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THE NETHERLANDS

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REPORT FROM THE COMMISSION

**presented under Article 8 of the Treaty on Stability, Coordination and Governance in
the Economic and Monetary Union**

THE NETHERLANDS

The Netherlands deposited its instruments of ratification of the Treaty on Stability, Coordination and Governance in Economic and Monetary Union (TSCG) with the General Secretariat of the Council of the European Union on 8 October 2013.

National provisions considered in the assessment are essentially those provided for by:

- the Law on the Sustainability of Public Finances (LSPF) adopted on 11 December 2013,
- the Council of State Act as amended by the Act of 22 April 2010 (the CoS Act),
- the Internal Rules of the Dutch government,
- the Internal Rules and Procedures of the Advisory Division of the Council of State,
- the Memoranda of Understanding signed between the Council of State and the Ministry of Finance and the CPB, respectively.

1. Legal status of the provisions

The LSPF is an ordinary law and as such a regular budget law may in theory overrule it. However, due to the monist nature of the Netherlands' legal system, international Treaties which are binding on all persons by virtue of their contents will become binding after they have been published (Article 93 of the Constitution). National statutory regulations are not applicable if conflicting with international law (Article 94 of the Constitution), with national courts being deemed to apply international law. Therefore, the TSCG itself forms part of the national legal order and it has, in the national hierarchy of legal norms, a higher status than the annual budget laws.

Since the LSPF does not enjoy hierarchical superiority over budget laws, it is necessary to examine the availability and effectiveness of (judicial) control in case of a potential breach of the Fiscal Compact. The Netherlands has explained to the Commission that for each draft bill the Council of State carries out an ex ante control, examining its conformity with the Constitution and ratified international treaties. However, the role of the Council of State in that matter is nevertheless advisory. Moreover, once a (budget) law is adopted there can be no judicial control as to its compatibility with the Fiscal Compact.

The uncertainty and the apparent weakness of the available legal review should nevertheless be balanced by two important considerations.

As regards the legal status of the provisions, the Netherlands authorities formally committed that their national legal framework obliges the annual budget bill to be adopted in compliance with the provisions of TSCG and the LSPF¹.

Secondly, the strict enforcement of the LSPF appears also to be guaranteed by the robustness of the monitoring mechanism set up in accordance with the TSCG (see Section 4 below).

Against that background, and in the light of the formal commitment provided by national authorities that the Dutch legal framework obliges the annual budget bills to be adopted in compliance of the provisions of the TSCG and the LSPF together with the positive assessment

¹ Letter of the Dutch authorities of 19 August 2016.

of the existence of an independent and operational monitoring institution, the provisions of the Netherlands comply with the criterion of being of "binding force and permanent character, preferably constitutional, or otherwise guaranteed to be fully respected and adhered to throughout the national budgetary processes".

2. Balanced budget rule

Formulation: The balanced budget rule is set out in the LSPF and has been incorporated in Article 2 as part of the so-called "trend-based" fiscal policy.

Article 2(3) stipulates that the "trend-based" fiscal policy must respect ("*met inachtneming van*"), among others, the medium-term objective (MTO), the procedures related to it as well as the related recommendations issued by the Union institutions. The MTO is defined in Article 1 as a medium-term objective set for the structural balance, as established by the Council of the EU. Moreover, the authorities confirmed to the Commission, in their letter of 19 August 2016, that provisions stemming from the TSCG are of direct effect in national law. As the lower limit is explicitly stated in Article 3(1)(b) of the TSCG, its effective incorporation in national legal order is ensured without further specification in national provision.

Convergence towards the MTO: The legislation does not contain specific provisions regulating the convergence towards the MTO. However, Article 2(3)(b) requires fiscal policy to be conducted respecting ("*met inachtneming van*") procedures laid down by the Union institutions for complying with, among others, the MTO. In addition, Article 2(3)(c) requires the recommendations by the Union to comply with, among others, the MTO to be taken into account ("*rekening houdend*"). According to the interpretation submitted by the authorities, that requirement would also cover a situation when the Council recommends the Netherlands to accelerate its convergence path towards the MTO.

