The European Union in Crises or the European Union as Crises?

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Introduction

For more than six years we have been literally obsessed with crises. First it was American banks and other financial institutions that were in crisis. In late 2006, the floor fell out of the housing market. That market had previously been propelled by the growth of subprime mortgages, and the sudden turnaround hit banks and financial institutions. By the autumn of 2007 the waves of the American financial crisis hit the European shores. The bank run on Northern Rock was the first in Western Europe for seventy years. The collapse of Lehman Brothers in September 2008 rendered clear that this was more than a temporary financial setback. The global financial markets came close to meltdown. Collapse was avoided thanks to massive interventions by public institutions. Massive amounts of private debt (fictitious capital produced by financial institutions in the previous decade) were nationalised at a very high cost to exchequers. Radical neoliberals such as Bush II woke up and realised that they had become the biggest socialisers in history. Nationalisation was however resorted to not in order to transform society, but to preserve the value of financial assets. That did not do much to help the 'real economy' (the non-financial sector), and in late 2008 there was a drastic reduction of international trade that triggered a severe global recession. The worst was avoided due to massive public interventions (largely thanks to the much maligned welfare states).

For a while, there was much (cheap) talk of reforming capitalism. Such proposals were quickly shelved as political sentiment turned upbeat again. By summer 2009, there was general talk of 'green sprouts', or what is the same as recovery. The peculiar theme of growth through austerity became dominant. Then Europe became the main crisis scenario. A change in government in Greece revealed an enormous hole in Hellenic public finances (a hole that in fact predated entry into the Euro, and had been benignly neglected by international and European institutions in the late 1990s and early 2000s). The financial crisis mutated (or better, seemed to mutate) into a fiscal crisis which dragged the whole eurozone and indeed the entire European Union down. By 2010 the hype was the 'spread', the difference between what the eurozone core (Germany, the Netherlands, Austria and to a certain extent, Finland) had to pay for issuing public debt and what the rest, especially Mediterranean countries (relabelled PIGS, PIIGS or more euphemistically GIPSI) had to pay. Just at the same time that European institutions and many scholars and pundits were celebrating the successful first decade of the Euro (which had allegedly sheltered Europe from the worst of a crisis 'imported from America', a claim that with the benefit of hindsight is cruelly humorous), the structural defects of European Monetary Union were exposed. The ideology that came hand in hand with the successful introduction of euro banknotes crumbled. The folly in the belief that monetary union had abolished economic crises was difficult to miss.

Six years after a whole series of punctual policy decisions and a whole array of structural reforms, all presented at the time as the decisive move to end the European crises, the future of the euro and even of the European political project still hang in the balance. In the last months, calm has returned to European financial markets. General consensus points to the announcement of 6 September 2012 by the European Central Bank (ECB) to do 'whatever it would take' to save the euro as the game changer. That would include acquiring the debt of ailing states (under a European programme) in apparently unlimited amounts. It is true that since Draghi, *modo Delfico*, spoke, the 'spread' of all peripheral states of the eurozone has declined steadily. Unsurprisingly, Draghi was quickly trumpeted as the 'man of the year' by several media. The ECB seemed to have saved the hour for the eurozone.

But this development in the eurocrisis saga invites serious reflection. For one, it reveals the extent to which central banks have become key players in contemporary European politics. That the fate of the eurozone was in the hands of the ECB should make us ponder whether we have not entered the era of post-democracy, to use the apt term coined by Colin Crouch (2004) more than a decade ago. Can it ever be a good thing that the fate of a polity de facto rests on the words of a central banker? Further, the ECB announcement worked, but was it backed by real substance? What form of convincing sustained action is available if the statement is put to the test? In the short run, it is important to take into consideration that the ECB does not have as counterpart an Exchequer that is ready to print money. Rather, the ECB represents a collection of exchequers, which, were the buying of debt to go really wrong, has to recapitalise the bank. Moreover, it is national banks, not the ECB, that actually buy securities. Were serious doubts about the European or national constitutionality of unlimited debt acquisition to emerge, the governing board of the ECB would be essentially powerless if faced with a rebel national central bank (or banks). And indeed the fact that the feet of the September 6 giant are made of clay has started to become clear. The OMT interim ruling of the German Constitutional Court may or may not lead to a final declaration of unconstitutionality of the programme, but what is certain is that the initial magic spell of OMT has been broken for good. The German Court has flagged (and not without reasons) that a genuinely unlimited OMT will be unconstitutional. Will the OMT do the trick if the ECB cannot pretend that it will buy unlimited quantities of debt? In the long run, it is unclear for how long a structural and deep crisis can be contained by short-term expedients which merely postpone the day of the reckoning by moving around debt. The over-optimistic discourse of an 'imminent recovery' peddled by European and national institutions is still to be supported by hard data; and as time passes, it is projected further ahead in time (at the time of writing, Greek recovery, which will not translate into massive job creation, is scheduled for 2015). There is also the uncertainty and volatility that the complex European scene of multiple electoral cycles and attendant political changes brings up. With elections to the European Parliament to be held at the time this report goes to press, there are good reasons to question the commitments of politicians who may not be re-elected.

There are, in brief, very good reasons to assume that the crises may be here to stay. That in turn raises the question: Which and whose crises? Given the sheer complexity of the scene and an underlying uncertainty as to whether what we confront is at base one crisis or a multitude of crises, confusion abounds. A first goal of this report is to cut through this confusion. Are we experiencing what boils down to a financial crisis, to be blamed on greed and rotten apples in financial institutions? Or is it a fiscal crisis due to lax ethical standards in Southern European politics? Or is it a structural crisis of capitalism, perhaps of financial capitalism? Are allegedly spendthrift and lazy Mediterraneans to be blamed for getting hooked on cheap inflows of capital? Or are we to blame allegedly greedy German bankers for pushing credits without doing any minimal credit assessment? Whose crisis is this indeed? Who is suffering? And who is benefitting from it? Is debt an 'intergenerational' problem? Or does it keep on being true that there is no debtor without a creditor? If everybody seems to be deeply in debt, who are those so deeply in credit?

Europe in crises, Europe as the crisis aims at clarifying what kind of crises the European Union is going through, what kind of actions the European Union has taken to govern the crises, and how the European Union and its member states have been changed by the crises, including the attempts at governing them.

Three main topics that are considered in the report are:

- The structural roots of the present manifold crisis of the European Union. Europe is in crisis, but is it just one crisis or several overlapping crises? If the latter, which crises? And whose crises? How are the consequences and effects of the crises being suffered? Who pays for the crises?

- The policy decisions and the structural measures that the European Union has taken to deal with the crises. What has been done in contrast to what has been said to have been done? Has there been any consistency in the crisis fighting measures? Or has it just been a collection of policy measures on the hoof? Is there any chance of these measures tackling the causes of the crises, or will they fail on account of their being based on wrong policy assessments?

- The changes that the crises, and the measures taken to govern them, have brought to the European Union and its Member States. We are more than five years into the crises, and it is consequently untenable to assume that the measures are temporary and exceptional, and will be rolled back when the crises are over. The Union has already changed. But how? What have been the actual changes to the distribution of competences, the institutional structure, and the substantive contents of European constitutional law?

Which crises?

To make sense of the crisis it is necessary to do two simple things.

Firstly, to distinguish between what triggered the crisis (the subprime crisis) and the structural weaknesses that have cumulated over decades and turned into acute crises by the release of the trigger. Secondly, it is to shift from talk of crisis in the singular to talk of crises in the plural. We need indeed to distinguish the different structural weaknesses that have overlapped and make up the crisis. Insisting on talking about one crisis is the quickest way to collapse all arguments and render the crisis an unintelligible process, and thus render it impossible to put forward meaningful proposals to tackle and overcome the crises.

A trigger need not have much connection with an underlying cause. The shot in Sarajevo triggered World War One but cannot be attributed much causal significance beyond that of a spark – the point is that in a gas-filled room any one spark can cause a major fire. By the same token, the subprime crisis did not cause the crises; it was merely the last straw that when added to all the previous ones ended up breaking the camel's back. It is simply counterintuitive to assert that a mortgage market which represents a minor part of one (big but still only one) mortgage market, itself a fraction of the total global financial market, could unleash one of the biggest global crises in history. We should do well to share Queen Elizabeth II's astonishment and ask again, as she did at the LSE in early 2009, how could that happen? The effects of the subprime crisis are not to be sought in the subprime crisis itself, but in the manifold structural weaknesses of the Western socio-economic models, weaknesses that had cumulated over (at least) three decades.

We may identify five such weaknesses. First, there was an economic weakness. The long postwar 'golden age' was rendered possible by a socio-economic model grounded in the feasibility of high and sustained economic growth, of at the very least 3 per cent per annum. With growth in the whole Western World proceeding at a much lower (and indeed diminishing) speed since the 1970s, social and economic tensions have only kept on piling up. Neoliberalism promised to sort that out, but in reality it only gained time by unleashing an unsustainable growth in private debt. Second, there was a financial weakness. Low levels of real economic growth fostered the search for an alternative 'growth' drive, which was said to have been found in the exponential growth of 'financial services'. This was a mirage (financial activity cannot but be auxiliary to non-financial activity), and a very dangerous mirage for that, because it led to financial institutions ceasing to discharge their basic social functions, namely, intermediating between savers and investors, and assessing credit risks. Instead of boring but reliable financial institutions, we got very entertaining, flamboyant and speculative banks and shadow banks, which progressively put more and more sand in the economy by their frantic creation of fictitious wealth. Third, there is a fiscal crisis. The liberalisation of capital movements, led by Thatcher and Reagan, undermined the actual capacity of tax authorities to know the income and wealth of taxpayers. The gap between tax design and the reality of tax collection started to grow. Impotent tax states started to adapt. Scandinavian countries showed the way by reintroducing lower taxes on capital income in the (rather vain) hope of alluring taxpayers by reducing their obligations. The United Kingdom excelled the technique of attracting financial institutions and profited (for a while) from their tax returns, while the Benelux specialised in providing the legal and accounting services that allowed (wealthy) taxpayers to dodge taxes (the possibilities of doing so were multiplied by several judgments from the European Court of Justice (ECJ) in Luxembourg which fostered a peculiar understanding of tax avoidance as a legitimate exercise of economic freedoms; Harries could not be happier indeed). Fourth, there were major macroeconomic weaknesses, in particular, a deficit in macroeconomic steering capacities. The pulls and levers of macroeconomic policy were rendered inoperative by structural changes in the world economy (such as the sinking of the Bretton Woods international monetary system in 1971) or were simply abandoned in the name of the self-stabilising capacity of markets, as indeed was the case with Economic and Monetary Union (EMU) in the European Union. Fifth, there is a political crisis. The developments leading to the just mentioned structural weaknesses came hand in hand with the growth of transnational economic activities. Thus, the nation-state remained the key political unit while it progressively lost the economic and institutional means with which to discharge the constitutional mandates of full employment and rising living standards. That was bound to create a growing political unrest, at heart resulting from the growing gap between what politicians pretended they were capable of doing, and what they were actually capable of doing. By inflating social expectations at the very time that they found themselves with ever fewer means to realise them, political representatives set the stage for a structural political crisis. Whether a brutal deflation of expectations through repudiating the promises of the welfare state – a process that is now at full traction as part of the structural reforms imposed upon peripheral countries – would not lead to social explosion is an interesting question that, unfortunately, it seems, we will have to come to terms with in the coming years.

The deadweight of the past: Why is it Europe that deeply engulfed in crises, and not the USA?

Public discourse offers little clarity and much confusion on the nature and implications of the crises. But most people are even more puzzled by what may be called the one million euro question: How come what seemed to be a US-made crisis, a crisis deeply connected with the American way of doing finance, ended up causing a deep and existential crisis for the European Union, and particularly the eurozone, rather than for the most obvious addressee, the United States? European integration was said to be a means of rendering Europe capable of playing a role in world affairs. The euro was advertised as enhancing the autonomy of Europe in monetary affairs. So why did the crisis not only hit Europe, but hit it much more severely than the United States? Why is the euro, not the dollar, at risk? There are three main reasons why it is Europe, and not the United States, that is suffering most.

Two are rather straightforward. Firstly, it is true that both the subprime crisis and the underlying financial crisis were largely manufactured in the USA. The transformation of banks from boring but reliable institutions into planks of the financial casino was conceived and first implemented in the USA. Similarly, the 'financial models' which turned the financial markets into huge Ponzi schemes were developed by American investment firms. However, the buyers of all those toxic financial products were not only American. Indeed, they were also European. When the US Treasury bought massive amounts of dubious loans in October 2008, German and French banks were among the main beneficiaries (Deutsche Bank and BNP-Paribas). As Michael Lewis (2011) has told with cunning sarcasm in his recent *Boomerang*, German banks were the last ones to realise that the 'music had stopped'. Indeed, some German regional savings banks kept on buying toxic financial assets when everybody was already trying to sell them. They were among the first to be bailed out in the fall of 2008. Furthermore, while the financial technology was put together in the USA, London was the global hub which connected financial creators and financial investors. And London, as we know, is part of the European Union, even if financially speaking it may be said to be the capital of the tax haven network.

Secondly, the policy response to the crisis was different in the USA and in Europe. The Bush administration suspended its belief in the self-regulating capacity of markets and launched the biggest socialisation programme in history (a peculiar socialisation that ended up redistributing money from the poor to the rich), at the same time that the FED started printing money like mad. More dollars have been created since 2008 than were coined or printed in the 200 plus years of US history. When Obama was elected president, the new administration paid more attention to growth than to balancing the books (allowing the deficit to be close to 10 per cent of the GDP). Although Republican victory in the mid-term elections forced a degree of budget-cutting and austerity, there was a constant anti-cyclical effort. Things have been very different in Europe. Some states (outstandingly, Germany) have been highly reluctant to engage in any kind of stimulus. Other states (like Spain) engaged in some form of 'Keynesian policies' for a period. But the Greek fiscal crisis of late 2009 led to an imposed convergence on so-called austerity. The German government has essentially exchanged its underwriting of loans to fiscally asphyxiated Mediterraneans for the generalisation of draconian budgetary cuts, even where such cuts can only lead to economic collapse. We will go back to the question of whether this was good policy, and whether the Mediterranean taxpayers should pay the credits that German banks now find difficult to get restituted, but what concerns us now is that fiscal policy in Europe since 2010 has focused on balancing the budget even when that has aggravated the unfolding economic crises. If the USA are doing somehow better than Europe, that is not a surprising, but rather an entirely foreseeable consequence of the policies being implemented in the USA and Europe. It could be said that European states have bigger social and welfare programmes than the USA, and such programmes largely do the job that Obama is forced to do through specific new expenditure programmes. And it could be added that a Keynesian stimulus programme in Europe cannot be implemented at the national level, where the competence to do so lies, because a German programme will not create jobs in Germany, but in Hungarian car factories. Or even that the USA is only postponing the day of the reckoning, as the actual policies being implemented only aggravate the imbalances in the American economy. There is some truth in all that. But still, there is no mystery in Europe going into a new recession if draconian cuts to public expenditure are implemented in the middle of the worst crises in memory. Even Germany is starting to feel the pinch. For all the exporting might of the teutonic heartland, the fact of the matter is that more than 80 per cent of the surplus comes from trade with the other EU member states. And when these states go into recession, fewer washing machines are sold.

There is a third, and perhaps decisive, reason, why it is the EU, and not the USA, that is suffering most. The reason itself is a simple one: Europe was a much more fragile polity than the USA when the subprime crisis hit the world economy. And both the EU and the USA were much more fragile in economic and financial terms than they both were in the 1970s. In the same way that the flu is a lethal disease for those who are very frail, a serious problem for those who have a previous condition, but only a temporary setback for those whose immune system had been shaped up by a previous flu, the present crisis may end up being lethal for the eurozone and perhaps even for the European Union as a whole. While the claim that the Union was very fragile was ridiculed in the early stages of the crisis (2009 was after all the tenth anniversary of the monetary union, and European institutions, pundits and scholars were still in celebratory mood), now it has come to be widely subscribed. What remains rather contrarian is to claim, as we do, that the fragility is not merely a matter of Europe not having developed enough, of Europe being still insufficiently powerful (which is the basis of the constant calls for 'more Europe'), but of the institutional structure and policies of Europe being the wrong ones. We can trace some of the roots of the structural fragility of the Union back to two key decisions, taken in the 1980s and 1990s, which radically transformed the European political project, even if that transformation was not widely noticed by the public. These two transformative events were the redefinition of economic freedoms, the result of the Commission and the European Court of Justice favouring a neoliberal understanding of the Union in line with the transformations taking place in some member states, and the decision to launch a monetary union grounded not on an economic and political union, but on the self-stabilising capacities of markets, including financial markets.

Firstly, economic freedoms were radically transformed in the 1980s, and with them, the very understanding of the European political project. The original treaties and the laws approved to implement them gave place of pride to free movement of goods, a secondary role to freedom of movement of workers and freedom of establishment of companies, and a purely auxiliary role to free movement of capital, which was actually the freedom to make payments on account of goods or services, not to engage in transnational financial speculation. That mix required member states to treat economic actors from all over the Community as if they were nationals, but did not predetermine how all economic actors should be treated. In other words, member states had to open their markets, but retained the capacity to regulate the markets and to undertake social and redistributive policies according to the political preferences of their citizens. Starting in the late 1970s, a new understanding of European economic freedoms was proposed. All economic freedoms, and not only free movement of goods, were to be given place of pride, something that entailed making of free movement of capital a full-fledged freedom. That would lead to a 'single market', not as a result of political decision-making, but out of the pressure exerted by economic actors empowered by Community law to exempt themselves from regulatory, social, and redistributive policies. While the political initiative came from transformations in member states (outstandingly the United Kingdom, where full employment was abandoned as an overriding policy goal under Labour in 1976, only for neoliberalism to become constitutionalised under Thatcher), the Commission and the ECJ were instrumental in turning this new blueprint into positive law. It took a long time before the European public realised the breadth and scope of the transformation. But when the right to strike was given the back seat to freedom of establishment in the famous cases of Viking and Laval, the outcry was phenomenal. Leaving aside the social consequences, what is of essence for our present purpose is that this new understanding of economic freedoms played a fundamental role in fostering the financial and economic weakness of the European Union. Without the 1988 Directive making free movement of capital a fundamental right of all capital holders, Europe might have been much less exposed to US financial technology; without it, the degree of financialisation of the European economy would have been lower; and there would have been less erosion in European states' ability to collect taxes.

Secondly, an unprecedented form of asymmetric monetary union was launched in 1999. Twelve member states of the Union decided to give themselves the same currency. Monetary policy was trusted to a federal but 'technical' (i.e. non-democratic) institution, the ECB, which was given the sole mandate to keep prices stable. Economic and social policy was said to remain in the hands of member states, and thus subject to national democratic decision-making. As it was obvious that one single monetary policy and twelve fiscal policies could be colliding all the time, there was a need of some form of bridging arrangement. But lacking political agreement on the shape of the bridge, none was erected. Instead, and under the pressure of the German government and central bank, a 'soft law' arrangement was established, setting maximum deficit (and theoretically) debt levels. More importantly, states renounced key fiscal powers. While federalising monetary policy eliminated the possibility of funding the debt by means of printing money, EMU further entailed the prohibition of imposing forced loans on financial institutions (not rare in the past), a prohibition against requesting and granting financial assistance to other eurozone states (the famous no bailout clause) and indeed the intentional elimination of the bailout fund foreseen in the original treaties and put to use in the 1970s for the benefit of Italy and Ireland. This unprecedented union seemed to work fine during the sunny days of the early 2000s. Statistics seemed to point to a progressive convergence within the eurozone. But the glittering figures hid in plain sight that the massive flows of capital from North to South were creating colossal imbalances. These massive and constant flows of hot money were predictably invested in non-sustainable activities (real estate speculation) or fuelled public and private debt that merely compensated for the growing incapacity of Southern economic models to sustain themselves within the framework of monetary integration. Asymmetric monetary union thus nurtured (and allowed hiding) the structural deficits of the famous PIGS states, at the same time that the constitutional framework of EMU rendered the eurozone states structurally incapable of ensuring both the safety of their debt (which in the last instance is guaranteed by the printing of money, as we have seen in practice in the United Kingdom) and to govern the crisis by means other than reducing taxes and devaluing social and labour rights.

Which and whose government of the crises?

The governing of the crises has produced deep changes in the European Union's material constitution. The depth and breadth of these changes may not be readily apparent and may also have been downplayed. Three related reasons may account for this neglect or oversight. Firstly, crisis measures tend to be presented as mere temporary measures. In contrast, we see that some of the changes have been written into the hard not very malleable fabric of the primary and secondary law of the European Union. That only serves to underline that many of the consequences of seven years of crisis government may to a large extent be irreversible. There is thus no simple way of returning the European Union as a polity steeped in European law as a legal order to the status quo ex ante, to the way in which it was before the crises exploded. Secondly, most relevant changes have been made in rather *unconventional ways*, or what is the same, have been taken through procedures out of the beaten constitutional track. Transformations of constitutional nature have been enshrined in Regulations and Directives, as well as in odd intergovernmental Treaties, outside, but at the same time inside the province of European Union law. That ambiguity has obvious bearings on the constitutional stature of European law and on the EU as a polity. Thirdly, the governing of the crises has been *narrated* as if it was a permanent stream of measures to handle contingencies, issues arising out of the dynamics of the unfolding crisis. But, quite obviously, crisis handling can be turned into a governing technique (and there are many precedents, with Cicero's move against Catilina among the most famous ones). At any rate, we can now by looking at the cumulative effects of the crisis responses start to discern clear patterns of transformations.

The material European constitution has been transformed in three main ways: Firstly, competences have been centralised; secondly, the old institutional balance which ensured that supranational decision-making served as a democratic transmission belt, shifting legitimacy from the national to the supranational levels, has been reshaped to a more streamlined division of powers, much tilted in favour of the least representative institutions, which are allegedly more capable of governing efficiently; and thirdly, the principle of equality between member states has been set aside at important instances, with different legal regimes emerging not only for eurozone and non-eurozone member states, but also, and critically, for creditor and debtor states.

