Is the EU becoming more like the UN? Paradoxes around EU institutional developments in 2011 and risks for future integration

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2011 was a year which highlighted the European Union's response to the economic and Eurozone crisis. Decisions were taken in an often chaotic fashion, and in a number of stages. The strategy followed in 2011 was evidence of what we could call the 'UN-ification' of the European Union (EU). European integration is increasingly characterised by the following features: difficulty in taking decisions, defence of national interests, and supremacy of the larger countries (in particular the partnership between France and Germany).

This trend is the result of two ever more obvious sets of contradictions. Firstly, while the intergovernmental approach seems to have the upper hand, we are at the same time seeing the emergence of an embryonic budgetary and fiscal federalism. Secondly, the EU has received greater economic powers, yet it is not able to offset these (by direct or indirect redistribution) through the EU budget, and nor has it been given any further powers in the area of social policy. There has, moreover, been no strengthening of the democratic legitimacy of the EU. The future, therefore, gives cause for concern: further integration does not seem to be a viable option, involving as it does the risk of serious popular protests against the European process.

After the introduction, this chapter gives a chronological description of the new instruments developed in response to the crisis. The chapter by Patrick Diamond and Roger Liddle concentrates on the substance of the new economic governance, and the one by Degryse and Pochet focuses on the need for a new growth paradigm; we, in the next few pages, look at institutional issues.

In an initial section, we refer to management of the public debt crisis, beginning with the crisis in Greece between 2009 and 2011, which marked the real start of institutional change. A key feature of the EU's response was inconsistency between a revision of the Treaty and the use of agreements based on international law (to overcome the vetoes within the Union). The main stages in the process were the support mechanism to provide stability for Greece, limited revision of the Treaty of Lisbon, and enhancement of the European Financial Stability Facility (EFSF).

In our second section, we examine the development of the concept of 'economic governance'. The key points have been a strengthening of the role of Germany and France within the European Council, of the ECB and of the Commission, as well as the creation of new governance measures: the European Semester, the *Six Pack* (a revision of the Stability Pact), and the Euro Plus Pact. While the response to the sovereign debt crisis has been inconsistent, the approach taken to economic governance has clearly been a federalist one, even if not completely so.

The third part of this chapter looks at the texts currently being negotiated. It also examines the increased risk of the Union losing credibility as a result of the many Treaty revisions taking place within – or outside – of Union structures in order to strengthen a reluctant 'budgetary federation'.

In our fourth and final section we turn to future prospects for European integration. Two future scenarios seem possible: a qualitative leap forward for European governance towards political federalism, or a rise in populism followed by a crisis in the EU.

1. The sovereign debt crisis

Table 1 shows the institutional measures taken as part of the EU strategy to address the public debt crisis, focusing on the case of Greece which was so prominent in the last year.

Table 1 **Key steps in the EU crisis strategy**

April 2010	1st rescue plan for Greece (support package to preserve stability in Greece), bilateral loans
2 May 2010	Memorandum of Understanding with the Troika
11 May 2010	European financial stabilisation mechanism (EFSM)
7 June 2010	European financial stabilisation facility (EFSF)
March 2011	Limited revision of the Treaty
July 2011	ESM Treaty
July-Oct. 2011	2nd rescue plan for Greece

1.1 The Greek crisis (2009-2011)

In order to understand the response of the European institutions to the crisis, we must take a look at the events of 2009. This was the year when the foundations were laid for a two-stage response: providing assistance to Greece as well as the possible establishment of a support mechanism if the crisis were to spread.

In 2009, the Papandreou government announced a public deficit that was higher than had been suggested by the figures provided by the outgoing government. In December 2009, a ratings agency denounced Greece for not complying with the Stability and Growth Pact, although it was not concerned that the difficulties might spread to other euro area countries, and spoke out in favour of retaining the recovery plans. This was the beginning of the process that would increase 'market pressure' on Greece. Germany hesitated, so the key principles for a European plan were adopted only in April 2010.

Following a request from the Greek authorities, the euro area Member States decided unanimously, on 2 May 2010, to activate the support mechanism to preserve the financial stability of Greece. This made use of bilateral loans from the other euro area Member States, pooled by the European Commission, and under the conditions set out in the statement of 11 April 2010. The financial assistance to Greece, set at 110 billion euros, was part of a joint programme with the IMF. To obtain these loans, Greece was required to conclude a *memorandum of understanding* with the European Commission, the IMF and the ECB (the so-called Troika), listing the reforms to be carried out. Greece was a particular case, but it highlighted the fact that the surveillance system for public finances had not worked properly.

1.2 The 'European stabilisation mechanism'

Irrespective of the assistance provided to Greece, the key features of the European response were a limited revision of the Treaties and recourse to international law. The end result was that European integration would become even more complex and incomprehensible to the general public.

Europe's institutions had decided to establish the European Stability Mechanism, which encompassed the Agreement on a European Financial Stability Facility (EFSF, in English, but known as the European Financial Stability Fund) as well as the European Financial Stability Mechanism (EFSM). These are tools for managing government debt crises. Both funds (EFSF for the euro area alone; EFSM for the EU countries) along with IMF activities, were jointly responsible for setting up loans for countries encountering solvency problems. The lifespan of the EFSF is confined to a three-year period (Barbier, 2011).

For the record, the EFSM is based on Article 122(2) of the TFEU (Council of the European Union, 2010). According to this second paragraph, the Council may decide by a qualified majority to grant assistance to the requesting country. The EFSF, governed by a framework agreement of 7 June 2010, is a Luxembourg-based limited company, which can issue bonds backed by guarantee commitments from the euro area Member States up to an amount of 440 billion euros. The fund could only be activated once it had been ratified by Member States representing 90% of its capital.[1]

1. According to the EFSF definition of 7 June 2010, the obligation on euro area Member States to issue guarantees for the EFSF debt instruments will enter into force as soon as a critical mass of Member States, representing 90% of shareholding, has completed the relevant national parliamentary procedures. *Terms of references of the Eurogroup. European Financial Stability Facility,* 7 June 2010 (http://www.consilium.europa.eu/media/6906/euro group_ statement on efsf.pdf).

