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Money Makes the World Go Round: How Much Difference Do **Recovery and Resilience Plans Make to EU Reform Governance?**

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Abstract

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The Next Generation EU (NGEU) package transformed European economic governance. This article examines the implications of this change in terms of EU polity formation and in terms of social policy content. It asks whether the temporary availability of large funds increases the leverage of the Commission in the European Semester and how this innovation affects sensitive policies. In the tradition of Stein Rokkan, the article advances a conception of the EU as a compound polity that needs to reconcile dispersed authority with second-order loyalty. We then contrast our theoretical expectations with traditional reform surveillance and experimentalist governance theories. The drafting of Recovery and Resilience Plans for Italy and Spain provides the empirical basis for assessing these expectations. The analysis shows a dual effect: adding fiscal capacity to the European Semester enhances the Commission's hierarchical power whilst the need to ensure member states' loyalty leaves room for national executives to insist on their priorities.

Keywords: fiscal governance; European Semester; Recovery and Resilience Facility; Next Generation EU; social policy

I. Authority and Loyalty in the EU Polity

With the Next Generation EU (NGEU) package, the EU has arguably moved away from primarily disciplining national budgetary policy towards augmenting member states' fiscal capacities in difficult times. This entails an expansion of the Commission's mandate and a paradigmatic change of its role: from the agent of fiscal surveillance to the broker of EU-financed public expenditures. The purpose of this article is to explore the implications of this change on EU polity formation, multi-level governance and policy content. Does the temporary availability of large funds give fiscal governance in the EU a hierarchical lever and make it more intrusive? What effect does EU funding and monitoring have on the content of sensitive policy areas like social policy? We focus on social policy examples as this has always been a particularly contentious domain in EU fiscal surveillance.

Our guiding hypothesis is twofold. First, funding indeed adds leverage to the EU level and thus strengthens top-down authority over national fiscal policy. However, and second, to avoid member states' potential pushback against an overpowering role of the EU (van der Veer, 2022), the drafting of these expenditure plans affords national authorities more influence on policy content, implying a more protective thrust compared with the traditional EU stance on social policy reform (Copeland and Daly, 2018). At first sight, our hypothesis about this dual effect is counter-intuitive: why should more fiscal power at the top should go

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hand in hand with more room for social policy design by the recipients further down the hierarchy? That money cannot buy obedience but must trigger engagement with the process makes sense for a theory of the EU in the tradition of Rokkan et al. (1999), including Stein Rokkan's incorporation of Albert Hirschman's (1970) model on *Exit, Voice and Loyalty*. This Rokkan–Hirschman model suggests that in a compound polity like the EU, the expansion of authority depends on building loyalty (Ferrera et al., 2023).

Two elements are crucial from our theoretical perspective. First, *compound* means that the EU polity has a diverse membership. Those who benefit less from the funding and/or are in any case sceptical of joint fiscal capacities will be attentive to its use by the main beneficiaries (Miró, 2022). Loyalty to the EU polity is thin or second order and has to be ensured by the Commission closely monitoring the intended use of the funds. Second, a characteristic of the EU polity is the *political weakness of its executive centre*: the Commission has no strong own source of legitimation, such as being directly elected. And even though the Commission has enforcement measures at its disposal, its effectiveness rests strongly on the co-operation of member states, here in the intended use of the recovery funds. This can only succeed if the loyalty of the main beneficiaries is also ensured. Hence, the politically weak centre must use its greater policy authority to steer member states towards spending plans that find favour with domestic audiences but also pass the self-governing body of member states, the Council.

In the next section, we will contrast this Rokkan-Hirschman model of polity formation with two normative theories of how governance of member state policies should work: either through surveillance of compliance with prudent policies (Beetsma et al., 2021; Giavazzi and Pagano, 1988) or through experimentalist peer review of continuous reform (Sabel and Zeitlin, 2008; Zeitlin, 2016). We translate these alternatives into observable empirical expectations for how the Recovery and Resilience Facility (RRF) works that contrast with our own approach. To see which approach captures the process more accurately, we study the experience of national and EU officials in the drafting process of National Recovery and Resilience Plans (NRRPs) for Italy and Spain. We opted for an in-depth comparison, given that studies with a larger set of countries (e.g., Bokhorst and Corti, 2023) and single case studies (e.g., Domorenok and Guardiancich, 2022) are already available.

The article proceeds as follows: in the next section, we review the literature on governance in the EU and what it implies for the newly created RRF, the central instrument of the NGEU package. We then outline our analytical framework. Our empirical evidence, presented in the fourth section, consists of a document and interview-based reconstruction of NRRP drafting (see Appendix A for the list of elite interviews). The fifth section concludes.

II. Theories of Fiscal and Social Governance in the EU

There is already a literature on what EU institutions – created during the long crisis decade generally and the NGEU package specifically – mean for governance and policy in the union (e.g., Bokhorst and Corti, 2023; D'Erman and Verdun, 2022; Martinsen and Goetz, 2022). We focus here on a stark contrast to derive observable implications for our empirical study.

There is first the time-honoured literature on fiscal surveillance. It sees European integration with its implicit or explicit guarantees of mutual support as a pervasive moral hazard problem for good policy-making in democracies. Opportunistic governments will take more risks, possibly by being complacent about reforming unsustainable policies that require more debt finance, in the knowledge that they can offload costs of downside risks onto others. The EU can redeem itself by providing the discipline that national democracies do not have. Fiscal rules, the no-bailout clause and central bank independence were the original commitment devices that tried to rein in governments' moral hazard problems inherent in European (monetary) integration. These commitment devices should be simple, uniform and transparent to create a clear link between violations of a commitment and sanctions.