Centralisation of competences

Six major socio-economic competences have been: shifted from the national to the supranational level; or recreated at the supranational level; or the powers of the supranational level have been drastically increased.

- The power to monitor and discipline national financial policies (comprising both tax and expenditure, and the overall relation between the two) in the hands of the Eurozone Council and the Commission (as we will clarify infra, perhaps it would be more precise to refer to the Commissioner of Economic and Financial Affairs and not to the Commission as a whole) has been much strengthened. This is so because supranational institutions have not only been given new powers over macroeconomic policy, but the indicators and benchmarks characteristic of soft law have been replaced by rather concrete fiscal rules on what concerns fiscal policy (with a very tight definition of medium-term deficit objectives, and the introduction of precise deficit and debt reduction trajectories) and new decision-making procedures (the European Semester, but not only) that guarantee that the views of supranational institutions will be decisive in the shaping and moulding of five-year budgetary perspectives and annual budgets (the latter losing the central position they used to occupy in national politics). To this we must add the fundamental change introduced in the voting rules regarding monitoring and sanctioning. The Stability Treaty replaces qualified majority voting with qualified *minority* voting (usually referred to by the cloaking term reversed qualified majority voting).

- The margin of discretion and latitude with which the ECB can conduct its monetary policy has been drastically increased through emerging constitutional conventions. In the name of saving the euro (in particular, in the name of avoiding that any of the present member states would be forced to exit the eurozone), the ECB has taken a number of unconventional decisions apparently underpinned by the meta-principle of avoiding the collapse of the eurozone, a meta-principle that would trump even explicit mandates to the ECB enshrined in the treaties, including the mandate to ensure that capital is allocated through undistorted markets and not public fiat. The ECB became the lender of *first* resort of European banks in 2007, and retains that condition at the time of writing, despite articles 127.1 and 119 in the Treaty of the Functioning of the European Union (TFEU). Through its Securities Markets programme, and now through the (untested) Outright Monetary Transactions programme (and in-between, albeit indirectly, through the three-year Long Term Refinancing of private financial institutions), the ECB has become the lender of *last* resort of eurozone states. These new roles lead to monetary policy deeply influencing the shape of fiscal policy, which was supposed to be kept autonomous from monetary policy, not only on account of the division of labour between the Union and the member states, but also on account of the limited legitimacy basis of the ECB.

- The new European Stability Mechanism, which is the successor of the odd duo, the European Financial Stability Mechanism and the European Financial Stability Facility created in 2010, has been attributed the power to grant financial assistance to eurozone states suffering liquidity problems (although, as should be clear by now, the distinction between liquidity and solvency is in the eye of the beholder, or perhaps we should say in the eye of the creditor).

- The Systemic Risk Board, led by the ECB, and where all supranational financial supervisors are part, has been granted the power of macroprudential supervision of European financial markets. This power has been genuinely recreated at the European level. Before the crises hit Europe, it was widely believed that macroprudential supervision was obsolete, and that modern financial markets were capable of self-stabilising.

- The ECB has been granted the power to supervise 'relevant' financial institutions (microprudential supervision). At the time of writing, it remains unclear whether the power of the ECB, which will extend to the birth of banks, will also comprise meaningful powers concerning the death of banks, powers which need to be backed up by sufficient amounts of resources that can be mobilised. There are good grounds to believe that for the time being, the banking union will remain asymmetric, a quid (Europeanisation of supervision) without a quo (mutualisation of funds with which to solve banking crises).

- Article 8 of the Stability Treaty grants the ECJ the power to review the European constitutionality of the national constitutional reforms through which signatories of the Stability Treaty will patriate the principle of budgetary balance, in the terms established in the Treaty. This entails an explicit extension of the powers of the ECJ to the hard core of national constitutional law. An extension which may probably be possible under the condition that such a power will never be actually used.

From institutional balance as democratic transmission belt to efficient institutional mix

Power has not only shifted across levels of government, but also among institutions. The overall impact of the government of the crises has been the empowerment of the least representative institutions (ECB, ECJ, Commissioner of Economic and Financial Affairs, Eurozone Council), while directly representative institutions (the European and the national parliaments) emerge as net losers, and debtor state parliaments in particular so. The ECB, and to a much lesser extent, the ECJ, have seen their powers grow in a steady manner. The Bank does not only lead macroprudential supervision, it is now also in charge of microprudential supervision. At the same time, it does not only play a fundamental part in the three-headed missions that supervise financial assistance on the ground (the troika), but also exerts massive political authority as a lender of last resort of states and lender of first resort of financial institutions. While the Commission as a collegiate organ may well have lost much of its central position as a driver of the processes of European legislation and decision-making, the Commissioner of Economic and Financial Affairs has gained new powers on what concerns the monitoring and disciplining of national fiscal policy. And the Eurozone Council, acting in impeccable secrecy, is a net winner. We can speak not only of a reinforcement of the trend toward executive dominance, but also of dominance of the Eurozone Council over the European Council tout court. The European Parliament, despite its rhetorical protestations to the contrary, has not gained any substantive power. The European economic dialogue may turn the Parliament into the foremost European debating society, bereft of much power.

The asymmetric character of the crises, the very fact that some states seem to have managed to keep their national sovereignty quite intact (which will now be measured, for all practical purposes, by reference to the rates states have to pay for issuing debt)[1] may require qualifying the previous claims. Germany and German institutions may be regarded as testimony to that. However, even German institutions are being radically reshaped by the crises. It is true that the German Parliament has been formally empowered (largely on demand of the German Constitutional Court) to monitor quite closely the decisions taken by the German government as part of the Eurozone Council, so indirectly the German Parliament may be enjoying a veto power over European policy. But it remains to be clarified whether national parliaments have the means to actually make use of that power, and whether its exercise may not lead to its destruction (exerting the veto may well lead to the collapse of the Union, and German parliamentarians are very conscious of this being the case). The semblance of power may bring authority, but only as long as the power is not really exercised. That is perhaps the key to the construction of the case law of the German Constitutional Court, including the recent OMT ruling (even if in the latter one can discern a growing sense of despair about the mounting constitutional problems stemming from the crises).

[1] A far from stretched metaphor suggested to us by José María Baño.

From equality to inequality of states

While member states are far from equal in material terms, formal equality used to be a fundamental principle of Union law. Not any longer. Firstly, the crises have led to a markedly different constitutional and legal regime for eurozone states on one hand and non-eurozone states on the other. The moment in which monetary union is no longer anchored to the single market, but to a complex web of institutional and procedural public structures (the thickening set of rules and procedures described above regarding the monitoring and disciplining of national financial policy), then being inside or outside makes a major difference. Unsurprisingly, four of the eight pieces of secondary legislation through which European economic governance has been structurally modified are addressed to eurozone states, and eurozone states only. The number of signatories to the Stability Treaty reveals that non-eurozone states are concerned with not being left wholly outside. 26 of the 28 (all bar the United Kingdom and the Czech Republic) have signed the Treaty, and Denmark and Romania have declared that the treaty will be fully applicable to them.

Secondly, and even more decisively, different rules have been developed and codified for creditor/surplus states on the one hand and for debtor/deficit states on the other. Quite clearly, fiscal rules will be different depending on the present deficit and debt differentials, and arguably, the past record of each state. More decisively, the voting rules enshrined in both the Stability Treaty (qualified minority voting) and in the Stability Mechanism Treaty are biased in favour of creditors. Creditor states that make up a qualified minority. And it is only Germany that could de facto exert veto power under the voting rules of the Stability Mechanism Treaty.

So, after all, whose crises?

The subprime crisis was the trigger that made the five weaknesses listed above turn into the set of manifold crises currently facing the Union. Public discourse refers to this as the crisis taking on an altered nature as it unfolds, but that is a misleading rendition, because the crises are simultaneous and indeed tend to reinforce each other. But they are distinct and different crises, not the least because they have hit different entities so differently (just consider the difference between the EU and the USA discussed above). The European Union has failed to take seriously this manifold character of the crisis, or what we prefer to refer to as crises. Many of the 'solutions' have failed because they only set out to tackle one dimension, and in doing so may actually make other crises more acute. But before we deal with that, it is perhaps pertinent to add some words on whose crises they are. All crises, even crises caused by natural phenomena, tend to have highly uneven impacts on society. There are some that are indeed more equal than others when crises hit. Who have been the hardest hit by the crises? And who have, on the contrary, profited from the crises? Public discourse tends to tackle this question along national lines. The PIGS countries are doing very badly, Germany is doing fine (with record levels of employment and an ever growing export sector). There is no doubt that the 'national', 'aggregate' level of analysis is important in some respects. Considering the performance of states is for example fundamental to determine whether the euro will survive. There is some point at which divergence within a monetary area will result in political unrest of such intensity that the union will break up. But while interesting in that regard, can the aggregate national level really be the only relevant perspective to discuss the question? Not in our view. If we take the idea of individual rights seriously, we should focus on which individuals are indeed suffering more. That perspective offers a very different perspective on the crisis. Those who suffer more are not all Mediterraneans, but are also the growing number of precarious workers in Germany and Finland. We must pay attention to the class dimension of the crisis; it does not oppose Northern against Southern European countries, but the wealthy against the less well-off, a divide which these days revolves around wealth invested in capital assets. That is not intended to diminish the importance of the suffering in Mediterranean countries. Far from it. The 'precariat' is more numerous in the South, as the growing rates of suicide and mental diseases reveal with crude clarity. But it simply shows that the public discourse keeps on recreating cleavages on a national, not a class, basis.

Contents of the report

How to research a structural and multi-dimensional set of crises in such a complex entity as the European Union? The workshop from which this report emanates was held in Oslo in March 2013 and was premised on the urgent need of bringing to this theme a broad repertoire of scholars from different disciplinary backgrounds. We accordingly brought together political scientists, economists, sociologists, historians and lawyers, in recognition of the fact that the EU's structural and manifold crises cannot be adequately understood from a single disciplinary standpoint, but requires concerted efforts at transcending academic boundaries and discipline-specific orientations and discourses. Moreover, the report reflects a wide range of views and understandings of the crises, anchored in very different understandings of the history and the present of European Union. To some extent these differences also stem from the different sensitivities that academic disciplines instil in their practitioners. For instance will some academic disciplines be particularly attentive to the contingency of context; others will look more to patterns of norm- and rule-based behaviour; others again will be particularly attentive to regularities or laws associated for instance with the operation of markets. These different sensitivities are important to tap and to combine, in particular in instances of transformation where it is necessary to question established truths and truisms.

If the crises teach us something it is precisely the need to be wary of the taken-for-granteds – what we thought and had established as 'truth' prior to the crises cannot simply be relied on as having full purchase today. Facile embrace of what was is obviated by the rude awakening of the lingering crises. The challenge is to establish with a measure of certainty what remains valid and what has been transformed. In lieu of that, we are pleased to note that indeed, all contributors have deliberately or subtly engaged in self-subversion and self-criticism in writing their chapters, precisely because they are concerned with getting the balance right, through establishing what counts as facts now. The crises have not only revealed the structural shortcomings of the institutional design of EMU, but also the lack of resilience of some of the assumptions that we consciously or unconsciously used to take for granted. Here we as editors would like based on our own experience to underline that there is much to learn from Neil MacCormick whose incisive works stemmed in no small measure from an intellectual integrity and propensity for self-questioning and self-subversion, qualities much needed when dealing with the present challenges.

The report is divided in four parts, dealing with the economic, the historical, the legal, and the political aspects of the crises. The contributors are assigned to these broad categories either because the given category marks the author's centre of disciplinary gravity, or because of the substantive contents of the contribution. The delineation does not reintroduce bounds. It is precisely the merit of these contributions that they reach out so far and so well beyond these categories.

Economics matters!

In chapter 1, Jeremy Leaman offers a compelling account of the deep structural roots of the European crises. A key element in the present European predicament is the destruction of value resulting from overconsumption, underinvestment, and reverse economic redistribution (from the worse off to the better off) resulting from the ideological and political triumph of neoliberal ideas. The subprime crisis of 2007 and the collapse of Lehman Brothers in 2008 revealed the long-term cost of the dominant economic policy paradigm of the last twenty to twenty-five years. The rampant growth of the financial sector, and the (perhaps) even more toxic process of financialisation of the whole economy, including non-financial undertakings, was presented as an alternative to the weak non-financial levels of growth. There was a triple financial illusion: the illusion that finance created wealth (which was a claim of dubious standing before 2008, and proven plainly wrong after 2008); the illusion that financial growth could be an alternative to non-financial growth (as if finance could be 'emancipated' from the non-financial economy); and the illusion that the rates of profit prevailing in the 80s, 90s, and early 00s in the financial sector (over 20 per cent annual return) should become the new standard for the whole economy. Privatisation processes, which essentially consisted in guaranteed monopoly rents (through the privatisation of natural monopolies under some form or another of regulation, or through the so-called public-private-partnerships), created further illusions regarding capital return rates, at the same time that they rendered more acute the problem of under-investment. The increasingly self-confident and de facto when not de jure independent central banks pretended to steer monetary policy in a rule-based, 'technocratic' manner, but actually steered the economy in a discretionary manner which was extremely favourable to the short-term and mid-term interests of capital holders.

Leaman notes that while the crises led to a short revival of interest in public macroeconomic and fiscal steering, this interest was short-lived, and gave way to the reaffirmation of the neoliberal paradigm that was at the very root of the crises. This is nowhere truer than in the case of the eurozone and the European Union. The fiscal crises that have hit several of the peripheral countries of the eurozone have led to diagnoses which either avoid any serious consideration of the structural defects of EMU or of the deleterious effects of neoliberal policies, or noting them, fail to derive any operational policy conclusions. The ultimate root of the crises is found in the 'wrong' fiscal policies that the peripheral states pursued; a diagnosis that goes hand in hand with the imposition of the whole burden of fiscal, financial and social adjustment on the taxpayers and workers in the eurozone periphery. In particular, Leaman shows the many contradictions that European policy recipes fall into. Expecting the whole of the eurozone to become in surplus vis-à-vis the rest of the world is a hope that does not stand up to serious examination, given the fact that a stronger demand for European products could only result in further asymmetries between the eurozone core (producer of the more demanded European goods) and the periphery, and that such growth will not solve the real European problem, namely, asymmetries *within* the eurozone.

Neoliberal policies, amplified by an EMU that has structurally increased divergences among member states, have resulted in a destruction of value that can only be compared to that resulting from a major war. We need policies that are grounded in a proper understanding of the size and dimension of the problems that we face. There is a need for a radical change in the social function played by the financial sector, a reorientation of the way it works so that it stops subtracting social value and re-emerges as a sober but fundamental inter-mediator between saving and investment. We need to tackle the inequality created by market distribution, and to reimagine redistribution in a low or zero growth scenario. We need a strong programme of re-nationalisation of natural monopolies, strong public investment, and reconstitution of the tax capacities of the state. Regarding the latter, the recovery of the capacity of public steering much depends on the creation of a European framework that *rescues* the national tax state through harmonized tax norms.

In chapter 2 and the subsequent commentary, Fritz Scharpf deals very incisively with the key question of the relationship between the depth and breadth of the European crises and the fundamental institutional and substantive choices underlying both the original EMU and the governing of the crises.

Scharpf's central thesis is that the present European crises have revealed the massive legitimacy implications of EMU. The 'mixed' European constitution, in which national governments seemed to play a key role in modulating European law, used to shield the European Union against a legitimacy crisis, notwithstanding the growing depth and breadth of integration, and the fact that the legitimacy of the Union was either derived from national polities or was output-oriented. The crises unleashed in 2007 have not only blown up that mediating shield, but have disabled national democratic legitimacy for good (the onus on saving the euro forces the hands of all governments, so that parliaments and courts simply cannot say 'no'). Now the very design of EMU was based on depriving member states of macroeconomic controls over their national economic fates and trusting stability to a non-democratic supranational regime (at the core of which was the independent ECB, apparently, but not substantially, modelled on the Bundesbank) whose claim to output legitimacy was backed by monetarist theory. The crises have revealed the extent to which there was not so much a monetarist theory as a monetarist fallacy. Saving the euro has required doing something else, and that something else has been a mixture of financial assistance – targeted not to the economies of the peripheral states, but to prevent both peripheral states and banks in the periphery from becoming insolvent – and conditionality, which has resulted in a fully discretionary micro-management of the economies of states in the periphery. These actions may have passed through as part of the *alternativlos* crisis-led Council decision-making process, but what is their legitimacy basis? It cannot be one based on input, and there are already very good reasons to conclude that their output legitimacy is highly dubious. Scharpf's chapter finds that either the costs of non-disintegration are factored in, or there is a need for an alternative to the failed monetarist output option, with a degree of monetary financing through the ECB being a potential bridge (and time-buying device) to get to that solution.

As Scharpf clarifies in the postscript to the chapter, the present crises of the European Union are very much the late inheritance of monetarist and supply side economics, core tenets of the 'neoliberal' socio-economic theory. The move from common to single market, the trust in mutual recognition providing an alternative to harmonization, was closely related to the rise and spread of neoliberalism. But can the same be said of EMU? The story is more complex, and is worth disentangling. While the EMU project was not *neoliberal* per se (and indeed the creation of the Euro did *destroy* some markets, including the market on foreign exchange) and while *monetarist economists* such as Friedman warned about the risks of moving to EMU because the eurozone was not an optimal currency area (OCA), the fact that these (and other) warnings were ignored was itself very much the outcome of the dominance of neoliberal theory which by the 1990s had contributed to a shift in the monetarist mainstream to reject OCA theory. The very belief that macro-economic policy was irrelevant, the belief that market pressure could be enough to stabilise economies, was at the root of the belief that asymmetric monetary union will lead to convergence, not divergence, among member states.

Scharpf further argues that the way in which the crises have been governed does not reflect so much the persistent influence of neoliberalism, as the fact that by now neoliberal policies have been structurally embedded. When Greece's fiscal crisis exploded, the constellation of political interests in Europe (in both creditor and debtor states) plus the existing constitutional framework, led to policies being locked in. The net result is that the present constitutional and legal framework institutionalises a permanent race to the bottom, as the only way in which member states can expect to overcome an asymmetric crisis is through *beggar thy neighbour* policies. The cost of non-disintegration is bound to be a deep (and persistent) increase in social inequality.

History matters!

Crises are always steeped in context. Even if at the time of unfolding that context is difficult to grasp, careful reconstruction shows how (and the extent to which) the factors active in the launch and unfolding of the crisis were rooted in history and context. Such attentiveness to context and history is a quality that is particularly nourished by historians, anthropologists, and sociologists.

In chapter 3, Dennis Smith reflects on the political, economic and constitutional identity of Europe and usefully searches for the most proper *collective metaphor* to represent Europe, the one that best captures the complex and multifaceted history of European integration. Smith finds that the sportive metaphor of the cycling *peloton* is one of the most promising ones. The very forming of the *peloton*, the founding and nurturing of the European Communities, was essential in the effort at transcending Europe's postwar condition, a collection of humiliated states, and forging it into a community of cyclists capable of handling the untangling of managed displacement. The Communities were largely successful at this task, but were also lured by the temptation of success. The single market project and EMU created the conditions under which the cheap flow of capital allowed relevant and fundamental decisions to be postponed. But the life of the cyclist is a dangerous one, and is bound to be disturbed by mud and hail. And the crises of 2008 have created the conditions under which the European *peloton* has been confronted with mud and hail galore. It is in the crisis situation that the clashes between different understandings of what politics is about, and what the European Union is, come to the fore, represented by different political actors (which Smith represents with the help of – again – very vivid metaphors: the high priests, the political cavaliers, the puritans and the buccaneers). It is in the midst of this mud and hail that the Union presents us with different possible futures: to become a corporate milk cow, to turn into an arena of resentment and revenge, or more hopefully, a post-humiliation society. Smith strikes a note of caution, as the way in which the crises have unfolded and have been governed have already re-awakened the spectre of humiliation politics, as his field work in post-crisis Greece testifies to.

In chapter 4, Mark Gilbert makes a plea for modesty rooted in a deeply humanistic understanding of what history is (inspired by Lamier's understanding of the *beruf* of the historian as a 'painter', as somebody capable of discerning what facts are relevant and to reconstruct history around them). Gilbert dissects the narrative which is not only implicit but also explicit in European policy making and policy discourses and finds a propensity for presenting European integration as the unfolding of progressive forces (the 'founding fathers', the pro-integrationists) that are put to the test by regressive forces, equated with all those who oppose integration. This makes for a rather straightforward 'Whig' history, in the term coined and made famous by Butterfield. But does Whig history render good history in the sense of being factually correct? Could it not be that the propensity to tell and retell a 'Whig' narrative of European integration is at the core of our present troubles? That Whig history makes bad history is shown by Gilbert in the total lack of attentiveness to facts and nuances in the way in which one 'saint' (Spinelli) and one 'sinner' (Thatcher) are portrayed. What Gilbert, following the core intuition of Butterfield, proposes, is to escape from Whig history and take seriously the extent to which both 'saints' and 'sinners' were engaged in a clash of political wills; it is out of this clash, and not out of an alleged teleology of European integration, that the actual European Union stems. So we do not only need to make a history of European integration that makes sense of the Europeaness of both the saints and the sinners, of the Whigs and the Tories, but one which sees the shadows of Toryism in 'Whig' positions, which, in brief, escapes the easy simplification implicit in rationalist teleologies, and as Namier's painter, embraces human complexity à la Oakeshott. Otherwise, as Gilbert tells us, we run the risk of not only writing bad history, but of failing to come to terms with Europe's present predicament. Might it not be that a large portion of our problems are deeply associated with a Whig understanding of European history? Was not the asymmetric monetary union a policy that could only have been launched by Whigs? And are not the present remedies based on new rationalist blueprints in which little space is left for nuances and contingencies the ultimate proof that not much has been learnt from the present crises? Then it is persistent embrace of the Whig ways of old, and not the success of the 'sinners', as such, that is the real existential threat to European integration.