1.3 A limited revision of the Treaty of Lisbon

The second stage in the process was the revision of the Lisbon Treaty. Faced with public hostility to European assistance plans and uncertainty as to the opinion of its Constitutional Court, the German Chancellor had raised the question of possible revision of the Treaties. The European Council had agreed in principle to a change, to include a reference to a 'permanent mechanism [...] to safeguard the financial stability of the euro area as a whole' (European Council, 2010). This was the first use of the simplified revision procedure, designed to allow amendments to Part Three of the Treaty on the Functioning of the European Union, which includes provisions on economic and monetary union and those applying more specifically to the euro area Member States (de Witte, 2011). The European Council conclusions stated that 'this mechanism will replace the European Financial Stability Facility (EFSF) and the European Financial Stabilisation Mechanism (EFSM), which will remain in force until June 2013.'[2]

In its opinion on the draft revision to the Treaty, the ECB defended its concept of the future European stability mechanism (ECB, 2011).

In March 2011, the European Council adopted the limited revision to the Treaty. A new paragraph was added to Article 136 of the Treaty on the Functioning of the European Union: 'The Member States whose currency is the euro may establish a stability mechanism to be activated if indispensable to safeguard the stability of the euro area as a whole. The granting of any required financial assistance under the mechanism will be made subject to strict conditionality' (European Council, 2011a: 21). This wording was compatible with the position of the United Kingdom, which meant that the Prime Minister, David Cameron, could then defend before Parliament a revision bringing the United Kingdom's participation in the current mechanism to an end as of 2013.[3]

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2. 'As this mechanism is designed to safeguard the financial stability of the euro area as a whole, the European Council agreed that Article 122(2) TFEU will no longer be needed for such purposes. The Heads of State or Government therefore agreed that it should not be used for such purposes'.
3. This revision, as it did not apply to countries outside the Eurozone, did not require a referendum to be organised, as it did not fall under Section 4 of the *European Union Act*, which sets out the measures to be taken to organise a referendum concerning any future extension of European Union powers, *European Union Act 2011* (http://www.legislation.gov.uk/ukpga/2011/12/pdfs/ukpga_20110012_en.pdf).

1.4 Treaty establishing the European Stability Mechanism (ESM)

In June 2011, the European Council Conclusions announced that 'agreement has been reached on the European Stability Mechanism Treaty and on the amendment to the EFSF' (European Council, 2011b: 5).

The ESM Treaty, signed by the euro area Finance Ministers on 11 July 2011, is a treaty under international law setting up an international financial organisation with a subscribed capital of 700 billion euros, with its headquarters in Luxembourg. Other States may accede to this Treaty, currently signed by 17 countries, once they have joined the euro area. This Treaty enshrines in international law the principle of a support mechanism available to assist euro area Member States at risk of severe financing problems, if this is indispensable in order to preserve the financial stability of the euro area as a whole. Unlike the limited revision of the Lisbon Treaty, which required all countries to ratify, this Treaty did not require unanimous ratification. According to the version of 11 July, which would later be amended (cf. Section 3), it would enter into force as soon as the instruments of 'ratification, approval or acceptance' had been deposited by signatories representing 95% of the subscribed capital. Following this, national parliaments would have no further involvement at all in ESM procedures.

Significantly, the text makes many references to the European Treaties. In particular, it gives the Court of Justice the power to settle any disputes which might arise concerning its implementation. Basically, then, it was decided to continue with the usual *modus operandi* for managing the sovereign debt crisis. The method to be used was that of a 'memorandum of understanding', setting out the economic policy conditions applying to financial assistance, contained in a macroeconomic adjustment programme. The Treaty stated that in exceptional cases, the Board of Governors could organise the purchase of bonds of an ESM Member State on the primary market.

1.5 A second plan for Greece

In early June 2011, the press referred to an alarmist report from the Troika.[4] Greece would not be able to return to the financial markets in 2012, but would require a second rescue plan. The Greek government tried its hardest to push through increasingly severe austerity plans, and announced imminent privatisation measures. On 20 June 2011, the euro area Ministers of economic and financial affairs called upon all political parties to support these measures, since 'national unity' was a prerequisite for success. The euro area had decided on the 30 June 2011 as the date for adoption of further measures. On 29 and 30 June, the Greek Parliament adopted a further austerity plan containing savings of 28.4 billion and privatisation to the tune of 50 billion euros.

In July 2011, the Heads of State or Government of the euro area and the European institutions took note of the main principles to be contained in a second rescue plan for Greece (Council of the European Union, 2011a). Following activation of the first, May 2010, plan, the financing available under the new plan was estimated at 109 billion euros. It allowed for an extension of the repayment deadlines (from 7.5 to a minimum of 15 and maximum of 30 years, with a grace period of 10 years). It also provided for a reduction in interest rates, as well as voluntary and exceptional involvement of the private sector (to a level then estimated at 106 billion euros). For the second plan, the euro area Member States intended to use the EFSF. The agreement of 21 July foresaw the enlargement of the EFSF, to allow it to lend money to Member States, even to those without a programme, to finance the recapitalisation of their banks, and to buy sovereign debt securities from countries in financial difficulties on the secondary market, on the basis of an analysis by the ECB.

4. 'Exclusive: Troika says Greek aid hinges on new financing plan', Reuters, 8 June 2011 (http://www.reuters.com/article/2011/06/08/us-eurozone-troika-report-idUSTRE7574JM 20110608).

1.6 Enhancing the EFSF: using international financial techniques

A ‘Euro Summit’ of the euro area States was organised on 26 October 2011, after the German Parliament had voted on the outlines of the new rescue plan for Greece. According to the terms of the agreement, the German government would act in support of the European Financial Stability Facility (EFSF) to guarantee the newly issued debt of the countries in difficulty. This arrangement would preserve the independence of the European Central Bank (ECB), which Germany saw as a sacrosanct principle. France supported the idea of giving a banking licence to the EFSF, which would enable it to refinance itself from the ECB.

The Euro Summit agreed in principle to an arrangement intended to dramatically increase the firepower of the EFSF. It would have 1,000 billion euros at its disposal, instead of 440 billion, an amount beyond which Germany refused to go. To reach the sum of 1,000 billion euros, a *special purpose vehicle* would have to be used. This was essentially very similar to the type of financial technique so strongly criticised at the time of the sub-prime crisis in 2008.

