Established outside the Community framework by an intergovernmental treaty, the European Stability Mechanism (ESM) is a permanent rescue mechanism aimed at safeguarding the financial stability of the euro area. It was created at the height of the sovereign debt crisis in order to help governments which had lost, or were about to lose, access to financial markets. It entered into force in October 2012, replacing several other ad-hoc rescue mechanisms. Help provided is subject to strict conditionality.

Attempts to create such a mechanism for the euro area under Community law failed for legal reasons. Article 136 TFEU was modified, stipulating that the 'Member States whose currency is the euro may establish a stability mechanism ... subject to strict conditionality'. This gave the green light to create the ESM on an intergovernmental basis, but not as a Community instrument. The legality of the ESM was challenged, but in its Pringle case, the European Court of Justice (ECJ) ruled that the Member States had the right to establish the mechanism on an intergovernmental basis.

The ESM treaty stipulates that an annual report be made available to national parliaments. The intergovernmental character of the ESM explains why the European Parliament has no scrutiny rights. However, the ESM accepted to informally exchange with the relevant EP committees. In its resolution of 10 June 2013 on strengthening democracy in the future EMU, and repeatedly since, the Parliament reiterated its demand that the ESM be integrated into the Community framework and be made accountable to Parliament.

On 6 December 2017 the Commission made a proposal to create an EMF anchored in the Union legal framework. The tasks and the financial means of the ESM would be transferred to the EMF, and other tasks could be added at a later stage, such as serving as a common backstop to the Single Resolution Fund. The management and decision-making mechanism would be changed by departing - in selected cases - from the principle of unanimity. The possibility over time to develop new financial instruments to support other EU programmes is given, and a possible stabilisation function for the economy is envisaged. If wishes of the Commission were to come true, such as that of a Commissioner also being elected at the helm of the Eurogroup, then the its role within the EMF might be substantial, to the expense of the national ministers of economy and finance and possibly also of national parliaments.

At Council level, the discussions on a possible creation of an EMF (but not forcefully of the same kind as the one proposed by the Commission) was spearheaded by French President Emmanuel Macron. However, on 6 March 2018 the schedule for modernising EMU was de facto put into question after eight - mostly North-European - countries known as New Hanseatic League openly cautioned
against a far-reaching development of EMU.

On 19 June 2018 President Macron and Chancellor Merkel agreed (Meseberg Declaration) on proposing to the other Member States to transform the ESM into an IMF, adding tasks such as a backstop for the SRM. However, they foresaw to keep the ESM intergovernmental. Only in a later step would they envisage incorporating the ESM into EU law, but would do so while preserving the key features of its governance, i.e. the decision-making would stay with the Member States. They also suggested to also provide the ESM with tasks related to fiscal surveillance.

Although the Euro Summit of 29 June 2018 had been anticipated as a milestone in further developing EMU, the only palpable progress achieved was the decision to use the ESM as a backstop to the SRM, without going into details.

On 8 November 2018, the Hanseatic League issued a statement specific to the ESM. They support a reinforced ESM, provided it stays intergovernmental, i.e. it is not based on the Commission proposal. Further, the granting of financial support needs to be made under strict conditionality, the borrower’s debt sustainability and repayment capacity needs to be verified, and single limb collective action clauses must be introduced. The League also wants to increase the ESM’s analytical expertise, and have the ESM participate in all stages of program preparation and ex-post monitoring. An agreement was since found between the Commission and the ESM.

The Eurogroup and Eurosummits repeatedly discussed the matter, putting much emphasis on a possible role for the ESM as a backstop to the single resolution mechanism, but gradually moved away from integrating the ESM into EU law body. This was confirmed on 30 November 2020, when the Council decided to proceed with the reform of the ESM by further developing the ESM toolkit and by establishing a common backstop to the Single Resolution Fund (SRF), while keeping ESM intergovernmental.

In the European Parliament the Economic and Monetary Affairs Committee (ECON), rapporteur Pedro Silva Pereira (S&D, Portugal) is dealing with this file together with the Committee on Budgets (BUDG), rapporteur Vladimír Maňka (S&D, Slovakia). This is a consent procedure, where Parliament can only accept or reject the Council’s position, once that was reached. In order to nevertheless provide an input to the discussion, the EP decided to prepare an interim report. The committees’ interim report, which was adopted on 20 February 2019, welcomes the Commission’s proposal, suggests that the ESM retains both its current name and its intergovernmental character, and calls for a swift reform that also redefines its role, functions and financial tools. A fiscal backstop function for the SRF should be added and made operational as soon as possible. Fiscal and democratic oversight prerogatives of national parliaments should be maintained, and the European Parliament’s interaction with the ESM should be established. In the longer term, the ESM should be integrated into EU law. The interim report was adopted in plenary on 14 March 2019.
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Further reading:

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