EU uses new budget powers to demand more austerity in Italy and Spain

Spain and Italy have been warned that their budgets for 2014 are in breach of European Union rules as Brussels uses new powers to force governments to revise spending plans before national parliaments vote on them.

France was also cautioned that plans for painful economic reforms represent only “limited progress” as the European Commission exercised new eurozone powers in a historic shift of sovereignty away from elected governments.

“Because in an economic and monetary union, national budgetary decisions can have an impact well beyond national borders, member states have given the commission the responsibility,” said Olli Rehn, the commission vice-president in charge of the euro.

“I trust that they will thus be taken on board by national decision makers.”

Germany, Europe’s largest and most successful economy, was also criticised for making “no progress” in following EU recommendations to help its eurozone neighbours by spurring domestic demand and imports.

Despite disappointing growth figures and mounting concern that eurozone austerity policies are killing off recovery and locking southern European countries into protracted slump, the commission ruled that “further consolidation in euro area countries is necessary”.

For the first time, the EU’s Brussels executive has reviewed draft national budgets before national legislatures have voted on them, flexing political muscles aimed at preserving stability for Europe's single currency and at preventing a future eurozone debt crisis.

"This a historic moment," said an EU diplomat. "One has to ask whether the eurozone's voters yet appreciate what a huge shift in sovereignty this is away from national parliaments to conclaves of finance ministers and commission officials."

Italy and Spain, the third and fourth largest economies in the 17-strong eurozone, were upbraided for breaking debt reduction targets in breach of spending caps that are enshrined in the Maastricht Treaty that created the euro.

Backing off demanding the revision of budgets or penalties for now, Mr Rehn said he was "inviting" governments and parliaments to bring their budgets for next year into compliance with the rules as interpreted by the commission. "This exercise is much more about partnership than penalties," he said.

The commission's Italy verdict is political dynamite in a situation where Enrico Letta, the country's prime minister, is besieged in parliament by coalition disputes over tax reductions and Left wing opposition to austerity cuts.

Italy has the second-highest level of gross government debt in the eurozone, which is projected to rise to 133pc of the economy, second only to Greece, but it is in line with an annual target requiring annual debt to be under 3pc of annual GDP.

"We count on strong and effective delivery of these commitments by the government and parliament," said Mr Rehn. "Every day this year has been a politically sensitive moment in Italy. We just have to do our job."

Fabrizio Saccomanni, the Italian finance minister and a technocrat imposed on the Italian government at the behest of

EU officials, could be fatally weakened by the Brussels intervention, especially after Mr Rehn ruled out an exempting €3bn in investment spending that the Italian government has included in its 2014 budget.

Mr Saccomanni warned that Italy could not take the investment spending from the national budget to meet EU rules because the cut would threaten the country's already weak economic recovery and inflame opposition to austerity.

"We could have taken even more restrictive measures to reduce our public spending, but I imagine there would be even more cries of pain. I believe our approach is balanced," he said. "It is not necessary to change the budget."

Spain was told that its "draft budgetary plan is at risk of non-compliance with the rules, as the headline deficit target may be missed and the recommended improvement in the structural balance is currently not expected to be delivered".

France was given the green light on its budget but the commission warned that next year's budget leaves "no margin" for deviation and reforms "constitute limited progress" in addressing structural targets.

"A significant set of measures on top of those already specified will be needed to ensure that the target for 2015 is reached," said the commission.

The commission also cautioned Finland, Malta and Luxembourg, asking the three countries to review their 2014 budgets to ensure that they meet eurozone targets.

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