It proved, however, difficult and laborious to boost the EFSF under the terms of the October 2011 agreement; nor was it sufficient to ‘reassure the markets’. Many economists felt that the only way to deal with the problems faced by euro area Member States in trying to seek finance would be for the ECB to play its full part as the lender of last resort, by buying up unlimited amounts of sovereign debt in order to maintain financial stability. The German government, however, refused to alter its strict views, and would not go along with the many voices asking for this sort of intervention from the ECB.

Typical, therefore, of the EU’s response to the debt crisis was a complex and inconsistent interplay between a (difficult and partial) revision of the Treaty and the recourse to international agreements to overcome national vetoes.

2. 'Economic governance' develops in parallel

The setting up of the financial stabilisation mechanism was not the only measure planned by the EU to mitigate the crisis. In parallel, European political decision-makers worked to enhance economic governance (cf. Table 2).

Table 2 **Stages in the process of strengthening economic governance in the EU**

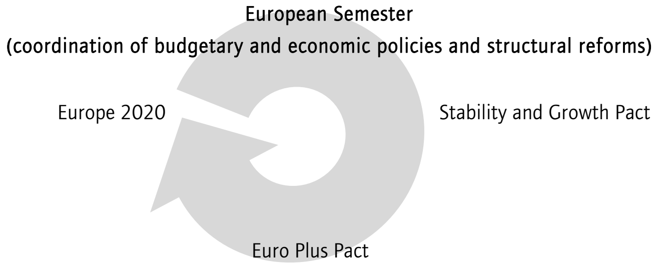
January 2011	European Semester (annual growth survey)
March 2011	Europe 2020, Joint employment report
June 2011	Recommendations
November 2011	Revision of the Stability and Growth Pact, *Six Pack*
December 2011	Agreement on the conclusion of an international treaty

Whilst the EU response to the debt crisis was characterised by the wearisome interaction of national interests, the strengthening of economic coordination shows that progress was being made towards a still incomplete form of budgetary federalism, one which, above all, reflected the general mood of austerity. In sub-sections 2.1 and 2.2 we describe the various initiatives taken, such as the European Semester, Europe 2020, the Stability and Growth Pact and the Euro Plus Pact. In sub-section 2.3 we give a brief description of the enhanced role of the institutions.

2.1 The European Semester and Europe 2020

The beginning of 2011 marked the start of the first 'European Semester', a six month period during which the European Union would try out the new arrangements for economic governance. The aim was to harmonise the timetable for the presentation and evaluation of the stability and convergence programmes (SCPs) set out in the Stability and Growth Pact and the National Reform Programmes (NRPs) required under the Europe 2020 strategy (Barbier, 2011) (cf. Figure 1).

Figure 1 **Economic governance of the EU, the pillars**



The 'Annual Growth Survey' report, presented in January 2011 as part of the first *European Semester*, listed the various measures which the Commission felt were essential to strengthen the recovery in the short term (European Commission, 2011a).

In the view of the Commission, fiscal consolidation, structural reforms and growth enhancing measures should be key elements of a euro area response to the crisis. As part of Europe 2020, the draft joint employment report stressed the need for structural reforms of the labour market. Unsurprisingly, it stated that 'fiscal consolidation will also require a better targeting of social expenditures' (cf. the chapter by Diamond and Liddle in this volume). The joint employment report adopted in March 2011 by the EPSCO Council repeats this and adds that 'the need for fiscal consolidation in order to restore sound public finances intensifies the urgency of speeding up reforms of social protection systems, with particular attention to pensions and health care' (Council of the European Union, 2011b: 24).

Another important initiative was the Euro Plus Pact. In January 2011, at the beginning of the first European Semester, the European Commission had proposed an increase in the lending capacity of the EFSF (European Commission, 2011a). Germany, hesitant as to the idea and wary of considerable public hostility back home to European assistance plans, made its agreement dependent on the adoption of a 'competitiveness pact', to lead to 'stronger economic convergence' within the euro area. Under this 'competitiveness pact', in particular, a principle would be enshrined in national constitutions, as had already been done in Germany in 2009, making it a violation to exceed national limits on national debt. Initial agreement was reached on a more acceptable version of the competitiveness pact, now called the ‘Pact for the Euro’, by the euro area Heads of State or Government on 11 March 2011 (Council of the European Union, 2011c). Member States outside of the euro area were irritated by the prospect of a ‘two-speed Europe’. The ‘Euro Plus Pact’ – extended to a number of countries outside the euro area – was therefore adopted at the European Council of 24 and 25 March 2011 (European Council, 2011a).

The intention of the signatories was to adopt, on a voluntary basis, measures falling within national competence, with a view to enhancing the competitiveness of the euro area and the European Union. In the context of the European Semester, these choices are indicated in the stability and convergence programmes (Stability and Growth Pact) and in the national reform plans (which also contain reforms aimed at achieving the objectives of Europe 2020). These plans are examined by the European institutions together with the stability or convergence plans.

At the beginning of June 2011, the Commission published its guidance for national policies as well as recommendations for each country and for the euro area. Generally speaking, the Commission felt that the Member States had respected the guidelines set out in the Annual Growth Survey, but that some would have to make further efforts. As part of the Euro Plus Pact, several countries had already announced their intention to introduce further measures. The country-specific recommendations are the Commission’s response to the national programmes (SCPs and NRPs). They were discussed at the Employment and Social Affairs Council (EPSCO) on 17 June 2011 and the Economic and Financial Affairs Council (Ecofin) on 20 June, before being adopted by the June 2011 European Council, at the end of the first European Semester.

For the euro area Member States, the European Commission recommended stepping up the relevant Broad Economic Policy Guidelines (BEPGs). In the wake of the Annual Growth Survey, the Commission proposed that, for euro area countries, the BEPGs should also include reforms of national social policies. These could be reforms to social security systems with a view to achieving budgetary sustainability, with particular attention given to pension and social welfare payments, notably by adjusting pensions systems to the national demographic situation or making changes to training or salary-indexation systems, to ensure that these develop in line with levels of productivity and competitiveness. All this would be done 'in consultation' with the social partners.