A more recent strand of this literature acknowledges that unsustainable policies may not all be due to moral hazard but caused by events beyond governments' control. Risk sharing may be an explicit goal of the EU despite its incentives for moral hazard. This scholarship considers ways of helping reformers achieve their preferred policies (Beetsma et al., 2021). The European Semester with fiscal capacity can be rationalised as a constructive way to give governments and their constituencies the incentives to do the right thing (Freier et al., 2022). The Semester's original establishment in 2010 was seen as indicating a shift towards more stringency in EU governance through surveillance and guidance (Bauer and Becker, 2014). In this perspective, agenda setting and monitoring must be done by the EU: '[the arrangement] is meant to be a contract whereby money is intended to serve certain goals, and the EU checks that the conditions to achieve them are in place' (Pisani Ferry, 2020).

More explicit is the effort of scholars of experimentalist governance to understand how the EU differs from, and possibly improves on, the hierarchical government of nation-states (Sabel and Zeitlin, 2008). Experimentalist governance captures the general elements of a non-hierarchical method of policy co-ordination between equal partners: a structured process of searching for solutions amongst peers guided by a battery of indicators and grappling with similar problems but different institutional settings and capacities (Zeitlin, 2016). The European Semester, which structures various co-ordination processes in a reform and peer review cycle, presents several characteristics of an experimentalist governance architecture. This literature expects a positive feedback from the method of governance to the content of policy that reflects more closely the preferences of stakeholders, in particular in the social policy domain. Zeitlin and Vanhercke (2018, p. 150) claim that integrated governance has 'offered new opportunities for social and employment policy actors to defend and mainstream EU social objectives' that they successfully used to 'socialise' the European Semester. In this vein, Vanhercke and Verdun (2022, p. 124) conclude that the 'carrot' of available funding and the 'stick' of being able to withhold this funding will make the experimentalist governance of the European Semester more effective and social policy oriented.

The two literatures imply that governance and policy substance are closely linked, although in opposite ways. Our theoretical point of departure suggests that policy and

¹This literature was started by the rational expectations school in neoclassical economics, with a particularly relevant contribution by Giavazzi and Pagano (1988). The focus on 'credibility' and 'dynamic consistency' of policy-making has then been applied widely, not least in the EU.

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governance, function and form, are separable issues in the EU's compound polity. Policies can be used to build the loyalty of constituencies, whilst governance can use authority in different ways to enforce these policies. Funding is a persuasive way of making collectively decided policies happen: those who receive it tend to be grateful for the increased room for manoeuvre, whilst those who give or administer the funding have the power of the purse and can leverage it, without changing the function.

Our proposition is therefore that RRF planning follows a hierarchical mode of regulatory governance, in line with a stronger hand for the Commission. But there is also more pressure to deliver on it, to use its new power as a carrot and facilitate reforms proposed by national administrations, within parameters set by collective decision. This counter-intuitive combination can be explained by the diversity of the EU with its weak centre in terms of political legitimation and fiscal capacity. In contrast to experimentalists, we expect a hierarchical, rather than deliberative, mode of governance because the Commission must avoid challenges to its authority in the Council by RRF sceptics. Timely and abuse-free delivery of the policy will also ensure their loyalty or rather ensure that sceptics do not engage in disloyal public statements about the policy. In turn, providing the main beneficiaries with the means to do reform of their own choosing is more likely to succeed than the threat of fines, given the dispersed authority of the EU. In this, we depart from the original proponents of surveillance governance.

Hence, we hypothesise, similar to Bokhorst (2022), that RRF planning shows continuity in the (fiscally reinforced) hierarchical governance method, with the Commission setting the agenda with detailed regulation, but leaves more choice to member states in relation to specific policy choices. The narrow time frame for NGEU funding creates a sense of urgency on all sides.

III. Analytical Framework

Our analytical framework tries to distinguish empirically between the three plausible theoretical interpretations of what adding substantial fiscal resources to the European Semester potentially does to fiscal governance and social policy. It is not purely deductive but informed by the first studies of the process (Bokhorst, 2022; Bokhorst and Corti, 2023; Vanhercke and Verdun, 2022).

The authority dimension of polity formation is captured by changes to governance. The governance of the RRF can be operationalised in four aspects (Table 1). Our compound polity perspective leads us to expect the *agenda setting for the policy process* to come from the Commission although the promise of funding creates incentives on the member state side to play a more active part than in the European Semester. The Commission is likely to intensify its agenda setting with the significance of the financial allocation because more is at stake. This selectivity contrasts with the requirement of recipients' formal equity in the other two interpretations, as peer review plays a crucial role in both. Second, in the *resolution of conflicts* that inevitably arise in the drawing up of plans, testing hierarchical power, the Commission presumably seeks compromise and co-operation, rather than escalation to the Council. It is a mixture of commitment seeking as in surveillance, but retaining it inside the regulatory-administrative community and hence with elements of consensus building through peer pressure as in experimentalism. Third, *monitoring* is expected to be close and consultative, clinging to the regulation as agreed

Table 1: Overview of Different Interpretations of Next Generation EU.

