the traditional professional skills of human resources. If EU countries with low fiscal capacity had to account the consequent public expenditures in their balance sheets, they would be unable to meet the commitments agreed with the Commission in terms of long-term adjustments of their fiscal disequilibria. On the other hand, if these same countries had to give up or reduce their 'green' or 'digital' public investments and the related public expenditures to be compliant with their long-term adjustment plans, they would be excluded from the European transition processes and would diverge from the other member states. Particularly in the case of big countries (such as Italy), the latter solution would further compromise the successful transition towards carbon neutrality and digital transformation for the EU as a whole.

It follows that the European institutions should activate funds to financially support these public expenses at the national level, thus allowing the exclusion of these expenses from the national balance sheets[5]. As far as the grants are involved, the RRF offers a solution to the European financing of a significant part of the European 'green' and 'digital' investments and to a smaller part of the training programmes of human resources until the end of 2026. However, as repeatedly stated, the horizon of the 'green' transition (and, maybe, even of the digital transformation) goes far beyond the end of the NGEU. Moreover, in the period 2023 – 2026, the new European funds should also cover that part of the 'green' and 'digital' investments financed by the RRF's loans.

In order to put the possible opportunistic behaviours by the national policymakers (mainly, in countries with low fiscal capacity) under strict control, we suggest limiting the use of the European funds to those emergencies requiring a huge amount of public investments that produce inadequate monetary returns in the short term but crucial externalities in the medium-long term (currently, the 'green' investments and, perhaps, some of the digital investments). Moreover, we suggest the utilisation of these same funds to cover a pre-

[5] This aspect is emphasised by Draghi and Macron (2021). The implementation of a 'golden rule' to selectively support public investments is the 'strong point' of Mario Monti's position on the evolution of the European economic governance for a long time (since 1997, during the debate within the European Commission, of which Monti was a member: *see*: Di Vico 2008). On this point, see also: De Grauwe (2021).

determined percentage of the current public expenditures strictly related to those public investments; this percentage could be calculated as a fixed percentage of the relative investments. **In this framework, a sort of new specific 'golden rule' would come to the fore, again with no need of changing the current Treaties** (Tosato, 2021 b).

Despite our attempt to define a clear-cut general framework and to state transparent constraints to the country-specific FSPs and to the new 'golden rule', our approach to the new EU's fiscal rules attributes a significant discretionary power to the European institutions and – first of all - to the Commission. The latter enjoys a degree of discretion in reaching a bilateral agreement with each of the EU's member states, in assessing the execution of the country specific FSPs, and in handling the allocation of the European funds, subject to the final approval by the EU Council. From our perspective, this is not a weakness of our proposal. We are convinced that the positive evolution of the European economic governance must be based on a sequence of temporary and changing equilibria between rules and discretion. The political wisdom resides in the ability to identify the right compromise in each specific circumstance, avoiding in any case the excess of rules or the arbitrary prevalence of discretion. However, an appropriate institutional setting can help the identification and implementation of effective compromises.

A crucial ingredient in the construction of this institutional setting is the surveillance and the sanctioning power towards member states. Both these instruments should incentivise the actual compliance of each country with the general rules and its specific commitments; and should allow early corrections in case of deviations. The current European fiscal rules are based on a complex set of controls that include a preventive arm and a corrective arm. Both these arms have been strengthened by the implementation of the Six Pack and the Two Pack. However, the recent empirical evidence shows that member states have systematically met the ex-ante constraints but have not been compliant with them in term of ex-post achievements, without incurring in any significant sanction. This means that the current set of controls is inefficient and ineffective.

Our suggestion is to simplify the EU's supervisory and sanctioning tools by going back, even in this case, to the original European Treaties.

According to this approach, the European Commission should control the national management of public finances to avoid opportunistic behaviours and the consequent negative externalities to other member states; to this aim, the Commission should involve other European institutions (the EU Council and, possibly, the European Council) in the correction and sanctioning of "gross" fiscal errors.

According to our new suggested fiscal rules, this is equivalent to state that the Commission should check the execution of the national FSPs and the actual utilisation of the European funds. Under normal circumstances, should a member state deviate from the path designed by its FSP, the determinants and the importance of this deviation would be assessed by the Commission. In an emergency, an analogous assessment should be applied to a deviation in the utilisation of European funds. If these deviations result from a "gross error", the Commission will propose to the EU Council to place the country involved into Excessive Deficit and, as is the case under the current rules, it will set the deadline and the fiscal targets that the country should meet to exit the procedure. The initiative of the Commission would acquire special weight by applying the reverse voting rule to the deliberations of the EU Council. If the member state failed to take 'effective action' to meet these targets, it would remain subject to the new SGP but its gradual adjustment process and its access to the European funds would be suspended until these actions were successfully implemented.

6. *Conclusions*

The adoption of new fiscal rules, along the lines specified above, would not simply affect the EU economic governance. These new fiscal rules could also ease a positive evolution of the EU economy and society. In this respect, let us specify five points.

First, these fiscal rules would make the 'green' transition convenient not only at the macro-level but also for the individual economic agents. Differently from a successful digital transformation, the 'green' transition is not largely based on private innovations because a significant part of the 'green' investments cannot obtain high rates of return in the short term. However, if it was made compatible with social inclusion, the 'green' transition would create the most important common good: the survival of human beings and of our planet. Hence, it is reasonable to utilise the fiscal rules to make the 'green' transition convenient also for individuals by producing positive externalities through the European support of public investments and of nationally subsidised private investments. In our market-based organisation, this step is necessary to implement a successful 'green' transition.

Secondly, the 'green' economy is a strength point of the EU in the international relations together with the social protection (welfare state) and the economic regulation. However, the EU economy is losing its centrality in the international markets due to its severe delay in digital transformation towards the USA and China. Our suggested fiscal rules could

incentivise those ‘green’ public investments that also trigger digital transformation. In this perspective, the new fiscal rules would contribute to the improvement of the European role in the international markets.

Thirdly, our suggested fiscal rules reduce the probability of failures in the country-specific FSP and contribute to the overcoming of the lack of public (and private) investments and of the related excess in aggregate savings characterising the EU economy for a long time and causing negative long-term interest rates. Hence, these new fiscal rules could make national public debts more sustainable in the medium-long term and, by supporting economic and social development, could strengthen the convergence between member states.

Fourthly, by resorting to European funds in a long-term sequence of events beyond the control of national policymakers, these same fiscal rules make the vertical coordination between a European fiscal policy and national fiscal policies *de facto* likely. This coordination creates a ‘coordination space’ that can help overcoming the intertemporal inconsistency between the implementation of the RRF and the adjustments in the country-specific fiscal imbalances. A by-product of this coordination could be a gradual progress in the collection of EU’s own resources.

Fifthly, our suggested fiscal rules could force in the background the intergovernmental approach and put the communitarian approach at the centre-stage. This evolution in the economic governance of the EU could represent the first step to build innovative relations of the European institutions with each of the member states.

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