Escape clauses: The legislation does not contain specific provisions concerning escape clauses. However, the general requirements contained in points (b) and (c) of Article 2(3) can also be interpreted as covering the SGP provisions related to deviation from the MTO in the event of exceptional circumstances.

Overall, the balanced budget rule is compliant with TSCG requirements. Given that the TSCG takes effect in the national law directly, the formulation of the balanced budget rule can be considered in line with the TSCG. That reasoning has been conveyed by the authorities to the Commission.

3. The correction mechanism

The provisions laying out the correction mechanism are mostly found in Article 2 of the LSPF, notably paragraphs (4) to (8) thereof.

Activation: Two situations lead to the activation of the correction mechanism. The first (Article 2(5) LSPF) is when a competent body at Union level establishes that budgetary policy does not sufficiently comply with the medium-term objective norm and makes a recommendation to that end. As clarified by the Dutch authorities, that provision ensures in particular that a Council recommendation to take additional measures following an observed significant deviation would automatically trigger the correction mechanism.

The other possibility for activation (Article 2(4) LSPF) is for the Ministry of Finance on its own initiative to establish insufficient compliance with budgetary norms (of which compliance with the medium-term objective and the adjustment path thereto is part). That

second option may allow for earlier corrective action to be taken. However, the legislation is not specific as to the precise circumstances that would lead to identify such a situation, which leaves discretion to the Ministry of Finance.

The monitoring institution, the Council of State, has to deliver its views on the observance of the rules (Article 2(8) LSPF) once a new budget is presented or once corrective measures are already proposed.

Substance of the correction: In the event of activation, the government has to present to Parliament a corrective plan (Article 2(6) LSPF), which in practice is likely to take the form of a supplementary budget.

The law requires the corrective measures to address the non-compliance with the budgetary norms (Article 2(4) LSPF), and, in the event that the procedure is triggered by a significant deviation procedure at the level of the Union, to comply with the recommendation of the relevant Union body (Article 2(5) LSPF). The latter obligation refers to both the size and the timing of the corrective measures. The Council of State assesses the corrective plan, and that assessment is presented to Parliament.

The main characteristic of those requirements is to focus on consistency with Union recommendations while preserving national flexibility. The legislation does not contain specific national corrective rules. The duty to strictly abide by recommendations made by the Union institutions is thus the principal means to ensure compliance with the TSCG requirement of correcting the deviations "over a defined period of time" and with the common principles.

In addition, the "trend-related" budgetary framework relies significantly on multiannual expenditure ceilings, and on floors on the yield of tax measures, covering a large fraction of general government and agreed upon at the beginning of legislative periods. Adherence to those objectives may be instrumental in delivering corrections. Besides, the law includes specific provisions aimed at ensuring that local and regional authorities deliver their agreed share of the fiscal effort. Deviations are addressed in the formal intergovernmental meeting, backed by the possibility of a cut in transfers to those entities (Article 6 LSPF). Other mechanisms are in place for other non-central government entities, such as the social security funds.

Overall: The correction mechanism is compliant with the TSCG requirements and the common principles. It stresses consistency with the Union budgetary surveillance framework, whereby the activation and substance of the correction are linked to recommendations made by the Union institutions. Specific national provisions directly impinging on the substance of the correction are limited in the legislation, though multiannual expenditure ceilings may be instrumental in delivering effective corrections.

4. The monitoring institution

The Dutch monitoring institution is the Advisory Division of the Council of State (CoS-AD).

Set-up and statutory regime: The Council of State (CoS), which dates back in a different format to the sixteenth century and which is officially headed by the King, is a body founded in chapter 4 of the Constitution, whose activity is regulated by the CoS Act. It is the principal advisor to the government and Parliament on national laws and international treaties, as well as the Netherlands' highest administrative court. It consists in two divisions, namely the Advisory Division and the Administrative Jurisdiction Division. The CoS, its divisions and its committees are composed by State Councillors and State Councillors in extraordinary service.