2.2 Enhancing the Stability and Growth Pact: the Six Pack and the Two Pack

One of the key elements of the new economic governance was the revision of the Stability and Growth Pact. This package of economic governance measures, the so-called *Six Pack*[5], was adopted by the European Parliament on 28 September 2011 and by the Council on 8 November 2011 (cf. Box 1).

On 26 October 2011, building on the legislative package just adopted, the European Semester and the Euro Plus Pact, the euro area Heads of State or Government undertook 'to implement additional measures at the national level' (Council of the European Union, 2011d). The statement issued by the Euro Summit of euro area States contains commitments to 'translate the Stability and Growth Pact into national legislation, preferably at constitutional level or equivalent, by the end of 2012' and 'to stick to the recommendations of the Commission and the relevant Commissioner regarding the implementation of the Stability and Growth Pact', points 26 a) and e). For those euro area Member States subject to an excessive deficit procedure, this means that the Council and the Commission may examine their draft national budgets and give an opinion on these 'before their adoption by the relevant national parliaments' (point 27). The Commission 'will monitor budget execution and, if necessary, suggest amendments in the course of the year', and, 'in the case of slippages of an adjustment programme closer monitoring and coordination of programme implementation will take place'. The statement also expresses the intention to move towards closer monitoring of euro area Member States, subject to an excessive debt procedure pursuant to Article 136 (point 28).

5. The package is made up of amendments to Regulation (EC) No.1466/97 on the surveillance of the budgetary positions and economic policies of Member States; to Regulation (EC) No.1467/97 on the excessive deficit procedure; a regulation on implementing budgetary surveillance in the euro area; a regulation on the prevention and correction of macroeconomic imbalances; a regulation on enforcement measures to correct excessive macroeconomic imbalances in the euro area; and a directive on requirements for budgetary frameworks of the Member States, OJ L 306 of 23 November 2011.

Box 1 Adoption of the *Six Pack*

The Council adopted on 8 November a package of six legislative proposals aimed at strengthening economic governance in the EU – and more specifically in the euro area – as part of the EU's response to the current turmoil on sovereign debt markets. More precisely, moreover, according to the Council, these measures set out to:

- enhance budgetary discipline under the EU's Stability and Growth Pact, in order to ensure a satisfactory decline of public debt in the Member States, as well as a decrease of high deficits to be followed by achieving ambitious, country-specific medium-term budgetary objectives (four proposals). This involves enhancing the surveillance of budgetary policies, introducing provisions on national fiscal frameworks, and applying enforcement for non-compliant euro area Member States more consistently and at an earlier stage;
- broaden the surveillance of the Member States' economic policies, so as to cater adequately for macroeconomic imbalances (two proposals). An alert mechanism is introduced for the early detection of imbalances, to be assessed using a 'scoreboard' of economic indicators. An 'excessive imbalance procedure' is also introduced, with enforcement for non-compliant Member States

In November, as part of its preparations for the second European Semester, the European Commission presented a set of measures and acknowledged a 'need' to go beyond the *Six Pack*. It proposed two new regulations (the *Two Pack*) putting into legal form the undertakings entered into at the Summit of 26 October 2011. The first of these relates to enhancing the surveillance of budgetary policies in euro area Member States. It proposes the drawing up of a common budgetary timetable, and that the Commission should have the right to issue an opinion on draft budgets before their adoption by the relevant national parliament (European Commission, 2011b). Article 4 of the proposal states that the budgetary rules shall be of a 'binding, preferably constitutional, nature'. The Commission was thus creating an across-the-board mandatory 'golden rule' for the balancing of budgets, something requested by Germany and France in August 2011 (cf. below). The second regulation concerned a strengthening of the economic and fiscal surveillance of euro area countries facing or threatened with serious financial instability (European Commission, 2011c). This regulation includes a principle whereby European structural fund payments to a country under surveillance or receiving assistance will be suspended if it does not respect its adjustment programme.

2.3 Role of the European Council, ECB and Commission

In parallel to these reforms of economic governance within the EU, institutional developments have affected the relative weight of the institutions.

Firstly, the European Council has taken on a more central role, and, within it, the partnership between France and Germany has become increasingly prominent. In mid-August 2011, the German Chancellor, Angela Merkel, and the French President, Nicolas Sarkozy, proposed that the President of the European Council should chair the Eurogroup meetings of the Heads of State or Government, and should create an official provision stating that these meetings would be held twice a year (Joint letter, 2011a). These measures, proposed on the basis of the 'existing Treaties', were presented as a way of strengthening 'economic governance' of the euro area. They were agreed to and confirmed by the euro area Heads of State or Government on 26 October 2011.

The second set of Franco-German proposals were an attempt to implement the undertakings entered into as part of the Euro Plus Pact. The most widely reported of these was the demand for the adoption, 'by the summer of 2012', of a 'golden rule' requiring governments to add a provision on balanced budgets to their national constitutions (as Germany had done in 2009), or to equivalent national legislation. In section 4, we emphasise the role-reversal which has taken place within the Franco-German partnership. For many years Germany had to make political concessions as a result of its post-war status, yet today Germany can impose its views and choices, since no other country is in a position to propose and impose alternative solutions.

The role of the ECB has also changed. Despite the adoption of the 21 July plan which was supposed to 'rescue' the euro area, Italy and Spain suffered speculative attacks in the summer of 2011. In order to combat this, the ECB intervened on the secondary debt markets for Spanish and Italian debt, since Article 123 of the Treaty on the Functioning of the European Union did not rule out this sort of intervention. In fact the ECB had already taken similar measures since the adoption of its Securities Market Programme (SMP). This action by the ECB was strongly criticised in Germany, and led to the resignation of Axel Weber, President of the Bundesbank, followed by that of Jürgen Stark, member of the Executive Board of the ECB, both of whom were believers in strict monetary orthodoxy. Interventions by the ECB, however, also come with certain conditions attached.