In chapter 5, Giandomenico Majone undertakes an incisive reconstruction of European integration that provides the reader with a diagnosis of the 'endogenous' causes of the crises, or what is the same, with the features and characteristics of the European Union and the process of European integration that have played a major role in the gathering of the crises. Despite the fact that Majone and Gilbert come from different national and disciplinary backgrounds (although Gilbert has been in Italy for quite a few years), there is a striking methodological affinity between following Namier's approach to history and opting for a genetic reconstruction of the crises. Majone's main thesis is that the crises are closely related to two key developments: First, excessive integration, or what is the same, a level of centralisation of powers in European institutions which was ill-suited on both efficiency and legitimacy grounds. Second, the underlying and growing divergence between member states, resulting from the Communities' growing size and from member state transformations. Majone does not only claim that over-integration and growing divergence are the two main causes of the crises, but that these two causes are largely the result of the structural features of the process of European integration, features that have been aggravated in the last decades. In his chapter, Majone considers five of the key features of European integration:

- *primacy of process over substance*, which leads to a culture of ungrounded optimism, in which any agreement among the members of the Council is equated with an historical success, no matter how thin and ambivalent the agreement);
- *decision-making through chains of faits accomplis,* a style of decision-making justified by the so-called bicycle theory of integration, which requires ensuring the success of integration with a constant supply of new integration steps;
- *the totemisation of the acquis communitaire*, or the sacralisation of past decisions as codified in European law, which are presented as a civilizational achievement, to be imposed on new states even if that implies side-lining democracy and even undermining existing legal standards, and to be honoured even if constantly breached, as was the case when EMU was launched, and all states resorted to more or less ingenious forms of creativity in their national accounts;
- *the total side-lining of feasibility considerations*, which leads to a culture of total optimism based on a voluntarism with very weak factual underpinnings, as proved in the original Werner Plan design of monetary union, in the actual design of EMU, and which accounts for the hubris with which the 2008 crisis was handled until the end of 2009;
- *the intangibility of the Community method*, despite its cumulating inefficiencies (as exemplified by the baroque and cumbersome co-decision procedure), and the tension between the calls to abolish national vetoes and the persistence of the Commission's right of veto through the exclusive right to initiate legislation.
- *The 'real' constitutional moment* – the decision to go ahead with monetary union in 1999 marked the clear decisive stage in the process of over-integration. Monetary union has made it impossible to hide in plain sight the impact and consequences of integration. The very structure of asymmetric monetary integration, coupled with the fact that eurozone states were far from being an optimal monetary area, made monetary union into a mechanism for increasing divergence. Monetary union thus becomes the policy that renders explicit the political implications

> of European integration; a fact that the governing of the crises has only rendered more explicit. It is at this point that Europe's democratic legitimacy becomes not only very visible, but very close to a democratic default.

Greece has been at the epicentre of the crises. As Asimina Michailidou reiterates in chapter 6, the Greek economy was the weakest link in the eurozone chain. What really calls for an explanation is not so much that Greece was badly hit (the Greek political, economic, and social crises were a disaster waiting to happen), but that European partners did not see the disaster coming (or if they saw it, the measures they took only aggravated it) and that the governing of the crises has unfolded in the way it has. On the one hand is the delinking of Greek political parties and constitutional authorities from citizens and democratic procedures coupled with the fact that measures adopted or half-adopted have accelerated the economic and political collapse. On the other hand political leaders have been struggling to be seen as taking the hard measures requested by Europe with the hope of that pattern of behaviour being seen as leading to the turnaround of the country. Michailidou reminds us of the peculiar political constellation that is generated by structural crises. Deep crises radically increase the political autonomy of leaders, and create space for rule bending. This is increased if a narrative is built which connects the present predicament with long unresolved contentious issues, which are now presented as the true causes of the crises. Both Papandreou's PASOK government, the technocratic interim government of Papademos, and the Samaras coalition have tried to increase their political capital by presenting the crises as the golden opportunity to right the many wrongs of the past, while engaging in very wide rule bending. In all cases, however, not only have the policies applied been of dubious efficacy, but it has proven impossible to implement them in a minimally consistent fashion. The state capabilities were not only weak and limited to start with, but the very policies that were implemented tended to undermine them. The net result has been that reforms aimed at solving Greece's structural problems have actually rendered them worse. And in the process they have pushed Greece close to democratic default. The party system has collapsed, and it can be doubted whether any coalition of classical political parties can be said to be a bearer of democratic legitimacy. The loss of votes has been so drastic that classical parties need to make enormously wide coalitions, which either indicates their ideological interchangeability despite labels, or bodes badly for the coherence of governmental action. At the same time, the parties of these *grosskoalitionen* have gotten stuck in a pathological gap between electoral pledges and the policies they actually supported when elected.

Law matters!

Public discussion has tended to portray the European steering of the crises as a mix of improvisation, reluctance to act (or acting at the very last minute), and muddling through galore. In chapter 7, Christian Joerges argues in a sophisticated and nuanced manner that analysing the crises through legal lenses may lead to more precise albeit sombre conclusions. Joerges' chapter draws on his constitutional theory of 'conflicts constitutionalism', which aims at finding a normatively grounded basis for a process of integration that takes the social functions of law as a means of social integration in the Social and Democratic Rechtsstaat. Joerges finds that the crises have revealed not only the gap that now exists between on the one hand the promising normative theories of European constitutionalism and on the other the Union's material constitution, but have also led to decisions and companion legal-theoretical justifications that run the risk of undermining law and reducing legal scholars to providers of justifications to policy makers. Joerges' diagnosis is largely similar to that put forward by Majone or Scharpf, but with a constitutional twist. The delicate and fragile balance between integration and diversity established in the founding treaties was seriously challenged by the decision to launch an experiment in asymmetric monetary union. The intervention of the German Constitutional Court with its *Maastricht* ruling pushed the experiment in a very problematic direction, something that was hidden in plain sight by the numerous commentaries on the ruling which focused on everything but the underlying understanding of the relationship between law and the socio-economic model. The transformation of 'stability' into a totemic concept has been completed in the rulings of the German Court after the crises, and very especially in the ESM ruling, which has come close to make the peculiar understanding of stability, a hybrid of ordoliberal and neoliberal understandings, in an alleged part of the 'intangible' hard core of the German constitution. The shortcomings of the German Constitutional Court are not balanced by the case law of the European Court of Justice, a Court that, Joerges argues, has produced in Pringle a ruling that fails in substantive, logical, and methodological terms. A failure that was largely unnecessary, because the court could well have saved the day making a judicious use of self-constraint. But the bigger failure of European law in the crises remains its sheer inflexibility, which makes of law an increasingly inept medium to articulate a democratically viable solution to the crises. That does not, however, lead Joerges to despair. He ends the chapter by vindicating the possibility of legally articulating sensible policies, provided that the normative spirit of unity in diversity, as articulated in his theory of constitutional conflicts, among other theories, is taken sufficiently seriously.

Even if not welcomed by the mainstream, maverick economists have engaged in earnest with a self-critical reflection on the role that economics as an academic discipline (and as a 'power technology' perhaps should be added) played in the gathering of the crises. But what could be said about European law, and very specifically, about the very concrete way in which European law has been written and debated in the transnational mainstream? This is the question which Michelle Everson addresses in chapter 8.

For one, she finds that Community law has been deeply affected by the search for a legitimacy basis in a very specific kind of *market* discourse. While the anchoring of the legitimacy of law to economics may well have been originally an American phenomenon, perhaps its biggest intellectual victory was gained in the transnational legal field of Community law. Propelled by the DG Internal Market and embraced enthusiastically by the judges in Luxembourg, EU primary law was 'reinterpreted' as an 'indispensable weapon' with which to 'dismantle the barriers to trade that distinctive national regulatory regimes constituted'. This did not only do away with paternalistic remnants of the postwar political and social world, but also, and fundamentally, with collective values of non-economic nature established at the national level. The European economic citizen has been turned into the *homo economicus* by a court that has increasingly leaned on a pseudo-scientific understanding of the normative underpinnings of its rulings. Everson finds that while there is much that can be found problematic from the standpoint of a normative position committed to the Social and Democratic Rechtsstaat, perhaps the most damning criticism comes ironically from the most Hayekian and robust wing of ordoliberalism. By clinging to a peculiar form of law and economics framework, European law commits the fundamental sin of anchoring its legitimacy to the factual world, when, as Maestmacker reminds us, the legitimacy of law can only be normative, not factual: from the 'autonomous mission of securing justice'.

Further, law has indeed become one of the techniques through which the illusion has been created and sustained that uncertainty could be done away with through structures, formulae and models that one way or the other pretend to complete the market when they simply mimic it in a grotesque fashion, through law, with the blessing of the law or with a mix of the two. The crises have indeed been the occasion for the strange non-death of alleged uncertainty emasculation through its conversion to risk. As Everson points out, the architecture of financial regulation decided in the wake of the crisis is built around the VAR risk, which played such a fundamental role in the gathering of the financial crisis; while the assignment of massive microprudential supervisory powers to the ECB is based on the (im)pious hope of keeping a wall of separation between monetary and prudential policy, a wall that is likely never to be properly built: the ground on which it is to be built is simply made of sand.

The chapter ends with a call to take seriously comparative constitutional history, to discern in the European constitutional past, and very especially in Weimar, the elements which make of law a means of social integration capable of adaptation to social and economic reality through politics, through legislative politics, something that could only be the case if law and lawyers become modest again, very conscious of the limits and fragility of the wool with which the legal net is to be woven.

In chapter 9, Michelle Everson and Christian Joerges really mobilise the stored potential of historically sensitive comparative constitutional law. The guardianship of custodianship of constitutions was not only a key issue in the interwar European constitutional debate, but one which played a fundamental (and tragic) role in the last days of the Weimar Republic. While the specific actors and questions may well be part of the German and European past, neither the questions nor the arguments which came to a sharp conflict eighty years ago have lost constitutional traction.

Everson and Joerges start from the premise that constitutional guardianship in the complex and pluralistic setting of European law remains a collective task, which both the ECJ and national constitutional courts discharge. For a while European legal scholarship entertained high hopes that supranational and national guardians of constitutionality could 'dialogue'; or what probably was meant, could discharge their tasks in a spontaneously, non-hierarchically structured, and harmonious, way. The dramatic growth of European law, in both depth and breadth terms, and the way in which the ECJ has shaped European law, undermined the factual and normative soundness of that expectation. The governing of the European crises through a variety of formal legal acts and non-law acts that not only undermine the integrity of law, but have led to a massive transformation of the material constitutional law of the European Union, especially on what concerns economic and monetary union, has made unavoidable a reconsideration in full of the constitutional guardianship question. This is what Everson and Joerges do by considering the two fundamental rulings on the government of the crises, the ERM judgment of the German Constitutional Court and the Pringle ruling of the European Court of Justice. The ERM ruling is found to be highly problematic on account of its autistic and unrealistic sacralisation of stability. Under the appearance of a brave vindication of the powers and prerogatives of the German Parliament, the Court has solved the contradiction between its ordoliberal-leaning reconstruction of the EMU since Maastricht with the radical transformation of the constitutional framework of EMU by turning stability into part of the metaconstitutional set of norms which are said to be part of the intangible constitution referred to by Article 79.3 of the Fundamental Law. This leads not only to a construction of German and European constitutional law that may be hard to generalise, that is oblivious to the fate of the constitutional law of other member states, and which, notwithstanding that, undermines the bite of constitutional law as limit to the use of power. The ECJ has managed to do even worse with its Pringle judgment, where one finds a lucid reconstruction of the conceptual and normative background of the original EMU provisions combined with a totally dis-ingenious expectation that conditionality could ensure the bridge between the old and the emerging (and radically different) EMU constitution. But conditionality fails to do the trick; it is in itself a toxic concept from a democratic perspective.

Agustín José Menéndez sustains four main theses in chapter 10. Firstly, he argues that a proper understanding of the crisis that is hitting the European Union requires taking proper historical perspective (and thus tracing the structural weaknesses that led to the explosion of the crises), disaggregating the *crisis* into *crises* (the several simultaneous, interrelated, and intertwined crises—crises which are global, not exclusively European), and identifying the triggering factor (the subprime crisis). The subprime crisis turned the economic, financial, fiscal, macroeconomic, and political structural weaknesses of the Western socio-economic order into at least five major crises. Secondly, the European Union bears responsibility for the crises. The European Union is not only experiencing these crises, but bears a heavy responsibility for the crises in the first place. The transformation of the institutional structure of the Union and the substantive policy choices made in the last three decades have fostered the very structural weaknesses that were turned into crises by the subprime crisis. In particular, the understanding of economic freedoms as self-standing and dis-embedded, as expressions of the right to individualistic private autonomy and the creation of an asymmetric economic and monetary union, played a major role in destabilising the Union. Thirdly, the measures taken at the supranational level to address and overcome the crises have been inconsistent, based as they have been on a shifting diagnosis of the cause of the crises and have led to contradictory policy options. A whole set of supranational policy decisions and structural reforms have been put forward in the last five years with the aim of governing the crises. There are good reasons to doubt that they have really contributed to overcoming the crises. Fourthly, the European governing of the crises has unleashed a process of European constitutional mutation. What have been presented as exceptional and temporal measures have indeed resulted in a major constitutional mutation that has aggravated the already looming tension between this European Union and the European constitutional and political project, as enshrined in the Social and Democratic *Rechtsstaat* at the core of postwar national constitutions, and largely underpinning the original European Communities. These four theses lead one to conclude that neither a reformist strategy (a change in the course of policy within the present Treaty and the emerging *para-Treaty* framework) nor a constitutional rupture strategy (via a constituting assembly with a democratic mandate) seem like viable strategies to undertake a democratic rescue of the European Union. If any path holds promise, it is that of national constitutional resistance, based on challenging the policies and decisions of the recent years – especially the last five years – on the basis of the deep constitution of the European Union, and the common constitutional law of the Social and Democratic *Rechtsstaat*. This might allow a reopening of political space and a return to a democratic understanding of constitutional law. The future, however, looks bleak.

In chapter 11, Klaus Tuori reconstructs and assesses the consistency and coherence of the transformation of the constitutional framework, institutional role, and policy tools of the ECB. Tuori offers the reader a reconstruction of the 'economic constitutional law' of the European Union from the ordoliberal conceptual and normative perspective, a perspective that was already influential in the design of the Rome Treaties, and proved decisive after Maastricht. In particular, Tuori highlights the constitutional impact and influence of four key constitutional principles that in a consistent way framed the EMU (the metaconstitutional value assigned to price stability, the prohibition of public financing – monetisation of debt, central bank acting as lender of last resort –, the independence of the EBC and of national central banks, and the mandate to render compatible the execution of monetary policy with the allocation of capital through financial markets). These four principles account for the institutional structure and position of the Bank, but also for its legitimacy basis, which in turn determines the tasks which the ECB is to discharge: '[i]ts role should be limited to pre-defined tasks that can be controlled also by judicial means. A corollary of the limited role and lack of democratic control is that it excludes any redistributive elements in the ECB policy as it is not given power to make value-based decisions'[2], and also the defined strategy and operational targets of the ECB.

On such a basis, what kind of institution is the ECB and should it be? Here Tuori distinguishes between two main paradigms: that of political actor and that of independent expert, which is complemented with a third, that of stakeholder. This allows the author to show that while the ECB should fit into the paradigm of the independent expert, and as such should be autonomous position vis-à-vis political actors, but also vis-à-vis stakeholders (which include social partners and financial markets). A great danger (perhaps *the greatest* danger) to the independence of the ECB is for it to become a

[2] Tuori: p. 495, this volume

stakeholder, as that condition would clearly be incompatible with its independence: 'The stakeholder role can complicate the accountability and legitimacy considerations […] as increases vagueness of actual roles', especially if 'the independent expert is not excessively open and transparent in its stakeholder role'[3].

Tuori then considers whether the ECB has remained within the boundaries of its constitutional design as an independent expert. The new roles that the ECB has assumed through the development of constitutional conventions that turn it into a lender of last (occasionally first) resort to European financial institutions and of (indirect) lender of last resort to eurozone states do indeed pose major challenges to the integrity of the independent expert role. Massive refinancing operations at fixed rates, for unlimited amounts, and backed by increasingly poorer quality collateral entail that the ECB can no longer be seen as unconcerned with the fact that its monetary policy may not erode its capital basis through losses incurred by banks. Similarly, the acquisition of sovereign debt in secondary markets creates a link between the ECB and the member state which issued that debt and is hard to reconcile with the paradigm of the independent expert. The ECB becomes exposed through a potential negative effect on its capital basis, and gets an incentive to try to shape national fiscal policy in ways not foreseen in the Treaties (as the letters addressed to the Italian and Spanish Prime Ministers by the President of the ECB in the summer of 2011 reveal).
This leads Tuori to the conclusion that the original constitutional framework was pledged to 'money and monetary policy' being seen in a monetarist or German ordoliberal perspective, or what is the same that the euro area monetary environment was closer to 'an enhanced gold standard than a field of activist monetary policy'[4]. The mutated constitutional identity and tasks of the ECB create a serious danger that the ECB pretends to keep on being an expert institution, but has actually become a stakeholder or a politician. Ordoliberalism should not welcome that development. If that were to be consolidated, it would be necessary to take stock of the changes, and transform the legitimacy basis of the ECB. If the ECB is a political actor, it needs to be politically legitimated. Tuori finds a massive tension building

[3] *Ibid.*: p. 506, this volume
[4] Tuori: p.514, this volume

up in the new role of the ECB as microprudential supervisor of financial institutions. That role is not only hard to reconcile with the paradigm of independent expert, but could be catastrophic when assigned to an institution that is given the independence that is proper and characteristic of independent experts.

In chapter 12, Pedro Teixeira provides the reader with a constitutional primer on the ongoing Europeanisation of banking supervision. His chapter not only sets the creation of the Single Supervisory Mechanism in the historical context of European integration, but also offers a descriptive and reconstructive account of the transfer of banking prudential competences to European institutions, and in particular, to the 'supervisory' branch of the ECB. In the first part of the chapter, Teixeira tells us the story of the slow but steady Europeanisation of banking services in the context of the different stages of European economic and political integration. The chapter is not only informative, but theoretically sophisticated, and shows how the 'waves' of integration through harmonizing law (sixties/ seventies) and integration through competition among legal systems (eighties onwards) led to different approaches to financial services in the single/common market. In the second part of the chapter, Teixeira offers a succinct description of the complex architecture of the new model of banking supervision in the European Union. The so-called Single Supervisory Mechanism raises a myriad of fundamental constitutional questions, ranging from the legal basis of the Regulation, to the complex interaction between the 'supervising' ECB, which is a eurozone institution and the single market of financial services. The new arrangements not only give rise to major constitutional questions, but can also be regarded as a case study on the European Union's pattern of evolution. Teixeira finds that this new and fundamental piece of legislation confirms some of the emerging trends in the post-crisis European Union (the move from soft governance to hard enforcement, the growing differentiation between eurozone and non-eurozone member states, usually complicated by the emergence of a third category of relatively 'in' member states, as is the case with the 'close cooperation mechanisms' through which non-eurozone states can be made part of the Single Supervisory Mechanism), but also breaks with some of these trends, in particular, the new framework of supervision points towards a centralisation of power away from the underlying intergovernmentalising trend.

In chapter 13, Hauke Brunkhorst contributes what may be called a *long durée* analysis of the paradoxical development of European constitutional law. Brunkhorst makes vivid the deep ambivalence of the process of European integration, which has been lost in the last decades as a result of a flattened constitutional narrative, a narrative that reflects the deepest roots of the European crises, the triumph of the managerial mindset, which aims at fully subordinating politics to the 'technical' imperatives of a 'sound' economy. Europe is not, Brunkhorst emphatically stresses, the legacy of the technocratic mindset that was so influential upon the Rome Treaties, but of the Kantian constitutional mindset given political substance in the mass political movements that in the aftermath of the Second World War radically transformed the constitution of European states. Reconstituted European states did not only become *Social and Democratic Rechtsstaats*, but also open and cooperative states. The democratised and re-democratised national *We the Peoples* provide a bridge towards a post-national democratic Europe. That bridge, however, was made of crooked timber. Not only the Political Community and its European constitution were democratically voted down in 1954, but the Treaties of Rome were much influenced by the managerial mindset. The German (and not only German: think about Jacques Rueff in France and Luigi Einaudi in Italy) ordoliberals managed to codify into the Rome Treaties an understanding of the socio-economic constitution which was very different, if not opposite, from that enshrined in national constitutions. Indeed, ordoliberals managed to get in Europe (thanks to their growing political influence at home) what they had failed to achieve at home). This led to a complex constitutional dynamics. European constitutional law made up of the *open and cooperative 'Kantian'* constitutions and Treaties much moulded by the *managerial constitution set*, interacted. Brunkhorst points out that the hegemony of the managerial mindset at the supranational level had the paradoxical result that the Kantian mindset was at the same time preserved and repressed, constitutionalised and de-constitutionalised. This led to a *constitutionalisation under private law.* Constitutionalisation *advanced*, but was at the same time *de-constitutionalised by its own advances.* The ordoliberal imprint was, however, to have a renewed opportunity to challenge the Kantian mould of European constitutionalism once the economic crises of the 1970s pushed off balance the paradoxical Kantian cum managerial European mix. The shape of economic and monetary union was one (even if fundamental) of the terrains in which the conflict was played out. There were victories for Kantian constitutionalism, as reflected in the growing powers of the European Parliament. But managerial constitutionalism left its imprint in the division of competences between the Union and the member states, and between different European collective will formation processes. The growing *constitutional asymmetries*, Brunkhorst reminds us, led to neoliberal victories in a terrain rendered propitious by the previous ordoliberal influence. But democratic constitutionalism, once out of the bottle, can be repressed or left aside, but not suppressed. And as the unsustainable character of the asymmetric constitutional choices has come to the fore (the stability of the self-steering economy dependent on exchequers depleted by the collapse of the tax state, its transformation into a debt state), the long latent crisis of legitimation has struck back. The fight for the social welfare constitution is thus back with a vengeance, and opens up the possibility of the reinvention of democratic class struggle at the supranational level.