| | | Compound polity | Experimentalist governance | Reform surveillance |
|----------------------------------|---------------------|---|---|---|
| Governance (authority) | Agenda setting | Commission, asymmetry of countries depending on financial allocations | Member states, formal equality crucial for peer review | Commission, formal equality crucial for credibility of surveillance |
| | Conflict resolution | Commitment seeking, avoiding escalation, relying on attrition | Consensus seeking, relying on peer pressure in periodic review | Probing, based on performance indicators |
| | Monitoring | Contractual, based on performance budgeting | Deliberative, based on peer review along with indicators | Commitment seeking, escalating to peer pressure and sanctions in the Council as nuclear options |
| | Inclusiveness | Desirable, but centralisation and financial stakes make this difficult | Mandatory, essential for the governance mode | Facultative, but possibly counterproductive for commitment |
| Policy substance (loyalty) | Problem definition | Innovation inducing, thanks to expansionary logic; but goal definition likely to be uncontroversial | Uncontroversial goals in search of pertinent solutions | Controversial goals for urgent problem solving, identified as domestic shortcomings |
| | Country specificity | Moderate, defines primarily new means for common ends | Strong, defines specific ends for which country-specific means are sought | Limited: 'one-best- practice-fits-all' approach |
| | Content | Based on member states' priorities, possibly at odds with the EU agenda | Based on member states' priorities converging in deliberation | Based on diagnosis of problems in periodic peer review |

by co-legislators and enshrined in goals that hold the member states accountable to their commitment. The monitoring is neither deliberative as in experimentalism nor probing as in surveillance. It is contractual as prescribed by the chosen method of performance budgeting that establishes a close link between defined policy outputs and incremental funding (Schick, 2003, p. 101). Finally, *inclusion of stakeholders* is a time-honoured principle of EU policy-making but easily crowded out by time pressure and domestic politics. For the compound polity, inclusion is desirable, but it is neither as essential as in experimentalist governance (Sabel and Zeitlin, 2008, p. 313) nor of doubtful relevance as in surveillance where national stakeholders are suspected to jeopardise prudent policy commitments.

Loyalty to the polity is created by support for policies. The change in policy substance that the RRF presumably generates can be formulated in three respects: problem definition, country specificity and content. First, the *problem definition* follows an expansionary logic: NGEU funds can finance innovation that was unaffordable before. The

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regulation itself seeks to build additivity of funding into common goals, such as digital and green transition, that are easily marginalised in national budgetary politics. Our expectations are closer to experimentalist governance scholars in that goals are formulated as uncontroversial innovations. By contrast, a reform surveillance perspective suggests that the EU must exert pressure for reform to counteract domestic shortcomings introduced by entrenched interests and re-election-seeking governments. Second, the country-specific choice of policy content can be embodied in the milestones and targets for spending that national administrations have to suggest. National priorities have presumably greater leeway as long as they show signs of adapting EU priorities to national conditions. Our expectation of country-specific policy content is midway between the two other interpretations because we expect a more visible hand of the Commission, but it should be less finger-wagging, so as to avoid the spectre of conditionality. Reform surveillance, by contrast, pushes member states towards controversial reforms in the name of best practice (Regan, 2017). Finally, for policy content, we expect a political bargain that reflects the recipient members' preferences and problem diagnoses more closely than in the pre-NGEU Semester. It should result in a discernible shift in more tailored policy outputs that can nurture loyalty. This is midway between experimentalist governance, in which national preferences and the EU agenda should be aligned thanks to the deliberative process of the European Semester (Zeitlin and Vanhercke, 2018), and reform surveillance, which would expect bargains to prevent desirable changes and therefore sees peer review as a necessary enforcement mechanism for pre-commitments.

IV. The NRRPs in Italy and Spain

For our in-depth analysis of the difference that the RRF makes, we selected Italy and Spain. In the context of the COVID-19 pandemic and NGEU recovery funding, they are the most similar cases: Italy and Spain experienced contractions deeper than in all other EU countries,² being tourism-dependent economies with a large share of employment in smaller enterprises. They also have comparatively weak protection systems; in particular, social investment services in education, training for the unemployed and childcare are underdeveloped (Natili and Jessoula, 2022). The euro area crisis left them in an exposed fiscal situation.

The NGEU programme was therefore key not only to support the post-pandemic recovery but also to address the weaknesses of their welfare states. Italy and Spain are, in absolute terms, the largest beneficiaries of RRF funding: Italy has asked for €191.5 billion in grants and loans, or 11.6% of its 2020 GDP; Spain has asked for €69.5 billion in grants, or 6.2% of its 2020 GDP (Freier et al., 2022). They also share challenges with regard to the management of EU funding and policy prescriptions. Previous studies have shown that both countries have a bad record in absorbing cohesion funds (Darvas, 2020). They perform somewhat better when it comes to implementing country-specific recommendations (CSRs) in the European Semester (D'Erman and Verdun, 2022, p. 7). We therefore do not evaluate the change that RRF funding makes against very low benchmarks.

 $^{^{2}}$ In 2020, the GDP loss was -10.8% in Spain and -8.9% in Italy, compared to an EU average of -6.1% (OECD online database).

