STANDARD FORM OF EXPLANATORY MEMORANDUM FOR EUROPEAN UNION LEGISLATION AND DOCUMENTS

8171/20
COM(2020)500

Communication from the Commission to the European Parliament, European Council, the Council, the European Central Bank, the European Economic and Social Committee, the Committee of the Regions and the European Investment Bank - 2020 European Semester: Country-specific Recommendations

8201/20
COM(2020) 528 final

Recommendation for COUNCIL RECOMMENDATIONS on the 2020 National Reform Programme of the United Kingdom and delivering Council opinions on the 2020 Convergence Programme of the United Kingdom

COM(2020) 557 final

Report from the Commission: United Kingdom: Report prepared in Accordance with Article 126(3) of the Treaty of the Functioning European Union

Submitted by HM Treasury 2 June 2020

SUBJECT MATTER

1. The ninth European Semester began in November 2019 with the publication of the Commission's Annual Growth Survey, which set out the EU's growth priorities for the coming year.

2. The next stage of the European Semester was the publication of Country Reports in February 2020. The reports contained an assessment of the implementation of the 2019 Country-Specific Recommendations.

3. Following this, Member Sates submitted their National Reform Programmes (NRPs) and Stability or Convergence Programmes to the European Commission. Country-specific Recommendations were drafted by the Commission on the basis of these reports.

4. An Explanatory Memorandum has been submitted in parallel covering CSRs addressed to Member States and reports in relation to Article 126(3) of the Treaty of the Functioning European Union (TFEU) on Member States' excessive deficits

and budgetary situations.

5. The United Kingdom submitted its 2020 National Reform Programme in April and Convergence Programme in May. Although the UK Convergence Programme was due to be submitted by 30 April, UK law dictates it must be debated in Parliament. This debate could not be held in April due to the extenuating circumstances of the coronavirus pandemic.

6. The UK's 2020 CSRs are drafted by the Commission on the basis of it's February Country report and then further informed by the information submitted by the UK in these reports. At this stage the CSRs are draft recommendations and will be discussed by in Council committees in June, before being adopted by ECOFIN Council thereafter. Under the terms of the Withdrawal Agreement the UK will not participate in these Council discussions, so exchanges with the CION on the UK's draft CSRs have been carried out bilaterally.

7. The recommendations are not binding on the UK and the UK cannot be subject to sanctions under any part of the Semester process. For euro area Member States, there are binding elements and a risk of sanctions.

<u>Overarching Commission Communication on country-specific reports</u>

8. The Commission Communication summarises the major policy issues currently faced by the EU; takes stock of progress achieved by Member States in implementing structural reforms and correcting imbalances; explains its objectives for the 2020-21 recommendations; and outlines areas of concern going forwards.

9. The communication initially focusses on the impact of coronavirus. It notes that the European Union is facing an unprecedented economic shock resulting from the coronavirus pandemic and a coordinated economic response is necessary. It iterates a desire for the recovery to be focused on sustainability in line with the European Green Deal.

10. The report notes that the prognosis for the European economy in 2020 is for a recession of historic proportions, despite the swift and comprehensive policy response to Covid-19 at both EU and national levels. It notes that consequences will differ across Member States and re-iterates the need for a collaborative approach on the recovery strategy. It predicts that despite effective measures being put in place to protect jobs, the pandemic will have a severe impact on the labour market. Monitoring the effective capacity of Member States to provide effective response to the crisis will be an essential element of this years' refocused Semester.

11. Due to the gravity of the economic downturn likely to result from the COVID-19 outbreak, the Commission considered in its Communication of 20 March 2020, considered in EM COM(2020)123 submitted simultaneously, that the current conditions permit the activation of the general escape clause. The general escape clause does not suspend the procedures of the Stability and Growth Pact. It allows Member States to depart from the budgetary requirements that would normally apply while enabling the Commission and the Council to undertake the necessary

policy coordination measures within the framework of the Pact.