Politics matters!

In chapter 14, Christopher Lord considers the general principles around which the democratic accountability of monetary policy should be built. Lord starts by distinguishing the independence of monetary policy (which in the case of the EU is institutionally inbuilt in the ECB as a radically independent agency, steering monetary policy fully solo, and with great latitude to determine what its constitutional mandate – price stability – entails) from the lack of democratic accountability of monetary policy. Indeed Lord argues that it could be possible and would be desirable to combine the independence of the central bank with its being democratically accountable to a set of institutional actors. Being subject to a plurality of actors would ensure that the ECB is accountable while not been subject to any specific and concrete institution. Then Lord claims that reinforced parliamentary accountability, being highly advisable and normatively desirable before the crises, has become even more so given the ECB's acquisition of a whole range of new powers, either through explicit and legally expressed mandate (macroprudential supervision of the financial system, microprudential supervision of financial institutions) or through evolving constitutional conventions (the massive refinancing operations addressed to financial institutions and the acquisition of sovereign debt through the securities markets programme and the outright monetary transactions). But what would that reinforced parliamentary control look like? Lord argues in favour of a joint and overlapping (i.e. not necessarily coordinated) empowerment of the European Parliament and national parliaments. National parliaments, which in the foreseeable future remain the institutions in charge of key taxing and spending powers, must play a key role in ensuring democratic accountability. But there are numerous reasons why they need to share that role with the European Parliament: among others, to ensure the completeness of democratic accountability (only the EP can properly control the European Council and the Commission), the mobilisation of expertise and the capacity to articulate the general European interest (while indeed national parliaments may engage in different forms of self-centered behaviour).

Chapter 15, by John Erik Fossum, focuses on how the crises affect the system of representative democracy in the European Union. In order to do so, the chapter first considers the situation prior to the crises in order to pay sufficient heed to the fact that the structure of representation that has emerged in the EU is quite unprecedented. Part of that can be understood from the fact that EU democratisation has occurred along two dimensions: a vertical dimension pertaining to the efforts at establishing representative arrangements at the EU-level, most closely associated with the development of the European Parliament; and a more horizontal dimension relating to the efforts at stabilise democracy across Europe (including through a system of democratic entrance requirements). The latter horizontal dimension includes the emerging system of interparliamentary coordination and testifies to the manner in which the vertical and horizontal dimensions are becoming imbricated. Increased national parliamentary involvement can have democratic merits but can also foster co-optation and requires rethinking the nature of authorisation and accountability in complex polities. These patterns must be considered in light of one central fact of the EU that sets it apart: In the EU it is *not* a matter of democratising an already established and existing system, but of establishing and democratising a supranational system at the same time. That is profoundly important because it places democratic institutions in a constant squeeze: contribute to foster integration even if it is not presently sufficiently democratic in the anticipation that it can be democratically reined in in the future, or risk inter-institutional democratic confrontations that will complicate future inter-institutional relations and put at risk the potential for the EP to gain added powers.

These were some of the challenges before the crises struck. Now well into the crises we need to seriously question the tenability of the long-held assumption of a positive (even mutually reinforcing) relationship between integration and democratisation. The crisis has generally speaking weakened the role and political influence of parliamentary assemblies, notably but far from exclusively, in the eurozone. The ability of parliaments to serve the interests of their citizens has clearly been weakened, as has their citizens' ability to hold those who are really responsible for the policies that afflict them have also clearly weakened. The pattern is however far from even across member states in the eurozone; it is clearly more so in debtor than in creditor countries where particular patterns of horizontal domination have emerged: with creditor states' parliaments influencing the decision-making processes and the priorities of debtor states' parliaments. The crises also further strengthen the role and salience of executives and experts, clearly at the behest of legislatures. As such, the crisis appears to reinforce certain built-in path dependencies in the EU structure, in particular executive dominance but now in a manner less constrained by legal regulations. That again relates to the fact that much of the crisis handling has reinforced a rather secretive intergovernmental bargaining approach that in turn weakens the integrity of the supranational structure by making it more transgovernmentalised.

Another aspect of the crises appears to be to render states not only unequal in substantive terms but to make the EU a system of states with different *statuses* within the European order. The crisis ushers in a situation of simultaneous differentiated integration (especially in the eurozone) and differentiated disintegration (especially pertaining to the UK's desire to renegotiate its status).

In this context, if parliaments are to re-assert themselves, barring major changes, inter-parliamentary coordination appears necessary to fill the gaps. The paradox is that whereas the crisis has rendered interparliamentary coordination more needed, it is also to a large extent undermining the prospects for effective coordination. Democracy hangs in the balance today.

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Part I

Does EMU really add up?

Economics matters

Chapter 1

Reversing the neoliberal deformation of Europe

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In 2007 Jörg Huffschmid, the German political economist and inspirational campaigner, marked the 50th anniversary of the Rome Treaties with a trenchant critique of the 'neoliberal deformation of Europe' in which he outlines the degree to which the integrationist ambitions of the original authors of the European project had been diluted, distorted or simply abandoned by the leadership of both the Commission and its core member states since the early 1980s (Huffschmid 2007). In particular, Huffschmid underscored the 'increasing intra-community asymmetries' which politically and economically 'contain an explosive potential […] which is massively endangering the unity of the EU in the medium term' (Huffschmid 2007: 314). Huffschmid survived to see the prescience of his remarks begin to take grim shape after the outbreak of the global crisis in 2008 before his untimely death in December 2009. His critique of the particular pathology of Europe's neoliberal illusions was matched by a refined understanding of the general pathology of financialised capitalism (Huffschmid 2002) and a deeply held apprehension of the imminent collapse of the house of cards. While the multiple crisis provided fairly unequivocal empirical proof of the long-term unviability of the neoliberal project and of the fundamental design weaknesses of the EU's policy architecture, the ideological illusions persist – for some inexplicably (Crouch 2011; Lehndorff 2012) – in 'zombie' form (Quiggin 2010)[1].

What follows below is an attempt to account for the 'persistence of failed ideas' in both the institutional arrangements of the European Union and the mindset of its defenders, to outline the severe damage they are doing to the peoples of Europe and their long-term prospects and to propose some alternatives to their deeply flawed policies. Let me start with two metaphors, described by Martin Jänicke in 1986 of the tank-driver and the cyclist in relation to two modes of policy-making:

> A tank driver can be stupid and blind. In contrast to the cyclist, he does not need to adapt to the annoying obstacles of the environment. Problems are 'externalised': It is not the tank driver that is damaged but the environment. In the case of the cyclist, on the other hand, the problems of an adaptive method of driving are completely internalised.
>
> (Jänicke 1986: 158)

The metaphors of cyclist (reflective adaptation) and tank-driver (blind refusal to reflect, learn and adapt) are arguably fully applicable to an analysis of the current dilemmas facing Europe. There are certainly few signs of adaptable cyclists in positions of power. The metaphors thus allow us to consider the reasons for Europe's fatal addiction to failed recipes, in particular to the straitjacket of a currency union, whose policy architecture is stubbornly resistant to reflection or change. Four-and-a-half years into Europe's worst social and economic crisis in many decades, the clinging of policy-elites to an intellectual corpse indicates above all a comprehensive misdiagnosis of the causes of that crisis. While the role of the financial services sector in triggering the crisis has clearly been acknowledged by EU-leaders, while regulatory reforms of banking have been initiated in most core member states, while even a Financial Transaction Tax within Europe is being proposed, these and related policy initiatives are dwarfed by the centrality of sovereign debt consolidation in Europe's 'reform' agenda. The priority of fiscal consolidation, before any other macro-economic preferences, implies the primacy of 'fiscal

[1] See also P. Krugman 'When Zombies Win', *New York Times*, 19 December 2010.

irresponsibility' in the causal chain resulting in the global crisis. This primacy is clearly evident in the contradictory persistence during 2008 and 2009 of the Commission's 'excessive deficit' obsession in relation to new member states (Leaman 2012a: 175ff), particularly when most Central and Eastern Europe countries (CEECs) had lower public sector borrowing requirements (PSBR) and debt ratios than their counterparts in the EU15. This obsession was given European Central Bank (ECB) support at an early stage in 2009, as Europe was experiencing the worst recession in 80 years, when Jean-Claude Trichet asserted that states had reached the limit of indebtedness and would need to start reducing their borrowing in 2010 in order to reassure consumers and financial markets.[2] In April 2010, Trichet surprised one questioner by asserting and, on request, repeating the conviction that 'the market is always right, and has to be completely respected at all times' (cited in Lehndorff 2012: 7). Finally, and shortly before his departure as President of the European Central Bank in 2010, in a speech declaring the imminent restoration of full health to European capitalism, Trichet stated that all the ECB had to do was to accompany 'the market as it progressively gets back to normal'.[3]

Defining market 'normality' in empirical-historical terms would be difficult enough, given the wide variety of market relationships and dynamics both at given times and over time. The normality of 'oligopolies' or 'monopsonies', where concentrated economic power determines those dynamics, will arguably not have been Trichet's understanding. However, neither can the increasingly bizarre market conditions of the neoliberal era be understood as norms of sustainable economic activity to which we should ever dream of returning. Trichet's simple invocation of an infallible market is nevertheless deeply worrying, particular in the context of the scientific ruins of the efficient market hypothesis and the continuing paralysis of financial and investment markets in Europe.

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[2] 'ECB chief Trichet says governments have reached borrowing limit', *The Guardian,* 21 June 2009, retrieved from: <http://www.theguardian.com/business/2009/jun/21/ecb-trichet-budget-deficit-warning> (last accessed 1 October 2013).

[3] 'Interview with Jean-Claude Trichet', *Financial Times,* 8 September 2010, retrieved from: <http://www.ecb.europa.eu/press/key/date/2010/html/sp100910.en.html> (last accessed 1 October 2013).

Discounting market fallibility *à la* Trichet thus pre-programmes the colossal misdiagnosis of the extent, severity and implications of Europe's multidimensional crisis (See Box 1.1).

Box 1.1 Europe's multiple crises 2007–2013

1. A *functional crisis of the global system of financial services*; banking and related services have become incapable of 'servicing' the circuits of production, service-provision, investment and consumption;

2. A *cyclical crisis* of production, consumption, trade, investment and employment, which is threatening to become a regional 'slump' greater than that of the 1930s;

3. A *structural crisis of 'over-commitment'* to financial services as vehicle of growth; this in turn involves a fundamental crisis of capitalist commercial psychology, notably of the exaggerated profit-expectations underpinning Ponzi-capitalism; public and private pension funds, social insurance funds, private investment funds, private and corporate shareholders had become fatally addicted to the unsustainably high rates of return, provided by hyper-leveraging and hyper-appreciation of financial assets;

4. A *crisis of the 'growth' paradigm* as policy vehicle for ensuring economic and social equilibrium, where the simple saturation of markets and increasing elasticity of demand renders the delivery of convenient incremental increases in output less feasible; the temporary illusion of growth and affluence provided by Ponzi-style circuits of fictitious capital can be seen as a desperate attempt to defy the reality of the increasingly limited growth potential of affluent societies;

5. A continuing *crisis of the 'growth' paradigm as basis for planetary survival*; the depletion of resources, bio-diversity, habitat-quality, along with the consequences of man-made global warming, pose colossal challenges to current generations in their efforts to bequeath a viable bio-sphere to future generations.

6. The first four crises above amount to a clear *crisis of the neoliberal paradigm*; the bankruptcy of the 'efficient market' hypothesis and the illusions of 'the' market's self-healing properties are evident and crass.

7. The failure by 'epistemic policy communities' to acknowledge the intellectual bankruptcy of the neoliberal paradigm betokens a continuing *crisis of economic discourse*, characterised by an institutionalised resistance to reflection and to holistic, interdisciplinary approaches to human social and economic relationships which acknowledge the profound (global and societal) interconnectedness of those relationships;

8. This in turn has revealed a *deep crisis of economic management*, characterised by the utter powerlessness of monetarist inspired independent central banks to control the 'liquidity factories' of casino capitalism (Phillips 2008; Mellor 2010); the theological centrality of the quantity theory of money was rendered absurd by the embarrassing inability of either Bundesbank or ECB leaderships to explain the disparity between a ballooning money stock and low growth and low aggregate inflation (Leaman 2012b). Europe's policy architecture, built so confidently around the separation of a dominant central monetary authority and subordinate national fiscal authorities looks clearly inappropriate as a means of mastering the above multiple crises and maintaining democratic legitimacy in the process.

The above clearly betokens much more than a temporary cyclical or structural crisis of an otherwise secure mode of production, and rather an *existential crisis of capitalism itself*, unheeded by its corporate elites and its political 'managers' alike. It is thus very much 'different this time'. The resultant recoveries from 'the' crisis are therefore very unlikely to follow the patterns exhibited by states in earlier financial crises, as Reinhart and Rogoff (2009) suggest.

A central argument of this paper is that the scale and effect of Europe's on-going multiple crisis have been systematically trivialised by policy-makers, with corresponding implications for their crisis management priorities. There have been several attempts to quantify the scale of the global crisis in terms of output losses. One is in fact an occasional paper by staff at the Commission's Directorate General for

Economic and Financial Affairs (DGFEA) (European Commission 2009) which strikes a very sober note of warning in its preliminary assessment of the long-term effects of the crisis, presenting both 'optimistic' and *'pessimistic/realistic'* scenarios of losses in output and investment within the EU over twenty years. Both scenarios foresee permanent output losses: of 0.5 per cent in the optimistic variant and 4.5 per cent annually in the pessimistic variant (Figure 1.1). The findings of the DGEFA paper are in line with both specific studies of the 2008 crisis (Haldane 2010a) and the general conclusions of comparative studies of historical financial crises (Abiad *et al.* 2009); however, for whatever reason, the DGEFA paper does not translate the warning into a set of prescriptive policy proposals, in contrast to Abiad *et al.* (2009: 27) who at least imply that countervailing fiscal measures reduce the deviation from trend growth!

The DGEFA paper, even as early as 2009, nevertheless acknowledges that pessimism over recovery and long-term prospects represents the 'realistic' scenario. It also underscores the potential effects of an extended crisis on a broader set of variables within the economies of the EU27. Beyond the permanent loss of output and unused capital stock, the paper also talks about a possible 'permanent destruction in human capital, leading to an irreversible (sic author) rise in the structural unemployment rate' (European Commission 2009: 14); a 'protracted recession' might also reduce the labour force participation rate by 'discouraging vulnerable workers from seeking a job' (*ibid.*); furthermore growth rates and productivity could be adversely affected by specific crises in vulnerable branches of the economy like financial services, construction and motor vehicles (European Commission 2009: 15) and by a 'slow process of industrial restructuring'; finally growth and productivity 'could also be permanently affected by a reduction in innovative activities due to lower (private) research and development (R&D) investments, which tend to be cyclical, and more limited opportunities for the transfer of knowledge (*ibid.*).

- The permanent waste of human capital is already palpably evident in the high levels of *youth unemployment* in the whole region (Figure 1.2); November figures showed an average rate of youth unemployment at 23.7 per cent for the EU27 and 24.4 per cent in the eurozone, with Greece (57.6 per cent) and Spain (56.5 per cent) the leaders of a grim table of squandered 'human capital'. Micro-level studies of early career unemployment (Gregory and Jukes

2001; Gregg and Tominey 2004) have already identified a permanent *'scarring effect'* on later average earnings. The worsening of already high structural unemployment among 15–24 year-olds arguably allows us to conclude that such scarring in Europe will be

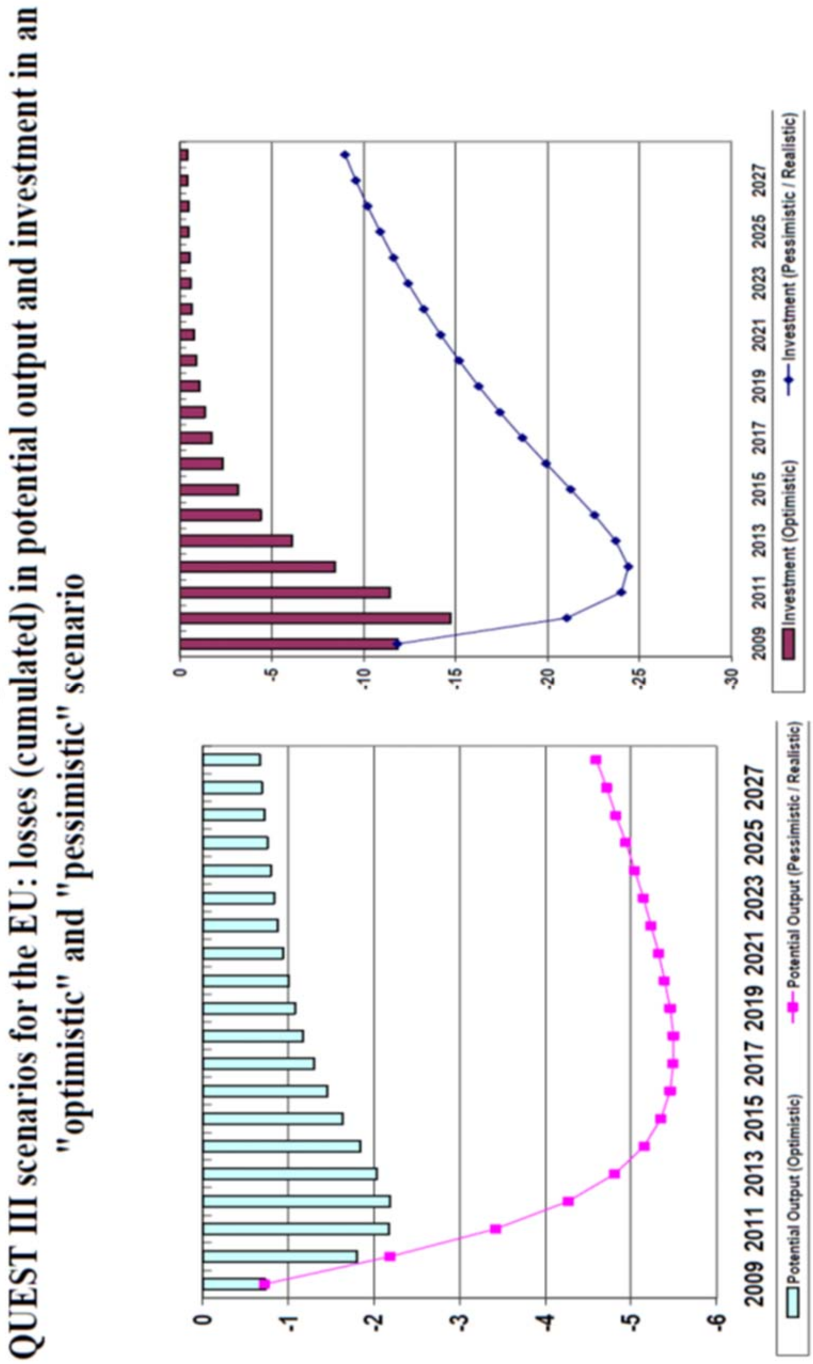

Figure 1.1: Losses in potential output in EU27 2008–2027 (estimated)

Source: European Commission (2009) *Impact of the Current Economic and Financial Crisis on Potential Output, Occasional Paper*, Brussels, p. 8.

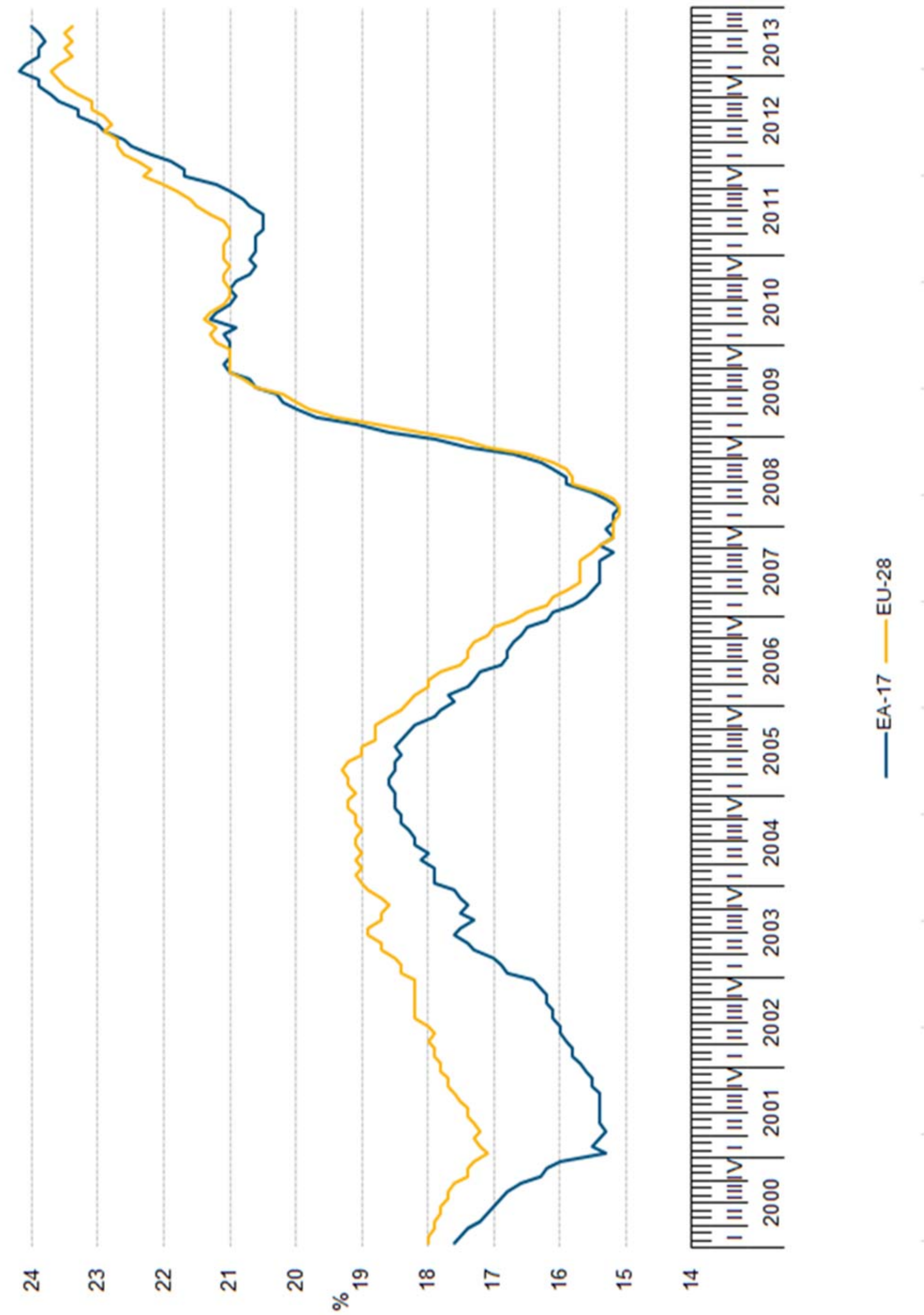

Figure 1.2: Youth unemployment in Europe (EU27 and eurozone) 2000–2012

Source: Eurostat (2013) 'Unemployment rate by sex and age groups – monthly average, %'. Retrieved from< http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=une_rt_m&lang=en> (last accessed 8 October 2013).

chronic for current generations. International Labour Office research also demonstrates the disproportionate level of youth unemployment in social groups with lower levels of educational attainment (International Labour Office 2012: 46).