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However, in contrast to Spain, Italy is known for being a reform laggard. Governments failed repeatedly to adopt the social investment paradigm promoted by EU institutions (Hemerijck, 2013, pp. 202–204). Spanish governments were very active labour market reformers, to the point where they could be accused of deepening insider—outsider segmentation (Picot and Tassinari, 2017). Given this different trajectories, we should be able to observe, first, whether generally the authority of the Commission is challenged differently in the two countries and, second, whether Italy now has to accept a similar reform agenda as Spain before or whether the Spanish government was allowed to mitigate adverse effects of earlier reforms. Our goal is to assess the different expectations for governance and policy substance summarised in Table 1, not the social policy content of the RFF (Corti and Vesan, 2023). Specifically, we want to explain in detail the process leading to the definition of priorities in the social policy field, the emergence of conflicts and how they were solved.

Governance

The political agreement on the NGEU package had been sealed by the European Council on 19 July 2020, and the draft regulation was tabled by the European Commission in September 2020. The Commission set up a specific Recovery and Resilience Task Force (SG RECOVER), which together with the Directorate-General (DG) for Economic and Financial Affairs (ECFIN) became the main interlocutor of member states. A number of domain-specific teams from other DGs assisted. All was up and running by October 2020, even though the RRF entered into force only in February 2021.

Agenda Setting

The agenda-setting dynamics of the national plans were shaped by this extremely tight schedule of RRF implementation. The time pressures on national administrations were enormous. Member states were required to submit draft NRRPs by 15 October 2020, well before the regulation had been approved. To steer this process, the Commission provided member states with templates and set a Q&A portal where governments could ask for information regarding the interpretation of the draft legal text (Interview 2). Subsequently, NRRPs had to be officially submitted for their approval by 30 April 2021. Once an NRRP had been submitted, the Commission had 2 months to assess it, before sending it to the Council for final approval.

Even so, the two governments started elaborating their NRRPs shortly after the July 2020 agreement. A first document was produced by Italy in September 2020 and shortly afterwards by Spain. In October, a close consultation process started (Interview 13). The RRF regulation establishes that the NRRPs have to address 'a significant subset' of the CSRs received by each member state in 2019 and 2020. The reliance on CSRs to guide member states' priorities is a key element of the European Semester integrated into the governance of the RRF; from 2021 onwards, RRF implementation had to follow the established annual timeline for European multilateral deliberation (D'Erman and Verdun, 2022, p. 9).

Despite the role of previous CSRs, Commission officials emphasise that the agenda was set by the member states (Interviews 1, 2, 5 and 8). This was confirmed by officials in both countries. In Spain, the government publicly communicated national authorship of

the plan (Sánchez, 2021; Interviews 10, 11, 12 and 15). A large number of the measures included in the Spanish plan came from the coalition agreement signed between Unidas Podemos — United We Can (UP) and the Partido Socialista Obrero Español — Spanish Socialist Workers' Party (PSOE) in December 2019 (PSOE and UP, 2019).

In Italy, the draft was delivered fast, but the Commission objected to the disproportionate share of investments relative to reforms (Interviews 4 and 5). It made the government – in particular under Prime Minister Mario Draghi – increase the number of reforms from 48 to 86 (Guidi and Moschella, 2021). In the social domain, a reform addressing undeclared work was included following a request by the Commission (Interview 16). Reforms of active labour market policies and public employment services, which were on the Semester agenda since the very beginning, were more detailed in the second version of the plan, again upon request of the Commission (Interview 16). As a Commission official put it (Interview 6), 'the initial input was of the Italian government, then the plan evolved, also due to our inputs'. But not all proposals of the Italian executive made it into the final version of the NRRP: the introduction of a statutory minimum wage or the reform of the short-time work scheme to protect precarious workers was in the first draft but eventually left out (Interviews 14 and 16). Commission officials objected that they would create significant ongoing expenditures, which was against the rules. Conveniently, the new Draghi government had different political priorities (see the Policy Substance section).

In sum, in Spain, the agenda was ostentatiously set by the government. The Italian government under Prime Minister Conte clearly wanted to take the initiative on investment. But subsequent interactions with the Commission changed this, and reforms were agreed primarily with the Draghi administration.

Conflict Resolution

According to the RRF regulation, the release of the funds is contingent on meeting the relevant milestones and targets set in the NRRPs. Both the Commission and the Economic and Financial Committee (EFC) provide preliminary assessments of the implemented reforms before the Council authorises disbursement. If the EFC concludes that the preconditions have not been fulfilled, 'no decision authorising the disbursement of the financial contribution [...] should be taken until the next European Council has exhaustively discussed the matter' (EU, 2021, preamble para. 52). Ultimately, the Council can suspend payments following a proposal by the Commission (EU, 2021, Article 10). Unsurprisingly, negotiators anticipate this possibility, thereby altering the entire policy-making dynamic: the Commission acquired additional leverage to steer the member states, but the Commission is also expected to prevent hiccups. As a Commission official put it, the principle was 'to push countries as much as possible [...] but of course not go towards full escalation' (Interview 1).

Very few but significant disagreements emerged during the drafting of the NRRPs. In Italy, conflict arose on three critical issues. First, the Commission demanded a more coherent and detailed plan, not a list of different initiatives to be financed (Interviews 5 and 14). Second, it criticised the draft for not addressing a 'substantial' subset of the policy challenges identified in previous CSRs (Interview 5). Third, the Commission objected to the lack of reforms in the first draft (Interviews 3 and 4). This triggered a domestic pushback against the Commission's pressures (Domorenok and Guardiancich, 2022). Tensions between the centrist Italia Viva and the Five Star Movement over the allocation

of EU resources mounted, weakening the already fragile Conte II government further. In January 2021, at the end of a Eurogroup meeting, Commissioner Gentiloni declared that 'the Italian plan is broadly convergent with our overall goals and policies, but it needs to be discussed and strengthened as concerns reforms, accordance with EU recommendations, provision of a clear time-table' (Basso, 2021). But the process remained stalled.