12. The objectives of the 2020/21 recommendations reflect the new socio-economic reality of the COVID-19 crisis. The key objectives are:
    - Providing an immediate economic policy response to tackle and mitigate the health and socio-economic impact of the Covid-19.
    - Restarting the economic activity and putting growth back on track, fostering the green transition and the digital transformation

13. The Commission believes that surveillance under the Macroeconomic Imbalance Procedure is of the utmost importance, because government debt is expected to increase sharply in 2020, departing from the global trend of the previous 5 years.

14. The report highlights the role that the EU budget can play in the recovery. Close alignment between the EU budget and the European Semester is essential to ensure stability, productivity and fairness in the economic recovery across the EU with the twin green and digital transitions at its heart.

Draft 2020 Country-Specific Recommendations to the UK

15. The draft 2020 UK CSRs are to:
    1) In line with the general escape clause, take all necessary measures to effectively address the pandemic, sustain the economy and support the ensuing recovery. When economic conditions allow, pursue fiscal policies aimed at achieving prudent medium-term fiscal positions and ensuring debt sustainability, while enhancing investment. Strengthen the resilience of the health system.
    2) Ensure the adequacy and coverage of the social protection system to provide support for all and in particular those most affected by the crisis.
    3) Foster innovation and support human capital development. Front-load mature public investment projects and promote private investment to foster the economic recovery. Focus investment on the green and digital transition, in particular on housing, clean and efficient production and use of energy, sustainable transport infrastructures and high-speed broadband networks.

16. As recommendations under the Semester are non-binding on the UK, we are not obliged to act on them if they appear to impinge on UK flexibility to achieve policy outcomes in a manner that best fits the UK's national circumstances.

United Kingdom Report in relation to Article 126(3) of the TFEU from the Commission

17. The Commission has assessed that due to the coronavirus pandemic the UK's general Government deficit is likely to exceed 3% of GDP in 2020/21.

18. Due to the rise in borrowing caused by the pandemic, the Commission activated the general escape clause on 20 March 2020, as described in EM COM(2020) 123, which has been submitted simultaneously.

19. Regardless of the activation of the general escape clause, the UK cannot be subject to sanctions for an excessive deficit.

20. An Explanatory Memorandum has been submitted in parallel covering the Reports in relation to Article 126(3) of the TFEU and the country-specific recommendations addressed to the EU Member States.

21. The report assesses the UK's medium-term economic position, medium-term budgetary position and medium-term government-debt position. It notes that the sizeable economic downturn due to the coronavirus pandemic significantly affects each.

22. According to the Commission 2020 spring forecast, the general government deficit in the United Kingdom is expected to have been 2.5% of GDP in the financial year 2019-20, while general government debt is expected to have been 85.2%. However, for 2020-21, the Commission forecasts that the United Kingdom's deficit is expected to be 10.7% of GDP in 2020-21, while debt is expected to be 102.5% of GDP. The Commission concludes that all the evidence available to the Commission, including that provided by the UK Government, suggests that the severe economic downturn associated with the COVID-19 pandemic will lead to a deficit significantly in excess of the 3% of GDP threshold in 2020-21. The Commission also predicts a general Government deficit of over 3% of GDP threshold in 2021-22.

23. The forecast excess is considered to be exceptional and not temporary as defined by the Treaty and the Stability and Growth Pact.

24. The Commission considers its current forecast of a deficit of 10.7% of GDP in 2020-21 as sufficiently compelling prima facie evidence of an excessive deficit defined by Article 126(2)(a) of the Treaty. Hence, the analysis suggests that prima facie the deficit criterion as defined by the Treaty and Regulation (EC) No 1467/97 is not fulfilled.

25. The report also surmises that UK general government gross debt is expected to have been 85.2% of GDP at the end of the financial year 2019-20, above the 60% of GDP Treaty reference value. The report states that the United Kingdom is not expected to have made sufficient progress towards meeting the debt reduction benchmark in 2019-20.