- Eurostat data for 2011 confirm a trend towards a lower *participation rate*, from 65.3 per cent of the 15–65 year-olds in 2007 to 64.3 per cent in 2011, but again with severe falls in Greece from 61.4 per cent to 55.6 per cent, and Spain (65.6 per cent to 57.7 per cent).

These figures, however, are clearly distorted by the wide variance in part-time employment (Figure 1.3), with an EU27 average of 19.4 per cent of total employment but with comparatively low part-time ratios in less developed and newer member states (the 12 new member states plus Portugal and Greece have an average of just 8.4 per cent part-time employment). It can therefore be argued that the higher part-time employment ratios in the old core member states of the EU15 mitigate the scarring effect of early career unemployment, even if those figures conceal higher levels of under-employment in more developed economies.

The pre-existing disparities in *Research and Development (R&D) Intensity* have been both acknowledged by the EU, and their reduction was made one of the main targets of the Lisbon 2020 strategy (European Commission 2007). Again the core-periphery distribution of R&D expenditure is marked, with Estonia, Slovenia and the Czech Republic the exceptions that prove the general rule of a high concentration in the northern core states. However, the EU average of 1.98 per cent of the gross domestic product (GDP) remains significantly behind that of both Japan and the USA, with China already converging on static European levels in 2005 (*ibid*: 76). The case of Greece is instructive, firstly because its R&D ratio is modest at 0.58 per cent of GDP and, secondly, because it is overwhelmingly represented by the public sector in contrast to the major players in the region where the public/private funding-mix is seemingly more balanced (*ibid*.: 82); this should not deflect attention from the general problem of cuts to research-funding that have been mooted at both MAFF-level and at that of member states. It nevertheless reinforces the suspicion that, without a radical redirection of Structural Funds or a general reversal of austerity programmes at member state level with a strong focus on modernisation through R&D, the Lisbon targets (Figure 1.4) will be missed, and that private funding

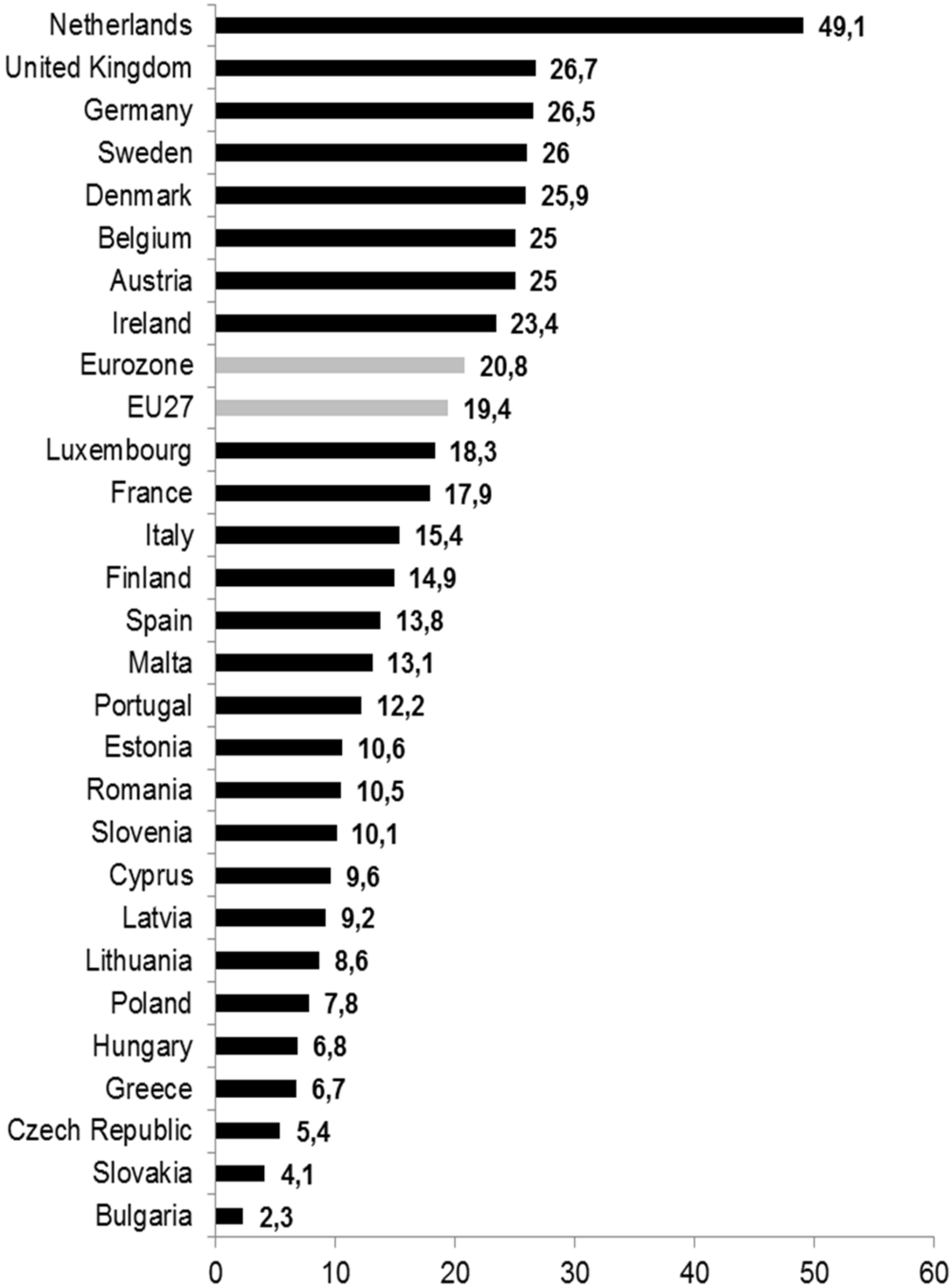

Figure 1.3: Part-time employment in the EU27 as a proportion of total employment in 2011

Source: Eurostat (2012) ‘Around 8.5 million part-time workers in the EU27 wished to work more hours’, Newsrelease 12/61.

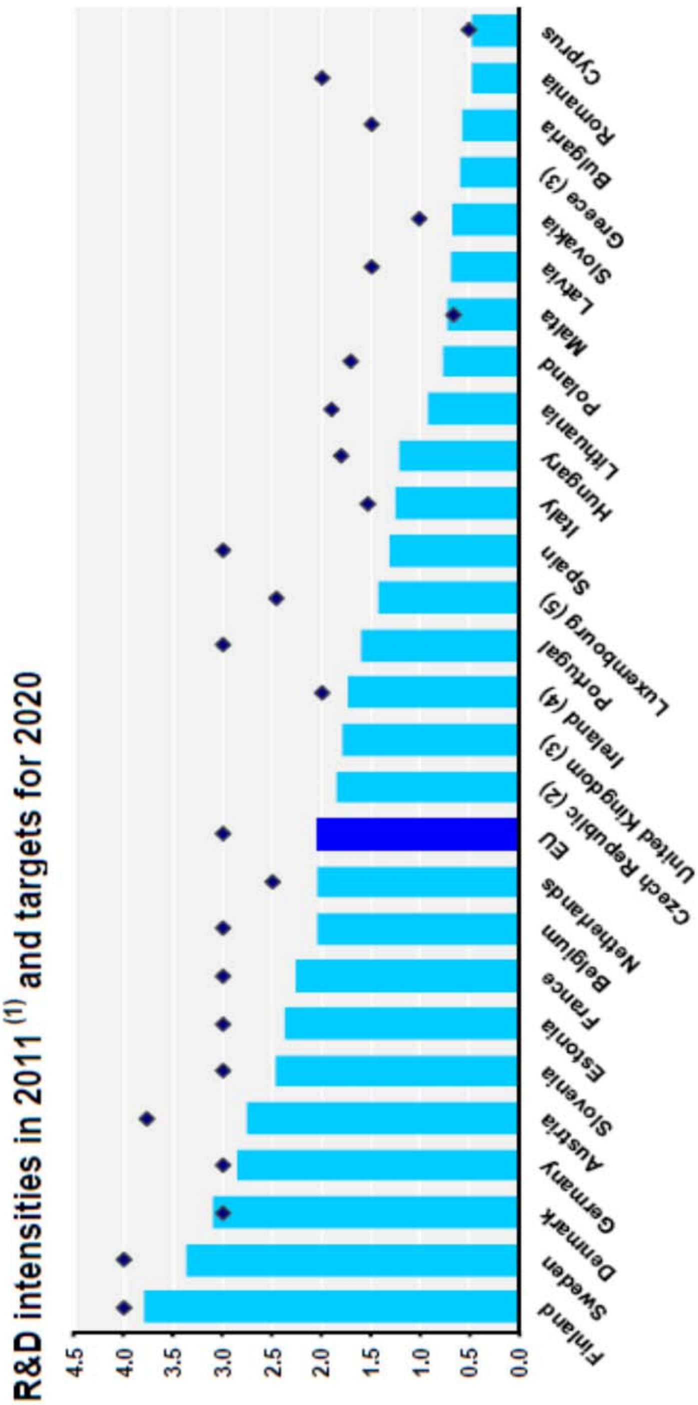

Figure 1.4: Expenditure on research and development as a proportion of GDP in per cent

Source: European Commission (2011) 'Europe 2020 Targets: Research and Development'. Retrieved from: <http://ec.europa.eu/europe2020/pdf/themes/15_research__development.pdf> (last accessed 13 August 2013).

Notes

(1) EL: 2007; PT: 2010; (2) CZ: A target (of 1 %) is available only for the public sector; (3) CZ: A target (of 1%) is available only for the public sector; (4) UK: A targets for 2020 is not available.

will gravitate towards the established centres of innovation. Greece, for example, has experienced six successive years of severe contraction in investment (a fall of 86.4 percentage points from 2006!)[4], and cannot realistically be expected to attract research-intensive monies from either domestic or foreign sources.

The DGEFA's pessimistic forecast of additional knock-effects of a 'protracted recession' (apart from permanent output losses of trillions of euros) would therefore seem to be grimly accurate, judged from this brief survey of the current situation, four years on.

Neoliberalism, monetary accumulation and the dilution of value

The neoliberal catastrophe is not confined to the recent bursting of financial asset-bubbles and its social and political aftermath, however. The process of *value-dilution* arguably began almost simultaneously with the conversion of policy-makers and their wider community of academic and administrative advisers (their 'epistemic' community) to monetarism and Thatcherite supply-sidism. A recent study of the British economy by Martin Weale demonstrates in graphic form two major periods of value-destruction since the 1920s, the first beginning in 1930 through to the end of the Second World War, the second starting in 1980.

Weale himself does not employ the concept of 'value-destruction' but of economic 'sustainability' threatened, as he sees it, by the decline of the UK's wealth-to-GDP ratio (Weale 2012: 62ff) – where wealth is defined as capital stock plus net foreign assets and net national saving. His analysis nevertheless provides an eloquent illustration of the similar effects of depression/war on the one hand and the neoliberal paradigm on the other, inasmuch as the weakening of the overall wealth ratio between 1930 and 1945 was followed by a gradual recovery up until 1980, 'after which it has declined sharply again' (*ibid.*), reaching the historically low level of 1945 again between 2000 and 2005 (see Figure 1.5). Weale stresses the significance of the weakened wealth ratio in terms of intergenerational equity, where the over-consumption of recent generations is judged to leave a less viable foundation for future welfare than the one inherited in 1980. However, Weale's data also provide ammunition for demonstrating the allocatory

[4] Figures from OECD *Economic Outlook* 92, October 2012.

diseconomies of the paradigm of 'monetary accumulation' as a function of poorer investment and saving between 1980 and 2005. These weakened the long-term resilience of the UK economy, even before the further wealth-destruction during the 2008–9 crash. His analysis also suggests that similar conclusions can be drawn from the general decline of the investment ratio in *all* advanced economies. The following remarks seek to demonstrate the destructive effect of neoliberalism in terms of both overall investment and the particular role of public investment in sustaining social and economic welfare.

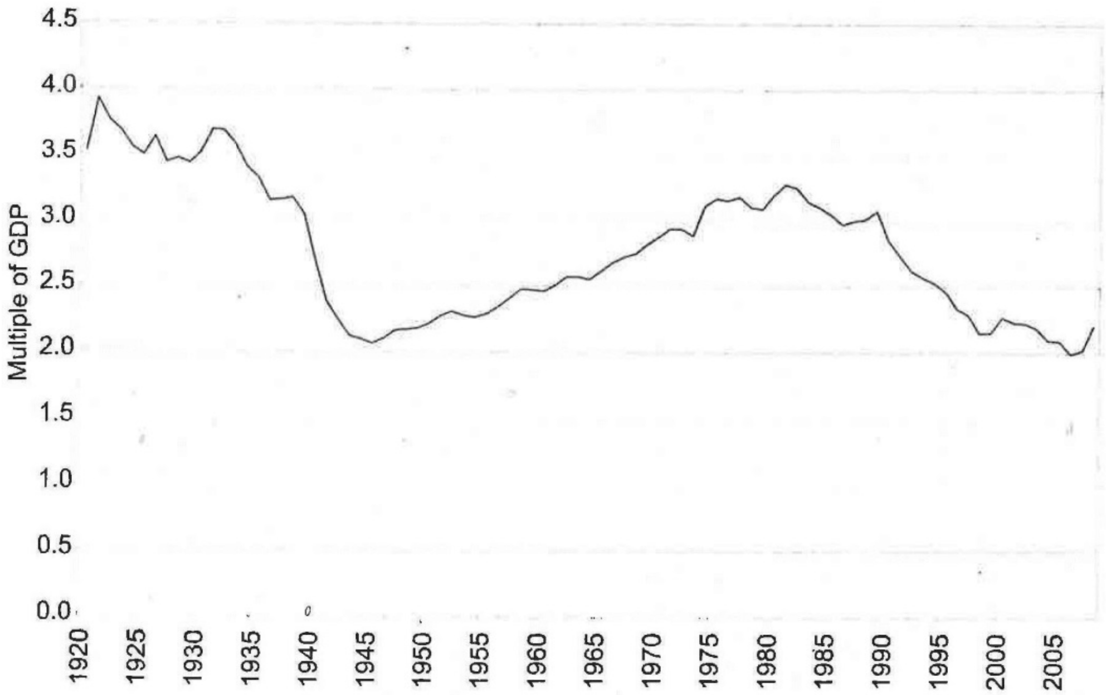

Figure 1.5: Ratio of produced wealth to GDP in the UK 1920–2005

Source: Weale, M. (2012) 'Unsustainable Consumption: The structural flaw behind the UK's long boom', in Giudice, G., Kuenzel, R. and Springbrett, T. (eds) *UK Economy: the Crisis in Perspective*, London: Routledge, p. 62.

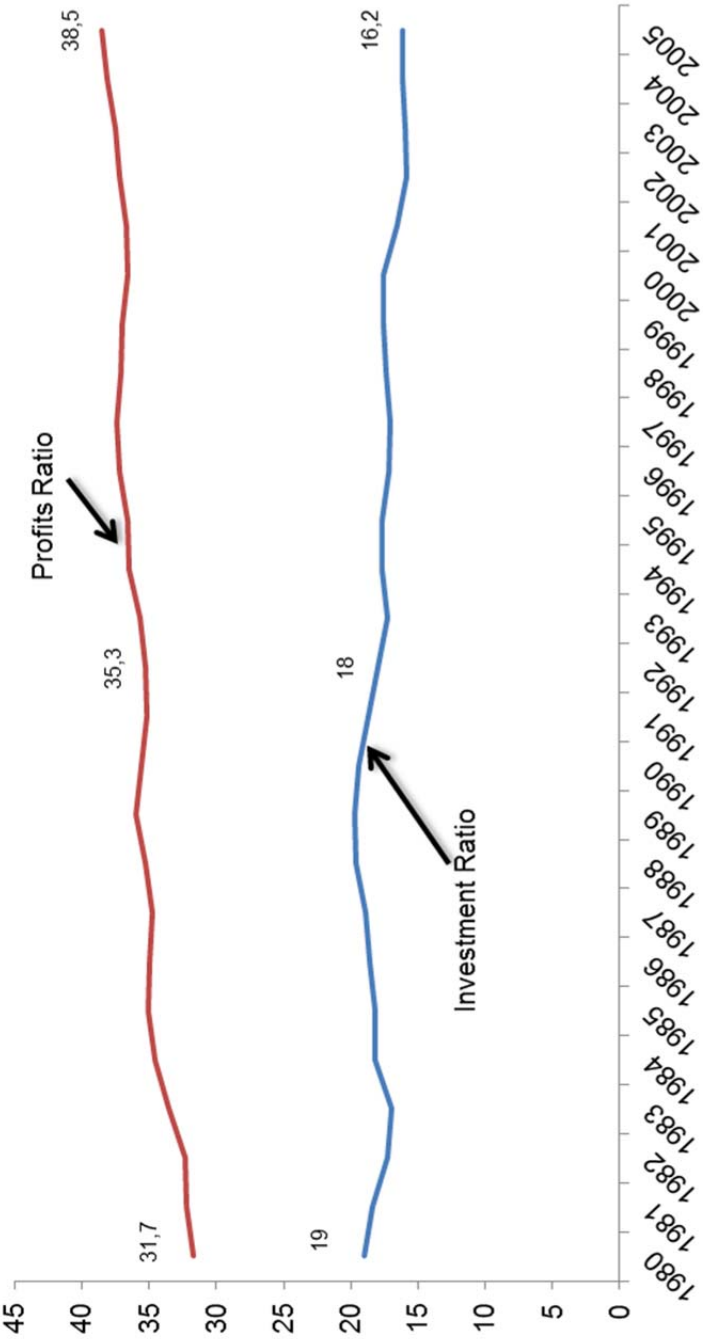

Figure 1.6: Profits ratio and investment ratio in advanced economies 1980–2005.

Source: International Monetary Fund (2007) World Economic Outlook, Washington, DC: International Monetary Fund. Retrieved from: <http://www.imf.org/external/pubs/ft/weo/2007/01/pdf/text.pdf> (last accessed 24 September 2013). Data from Charts 1.15 and 5.7; profits ratio defined as the share of income from capital in national income before tax and transfers; investment ratio is the proportion of gross fixed capital formation to GDP in any given year.

Figure 1.6 above provides strong evidence disproving neoliberal claims of the efficacy of supply-side reforms on real economic growth in the world's advanced economies. IMF data for both the share of profit income in net GDP (national income) and gross fixed capital formation as a proportion of GDP contradict the claim that higher profit income generates higher real investment; a 6.8 percentage pointrise in the profits ratio in advanced economies between 1980 and 2005 stands in stark contrast to the 2.8 percentage point decline in the investment ratio. The assumed virtuous circle of higher profits, facilitated *inter alia* by tax relief and labour market reforms, leading to higher investment, higher production levels, higher employment and a new sustainable, market-driven dynamic economy, falls at the first hurdle.

Given that the linkage between investment and growth is fairly robust (see Rajan 2010: 70), that the investment ratios of the EU's core economies have been on a declining trend for some time, that the rise in the European profits ratio in the observed period was even greater than the OECD average (at over 9 percentage points) and that Europe has been the world region with the most anaemic growth rates for two decades, one is justified in asking: what went wrong with the supply-side growth revolution? A very brief survey of the actual processes of the neoliberalisation of markets since the 1980s is necessary to explain the mal-functioning of supply-side transmission mechanisms in the macro-economy.

- Neoliberal reforms of the state included the extensive *privatisation* of state assets, many of them natural monopolies like the gas, power and water utilities or public transport networks and hubs (airports, ports); while telecommunications became increasingly subject to the competitive influence of cable and satellite technologies, most utilities remained natural monopolies, inaccessible to genuine market competition and its associated price efficiencies. The most popular solutions to the problem of the potential abuse of monopoly pricing in such utilities were the political regulation of rates of return (favoured in the US) or price/tariff changes (UK), with regular adjustments according to set formulae. Such regulatory systems operated on the assumption that there must be continuity of supply, provision for modernisation and long-term investment *and* (implicitly or explicitly) a guaranteed return on capital (see Stern 2003: 22). It is unsurprising that the performance of such regulated monopolies has ensured higher returns on capital than applies to the SME sector (Candeias 2009); their revenues represent *monopoly rents* guaranteed for given contractual periods. Such privatisation programmes became *core elements of state policy* in advanced states and of the development policy of advanced states and supra-national institutions like the World Bank and the European Union.