Needled by these dynamics, Conte's government resigned in February 2021. A new government led by Mario Draghi was sworn in, supported by a national coalition ranging from the radical right (the League) to the left of the Democratic Party. But even the Draghi government was aware that certain reforms were politically too sensitive. One example was the reform of the fiscal system: 'on this issue, there is a CSR, so there was a discussion. The [Commission] asked why it was not included in the NRRP, and the Italian response was that the fiscal reform is so important, it requires a political and social debate, and we cannot promise ex ante a particular reform. And [T]he EC [European Commission] accepted this reasoning' (Interview 5). Similar considerations excluded eventually some social measures to which we come back (Policy Substance). The thrust was to keep politically sensitive reforms outside the plan (Interviews 4 and 5), despite clear preferences of the Commission to the contrary.

In Spain, two components of the NRRP became a source of friction between the Commission and the government: the pension and the labour market reforms (Interview 15). In the first draft sent to the Commission in early January 2021, these two reforms were left out of the document, so that only 28 of the 30 components of the plan were specified. Disagreements existed both within the national executive and between the government and the left-wing parliamentary majority. Regarding the labour reform, Socialist ministers led by the Economic Affairs Minister, Nadia Calviño, argued for a reform limited to tackling dualisation; the ministers of the UP, by contrast, pushed for scrapping the entire 2012 reform introduced by the Conservative Rajoy government (2011–2018).³ The Commission supported Calviño's approach. She used the EU endorsement to justify her position for a less radical labour reform (Jorrín, 2021). Commissioner Gentiloni personally met with the three Spanish ministers involved, and the government included details on both reforms in its January 2021 draft (Alarcón, 2021). However, in October 2021, when the December deadline for adopting the reform set in the NRRP's schedule approached, the latent conflict became acrimonious. Commissioner Gentiloni intervened in the public debate, throwing his weight again behind Calviño: 'the labour and pension reforms should comply with what has been agreed [...] [T]he Commission is clear on the objectives of the labour reforms: it asks for job instability to be reduced, for collective bargaining to be improved, and above all it asks that any changes do not reduce the flexibility introduced by the 2012 reforms' (de Miguel and Gómez, 2021). The Commissioner also stated that the Commission favoured reaching an agreement with the social partners for the reform. This further undermined UP's position, as it had threatened to exclude the Spanish business organisation from the talks because of its intransigence. Ultimately, the stance of Calviño and the Commission prevailed. The risk of the Commission or the Council not approving the second disbursement of funds was very present in the public debate (Jorrín, 2021). Neither the UP nor the trade unions criticised the Commission publicly for the limited character of the reform (Interview 13).

³For details on the 2012 reform, adopted under the auspices of the European Commission, see Picot and Tassinari (2017).

These conflicts are noteworthy even though the public display of authority by Commissioner Gentiloni constitutes the exception rather than the rule during the drafting of most NRRPs (Bokhorst and Corti, 2023). But the exception reveals the new capacities that the RRF bestows on the Commission and that, in extremis, the Commission was willing to use its leverage in an overtly partisan way.

Monitoring

If the Commission showed some flexibility as regards most contents of the NRRPs, it adopted a stringent approach regarding the follow-up processes (Interviews 4, 5, 9, 14 and 15). The monitoring of the NRRPs was structured by performance budgeting, which is 'a budget that explicitly links each increment in resources to an increment in outputs or other results' (Schick, 2003, p. 101). The 'increments in outputs' are laid down in targets (quantitative indicators) and milestones (qualitative indicators) to track the achievement of investments and reforms. Targets and milestones were proposed by the member states, but the Commission advised them to reduce or increase their number. The detail is mind-boggling (DG ECFIN–SG RECOVER 2021): to receive 12 payments, Italy will have to meet 213 milestones and 314 targets, Spain 220 milestones and 196 targets. Funds are disbursed every 6 months on the condition that the corresponding milestones and targets are met. The advantage of performance budgeting is that reimbursement is less cumbersome and timelier as there is no need for receipts; the 'increments in resources' are pre-defined and pre-committed.

Italian officials stress that the intervention of the Commission, in comparison with the pre-2020 European Semester, 'has become more rigorous, tighter, punctual and cogent' (Interview 4). The Commission now scrutinises the 'whole process', including the policy coherence of different measures and how they overcome political obstacles that may impede their full realisation (Interview 4). For instance, in the area of education, the Commission assessed which training programmes civil servants have to attend as well as the precise number of people who will attend them (Interview 9); this was resented by the Italian administration.

Spanish national officials complained that the Commission was very reticent to amending even minor aspects of a plan during implementation. The chief of the State Secretary for Social Rights called the process 'rigid': 'Commitments have to be fulfilled, of course. But [...] when things are put in action sometimes they take another form, follow different schedules, and do not correspond exactly to what was proposed' (Interview 13). A member of SG RECOVER admitted as much (Interview 2), although some more flexibility has been promised following the approval of the REPowerEU plan in 2022 (European Commission, 2022).