SCRUTINY HISTORY

26. Country-specific Recommendations are given by the European Union on an annual basis. EM 6701/19, 6729/19 on the UK Country Report 2019 and a Communication from the Commission on the 2019 European Semester was submitted on 5 April 2019. It was cleared in the House of Lords European Select Committee Chairman's sift no. 1737 by the Financial Affairs subcommittee on 24 April 2019, and by the House of Commons European Scrutiny Committee considered in Report no. 64 on 1 May 2019 and did not warrant any further follow up and cleared.

MINISTERIAL RESPONSIBILITY

27. The Chancellor of the Exchequer has responsibility for United Kingdom policy on European Union monetary and economic issues. The Secretaries of State for Health; Work and Pensions; Business, Energy and Industrial Strategy; Transport; and Housing, Communities and Local Government have interests in the policy areas covered by the CSRs.

INTEREST OF THE DEVOLVED ADMINISTRATIONS

28. Policy on European economic governance is a reserved matter under the UK's devolution settlements. The Country-specific Recommendations were shared with Devolved Administrations by HM Treasury on 21 May 2020.

LEGAL AND PROCEDURAL ISSUES

i. Legal basis

29. The legal base for the Council Recommendations on Member States' NRPs is Articles 121(2) and 148(4) of the Treaty on the Functioning of the European Union (TFEU). The legal base for the Council opinion on Member States' Stability and Convergence Programmes is Council Regulation (EC) No 1466/97 of 7 July 1997. The legal basis for the Council Recommendation on the implementation of the broad guidelines for the economic policies of the Member States whose currency is the euro is Article 136 TFEU.

30. The legal base for the report on the UK's projected excessive deficit for 2020-21 is set out in Article 126(3) of the Treaty on the Functioning of the European Union.

31. The Justice and Home Affairs (JHA) opt-in is not a consideration for these documents.

i. European Parliament Procedure

32. Not applicable, this is not a proposal for legislation.

ii. Voting procedure

33. Qualified majority. For the measures adopted under Article 136 TFEU, only members of the Council representing Member States whose currency is the euro take part in the vote.

iii. Impact on United Kingdom Law

34. No impact.

iv. Application to Gibraltar

35. Not applicable.

v. Fundamental Rights analysis

36. No issues arise.

APPLICATION TO THE EUROPEAN ECONOMIC AREA

37. Not applicable

SUBSIDIARITY

38. The recommendations and opinions are based on the exclusive powers to make recommendations and opinions as set out in Articles 121(2), 136 and 148(4) TFEU.

POLICY IMPLICATIONS (including implications for the application of EU law during the Implementation Period and under the Northern Ireland Protocol)

39. The UK continues to participate in the European Semester process during the Transition Period as agreed in the Withdrawal Agreement but cannot be subject to any sanctions under the Semester, nor has any obligations to implement the recommendations set out in the Country-specific recommendations.

40. Nevertheless, the Government takes note of the Commission's draft CSRs to the UK. The Government considers that the CSRs appropriately capture the fiscal and investment challenges facing the UK and are broadly consistent with the Government's own priorities in these areas, which it has already been acting on.

41. The Government also takes note of the Commission Communication on the 2020 European Semester.

CONSULTATION

42. Not applicable

IMPACT ASSESSMENT

43. Not applicable

FINANCIAL IMPLICATIONS

44. None

TIMETABLE FOR ADOPTION AND IMPLEMENTATION IN THE UK (WHERE APPROPRIATE)

45. The UK does not have any obligations to implement the Country-specific recommendations documented. The UK's fiscal and economic policy is a matter for the UK Government to decide.

OTHER OBSERVATIONS

46. None

MINISTERIAL NAME AND SIGNATURE

STEVE BARCLAY MP

CHIEF SECRETARY TO THE TREASURY