In Italy, a secret letter from the President of the ECB, Jean-Claude Trichet, co-signed by Mario Draghi, his successor as of 1 November 2011, prescribed a programme of measures including reductions in civil service pay, hasty privatisations of municipal companies and amendments to labour law (extra flexibility in dismissal procedures, etc.). The letter, which was publicshed in the Italian press, also proposed a change to the national Constitution in order to toughen up fiscal legislation,[6] and was seen as a diktat setting out conditions for ECB intervention on the secondary debt market.

Similar events occurred in Spain. During the summer of 2011 the Spanish constitution was revised in the space of a few weeks, following agreement between the ruling majority and the opposition. Both the ‘indignant’ protest movement and the trade unions asked for a referendum on the change.

While some were in favour of a future hypothetical European Minister of Finance imposing budgetary discipline, others felt that this was a role for the European Commission. In September 2011, the Dutch Prime Minister and Minister of Finance had suggested the appointment of a Commissioner responsible for budgetary discipline, who could object to national budgetary plans not in line with European rules. They suggested that the ultimate sanction could be for a Member State to be excluded from the euro area. The Commission had then recalled that ‘neither exit nor expulsion from the euro area is possible according to the Lisbon Treaty under which the participation in the euro is irrevocable’. It was then realised that it would be possible to create the post of a Commissioner responsible for budgetary discipline on the basis of the current Treaties. On 27 October 2011, therefore, the President of the European Commission promoted the then Commissioner for Economic and Financial Affairs, Olli Rehn, to the post of Vice-President. This decision was justified by those taken on 23 and 26 October, reinforcing

6. Translated into French in the article ‘L’incroyable diktat de Trichet à Berlusconi’, *Challenges*, 30 September 2011 (http://www.challenges.fr/economie/ 20110929.CHA4869/l-incroyable-diktat-de-trichet-a-berlusconi.html).

'the central role of the Commission in economic surveillance and governance across the euro area and European Union'.

The Euro Summit of 26 October, moreover, adopted ten measures to improve governance of the euro area while maintaining the current Treaties (cf. Box 2) (Council of the European Union, 2011d).

Box 2 Ten measures to improve governance of the euro area

The annex to the statement issued by the Euro Summit stipulates the following:

1) There will be a monthly meeting of the President of the Euro Summit, the President of the Commission and the President of the Eurogroup.
2) The President of the Euro Summit will be designated by the Heads of State or Government of the euro area at the same time that the European Council elects its President, and for the same term of office. Pending the next such election, the current President of the European Council will chair the Euro Summit meetings.
3) The President of the Euro Summit will keep the non euro area Member States and the European Parliament informed of the preparation and outcome of the Summits.
4) The Eurogroup will strengthen surveillance of Member States' economic and fiscal policies as far as the euro area is concerned. It will also prepare the Euro Summit meetings and ensure their follow-up.
5) A decision on whether the President of the Eurogroup should be elected among members of the Eurogroup or be a full-time President based in Brussels will be taken at the time of expiry of the mandate of the current incumbent (June 2012).
6) The President of the ECB, the Presidents of the supervisory agencies and the EFSF CEO/ESM Managing Director may be invited on an ad hoc basis to participate in the meetings of the President of the Euro Summit, President of the Commission and President of the Eurogroup.
7) Preparatory work will continue to be carried out by the Eurogroup Working Group (EWG), drawing on expertise provided by the Commission. It should benefit from a more permanent sub-group consisting of alternates/officials representing the Finance Ministers, meeting more frequently and working under the authority of the President of the EWG.
8) This working group will prepare the meetings of the Eurogroup and will be chaired by a permanent President elected in principle at the same time as the chair of the Economic and Financial Committee (EFC).
9) The existing administrative structures within the Council (i.e. the Council General Secretariat and the EFC Secretariat) will be strengthened in order to provide adequate support to the Euro Summit President. Finally, clear rules and mechanisms will be set up to improve communication and ensure more consistent messages.
10) The President of the Euro Summit, together with the President of the European Commission, shall be responsible for communicating the decisions of the Euro Summit, and the President of the Eurogroup, together with the ECFIN Commissioner, shall be responsible for communicating the decisions of the Eurogroup to the Euro Summit President.

3. Final steps towards a reform of the Treaties

At the meetings of the European Council, on 23 October, and the Euro Summit, on 26 October, the idea of revising the treaty, making limited amendments, was put back on the European agenda.

The German Government claimed that a reform of the treaties would be necessary in order to 'reassure the markets'. Under the German proposals, the next steps to take would be to carry out a limited revision of the Treaty on the Functioning of the European Union, but also to transform the European Stability Mechanism into a real 'European Monetary Fund' (German position, 2011). These proposals would require the revision of certain articles in the TFEU and renegotiation of the ESM treaty. Once again this was a very complex strategy, broadly based on the concept of a multi-speed Europe.

According to the proposals, Article 126 of the TFEU would be revised to give the Court of Justice a role in the monitoring of budgetary discipline, and Article 121 TFEU would be amended by addition of the 'reverse qualified majority' procedure, which of course did not figure in the treaties as they stood. The procedure thus introduced in the *Six Pack*, and leading to the adoption of quasi-automatic sanctions, would therefore become a constitutional-type provision. This new procedure would result in a considerable strengthening of the European Commission's powers, since the Council, in order to oppose a Commission recommendation, would have to have a qualified majority of the votes.

Germany felt that the text of the ESM Treaty was insufficient. It suggested that the ESM should be given the right to intervene in the budgets of euro area Member States subject to an adjustment programme. If these States were unable to return to a situation of 'debt sustainability', the ESM should be able to set up defaulting procedures, involving the private sector.

Prior to the European Council of 8 and 9 December, France and Germany submitted their revision proposals to the President of the European Council, Herman Van Rompuy (Joint letter, 2011b). The letter was a compromise: France had had to drop the idea of Eurobonds, and Germany had had to renounce involvement of the private sector in the EFSF/ESM treaty. The interim report drafted by Herman Van Rompuy, in cooperation with the President of the European Commission, José Manuel Barroso, and the President of the Eurogroup, Jean-Claude Juncker, includes a number of these proposals. In terms of revising the treaties, the report from the President of the European Council suggests two possibilities (European Council, 2011c: point 15). The first of these takes up the Franco-German proposal to strengthen budgetary discipline by having a 'golden rule' inserted into national constitutions or equivalent legislation, including it in Protocol No. 12 on the excessive deficit procedure. The report specifies that countries would not need to ratify this protocol, a point which clearly raises a problem as to the legitimacy of the change. As requested by France and Germany, the Court of Justice would be charged with monitoring national transposition of this rule.