Not only does the Commission manage the implementation of the NRRPs, it also assesses plans for the EFC and the Economic and Financial Affairs Council (ECOFIN) Council. The detail of these assessments shows up in the length of both the Operational Agreement signed between the Spanish Government and the Commission, with timetables for every step necessary to implement each reform and investment (European Commission, 2021), as well as the Council's assessment of the plan. Whilst the Operational Agreement had 345 pages, the Council's assessment added another 294-page document. It reviewed not only how the Spanish plan addresses the specific stipulations under the European Semester (CSRs), the RRF and the Macroeconomic Imbalances Procedure but also the domestic governance for implementing the plan, the timing of the reforms,

the indicators relating to the fulfilment of the envisaged milestones and targets and the arrangements for providing access to the underlying data (Council, 2021).

The contractual character of an NRRP is thus very different from a deliberative or a probing peer review process. As a senior Commission official put it, 'In the implementation phase, [...] it is very clear that if the milestones are not fulfilled, we would need to suggest to the Council that the payment [...] related to a certain milestone cannot be paid to the full extent. Or if no milestone is fulfilled it could be even a non-payment' (Interview 2). The possibility of withholding funds not only changed existing peer review processes of the European Semester but also increased the 'horizontal accountability' at the national level, resulting from peer pressure in national bureaucracies (Interview 4). Different ministries or government levels do not want to be responsible for missing a target and thus jeopardise the disbursement of funds. This makes more sense for purposes of surveillance than better performance because performance is not easy to pre-define and control (Bokhorst and Corti, 2023, p. 2; Schick, 2003). This similarity to surveillance does facilitate the flow of funds later, however, linking tighter governance to more immediate reward and absorption (EU, 2021, preamble para. 51).

Inclusiveness

In Italy, the Conte II government already begun to collect proposals to relaunch the economy after the pandemic in June 2020. It invited international organisations, social partners and key civil society organisations to a 3-day event called 'Stati Generali'. However, this was the first and last attempts at including stakeholders. With very tight deadlines ahead, decision-making became highly centralised, both in the design of the NRRP and in its implementation (Interview 4).

Executive dominance was most pronounced in the Draghi administration (Interview 4). Decree Law 77/2021 introduced a *Cabina di Regia* (Steering Committee) within the Italian cabinet, chaired by the Prime Minister himself, thus indicating political responsibility at the top. The co-ordination and monitoring of the Italian NRRP were centralised in the Ministry of Economy and Finance (MEF) and, specifically, the Department of the State General Accounting Office (Art. 6 Decree Law 2021 No. 77). The MEF is the only interlocutor with the European Commission (Interview 6). The Italian Parliament had very limited possibility to influence the plan, not least because of the tight timetable (Interviews 4 and 9). Other possible stakeholders, such as representatives of sub-national authorities and organised interests, were largely marginalised (Interviews 4 and 9).

The formulation of the Spanish NRRP was also dominated by the central government, sidelining the Spanish regions (Autonomous Communities) and the Spanish Parliament during the drafting process. The Spanish Parliament did not even get the opportunity to amend and vote on the NRRP; the Prime Minister presented it to the legislature as a *fait accompli*. However, in contrast to Italy, the social partners had some room for intervention. In the contested pension and labour market reforms, they played a decisive role as requested by the Commission. The labour reform was agreed with both the two largest trade unions (Unión General de Trabajadores — General Union of Workers [UGT] and Comisiones Obreras — Workers' Commissions [CCOO]) and the main employer organisation (CEOE)

⁴However, the Ministry of European Affairs co-ordinated the drafting of the Italian NRRP from autumn 2020 to early January 2021.

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before being presented to the Parliament, whilst two pension reforms were agreed with the unions in 2021 and 2023 but failed to garner the support of the CEOE.

In both countries, regional authorities had to be given a say in the implementation of the NRRP, because policy competences are devolved. To steer the implementation phase, new governance structures were adopted with the participation of all sub-national governments. However, their role is limited, as they can challenge technical aspects of investments projects, such as costing, but they cannot change the nature of investments, nor the policy models guiding them (Interviews 13, 15 and 16).

In line with other studies (Vanhercke and Verdun, 2022), we find that the extreme time pressure implied a loss of voice for domestic stakeholders and parliamentary representatives compared with the 'socialisation' phase of the pre-2020 European Semester (Zeitlin and Vanhercke, 2018). Inclusion was also not helped by the performance-based, contractual character of the RRF defining ex ante what was allowed. The Spanish case shows, however, that this does not imply the complete marginalisation of non-executive actors when the Commission sought broader support for contested reforms.

Policy Substance

The regulation on the RRF sets out six pillars that NRRPs must address: (1) green transition; (2) digital transformation; (3) smart and inclusive growth, including jobs, productivity and competitiveness; (4) social and territorial cohesion; (5) health and economic, social, and institutional resilience; and (6) education and skills (EU, 2021). They condense the ideational change regarding economic and social policy that predates the pandemic (Natali, 2022). However, all spending must end in 2026. The rules confine spending to investments, that is, spending is allowed on initial training of a workforce but not permanent salaries. Nor should investments and reforms create future current liabilities, 'unless in duly justified cases' (EU, 2021, Article 5(1)). This is a kind of 'golden rule' restriction on the NRRPs.