- An extension of straightforward privatisation of state-owned assets was the introduction of *'public-private-partnerships'*, involving the private financing of public building and civil engineering projects and medium- to long-term leases granted to the companies with guaranteed income streams from the public institutions (in education, health, transport etc.), operating their services from the facilities. A strong determinant motive in such schemes was the desire by state authorities to minimise the effect of such public sector projects on the state's borrowing requirements in a period (1990 to date) dominated by the monetarist strictures of deflation and debt-consolidation. Such projects nevertheless also involved guaranteed monopoly rents within contracts that have been frequently criticised for their generosity towards the private partners. Recent official UK studies of the efficacy of the 700 or so PFI projects also cast serious doubt on both their underlying principles and their viability (e.g. House of Commons 2011).

- Against this background of state policies helping to engineer higher than average rates of return on capital through guaranteed monopoly income streams, the investment options open to companies with growing capital reserves already militated against the risk of simply expanding and modernising capacity in traditional commercial sectors; more significantly the privatisation programmes raised expectations of rates of return that would become increasingly difficult for such traditional sectors to deliver (see Haldane 2010b: 13). What then emerges from the parallel accumulation of corporate reserves in the MNCs of advanced states and the transfer of 'petro-dollars' from rich oil-producing states to the financial institutions of the North is a highly liquid global market for finance capital in search, not of secure but modest long-term returns on invested capital, but of increasingly high returns on capital that is committed for ever shorter periods of time (Huffschmid 2002).

- In addition to these determinants of rising ROR expectations, in the early 1980s the monetary authorities of the advanced economies – led by the Federal Reserve – presided over a sudden *increase in real interest rates* which increased bond yields to historic highs; this was driven both by orthodox monetarist deflationary policies via higher central bank base rates, but also by the fairly unorthodox strategic military programmes of the Reagan administration and their heavy reliance on deficit-spending. Accordingly, US 10-Year real bond yields reached 14 per cent in 1982. One commentator describes returns on bonds in recent decades as 'super-sized', noting that 'real bond returns after inflation in both the US and UK have been on average 5.9 per cent compound per annum – some three to four times the long term average respectively'[5]. Such returns on state guaranteed financial assets thus also contributed to increasing levels of expectation on the part of major investors, particularly in a period of low or negative growth, preparing the ground for the wholesale revolution in financial services that ensued (see Huffschmid 2002; Mellor 2010; Phillips 2008; Tett 2009).

The important feature of the paradigm shift to financialised capitalism and monetary accumulation was that it was constructed on the *illusion of enhanced wealth-creation*, of the appreciation of paper assets which of themselves would produce 'value' and improve the welfare of citizens on a sustainable basis. Even a UK Treasury economist, like Andrew Haldane, demonstrates rather that the contribution of the financial sector to growth and 'value' was in large measure a 'mirage' (Haldane 2010b). The mirage of seemingly effortless value-appreciation through the operation of financial circuits nevertheless maintained an astonishing level of credibility among policy-elites, credit-rating-agencies and the academic community, defying the warning signs of the East Asian Crisis of 1997, the Enron debacle of 2001 and the 'dotcom'-crisis of 2001–2, as well as the intuitive logic of observers who suggested it was difficult to create value out of 'thin air' (Mellor 2010 etc.). Nevertheless, the 'fool's gold' paradigm (Tett 2008) was only revealed to be what it was to wider sections of global civil society when the

[5] 'Are Government Bonds in Developed Markets Overvalued', *Gillen Markets*, 1 April 2011, retrieved from: <http://www.gillenmarkets.com/featured_articles/are-government-bonds-in-developed-markets-overvalued.cfm> (last accessed 13 August 2013).

affairs of Lehmann brothers, AIG etc. became public in the autumn of 2008. Haldane's account of the 'productivity miracle' of financial services is persuasively simple, inasmuch as he uncovers the basic accountancy tricks of banks and other institutions which allowed them to create vast quantities of liquidity without altering the 'health' of their visible balance sheets or increasing their basic capital. They achieved this through a combination of hyper-leveraging (borrowing) and securitisation (converting loans/liabilities into securities/assets based on future income streams). Far from suggesting a dilution of the asset-side of the balance sheet, such operations – often through so-called special-purpose-vehicles (SPVs) belonging to the same bank – the asset-side was seemingly increased by the on-going appreciation of the bonds (CDOs, ABSs etc.) on secondary markets and the persistence of triple-A ratings delivered by compliant credit ratings agencies. The colossal liabilities represented by leverage ratios of 'more than 50 times equity at the peak of the boom' (Haldane 2010b: 15) were thus spirited off balance sheets in smoke-and-mirrors operations involving multi-layered ownership structures, shell companies and offshore secrecy jurisdictions.

The deployment of so much liquidity in the febrile capital markets of the 1990s and 2000s allowed a corresponding increase in the rate-of-return on equity (ROE): 'the level of ROEs was consistently at or above 20 per cent and on a rising trend up until the crisis. This is roughly double ROEs in the non-financial sector over the period' (Haldane 2010b: 13). Moreover with the banks 'engaged in a highly competitive ROE race' (*ibid.*), the pressure to continue the leverage/securitisation merry-go-round was very high, suppressing what remained of scepticism and prudence at the level of executive boards, investment analysts, credit ratings agencies and institutional investors. Such *post hoc* insights by a Treasury insider beg the question as to why there were so few warnings from the policy elites of advanced states and of supra-national institutions, when financial ROEs were so clearly abnormal.

The dilution of real wealth in the decades of the recent three decades of financialised capitalism is also evident in the changing shape of the asset holdings of 'non-financial institutions' (NFEs) or 'non-banks'. Figures from the European Central Bank (2007) covering the balance sheet composition of all NFEs in the eurozone show that between

1995 and 2005, the ratio of their financial assets to tangible fixed assets more than doubled from an average of 0.53 to 1.18.

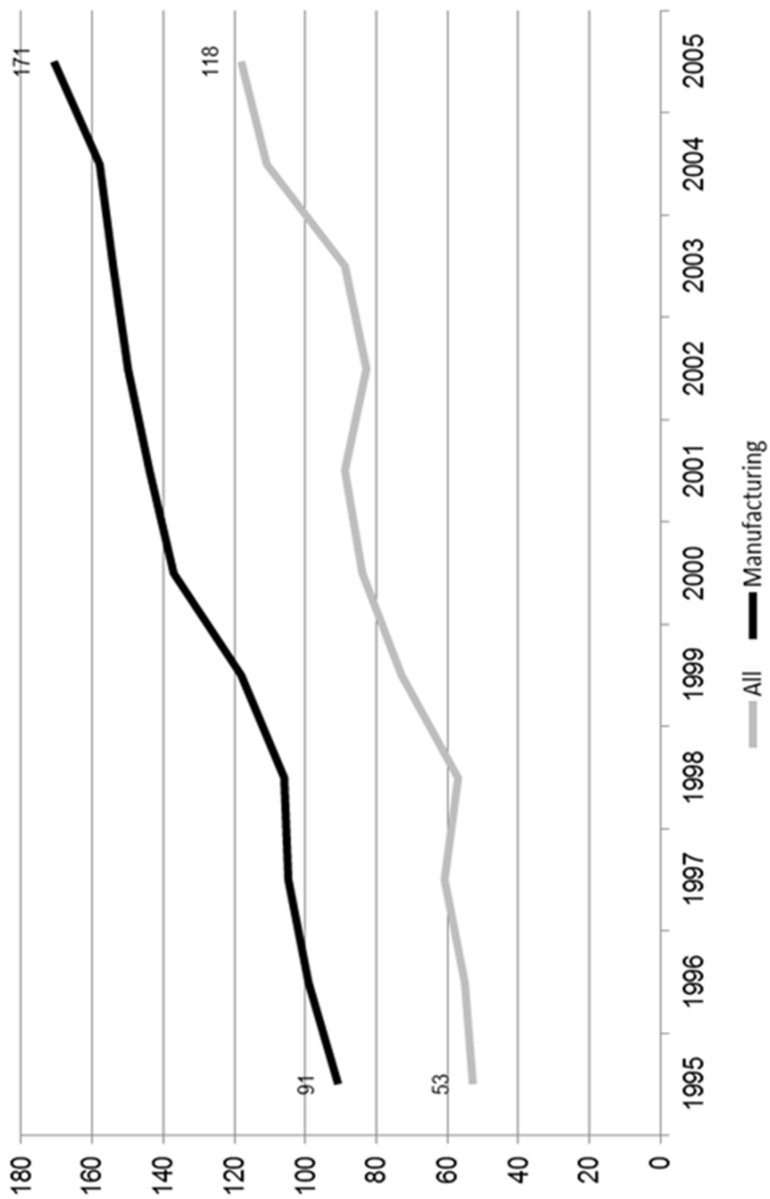

Figure 1.7: Ratio of financial to fixed capital in eurozone non-financial enterprises 1995–2005

Source: European Central Bank (2007) 'Corporate Finance in the Euro Area with Some Background Materials', Occasional Paper No 63/ June, p. 21.

Most striking is the transformation of the balance sheets of manufacturing enterprises with financial assets in 2005 totalling 171 per cent of physical assets (see Figure 1.7), a virtual doubling in just ten years. Figures for the individual branches of Germany's dominant manufacturing sector show a marked trend towards the financialisation of their asset portfolios in the previous decade-and-a-half between 1980 and 1985, with motor manufacturers reaching an average financial asset ratio of 1.57, electro-technical corporations 1.76 and German chemical TNCs a ratio of 2.0 (see Leaman 2009: 80f). The not infrequent references to Siemens and Daimler-Benz as banks with manufacturing subsidiaries find strong empirical support from such data.

A critical determinant of this historically unprecedented shift in the way in which industrial corporations valorised their capital, deriving sizeable proportions of their operating profits from financial securities, rather than the sale of products and services, was the adoption of 'shareholder-value' as the predominant measurement of commercial success. Lazonick (2011) identifies the particular role of stock (share) options in the remuneration packages of senior managers in driving this process in the United States. The option to be rewarded by extra tranches of a company's stock skewed incentives, according to Lazonick, particularly within larger corporations, towards short-term commercial strategies designed to drive bull markets.

With average compensation in the Top 100 US corporations varying from 'lows' of $18.2 million (1994) and $103.7 million (2000), stock options accounted for well over two thirds in most years in the period 1992–2008 (Lazonick 2011: 8). One of the most potent vehicles for generating significant increases in corporate share values was in the (frequently hostile) takeover of other enterprises or the acquisition of majority holdings in other corporations. Figure 1.8 shows how dramatic the two waves of global takeovers were between 1990 and 2006, with record deal values of $4 trillion in both 2000 and 2006. The efficacy of mergers and acquisitions activity, as noted above, is strongly contested by a number of studies, one suggesting that 70 per cent fail (Campbell *et al.* 2008), another that hostile takeovers have a generally worse record (Martynova *et al.* 2006); in the case of banks, Haldane cites research suggesting that 'economies of scale in banking are exhausted at relatively modest levels of assets, perhaps between $5–10 billion' and that subsequently there 'is no strong evidence of increased bank efficiency after a merger or acquisition' (Haldane 2010a: 11).

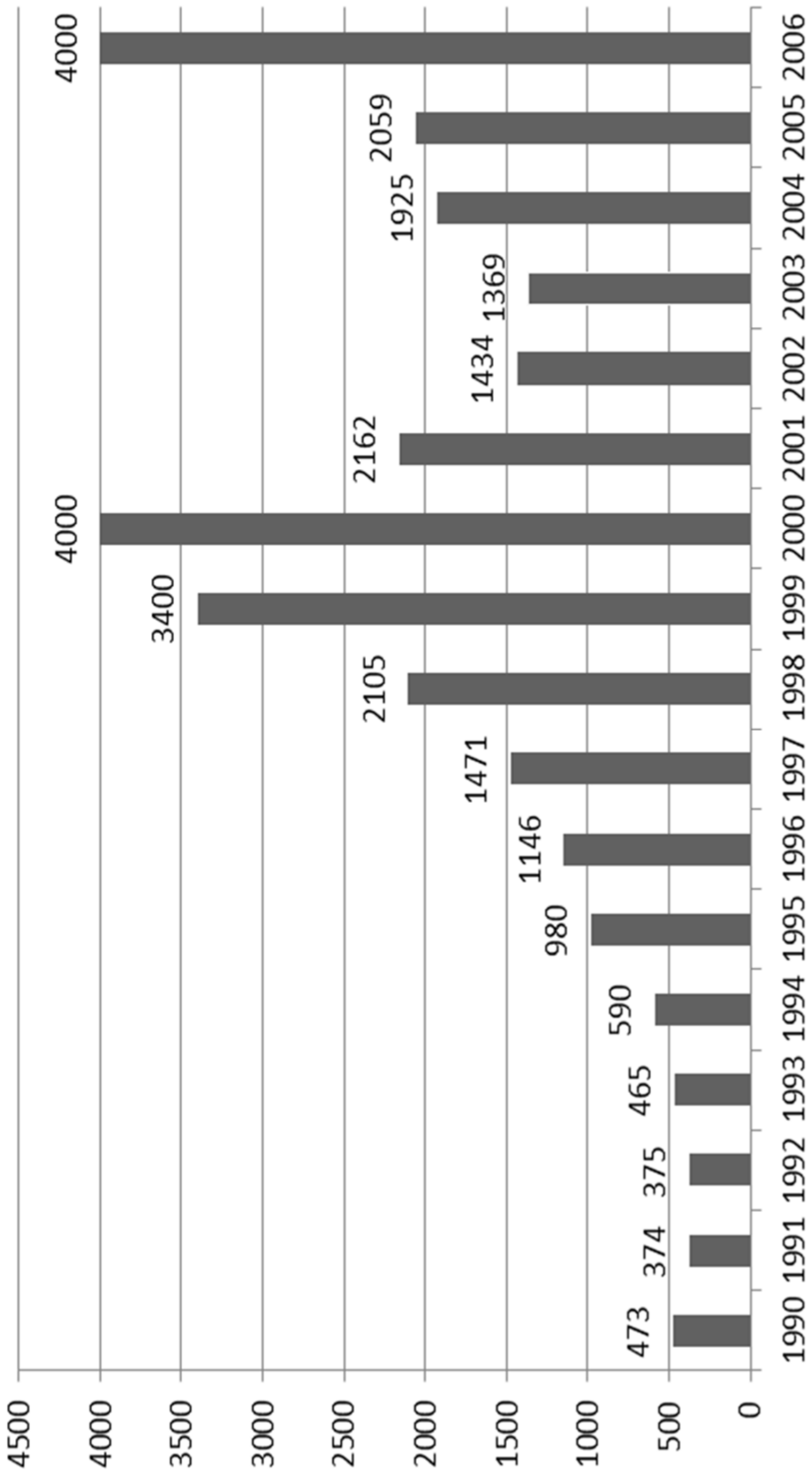

Figure 1.8: Global mergers and acquisitions 1990–2006. Value in USD billion

Source: Dealogic, M & A Analytics, statistical platform, available at <http://www.dealogic.com/investment-banking/ma-analytics/> (last accessed 15 October 2013).

Against the background of the 'common knowledge' that 'most M&A activity is value-destroying' , as asserted by a mainstream economist (Haldane 2010b: 21; my emphasis), his subsequent assessment of the extraordinary degree of concentration in the banking sector, particularly after the repeal of the Glass-Steagall Act in the US in 1999 (Haldane 2010a: 6 and 18) supports the view of many heterodox economists that the 'merger mania' of the last two decades generated colossal gains for the minority of banking and other corporate executives involved in hyper-leveraged buyouts, but equally colossal risks for the compliant and complacent states and their respective citizens, risks that exploded in the autumn of 2008 and the costs of which have not even yet been remotely grasped by policy 'elites' at political or corporate level.

The role of the neoliberal state in the transformation of European and global capitalism is inherently contradictory, inasmuch as the executive decisions of key national administrations have involved a conscious self-marginalisation, withdrawal from the responsibility of key allocatory functions within national and regional political economies. Both the territorial mobility and, above all, the effective privatisation of money-creation by corporations (Box 1.1 above), has rendered states and supranational political institutions increasingly powerless to manage either fiscal or monetary affairs effectively.

The political disempowerment of politics *qua* management of the political economy produced what Richard Murphy terms the 'cowardly state'. Of fundamental significance, finally, in the process of weakening the asset-base of European political economies has been the particular decline of *public investment* as a critical ingredient of social progress. Gomez and Pouget (2008) chart the decline of public investment in 21 OECD economies from some 4.5 per cent of GDP in the early 1970s to less than 3 per cent in the most recent decade (Figure 1.9). The pattern of decline is not identical in all economies, but most marked in Europe's core economies (France, Germany, the Netherlands, Britain). The authors seek, in particular to draw a correlation between the provision of public infrastructural assets and overall investment and align themselves with those who assert that (inward) real investment by private companies is more strongly determined by the provision of public goods than by benign corporate tax regimes, in that 'the provision of public capital creates rents for the firms' (Gomez and Pouget 2008: 7). They in fact go on to postulate both the positive multiplier effect of state investment on growth and private investment (as demand-side variables) and the negative effects of strategic reductions in both public investment and rates of corporation tax (as supply-side variables).

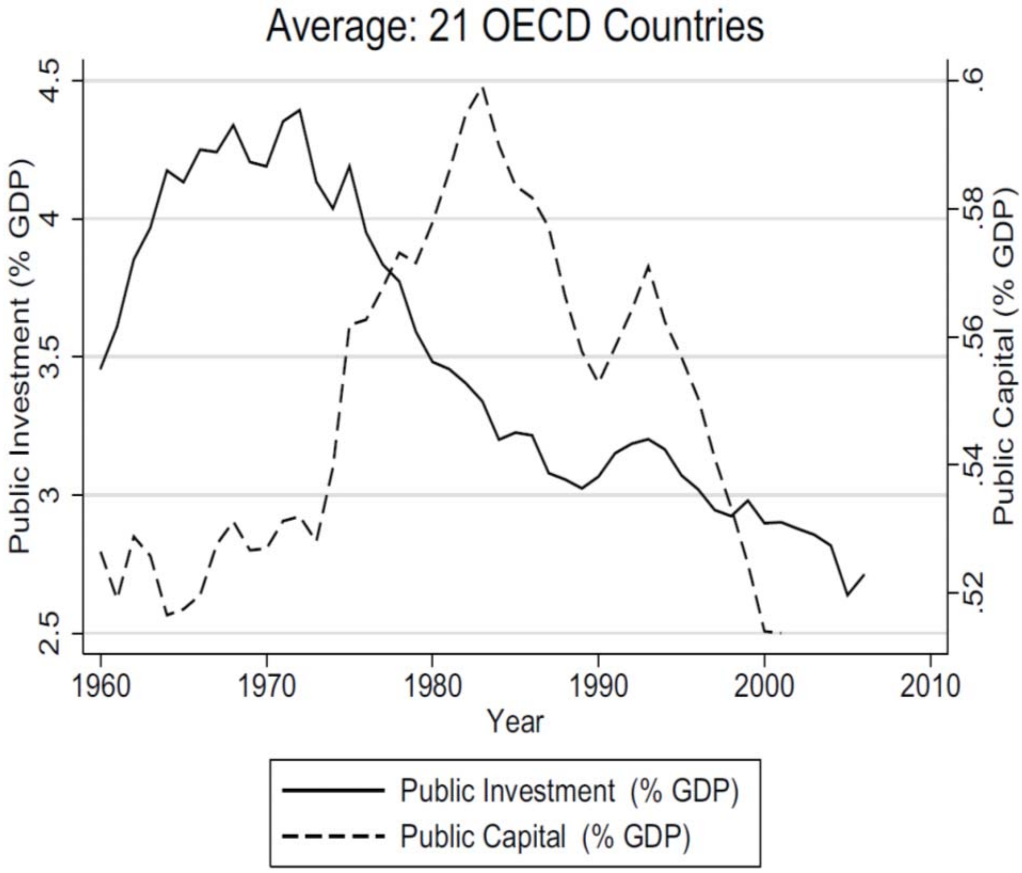

Figure 1.9: Public investment and public capital in the OECD 1960–2010

Source: Gomez, P. and Pouget, F. (2008) 'Corporate Tax Competition and the Decline of Public Investment', European Central Bank Working Paper 08/928, Frankfurt: European Central Bank, p. 7.

The findings of this persuasive working paper by staff at the European Central Bank cast serious doubt on neoliberal orthodoxy and strengthen the case of heterodox economists in their espousal of both demand-side strategies and a reinvigorated, active state. Moreover, these findings are supported by recent, persuasive research into fiscal multipliers (Coenen et al. 2012; Auerbach and Gorodnichenko 2011) as well as the extraordinary acknowledgement of mistakes by senior IMF analysts (Blanchard and Leigh 2013). The relevance of such findings (from, among others, staff of two pillars of the Troika) for the analysis of Europe's current crisis of economic management is, along with the evidence presented above, good reason to assert the catastrophic consequences of Europe's persistence with state inaction and austerity.

The tank-driver ploughs on: The destructive consequences of EU policy-paralysis

The reconvened budget summit of the European Council on 7 and 8 February 2013, produced a set of general conclusions (European Council 2013a) and a second document (European Council 2013b) devoted to the European Union's Multiannual Financial Framework (MFF). Both documents provide significant indicators of the mind-set that is driving the EU's macro-economic strategy. Both documents are a serious cause for concern. Their intellectual 'logic' defies both the evidence of the last thirty years of European economic history and the last four years of crisis-'management'. The 'triumph' of an agreed compromise[6] on the EU's budget for seven years from 2014 to 2020 should provoke the strongest possible response from academic economists and political economists, along with the rest of Europe's active civil society groups. The bankruptcy of Europe's 'depression economics' (Krugman 2008) and the imposition of Brüning-style austerity should and hopefully will be judged the most dismal 'triumph of failed ideas' (Lehndorff 2012; see Crouch 2011) in recent years.