The specific responsibility assigned to the CoS-AD in relation to the Fiscal Compact is provided by the LSPF and adds to its pre-existing mandate to provide advice on all draft laws, including budget laws. A Special Committee for Budget Supervision (SCBS) chaired by the Vice-President of the CoS was established in 2015 within the CoS-AD, pursuant to Article 7 of the Internal Rules and Procedures of the Advisory Division of the CoS². Its role is to prepare the assessments related to budget laws, which implicitly include the TSCG-related assessments. These assessments are then endorsed by the State Councillors of the CoS-AD in full composition.

Mandate: The CoS Act grants a broad mandate to the CoS-AD, including the provision of advice on draft laws to be presented to Parliament (Article 17). The scope of draft laws concerned includes annual budget laws and excludes laws amending the central government budget (Article 19). In addition, the LSPF explicitly mandates the CoS-AD to "be heard" on the annual budget law (Article 2(8)) and also specifically on the initial correction plan and annually on its execution (Article 2(4) to 2(8)). As such, the government informs the Parliament annually on the application of the correction mechanism through the budget law – noting that the budget law itself has to be assessed by the CoS-AD. That mandate based on the LSPF is explicit when the correction mechanism is triggered based on the detection of insufficient compliance with the MTO by the Union institutions. There are no similar specifications in case the insufficient compliance is detected by the Ministry of Finance. However, the CoS mandate of assessing annual budget laws is deemed sufficiently broad, and the obligation of the government to submit a correction plan and report on its progress to the Parliament appears sufficiently constraining so that the CoS-AD is effectively able to signal the necessity to activate the correction plan and to assess its progress. The assessment of escape clauses is not included in the CoS-AD mandate as no specific escape clauses are laid down in relation to the structural balanced-budget rule.

Comply-or-explain principle: The principle is reflected in the CoS Act (Article 26(2)), the internal rules of the Dutch government No 41 and No 42³ and the Memorandum of Understanding signed between the CoS and the Ministry of Finance. The CoS discusses its initial advice with the government. The government is requested to reply to the advice of the CoS in every case, by means of a "*nader rapport*", stating whether the CoS advice is followed (or else explain why not). After the discussions between the CoS and the government, the former has to publish its initial advice, the government's reply and its final advice.

Freedom from interference and capacity to communicate: Before accepting their office, the Vice-President and the members of the CoS are required to pledge that they will refuse any interference (Article 6 of the CoS Act). They cannot be dismissed by the government and are not allowed to hold a number of positions, including in public offices, if to do so would entitle them to any allowance or fixed remuneration and in public bodies if it is acquired via an election (Article 5 of the CoS Act). The TSCG-related assessments are prepared by the SCBS and endorsed by the CoS-AD in full composition, including those members who are part of the SCBS. According to the Dutch authorities, whereas the CoS-AD in full composition may suggest amendments or additions to the SCBS assessments, those will not be integrated unless the rapporteur of the SCBS – designated from among its members – can accept them as compatible with the assessment.

² <https://www.raadvanstate.nl/onze-werkwijze/advisering/regeling-werkzaamheden.html>

³ <https://www.kcwj.nl/kennisbank/draaiboek-voor-de-regelgeving/hoofdstuk-2-formele-wetten-op-voorstel-van-de-regering-n--8?cookie=yes.1469036157861177448984>

The Dutch Constitution states that all advice of the CoS is made public (Article 80). The Minister concerned by the CoS-AD advice (in this case, the Minister of Finance) is also required to publish the initial advice, the government reply and the final advice of the CoS. The Memorandum of Understanding between the CoS and the Ministry of Finance specifies that the CoS itself publishes its advice⁴.