Problem Definition

In Italy, the NRRP focuses on the underdevelopment of social investment services, whilst other pressing social issues - such as stagnating wages and acute labour market segmentation – are not addressed in the final version of the plan. The main policy initiatives followed an uncontroversial but expansive rationale: different ministries proposed projects they had in their drawers for decades but could not launch because of tight budget constraints. The main areas were expansion of childcare facilities, development of active labour market policies and hardware for healthcare and housing development. Reforms included first by the Conte government (such as the minimum wage or the reform of the short-time work compensation scheme) were left out under Draghi's coalition government as they were considered too contentious, as acknowledged by both sides: 'I think that the measures that are in the Italian NRRP - active labour market policies, funds for childcare, housing – are very important and not really controversial. The Commission had no interest in pushing for reforms that were not explicitly mentioned in the CSRs. In the end, important reforms were included, but were not "partisan" (Interview 6). The Italian government thus got leeway to define problems as too divisive for essentially executive decision-making.

The Spanish NRRP reflects the RRF priorities, in particular, the reduction in the segmentation of the labour market, the proliferation of low-wage jobs and the high incidence of household poverty. They were considered key problems by the centre-left Spanish government in its 2019 electoral programme (PSOE and UP, 2019) and were also policy issues signalled in the 2019 and 2020 CSRs. Structural reforms had already been facilitated thanks to the wider margin for fiscal manoeuvre that the activation of the escape clause of the Stability and Growth Pact provided since the beginning of the pandemic (Interview 13). The 2019 coalition agreement also contained the introduction of a minimum income scheme and the contested labour market reform, which could be funded by the RRF. A full reversal of the 2012 labour market reforms introduced by the Rajoy administration was not allowed, however; as indicated, the EU Commissioner intervened heavy-handedly in favour of the centrist side in the divided government coalition.

Country Specificity and Content

In line with the RRF regulation (EU, 2021), the overall goals of the plans in Italy and Spain are conforming with aims such as reviving growth in a 'socially inclusive' way. The means to achieve these goals, however, differs. In Italy, pension and labour market reforms do not figure prominently in the NRRP, in contrast with the 2010s, when they were stated as a priority by both EU and Italian policy-makers (Sacchi, 2015). The 'golden rule' constraint of the RRF biases reforms against the financing of personal services and in favour of hardware, such as hospitals, school buildings or one-off training measures for staff. Even so, in line with the social paradigm change (Natali, 2022), the plan manages to support social investment reforms financially by retraining existing staff, facilitating re-regulation and spending on transitional investments. These measures seek to reduce the curative cash-transfer bias of the Italian welfare system in favour of a preventative services orientation. But it also continues the pre-COVID-19 labour market reform path, in that the plan focuses on activating workers rather than addressing low work intensity, low wages and labour market segmentation.

These issues are exactly addressed in the Spanish NRRP. The 2021 labour reform reduces the scope of temporal contracts, restores sector-wide collective agreements for specific wage-setting aspects (although not for employment conditions) and re-instates the principle that collective agreements last for more than a year. The 2023 pension reform increases the sustainability of the system via increasing the social contributions of the highest earners. Moreover, the plan includes a plethora of social investment measures: reform of the vocational training system; the modernisation and digitalisation of public employment services; investment in education; measures for the care system, social housing and strengthening of the national minimum income scheme and more performance-based financing of education and research institutions.

The Spanish NRRP has therefore a protective orientation and a social investment orientation whilst the Italian plan has only the latter, a divergence that reflects the different party coalitions supporting the two governments. The track record of both countries was affected: Italy adopted reforms that were recommended for a long time but governments had repeatedly failed to implement before; and Spain was as reform active as before but corrected some of the former, EU-compliant reforms to reverse the dualisation they created.

We see these findings as a vindication of our view that recovery funding may leave member state administrations more room for manoeuvre as regards the content of policies. When goals were controversial, as in the Italian minimum wage or Spanish pension and labour market reforms, a bargaining process evolved. The drafting process is less forensic on the problems than on how the measures can be operationalised and implemented. This reproduces the differences between our two cases, Italy and Spain, one a reluctant reformer and the other a pro-active reformer. The financial support, however, made even the Italian administration engage with reforms under both a left-of-centre coalition and a technocratically led national coalition.

Conclusions: How Does Money Make Reform Go Round?

We asked two questions at the start. First, does the RRF give fiscal governance in the EU a hierarchical lever and make it more intrusive? We find that it largely does both. Only when the Italian government wanted some reforms excluded because they were domestically too divisive did the Commission back off. In the case of a Spanish labour market reform, Commissioner Gentiloni intervened publicly in an intra-coalition dispute to strengthen the EU's preferred option. The drafting of NRRPs is a tightly managed process that leaves little room for including other stakeholders, ending up with a plan full of targets and milestones for expedited funding.

Secondly, what effect does a stronger centre have on the content of a sensitive and contested policy area? Instead of documenting the details of changes in policy content, we picked significant social policy examples in which we could test our hypotheses (summarised in Table 1) on how, notably, agenda setting and conflict resolution changed thanks to funding. We find in both Italy and Spain that governments were pro-active in defining their own priorities, which were different for the countries despite their similar welfare state patterns and weaknesses. The governments' priorities were largely accepted as regards investment priorities whilst concomitant reforms were more controversial or the Commission demanded more ambition. This was helped by the largely consensual goals of social investment, which were long overdue but unaffordable in these crisis-ridden countries. This can also explain why social partners and sub-regional governments acquiesced: they did not dispute the policy content of the plans but rather the process that largely excluded them for lack of consultation time (Interviews 7 and 9).