The other procedure would use Article 48 of the TFEU. Applying to euro area Member States, it would take up the idea of including a reference to reverse qualified majority voting in Article 126, and extending its scope. The Commission and the Council (the Eurogroup) would also be able to request changes to the draft budget of a euro area country subject to an excessive deficit procedure, before the draft was put to the national parliament, if the budget were not in line with the country-specific plan. The Commission would have exceptional powers in its dealings with countries receiving financial assistance, such as a right to approve *ex ante* any major economic reform. Changes to economic governance would be included in Protocol 14, concerning the Eurogroup.

Finally, the European Parliament had already spoken out in favour of the creation of a European Treasury (European Parliament, 2011a). In a resolution on the European Semester, it asked for the convening a European Convention to discuss revision of the treaty (European Parliament 2011b). The resolution 'underlines, in light of the role the EFSF and the ESM are supposed to play, the need for the EP to conduct a hearing with their management staff'.

3.1 Institutional content of the agreement of 9 December 2011

Just before the European Council of December 2011, the ratings agency Standard and Poor's announced a review of the ratings of fifteen euro area countries, including the six countries with a triple A rating (Germany, Austria. Finland, France, Luxembourg and the Netherlands), followed by that of the EFSF. This move heightened the feeling of urgency and showed that the markets were waiting for the ECB to take action.

David Cameron had already announced his demand for exemption clauses to the working time and financial services directives if fundamental changes were to be made to the treaties. When these conditions were rejected, the British Prime Minister stood in the way of the conclusion of an agreement involving all 27 countries. A separate agreement would therefore be necessary (Council of the European Union, 2011e). The nine other non-euro countries did wish to participate in the process, although Hungary and Sweden first needed to consult their parliaments.

Decisions were taken concerning the EFSF/ESM. Implementation of the ESM treaty was brought forward to July 2012 (a year before the designated expiry date of the EFSF, to which it was intended to be a successor). This will apply as soon as countries representing 90% (instead of 95%) of the subscribed capital have completed the relevant procedures. The decision-making mechanism will be revised. Under the revised ESM treaty, well established IMF principles and practices will be 'strictly' adhered to. In their statement, the Heads of State or Government 'welcome the readiness of the ECB to act as an agent for the EFSF in its market operations'. The euro area States and other countries decided on an objective of additional resources for the International Monetary Fund 'of up to EUR 200 billion'. The statement announces that the availability of these resources will be confirmed within ten days. They will be made available in the form of bilateral loans, 'to ensure that the IMF has adequate resources to deal with the crisis.'

A draft treaty, drawn up by the Commission and Council services, was distributed on 16 December 2011. On the previous day, the European Parliament Conference of Presidents appointed three MEPs to take part in the negotiations, which began on 20 December.[7] The United Kingdom attended as an observer.

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7. The three were Elmar Brok (EPP, Germany), Roberto Gualtieri (S&D, Italy) and Guy Verhofstadt (ALDE, Belgium). Daniel Cohn-Bendit (Greens/EFA, France) was an alternate member within the delegation. All these MEPS were members of the Spinelli group.

The draft treaty makes it possible to enshrine in an international agreement the governance principles of the Stability and Growth Pact, revised and undergoing revision, as well as the budgetary golden rule already advocated in the Euro Plus Pact. According to the Economic and Financial Affairs Commissioner, the introduction and implementation of automatic sanctions can justify a revision of the treaty.

A new treaty would be necessary with a view to ratification by Germany of the ESM treaty. Such a treaty could be implemented ahead of time, which would confirm the view that the treaty revision of March 2011 was not necessary, except to justify the continuation of the European Financial Stability Facility (EFSF/ESM) in Germany, and to allow the United Kingdom to withdraw from the European mechanism.

4. Prospects for the future

It is difficult to take stock of a year of frenetic reform-minded activity under great pressure – even subject to threats – from the markets: both the processes themselves and their outcomes are confused and complex. In the next few pages, we report, first of all, on the most significant recent institutional developments. We then highlight the many contradictions therein. Finally, we consider the increasingly shaky prospects for the future of European integration.

4.1 Ever more rigid decision-making mechanisms

Particular procedures were often chosen partially because of the urgency of the situation. This is just one more sign that the inflexibility of the existing rules and procedures is not (or is no longer) suited to the requirements of a grouping which prides itself on being the world's largest trading bloc, with the second most important international reserve and exchange currency. Indeed, as has been rightly pointed out by Bruno de Witte (2011), as the European Union has developed, particularly since the Lisbon Treaty, its decision-making mechanisms have become increasingly rigid at every level: from those for micro-decisions to the procedures for revision of the Treaties. In the case of these latter procedures, the blockages which take place are due to the collective inability of the countries involved to break the supreme taboo: the need for unanimity. The value attached to unanimity is a last vestige of the traditions and conventions of international law, now applied to a system which, objectively speaking, no longer fits into the traditional mould of inter-State relations. Member States did not accept the inclusion in the European Constitution, or later in the Lisbon Treaty, of arrangements in step with the development of the European Union. Rather, they preferred to stick to the rules used in international law, which place supreme importance on the sovereign will of individual States. As a result, Member States now lack the necessary legal tools to deal with the successive crises which have occurred since 2007-2008.

The unanimity rule, which has been gradually sidelined from day-to-day decision-making processes in order to prevent the Union grinding to a halt, still applies fully to any revision of the Treaties. The necessary unanimity, moreover, has become even more difficult to achieve because of the complex institutional mechanisms within each Member State. In the good old days of diplomatic relations between the European powers, it was only the national administrations which had a right of veto. As notions of democracy have progressed, many Member States no longer hold with the illusory notion that sovereignty can be expressed by just one body. In some countries, therefore, the regions can block an agreement, in others it can be done by parliament, in still others the supreme court will rule what is possible, acceptable or out of the question. Sometimes the people themselves will decide, as was the case in Ireland. There is no longer just one State veto, but, rather, a multiplicity of potential vetoes which must be pre-empted or countered by administrations in order to prevent more serious difficulties. Worse still, while a State veto will be expressed at the negotiating table, vetoes from other institutions may only be voiced several weeks or months later, which adds confusion to uncertainty.