Nomination procedure: Articles 2-3 of the CoS Act describe the general nomination rule. State Counsellors are nominated by the Minister of Home Affairs in consultation by the Minister of Justice, taking into account the recommendation from the CoS for which the Advisory Division is consulted. The State Councillors are then appointed for life by Royal Decree. However, they could also be appointed for a fixed term of at least three years provided they are not entrusted with the administration of justice. State Councillors in extraordinary service can be appointed for limited tasks; they enjoy the same position and the same (voting) rights as other 'regular' State Councillors in the division in which they are appointed. With respect to the TSCG-related assessments specifically and as confirmed by the Dutch authorities⁵, the SCBS is chaired by the Vice-President of the CoS and consists of State Councillors and State Councillors in extraordinary service with relevant expertise and experience in public finance, macroeconomics, financial markets, tax matters, European law and/or government administration.

Resources and access to information: The SCBS is composed of State Councillors and State Councillors in extraordinary service, who are assisted in their activity by dedicated staff. The Dutch authorities have indicated that, in light of the CoS' new function as national monitoring institution for the purposes of the Fiscal Compact, the CoS-AD has been reinforced with three State Councillors in extraordinary service with specialist knowledge and expertise in the field of economics and public finance, who have been assigned to the SCBS. The resources available for the mandate related to the Fiscal Compact have to be considered in the context of the division of responsibilities between the CoS-AD and the Dutch Bureau for Economic Policy Analysis (CPB), as established in the LSPF. The CPB is institutionally attached to the Ministry of Economic Affairs but enjoys operational independence guaranteed by law⁶. The CPB is mandated by law to provide *inter alia* the calculation of the structural budget balance to be used by the CoS-AD for its assessments (Article 2(11) of the LSPF). The Memorandum of Understanding signed between the CoS-AD and the CPB adds that the CoS-AD can request economic analyses and reports from the CPB in order to carry out its assessment mandate. It should be noted that CPB has a separate sector which focuses on public finances and which, according to the Dutch authorities, employs a nearly 35 full-time equivalent staff.

The total annual budget of the CoS amounts to EUR 60 million, allocated as necessary across its divisions. The Dutch authorities have indicated that the CoS is free to scale up its Advisory Division in terms of resources and budget if it so decides, for example when the correction mechanism would be triggered⁷.

Articles 23- 25 of the CoS Act secure a broad access by the CoS-AD to information it requires. Also, the Memoranda of Understanding signed with the Ministry of Finance and the CPB respectively include detailed provisions to that effect.

Overall, the set-up of the Dutch monitoring institution is compliant with the TSCG requirements and the common principles in light of the clarifications provided by the national

⁴ The CoS website is available at: <https://www.raadvanstate.nl/>

⁵ Letter from the Dutch authorities of 19 August 2016.

⁶ "Wet houdende de voorbereiding van de vaststelling van een Centraal Economisch Plan" of 21 April 1947.

⁷ Letter from the Dutch authorities of 10 September 2015.

authorities on the functional autonomy of the monitoring institution and the competence requirements for its members. The CoS-AD is grounded in law with a broadly delineated mandate providing the basis for carrying out the tasks foreseen by the Fiscal Compact and the common principles. The legal and institutional framework includes appropriate safeguards for functional autonomy. The 'comply-or-explain' principle is provided for in the law and further elaborated in the Memorandum of Understanding with the Ministry of Finance. Adequate provisions and institutional arrangements concerning the CoS-AD's endowment with resources and access to information are in place.

5. Conclusion

The national provisions adopted by the Netherlands are compliant with the requirements set in Article 3(2) of the TSCG and in the common principles in light of the formal commitment provided by national authorities that the Dutch legal framework obliges the annual budget bills to be adopted in compliance of the provisions of the TSCG and the LSPF together with the compliant set-up of the monitoring institution, and the clarifications provided by the national authorities on the functional autonomy of the monitoring institution and the competence requirements for its members.