Others have found similar results. But it remains hard to explain how strengthened hierarchical power can go together with more leeway for policy priorities further down the hierarchy. Our contribution is to provide an explanation thanks to the theoretical starting point that the EU is a compound polity, with a weak centre governing a diverse membership. This led us to the paradoxical proposition that a massive recovery fund will strengthen the hierarchical authority of the centre but also empower national authorities to define their policy priorities. We expect this on the background of the Rokkan–Hirschman model of polity formation, emphasising that enhanced authority must be complemented by building loyalty; it cannot substitute for it. The massive funding changes the political dynamic: it puts pressure on both the recipients to unlock it and the Commission to make it flow; for the latter to happen, the plans have to be acceptable to the Council.

This marks the difference to the fiscal surveillance type of governance. It saw EU governance as committing national governments to economically sensible but politically unpopular reforms. The view of what is economically sensible has changed somewhat,

leaving a range of policies that make political—economic sense without performing a Uturn (Natali, 2022). The NGEU translates into a social investment orientation of reforms endorsed by the European Commission.

But enhanced authority also made us expect that governance will not go towards experimentalism in the Sabel and Zeitlin (2008) sense. Especially when financial stakes are high, as in our selected cases, governments who traditionally resent additional fiscal capacities must be assured that this is not a spending spree for national benefit that others pay for. The main beneficiaries will therefore have to let themselves be ostentatiously governed by arduous procedures, in return for being able to finance consensual policy priorities out of reach otherwise. The reciprocal relationship of authority and loyalty works both ways: loyalty in a diverse union can only be ensured if that authority is used in a hierarchical way.

Our findings broadly confirm our hypothesis, broken down into several features of hierarchy and loyalty in our analytical framework.

- In both Italy and Spain, the governments were able to pre-empt having their agenda set by the Commission. Yet, the EU insisted in Italy on adding reforms to the investment plans and followed up on the 2019/2020 CSRs.
- Open conflict was carefully avoided, and EU negotiators, whilst not consensus seeking, acknowledged that the governance method does not allow for notoriously contested reforms. This dynamic is consistent with the previous Commission's role in monitoring the stability and growth pact (SGP), in which legitimacy was sought through bargaining rather than confrontation with member states.
- Nevertheless, if the EU was more deliberative in the negotiation phase, it became more hierarchical in monitoring the fulfilment of the contracts. The funding of what was until now a pure co-ordination process, the European Semester, makes implementation now much more constant and insistent than previously, a process that was characterised in both countries as admiringly well informed but also quite 'rigid'.
- The policy content in the social policy domain shows a clear emphasis in both countries on social investment services, a centrist policy stance that can be agreed across the party-political spectrum. Reforms in the end were almost always uncontroversial in content. It was their operationalisation in milestones and targets that sometimes created tensions.

In conclusion, our case studies show that the RRF has given the EU more authority, but the implied coercion has rarely been used, even when conflicts arose. Even Commissioner Gentiloni, with his overtly side-taking interventions, needed support from relevant factions inside the government to get the EU's preferred way. Where it was missing, as in Italy, the Commission backed off. But we also sense that this was the honeymoon phase of RRF funding. Implementation is becoming a much harder test as the extremely demanding budgeting process takes its toll and the sidelining of other stakeholders has stoked up conflict. RRF money made agreement on reforms easier, but RRF money cannot buy the Commission loyalty.

⁵It is entirely compatible with the Rokkan–Hirschman model that different mechanisms are at play in countries that have more fiscal space and are beneficiaries of low RFF funding (Bokhorst and Corti, 2023).

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Appendix A: List of Interviews

| Interview number | Institution | | Name | Date |
|---------------------|----------------------------|--|-----------------------|-------------------|
| 1 | European Commission | SG RECOVER | Confidential | 25 March 2022 |
| 2 | European Commission | SG RECOVER | Confidential | 28 April 2022 |
| 3 | European Commission | European Semester Officer (Italy) | Antonia Carparelli | 3 May 2022 |
| 4 | Italian Government | Ministry of Economy and Finance | Confidential | 11 May 2022 |
| 5 | European Commission | European Semester Officer (Italy) and DG ECFIN | Confidential | 12 May 2022 |
| 6 | European Commission | European Semester Officer (Italy) and DG ECFIN | Confidential | 12 May 2022 |
| 7 | Spanish Parliament | Joint Committee for the EU | Mariona Illamola | 16 May 2022 |
| 8 | European Commission | European Semester Officer (Spain) | Confidential | 24 May 2022 |
| 9 | Italian Trade Union (CGIL) | General Vice Secretary | Gianna Fracassi | 25 May 2022 |
| 10 | Spanish government | Labour Ministry | Confidential | 27 May 2022 |
| 11 | Spanish government | Labour Ministry | Confidential | 27 May 2022 |
| 12 | Spanish government | Labour Ministry | Confidential | 27 May 2022 |
| 13 | Spanish government | Ministry of Social Rights | Ricardo Molero | 30 May 2022 |
| 14 | Italian government | Ministry of Labour and Social Policies | Confidential | 6 June 2022 |
| 15 | Spanish government | Finance Ministry | Confidential | 13 June 2022 |
| 16 | Italian government | Ministry of Labour and Social Policies | Confidential | 29 September 2022 |

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