If we take the MFF first, the trajectory of the proposed expenditure reductions is pro-cyclical in nature, compounding the thrust of member states' austerity programmes, and neoliberal in spirit, reducing an already modest pool of collective resources even further and, with it, the opportunity to promote shared prosperity through the financing of European public goods. Table 1.1 compares the most recent budget cycle (2007–2013) and the new MFF in terms of the proportions of EU Gross National Income represented by 'payment appropriations' (real planned expenditure) and 'commitment appropriations' (maximum hypothetical expenditure including contingency funds). Actual expenditure levels for the (current) 2007 cycle can be seen to rise from 1 per cent of the gross national income (GNI) to 1.05 per cent in 2013 (1.06 per cent average for the cycle), while the expenditure plans for the cycle beginning next year envisage a GNI-

[6] See 'Cameron's Euro Triumph', *The Telegraph*, 9 February 2013.

share falling from 0.98 per cent of GNI to 0.91 per cent in 2020, a drop of 14 basis points (over 13 per cent) in seven years.

Table 1.1: EU multiannual financial frameworks 2007–13 and 2014–20 compared

Appropriations as percentage of gross national income	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	7 Year ave-rage
Total commitment appropriations	*1.02*	*1.08*	*1.16*	*1.18*	*1.16*	*1.13*	*1.12*	*1.12*
Total payment appropriations	1.00	1.05	1.04	1.12	1.09	1.08	1.05	1.06
	2014	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	
Total commitment appropriations	*1.03*	*1.02*	*1.00*	*1.00*	*0.99*	*0.98*	*0.98*	*1.00*
Total payment appropriations	0.98	0.98	0.97	0.92	0.93	0.93	0.91	0.95

Source: European Council, Conclusions (Multiannual Financial Framework), EUCO 37/13, Brussels, 8 February 2013.

Notes
The 2014–20 budget cycle assumes an enlarged EU from 2013 to 28 member states, including Croatia.

It is also noteworthy that the starting-point for both expenditure ratios in 2014 is lower than the end-point ratios for the last budget-cycle (0.98/1.03 against 1.05/1.12). The process of budget reductions is described in §1 as 'smart fiscal consolidation', matching the 'smart growth' rhetoric of the Lisbon agenda, repeated in the MFF §13. It will not have escaped the attention of neutral observers that growth – smart, scruffy or otherwise – has been stubbornly elusive over the last four years. While the imminence of recovery has been regularly invoked since the second half of 2009, nineteen of the EU's twenty-seven member states had, by December 2012, still not recovered to the output levels of 2008, as evidenced by Figure 1.10. Furthermore, of the nine other states (Austria, Belgium, Estonia, France, Germany, Malta, Slovakia, Sweden, Poland), only three are showing recoveries of any note: Poland (+13 per cent), Sweden (+6.2 per cent) and Slovakia (+5.1 per cent).

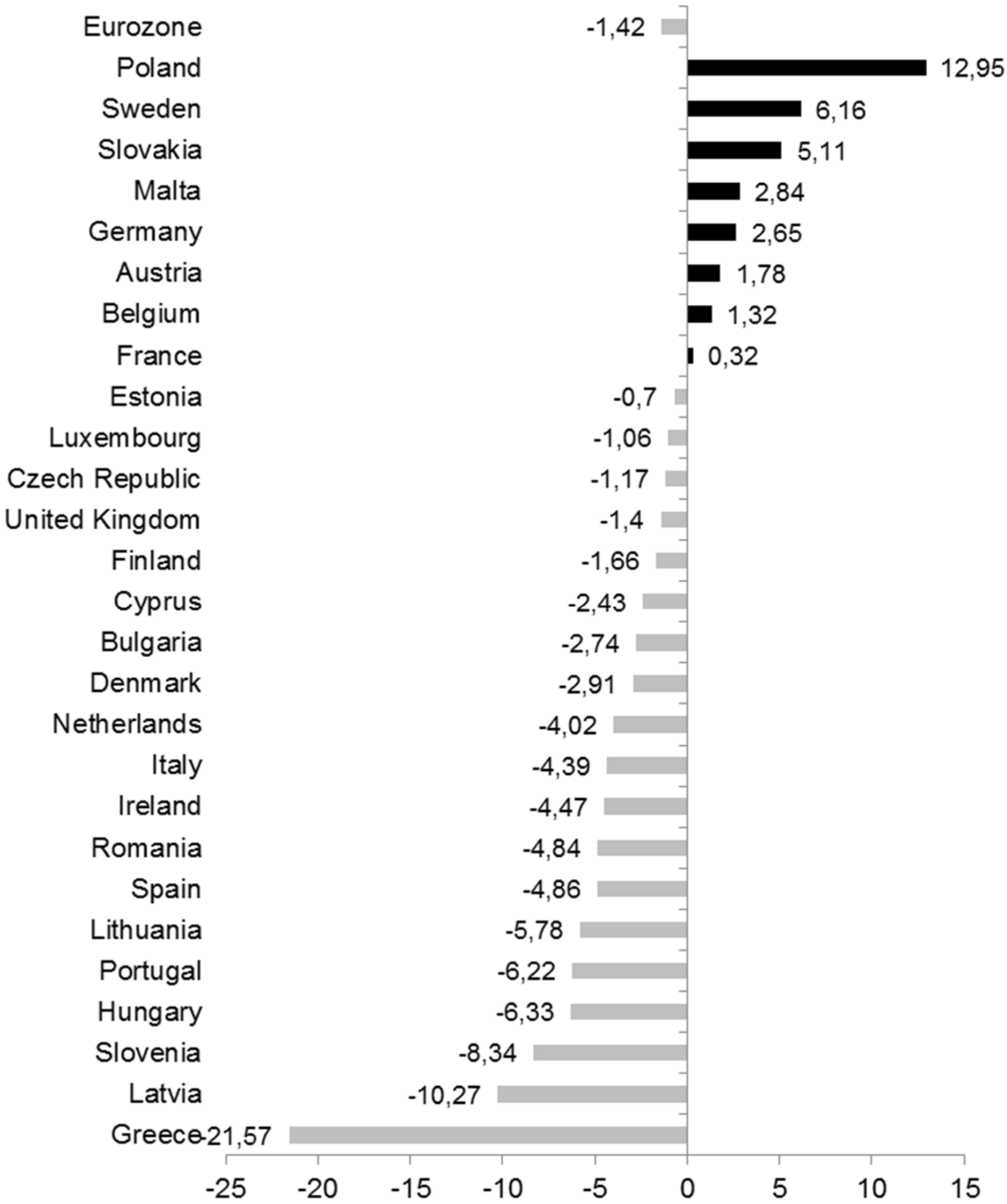

Figure 1.10: Real GDP growth of EU27 member states 2008–2012.
Source: OECD; Eurostat; own calculations.

Final quarter figures for 2012, published by Eurostat six days after the MFF, on February 14, confirmed that the eurozone had contracted by 0.9 per cent year-on-year in the last three months of 2012, with the EU27 averaging -0.6 per cent). The marginal recoveries of France and Belgium since 2008 are in reverse with year-on-year falls in GDP of -0.3 per cent and -0.4 per cent respectively (Eurostat 2013b). The OECD in December was forecasting a further decline of eurozone GDP of -0.1 per cent, with recessions in six of the EU27's

OECD members; Greece is due for a sixth consecutive year of contraction in 2013, Italy for its fourth year of negative growth out of six, Spain and Portugal (fourth in five years), Slovenia and Hungary (third in five years). The IMF's February update of its 2013 forecast suggests a contraction of -0.2 per cent in the eurozone. There is, however, a strong case to suggest an even worse outcome for European economies in 2013, given the constellation of domestic demand factors, all of which are set to contract further in the current year.

Most critically, eurozone gross investments – already at just 83.2 per cent of 2007 levels in 2012 – are forecast to decline further, by -1.9 per cent according to OECD December 2012 estimates. While the reluctance of Europe's (non-financial) enterprises to invest can be rightly blamed in part on the corresponding reluctance of banks and other financial institutions to provide affordable credit as a supply-side factor (European Central Bank 2013: 115), the persistence of very low levels of capacity utilisation – as indicator of demand – arguably represent an even more significant obstacle to any sizeable recovery of investments in either commercial property or equipment.[7] The European Union is thus set to remain the least dynamic economic region in the world.[8]

The absence of any signs of significant growth in all three components of domestic demand draws our attention to the other pillar of the European Council's strategy, revealed on February 8, namely trade as the primary vehicle for general economic recovery. Sixteen of the nineteen paragraphs in the general conclusions (EUCO 3/13) are devoted to the EU's 'ambitious trade agenda', outlining the way in which this can make 'a significant contribution' to (e)nhancing sustainable growth' (§1). Apart from the continued pursuit of 'free, fair and open trade' via multi-lateral 'regulatory convergence' (§2), this document stresses the particular importance of enhancing bi-lateral

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[7] Capacity utilisation, having slumped from 84.3 per cent in the EU27 (EU17: 84.7 per cent) in 2008 to 71.1 per cent in 2009, recovered to 80.5 per cent in 2011 but had declined to 77.4 per cent in 2012: IV (EU17: 76.9 per cent), with just a marginal improvement in January 2013 to 77.6 per cent (77.2 per cent). C.f. European Central Bank, *Monthly Bulletin*, various; European Commission 2013: 9.

[8] It is noteworthy that the CIA World Factbook places the EU in 189th position in its league table of GDP growth for 2012, with 22 EU member states in the bottom 60: <https://www.cia.gov/library/publications/the-world-factbook/geos/ee.html> (last accessed 14 April 2014).

links with ‘key partners’, most notably the USA, Japan, Canada, Russia, China, The Association of Southeast Asian Nations (ASEAN), the Common Market of the South) (MERCOSUR) and the eastern ‘neighbourhood’ (§6–8).

The reader is asked to believe that this ‘ambitious trade agenda’ will lead ‘in the medium term to an overall increase of 2 per cent in growth and to the creation of two million jobs’ (§1). Given the lack of supporting evidence for this claim, there are minimal grounds for optimism in the Council’s confident predictions. The reasons for a pessimistic assessment of the EU’s strategy are many and varied. The systemic factors which suggest short-, medium- and long-term failure will be examined later in this paper. At this juncture, a few remarks about a policy of export-led recovery in Europe will suffice:

- Over 60 per cent of the EU member states’ exports involve intra-EU trade; intra-EU trade declined by 6 per cent in 2012, intra-eurozone trade by 7 per cent (Eurostat 2013b: 28); with stagnation/austerity depressing domestic demand factors within the EU27, the predictable outcome for this predominant mode of European trade is a continuing contraction of intra-EU trade volumes.

- Exports to non-EU countries constitute 14.1 per cent of GDP in the EU27; furthermore, 73.5 per cent of extra-EU trade is accounted for by just six economies (Germany, Italy, France, UK, Belgium and Netherlands), slightly more than their share of regional GDP (70.7 per cent). The main thrust of any export-contribution to growth (net exports) will therefore come from these six economies and will have to be considerably greater than +2 per cent in order to compensate for the decline in both domestic demand and intra-EU trade. Net exports of the same order as Germany’s postwar average of some +3.2 per cent (1950–1980) would be required over an extended period to achieve this objective; even if such a strategy were considered desirable, its feasibility is very questionable.

- There is an assumption in the growth-through-trade logic that – in terms of extra-EU trade and payments – the EU27/EU17 is a unitary ‘actor’ where the standard dynamics of neo-classical international economic relations apply, i.e. there is a rebalancing of those relations towards equilibrium via the current account, the capital account and the exchange rate through the operation of open markets. That is, both Europe's problems of competitiveness and its growth weaknesses can be addressed by providing easier access for the EU's exported goods and services. There are several problems with this assumption, not least that the EU's aggregate external balances and aggregate growth rate are the primary measures of success when assessing the region's performance and the quality of the Commission's crisis management. While it might be possible to exploit hitherto untapped demand for European goods, there should be no illusions about either the likely beneficiaries of such demand (namely the core states noted above) or the predominance of high-grade industrial goods in such trade (vehicles, chemicals, electro-technical goods), again originating within the so-called 'blue banana').[9]

- An undifferentiated policy of growth through further trade-liberalisation reflects, above all, the critical neglect of *intra-EU/intra-eurozone trade and payments asymmetries* as fundamental features of Europe's structural problems. These and other asymmetries were ignored by the authors of the Maastricht Treaty in 1992, of the Stability and Growth Pact in 1997 and of the Fiscal Compact of 2012. The 'design faults of the European Monetary Union' (Arestis and Sawyer 2011) and to a lesser extent of the Single Market are rooted in large measure in this neglect and in the faith that such asymmetries are resolved through the operation of 'efficient' markets. The, now deeply entrenched, regional crisis triggered by the collapse of the global financial system in September 2008 has exposed both the huge disparities in external economic balances (Figure 1.11) and the folly of neglecting their macro-economic effects on the part of both the Commission and major member states, particularly in relation to the evolution of interest rate spreads on sovereign bonds (Figure 1.12).

[9] The 'blue banana' denotes the strip of highly urbanised, highly industrialised territory stretching from the North-West of England through France, the Benelux, western Germany, to northern Italy and which accounts for a high proportion of both industrial production and industrial and commercial innovation in Europe; machinery and transport equipment exports constitute a full 42.2 per cent of all extra EU-27 exports, with manufacturing accounting for 82.6 per cent (Figures from Eurostat 2011: 56).

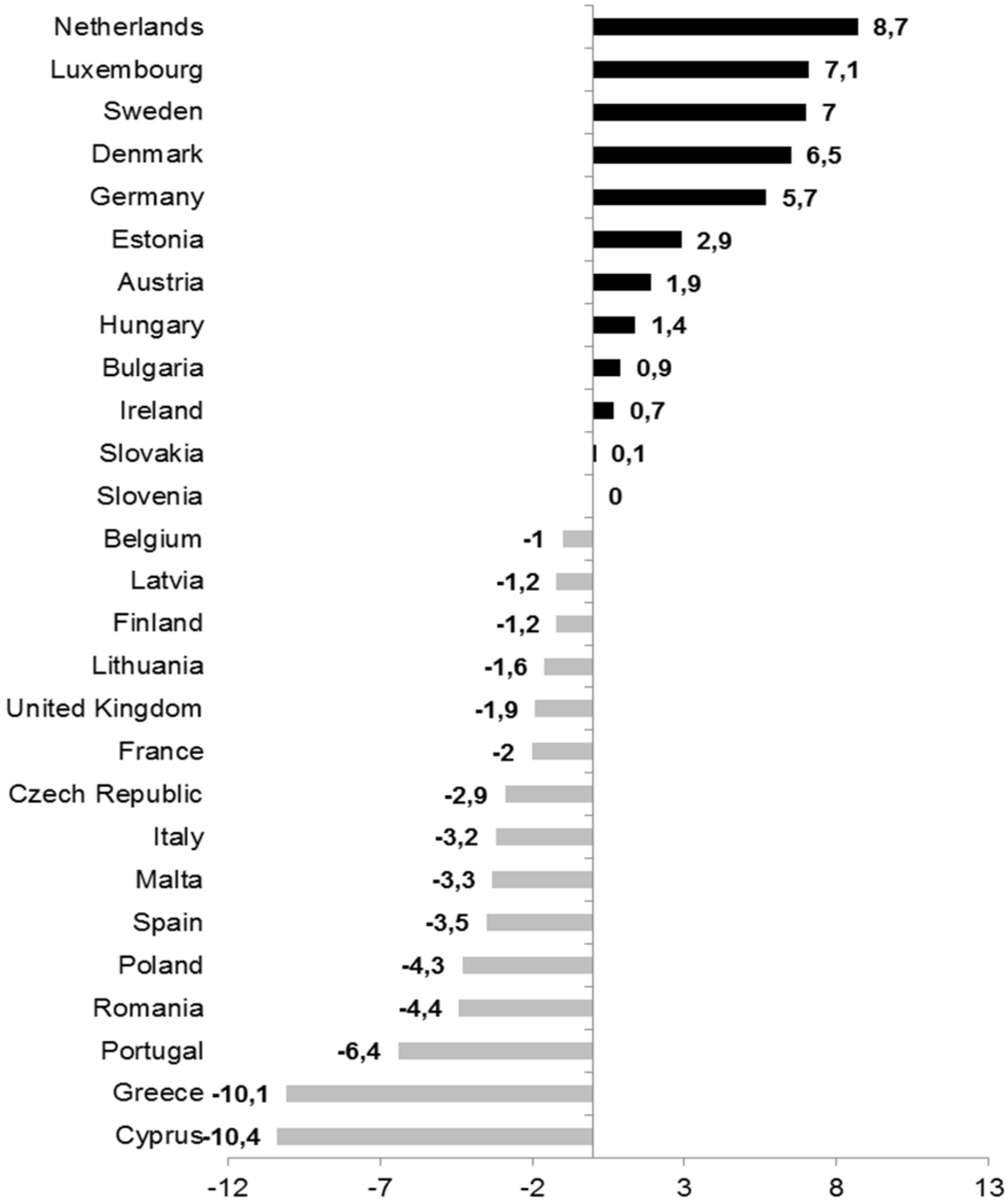

Figure 1.11 EU27 current account balances as a percentage of GDP 2011.

Source: Eurostat: European Union balance of payments [bop_q_eu]

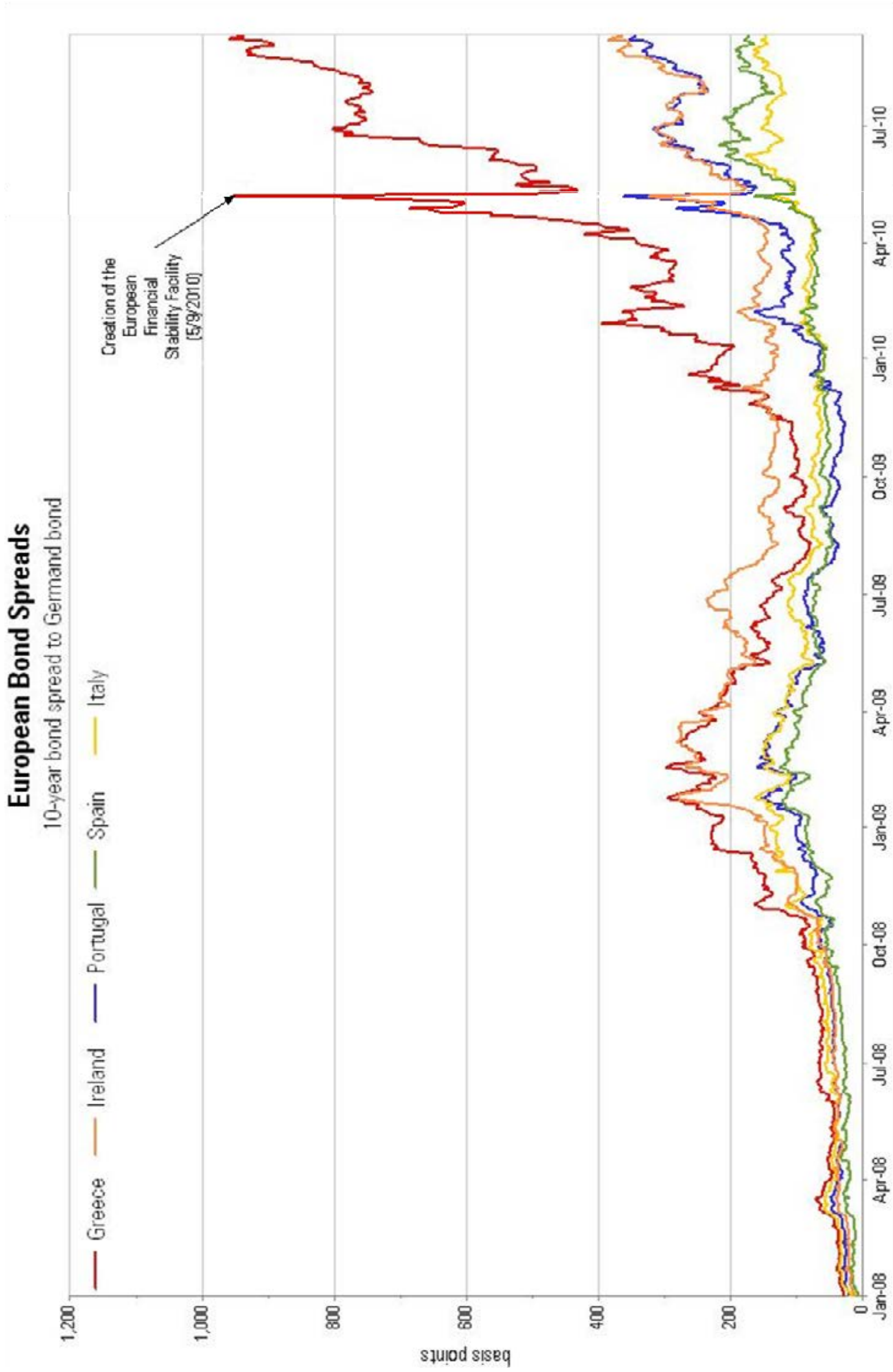

Figure 1.12: The divergence of interest rates on fixed interest sovereign bonds 2008–10.

Source: Econweekly, 10 September 2012

- 17 out of the EU's 27 member states have significant trade deficits; 15 member states have serious-to-chronic current account deficits and five member states have chronic current account surpluses (Netherlands, Luxembourg, Sweden, Denmark and Germany).

> With 9 deficitary states locked into a monetary union with key states with chronic surpluses (Germany and the Netherlands), their competitive disadvantages (of lower productivity and higher rates of inflation) cannot now be neutralised by exchange rate adjustments. Furthermore, those competitive disadvantages are amplified, firstly, by the need to balance current account deficits through the capital account, by persuading foreign investors to purchase sovereign bonds, secondly by both the upward pressure on interest rates and the associated speculative attacks on bond-related derivatives markets and thirdly by the down-grading of the sovereign bonds of individual countries by credit-rating agencies (EuroMemo Group 2012: 32).