Demonstrably then, the rules governing revision of the Treaties are no longer suitable: the Lisbon Treaty, a treaty supposedly intended to guarantee legal security and the proper functioning of the Union for the next fifty years, was ten years in the making. The ink of the signatures, however, was scarcely dry on the page before all sorts of ideas emerged as to how to carry out reforms without having to use the usual procedures, since the urgency of the situation called for action to be taken in a matter of days, not of months or years. Where unanimity was impossible, the Union had to resort to the tried and tested methods of international law, whereby a text was binding only on signatories, and which left by the wayside those who were against or unhappy with a measure. Official statements, of course, tried to avoid clashes with national constitutions by claiming that there had been no transfer of new powers, but rather a shifting around of powers already with the Union.

4.2 Contradictions in these institutional arrangements

In this slightly surreal situation, contradictions abound. To avoid the lengthy and complex procedures of a system which cannot correct its flaws sufficiently quickly, mechanisms must be developed which certainly address the particular situation, but which render the whole system even more complicated, incomprehensible and obscure to the average member of the public. These stopgap solutions, as they have been called, may (perhaps) help to deal with the emergency of the moment, but end up adding another layer to a baroque edifice which can only function with the help and vivid imagination of an army of hyper-specialised legal experts. As for the dream which justified the idea of a European Constitution - of creating simpler institutions, which would be easier to understand and closer to the general public – that dream died a long time ago.

There is another contradiction in the attitude of many of the Member States. These would like, on the one hand, to do without the Commission and the ‘Community method’, preferring to conclude direct agreements among themselves, but, on the other hand, they seem rather helpless when it comes to actually implementing the agreements in principle which they have reached. It might be some comfort to see the Commission brought back into the process through the back door, yet there are negative sides to this development. The situation is clearly inconsistent: the United Kingdom announced, in a spirit of generosity, that it would not fight to the death against the use of the Community institutions to prepare and then apply legal provisions falling under international law. This ‘variable geometry’ approach, moreover, puts the entire structure at risk. At first sight, but maybe only temporarily, the conclusion of these agreements suggests the triumph of the intergovernmental method. This particular intergovernmental method, however, seems somewhat strange, boiling down, as it does, to a cosy tête-à-tête between France and Germany, with other members being told, in the manner of Margaret Thatcher, that 'there is no alternative'.

Even within this Franco-German partnership, a role-reversal has taken place. For many years Germany had to make political concessions because of its post-war status, and showed itself ready to pay the bill for European integration if that were necessary. Now, however, Germany is able to impose its views and choices, since no other country is in a position to propose and impose alternative solutions. Its partners have no choice but to go along with German views, which will only change if Germany sees its interests directly under threat (through, for example, the collapse of the euro area). This 'reverse veto' is more suited to old-style international politics than to relationships within a quasi-federal Union, since, when it comes to monetary issues, the solid alliance between a country and a central bank developed according to the requirements of that country, removes almost any element of 'checks and balances'. 'Germany rules the waves!'

We have known for years that an intergovernmental Europe exists alongside the European Community; we likewise know that the Maastricht Treaty was what gave it resilience, tasks and procedures. Since then, however, the two Europes have followed parallel routes, except in the case of operational transfers from one to the other (as happened for a broad swathe of the so-called third pillar), as well as in the sense of building bridges to connect the two together (as happened for tools established by the Treaty to reinforce Community policies, used instead for the intergovernmental policies).

When the parallel routes of the two Europes interfered with each other in the past there was some confusion. Before the Lisbon Treaty this was the case of the combined international agreements: i.e. ones relating partly to Community responsibilities, but partly operating also as functions of the intergovernmental Union. In those instances, the same individuals took on two different negotiating roles – as Community representatives and as representatives of the individual States – and had to affix two different signatures. Yet the share-out between the two Europes was understandable (government responsibilities transferred to the higher European level/government responsibilities that remained governmental but were exercised jointly); similarly, the purpose and effects of the hybrid model were understood too.

By contrast, the hybrid model sparked by the Eurozone crisis has a completely new character, since it does not result in bridges between routes that remain parallel. Rather, it generates overlaps between the intergovernmental method and the Community method within a single route or a single procedure:

— a modification to the Treaty (additional amendment to Article 136) gives rise to an intergovernmental agreement (on the establishment of the ESM);

— an intergovernmental agreement on tightening up the Stability Pact produces a Community regulation that focuses on and organises these more rigid characteristics;

— or, thirdly, an intergovernmental agreement (the so-called Fiscal Compact) will spawn not only domestic constitutional amendments within the individual Member States, but also Community regulations.

It is difficult to form an overall opinion about all of this. Douglas Hurd, who was UK Foreign Secretary at the time, managed to explain the parallel routes of the European Community and intergovernmental Europe as being placed side by side and connected by means of Maastricht Treaty bridges, using the helpful image of pillars and an EU 'temple'. In this way he resorted to architectural imagery that was at least comprehensible. Today's choices appear to be dictated by political appraisals leading to a preference for any formula on which it is easier for national leaders to reach an immediate agreement, first and foremost the German Chancellor and the French President. This is the 'Union method' announced by the Chancellor herself in her memorable speech in Bruges in November 2010, when she defined that method as 'the one by which the agreement is reached'. That is indeed what will happen, but it has no prospects, is indistinct and poses problems that are difficult to solve, given the competition and conflict between Community sources and intergovernmental sources. In the best of all hypotheses it is the method defined by Carl Schmitt as that of items that govern themselves. But they do so with the far-sightedness and vision deriving from those items.

This new intergovernmental method, however, which is really intergovernmental in appearance only, is fragile and already beginning to show its limitations. The only country able to stand up to Germany – to defend its own interests rather those of the Union and the Community institutions – is the United Kingdom, largely because it does not belong to the euro area. Yet the UK preferred to use its right of veto and then withdraw, thus setting the scene for, at best, a two or more speed Europe, at worst the start of a gradual disintegration of the Union.

So we are now seeing the gradual emergence of a Europe of several concentric circles. At the centre is the biggest group: the euro area countries. Then we have the small group of countries which have refused to join the euro but have tied their national currency to the European currency (Denmark and Sweden). The third circle is made up of countries which aspire to join the euro at some point in the future. Fourthly there could eventually be those countries which have been 'thrown out' of the euro area, if the worst comes to the worst. And finally, seemingly on its own – but can we be so sure? – we have the United Kingdom, already outside of Schengen, and which might be tempted to go it alone, just maintaining the parts of the European construct which serve its interests: i.e. the single market. Since the common foreign policy currently seems to be going nowhere, since European defence policy exists only as bilateral arrangements, despite the presence of the military in the corridors of Brussels, and since Member States stubbornly refuse to establish a real Community budget, there is relatively little real substance to the 'Union'. Unsurprisingly, the 'intergovernmental method' can quickly become just a way to defend national interests, thus leading to a small-scale 'UN-ification' of Europe. There are many similarities: a large number of countries making it difficult to take decisions, the dogmatic defence of national interests, the dominance of the 'great powers' and an explicit or implicit right of veto.

All the evidence, then, seems to go against the Community method and institutions, and to argue in favour of intergovernmental decision-making processes and the supremacy of the State. However, can we be so sure?

4.3 Federalism that lacks democratic legitimacy and solidarity

Despite this description of the decision-making methods and the tools used in the recent crisis, the substance of the policies implemented or planned is very different. Those measures already taken or currently being implemented are clearly federal in nature, although most States are very quick to decry federalism as such. Great care has been taken to avoid the 'F word', as Philippe Schmitter (1996) calls it, to show how unacceptable the term 'federalism' has now become. Once again, European governments have accepted, rather than chosen, the inevitable, while denying the real nature of these so-called 'choices', and using the technical and somewhat obscure nature of most of the measures adopted to disguise that nature. They have also downplayed the political significance of these measures as far as possible, stressing their technical aspects. Nevertheless, the seeds of budgetary and fiscal federalism have been sown. The damage has been done, and once the immediate crisis has passed, it will become increasingly difficult for countries to hide behind ignorance and bury their heads in the sand.

Here lies the paradox. Member States have, reluctantly, had to accept a degree of federalism which was vital in order to shore up Monetary Union. This federalism, however, is still incomplete: it lacks the solidarity which is required by and part of such a system (as was seen with the Greek bailout, which occurred despite a ban in the Treaties). It also lacks a 'federal' budget, which could help offset any asymmetric effects of particular measures. Neither of these aspects is (yet) on the agenda. Worse still, since governments are in a state of denial, no significant proposals can be made as to how to strengthen democracy in parallel. The European Union and the governments guiding it are storing up trouble for themselves if they continue – reluctantly - transferring ever greater competences and responsibilities to a non-government which lacks the necessary legitimacy, and which is, ultimately, accountable to no-one. We may regret the British stance, and deplore the lack of support for Europe in the Conservative government and, more generally, among the British public, but we cannot deny the consistency of their position. The same cannot be said for most of the other European governments, which, somewhat against their will, are practising a closet and disguised type of federalism.

4.4 Future scenarios

This situation could work for good or ill. To take an optimistic viewpoint, the tension between increasing EU powers and sluggish democratisation may become unsustainable. In five or ten years' time, then, we may see the necessary quantum leap in European governance and an inevitable political federalisation. This optimistic scenario, however, could be ousted by a far more negative one, in which the crisis-stricken peoples of Europe rise up and blame the 'faceless bureaucrats' of Brussels for their troubles. There is a serious risk that the baby could then be thrown out with the bath water. We are already seeing numerous anti-European movements mushrooming in all Member States. On the European mainland, pro-European parties were ideologically dominant for the first fifty years of European integration, yet today the reverse is becoming true. The only potential bright spark on the horizon is that society might find itself divided along different lines. A new federal/anti-federal division could replace the old social divisions now becoming obsolete, such as that between the working class and the bourgeoisie: two social classes which have increasingly been replaced by a large middle class. The unbearable sluggishness of Brussels will not survive for long if nothing is done about the unbearable democratic lightness of the Union.

Democratically elected European governments, moreover, will find themselves increasingly bothered by the rise of populist and protest parties, objecting to the non-negotiable character of policies decided elsewhere. Parties which have always been the backbone of democracy, producing ideologies, defending interests, polarising opinions and votes in order to gain power and implement their choices, are now caught between their own national programmes and European policies over which they no longer have any control. There can be no national churches when the Pope himself is infallible! The only option, since the system itself offers no alternatives, is to create heretical churches, i.e. iconoclastic policies such as, for example, leaving the euro area, or even the Union. If the national electorate has no influence on policy, then, as has been commented by Peter Mair (Goetz *et al.*, 2001), opponents of particular polices have no choice but to oppose Europe itself.

The position of the national parties and governments is made even more uncomfortable by a singular division of labour between the 'federal' level and the States. The Union, then, holds almost all powers in the area of economic regulation, as well as a monopoly in trade negotiations. It is in no way required to concern itself with the collateral, unexpected or undesirable effects of its choices and decisions. It is the Member States – which are impacted in extremely varied ways by these policies – which must do what they can to deal with consequences which may be positive, but which may also be negative.

In the early years of the European process, Brussels held the economic powers, but could also use compensatory measures to make change more acceptable (for example the coal and steel policy or the agricultural policy). Union social policies, however, are rudimentary and involve very little, if any, direct or indirect redistribution of wealth. Many good reasons justify this division of labour, some of the most important being the very varied nature of national welfare systems, the considerable differences in income within the Union, and the enormity of trying to create a European redistribution policy, in terms of finance, management and political acceptance. Nevertheless, the facts remain. Redistribution represents the political decision par excellence, and national political parties are subject to certain constraints, whereas the Union can show a sort of 'benign neglect' in the matter. The long-term viability of this division of roles is questionable. We need only apply Machiavelli's subtle observation to the Prince as to why reform is difficult: the problem is, he said, that those who will benefit from a reform are unable to imagine the future benefit, while those who stand to lose are only too aware of the future costs. We could not put it better ourselves.

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