Figure 1.12 indicates the extent of the problem of bond-spreads for the eurozone and the rest of the EU from an early stage in the global crisis. Where pre-crisis spreads of Greek sovereign bonds against 10-year German Bunds had fallen to as low as 10–30 basis points (Tavlas, Hall and Gibson 2011: 6), 2009 saw an early destabilisation of the bond market, with spreads stretching to 300 basis points in the Spring, with later spikes in the winter of 2009–10, exceeding 900 basis points (9 per cent) in May 2010. From the outset, there were proposals for the issuance of common Eurobonds[10] as a means of preventing the destructive effect of wide bond spreads on sovereign borrowing costs and overall sovereign debt. All such calls have been resisted, in particular by the recent German centre-right coalition government under Angela Merkel. While the various stabilisation measures adopted by the EU (European Financial Stabilisation Mechanism, European Financial Stability Facility, European Stability Mechanism) have achieved a marginal narrowing of spreads, the overall damage inflicted on the Greek, Portuguese, Spanish and Italian economies by higher-than-necessary borrowing costs and by pro-cyclical conditionalities, attached to EFSM. EFSF and ESM loans, provides overwhelming evidence for the culpable dilatoriness of policy-makers in addressing the structural asymmetries summarised above. Münchau (2011)[11] talks rightly of 'financial illiteracy'.

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[10] See, for example W. Münchau 'The benefits of a single European bond', *Financial Times*, 25 January 2009.

[11] W. Münchau 'The only way to save the Eurozone from collapse', *Financial Times*, 13 November 2011.

Export-led growth, flanked by domestic deleveraging – of households, enterprises and states – is indeed a highly questionable strategy. Raghuram Rajan, former chief economist at the IMF, describes this strategy as one of the major 'fault lines' of the global economy in recent decades, in particular as it relates to states like Germany that have deliberately depressed domestic demand to optimise their international competitive advantages (Rajan 2010: 46–67). In particular the accelerated erosion of public investment in particular crisis-hit countries, like Spain, Greece and Portugal will compound their competitive disadvantages and postpone the economic convergence of peripheral economies that is the precondition for the survival of the European project. In Spain, government spending on R&D is reported to have been cut by 40 per cent since 2009, reinforcing a brain-drain scientists and technicians[12], mirroring similar developments in Greece (Trachana 2013) and Portugal (Caldas 2012). There is a grim irony to such death-blows to the 'Lisbon Strategy'.

End the tyranny of neoliberalism

In an interview with the German daily, *Die Welt*, the former president of the German Bundesbank, Helmut Schlesinger, suggested that the money issuance of the European Central Bank had reached 'dimensions that are reminiscent of war-financing' but unprecedented (and by implication unacceptable) in peacetime[13]; accordingly he warned of serious inflationary consequences for the German and European economies. The *war analogy*, designed by Schlesinger to ridicule the irresponsibility of the ECB and its departure from Bundesbank virtues, is in fact much more appropriate than he would ever be prepared to concede. The analysis above has attempted to demonstrate that the neoliberal paradigm (deregulation, financialisation and monetary accumulation) generated a two-fold destruction of value, akin to the devastating effects of war, with neoliberal austerity currently threatening a further period of destruction and depression. The dilution of social wealth since 1980 operated hand-in-hand with the most profound redistribution of income and wealth in modern times, generating serious *diseconomies* for current and future

12 'Brain Drain in Spain leaves scientific research on the wane', *Financial Times*, 14 June 2013.

13 'Das erinnert an die Kriegsfinanzierung', *Die Welt*, 13 March 2012, retrieved from: <http://www.welt.de/print/wams/wirtschaft/article13915232/Das-erinnert-an-die-Kriegsfinanzierung.html> (last accessed 8 October 2013).

generations, even before 2008. Counterfactual estimates would suggest that the well-being of future generations could have been better ensured if the investment ratios and wages ratios of advanced states had remained at their 1980 levels, indeed that their maintenance would have been reciprocally strengthened with the parallel improvements of productivity, wages and consumption. The factual destruction of potential value in the processes of financialisation and the sharp decline in public investments between 1980 and 2008 precedes and pre-programmes the factual and inevitable disaster of both the systemic collapse of monetary accumulation in the winter of 2008/2009 and the subsequent hapless attempts to manage the crisis.

The alarming estimates of potential permanent global output losses of up to $200 trillion – with current annual global GDP at around $78 trillion – do not actually begin to illustrate the challenges facing world policy-makers, particularly in the advanced economies. *Recovery from the cataclysm of the Second World War involved arguably fewer strategic challenges than the current mess*. For example, the evident need, after the War, to make good the colossal physical damage to commercial, domestic and public property, to urban infrastructures, to national and international transport networks, was combined with a state-welfarist policy consensus and a profound preparedness to cooperate within and between nations which allowed a rapid transition to growth and prosperity in the 1950s. This was reinforced by the emergence of both consumerism and the technical-managerial means (Fordism) to satisfy the burgeoning demand of increasingly affluent households. The *2008 crisis manifests none of these auspicious pre-conditions for recovery and reconstruction*:

- There are no general physical signs of a catastrophe to be remedied;

- There is no shared acknowledgement of the unnecessary follies of the neoliberal paradigm as there was of the need to reverse the (unavoidable) privations of war;

- There is no shared diagnosis of the causes and extent of the crisis; there have been no mass resignations from the Economics departments of universities and research institutes in OECD countries; there is no self-evident replacement for a discredited system;

- There is significantly no overwhelming need for a marked increase in consumer goods provision – saturation of markets and unpredictable elasticities of demand predominate;

- There is, above all, no common view about the need for an increase in the provision of public goods, even if an increasing number of voices are raised in support of public goods as vehicles for general human progress.

Policy options

There are new debates emerging about the nature of economic and social relations and in particular about the need for greater equity and 'fairness', and a central role for an active state. The continuing mobilisation of such forces and an intensification of public debate within and across borders is an urgent priority. A number of stark policy-options suggest themselves from the analysis above. These run counter to the policy preferences, currently being pursued by the European Union. The obsessive attachment of Brussels to the German 'model' of export-led growth and deflation on the one hand, together with its inexplicable thraldom to the wisdom of credit-ratings agencies and major banks, threatens to condemn Europe to an extended period of stagnation, protectionist nationalism and political fragmentation. The early signs of multi-lateral coordination within the G20 have all but evaporated, weakening one essential pre-condition for effective crisis management. If, however, the 'rebalancing' of Europe – as proposed in this paper – is to be achieved, and the destructive tyranny of neoliberal recipes undone, certain basic policy options would seem to be essential:

- **Regulatory Control and Limitation of Banking:** Given the dilution and destruction of value resulting from the irresponsible neoliberal experiment with financialised capitalism and the equally hazardous roll-back of the state, there is an increasingly strong case for the (temporary) *public control of the commanding heights of finance capital* as a means of restoring a modicum of allocatory good sense to the reinvestment of social wealth as a real basis for sustainable human development, along with a much higher level of legitimacy. Political economies that seek to promote the welfare of all of their citizens simply cannot afford financial services that are predominantly *self-serving*, which divert corporate reserves into value-destroying Ponzi-style 'financial investments' away from value- and welfare-enhancing real investments. They cannot operate effectively with a sector whose total balance sheets, as in the case of the UK, grew from just 50 per cent of GDP to 500 per cent of GDP between 1970 and 2008. Financial services essentially need to be returned to the service function of collectively beneficial and controllable circuits of investment, production and consumption.

- **Fairer Distribution:** Additionally, *policy-makers in advanced economies need to address the critical disparities of distribution within the future context of far lower and far less predictable trend-growth*; learning to cope with weak or zero quantitative growth while allowing poorer economies to converge towards a sustainable level of qualitative growth is arguably the most critical task facing post-crisis societies.

- **Public Goods:** Within qualitative growth scenarios, likewise, *the role of public goods in the broadest sense* (health, education, legitimacy, social inclusion, distributional equity as public goods) will inevitably become more rather than less significant, in line with Wagner's Law of state tax ratios rising with levels of civilisation. Central to this strategy is the restoration of a strong programme of public investment.

- **Realistic Rates of Return**: A further challenge to all participants in the recalibrated political economies of the OECD and of Europe is to overcome the structural addiction to unrealistic rates of return that have too long informed the investment strategies of the managers of sovereign wealth funds, pension funds and other investment funds and, by implication, generated the exaggerated management fees extracted from Ponzi-style investment vehicles. Above all, the current and future sustainability of retirement pensions will have to become increasingly the subject of general distributional debates within society concerning their intergenerational equity, rather than of intra-fund adjustments.

- **Deficit-Spending and/or Monetisation as Necessity**: The current contradictory trajectory of European states and their pro-cyclical strategy of growth through austerity (!), represents a public 'bad' which needs to be reversed as a matter of extreme urgency. The analysis above has attempted to demonstrate that the cumulative crises that have hit Europe since 2008 represent more intractable problems than those facing states in the reconstruction period after World War II. *The levels of sovereign debt in Europe generated by the 2008 crisis are accordingly by no means extraordinary by historical comparison*. The UK's sovereign debt in 1948 was 237 per cent of GDP, that of the Netherlands and Belgium 223 and 118 per cent respectively.[14] It took some 20 years before the debt of these states fell to Maastricht-compliant levels; expecting the EU17/EU27 to achieve these levels by 2013 indicated monumental stupidity. Against the background of the critical asymmetries generated by the neoliberal paradigm and the consequently greater challenges of promoting debt-reduction via growth, the case for tolerating higher levels of debt in the medium term to avoid even greater economic asymmetries and the collapse of the European project, is thus overwhelming, as is the case for Eurobonds within the eurozone. Beyond the simple toleration of debt- and deficit-ratios, however, there is growing momentum within both heterodox and, now, orthodox circles for more radical solutions to Europe's New Depression. These include:

- The **debt jubilee** idea, proposed by economists like Steve Keen (2009)[15] and Willem Buiter[16], and popularised by a number of financial journalists, e.g. Evans-Pritchard (2009)[17]; this proposal proceeds from the (correct) assumption a) of the impossibility of all economic actors in advanced economies deleveraging simultaneously without inducing long-term stagnation, and b) of the primary culpability of financial institutions in generating historically record levels of private debt. The 'jubilee' involves finance ministries (via central banks) financing the wholesale repayment of private debt by means of unsecured money issue as

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14 Reinhart, C. and Rogoff, K. (2012) 'This Time is Different: Eight Centuries of Financial Folly', Statistical database, retrieved from: <http://www.reinhartandrogoff.com/data/> (last accessed 13 August 2013).

15 See also 'Steve Keen on BBC Hardtalk', retrived from <http://www.youtube.com/watch?v=rGkmgnprrIU&feature=player_embedded> (last accessed 13 August 2013).

16 Buiter, W. (2009) 'Quantitative easing, credit easing and enhanced credit support aren't working; here's why', *Financial Times*, Willem Buiter's Maverecon, 3 July 2009, retrieved from: <http://blogs.ft.com/maverecon/2009/07/quantitative-easing-credit-easing-and-enhanced-credit-support-arent-working-heres-why/#axzz2r8j6hFl0> (last accessed 13 August 2013).

17 A. Evans-Pritchard 'Biblical debt jubilee may be the only answer', *The Telegraph*, 19 January 2009.

the most effective means of neutralising the current paralysis of financial circuits and encouraging growth via debt-free consumption and investment. Keen, who is strongly influenced by Hermann Minsky, asserts current crisis-management measures are entirely inadequate to cope with the colossal (and underestimated) scale of the crisis, equivalent to 'bailing out the Titanic with a thimble' (2009: 3). It arguably remains a question of faith, how the transmission belt of debt-forgiveness will function in revivified circuits of consumption, investment and finance, but the radical diagnosis is certainly apt, as is the perception of an urgent need to constrain speculative finance (*ibid*.: 21).

- A related but arguably more refined policy-prescription involves the creation of so-called **helicopter money** or the selective monetisation of government expenditure. This example of 'thinking the unthinkable' has been strikingly popularised by the *Financial Times*, in particular Martin Wolf)[18] and by the outgoing chairman of the UK Financial Services Authority, Adair Turner. Turner in particular takes issue with Germany's obsession with hyperinflation and its neglect of Brüning's depression economics and its ushering-in of fascism: 'Is [monetary financing] desperately dangerous because every pound of money financed turns into inflation? Absolutely not. There is no coherent rigorous bit of economics that takes you in that direction'[19]. In contrast to the debt jubilee stimulating private demand, the monetisation proposals behind helicopter money tend to focus on state-managed, targeted investment projects in infrastructure and other public goods. McCulley and Poszar (2013) provide the most coherent and persuasive argument for both helicopter money and for a more decisive coordination of fiscal and monetary policy as vehicles for

[18] M. Wolf 'A Case to Reconsider the Basis of Monetary Policy', *Financial Times*, 8 February 2013; M. Wolf 'The Case for Helicopter Money', *Financial Times,* 12 February 2013. See also 'Helicopter Money and Supply Siders', *Financial Times* (Editorial), 6 February 2013.

[19] 'Print money to fund spending – Turner', *Financial Times*, 6 February 2013, retrieved from: <http://www.ft.com/intl/cms/s/0/1be21d54-6fb5-11e2-956b-00144feab49a.html#axzz2hmaRZauF> (last accessed 15 October 2013). Wolf, M. 'The Case for Helicopter Money', *Financial Times,* 12 February 2013, comes to a similar conclusion: 'I fail to see any moral force to the idea that fiat money should only promote private spending'.

recovery; they also provide convincing arguments to demolish the inflation-fears of German and other opponents of monetisation.

Reconfiguring economic governance in Europe: public goods, taxation and the state

In December 2008, it seemed as if at least one practical lesson had been learned by both policy-makers and civil society, namely that the role of the state was, contrary to the prejudices of the preceding 30 years, central to the survival of capitalism and the continuous management of its deficiencies. The deployment of colossal volumes of public resources to provide life-support to national financial institutions as well as international networks of banking and payments, should at least have laid to rest the delusion of 'the' markets' self-healing properties. The call for decisive political action, for international cooperation and coordination was deafening; the response of EU, G7, G20, the Federal Reserve, the European Central Bank, Bank of England, the World Bank and the IMF was admirably urgent. National, international and supranational governance and re-regulation was seemingly acknowledged as pre-conditions for recovery. By the same token, the financing of salvage operations for banks and of counter-cyclical stimulus packages via budget deficits enjoyed at the very least the tacit support of the economic elites and the citizens of the advanced economies.

However, despite such auspicious beginnings, 2009 saw the rapid return of what Richard Murphy has recently coined 'the cowardly state' (Murphy 2011) with the re-assertion of the primacy of deflation and debt-consolidation among key EU states and at Commission level. The opportunity to reflect on failure and alter course has thus been woefully squandered, raising the suspicion that a neoliberal policy-elite is indeed using the opportunity to 'finish the job', to complete a pan-European neoliberal strategy (Buckel *et al.* 2012: 30ff) and weaken European social provision even further as a supply-side inducement to retain the loyalty of capital (Lehndorff 2012: 24).

The 'competitive state' (Hirsch 1995) is the opposite of the activist state of New Deal Keynesianism; it is not even the ordoliberal state, pursuing national mercantilist goals, but the subaltern set of institutions within an interdependent network, controlled by transnational capital as a hierarchised historical bloc. The capture of

Europe's advanced states by transnational capital epitomises Huffschmid's notion of 'deformation'. Replacing these deformed structures of governance Europe-wide with new institutions of collective, multi-level democratic control with strong commitments to harmonised principles of active and socially just fiscal policies is the fundamental challenge for this and future generations of European civil societies. The obstacles in the way of both salvaging what is left of 'social Europe' are considerable and have been multiplying since the aggressive reassertion of pro-cyclical, neoliberal debt-reduction programmes in 2009. What is also becoming increasingly evident is that the challenge is one of a fundamental, socio-cultural nature, made particularly problematic by the capitulation of many established, social democratic parties to key tenets of the neoliberal revolution; indeed the capture of these parties and of significant sections of both electorate and civil society by interest-driven media campaigns and their sanctification of consumerism and individualism helped to generate new waves of expectation in relation to lifestyle, income, expenditure, pensions which were critically dependent on Ponzi-style capitalism. These effects have survived the collapse of the latter and, at the very least, interfere with processes of reflecting on and recalibrating those lifestyles. The competition states of Europe have, through their collective powerlessness and their separate degrees of national failure, also contributed to a weakening of faith in conventional democratic politics, where resignation and cynicism would seem to be stronger than reflective, dynamic opposition to the historical bloc, even if that opposition is growing.

The neoliberal programme of crisis management is set to intensify the competition between member states as they dilute further their provision of public goods, services and social security; the 'race to the bottom' is accelerating (Genschel *et al.* 2011). Hitherto, this 'location competition' has increased the disparities in the external balances of the EU, in particular within the eurozone, with German current account surpluses growing in relation to most other member states (Lehndorff 2012: 92). The demand and supply asymmetries between eurozone members are mirrored by the shift in demand structures in individual countries, with weak domestic demand in Germany offset by increasing dependence on export demand as a vehicle for growth. Further demand asymmetries have been generated by the growing disparities in income distribution.

Persisting with the German 'model' will exacerbate rather than alleviate these asymmetries. Rebalancing them is a precondition to European recovery. A precondition for altering course is the *refining and radicalising of politico-economic discourse in the civil societies of all member states*. This requires, at the very least, a *coalition of forces against neoliberal orthodoxy and the influence of transnational capital*. The initial primary focus of this coalition must arguably be the restoration/creation of the active fiscal state which redistributes social resources for the benefit of the overwhelming majority of its citizens – the 99 per cent as the central banner of the Occupy movement suggests. Fiscal rebalancing has to be rooted in a *European consensus about the very purpose of taxation*. Annamaria Simonazzi summarises the challenge correctly as an educational task:

> The understanding of taxes has to be linked to the understanding of services: people have to learn again, that it is their health, that it is education, kindergartens and the care of the elderly, that they pay for.
>
> (Simonazzi 2012: 194)

Currently, the absence of a serious revenue dimension to fiscal harmonisation represents Europe's greatest structural deficiency in policy-making; monetarist strictures about debt and expenditure predominate. One of the few successful initiatives in the direction of tax harmonisation – the European Savings Directive – has been fatally weakened by the bilateral tax deals between Switzerland and two of the EU's major neoliberal strongholds, the UK and Germany. A sensible point of departure for a broad, pan-European opposition to the destructive effects of such wilful beggar-thy-neighbour policies and the EU's historical failure to promote tax harmonisation (Leaman 2012a) would include the elements outlined below:

Box 1.2 Towards a new fiscal consensus in Europe

1. A Fiscal Union and Settlement Union of the EU17 based on the long-term commitment to eradicating poverty, unemployment and social exclusion; as a Settlement Union the eurozone would deploy its resources collectively to ensure the relative convergence of external balances, of national and regional ratios of investment, private consumption and public consumption to GDP against the condition to outlaw fiscal free-riding with the abolition of tax and regulatory competition and a relative

convergence of states with low tax ratios (see Ireland, Greece, Portugal) to a higher average.

2. A constitutional rearrangement of Europe's policy architecture, removing the democratic deficit of an autonomous, unanswerable European Central Bank, establishing the obligation for policy coordination between fiscal authorities and monetary authorities and a policy brief based on economic, social and environmental sustainability.

3. The Fiscal Union of the EU17 would allow deficit-spending for anti-cyclical purposes and for structural modernisation, without the imposition of arbitrary ceilings to deficits or overall debt (no Debt Brake!) and with mutually assured Eurobonds.

4. Fiscal harmonisation within the EU27 which ends tax competition, establishing minimum standards for direct and indirect taxation, maximising transparency, automatic information exchange and compliance-policing:

   - Agreed minimum rates of personal income tax (PIT) and corporation tax (CT);
   - Commitment to the principle of progressive income taxation (phasing-out of flat-tax regimes and relative convergence of scales of progression);
   - A Common Consolidated Corporate Tax Base;
   - Country-by-Country reporting/Publish What You Pay;
   - Formulary Apportionment associated with CBCR;
   - Restriction of national variations of special allowances on both PIT and CT to the purposes of rectifying current account asymmetries and productivity disparities;
   - Outlawing of European tax havens/secrecy jurisdictions;
   - Boycott of financial corporations and other companies operating 'brass plate' business in overseas tax havens;
   - Tax avoidance to be made as ethically unacceptable as human trafficking.

The restoration of a strong and well-resourced fiscal state represents a *minimum consensus* around which progressive forces in Europe could and should be mobilised. On these foundations, the obstacles to sustainable social development could be removed and the objectives of a courageous, activist state could be addressed. The removal of the legal, institutional and organisational pillars of neoliberalism – as the historical means of social and economic 'deformation' – would be as radical as the original Thatcherite 'revolution':

- The public ownership of utilities as natural monopolies should be restored and other sources of monopoly rents (Private Finance Initiatives, e.g.) eliminated. The provision of water services, public transport, power distribution, health, education and social welfare as public goods is the natural function of the public sector; the commodification of those services as a vehicle for the direct valorisation of capital is incompatible with a society committed to collective responsibility for the welfare of its citizens, based on solidarity, social justice and democratic legitimacy. The recent accelerated privatisation of public utility companies and service providers as a condition for EU assistance for states with temporary sovereign debt problems (Greece, Portugal) must be reversed; securing comfortable income-streams from monopoly franchise/supply operations inflates rate-of-return expectations and reduces entrepreneurial incentives to invest in commercial activities that are subject to market pressures.

- The on-going paralysis of commercial investment in many EU countries is in part informed by the distortions in profit expectations generated by 30 years of neoliberal privatisation. This paralysis furthermore demands a long-term role for the public sector in underpinning national and regional investment demand and has consequently informed a number of proposals by progressive economists for the establishment of *state-owned investment banks* to fill the void left by coy private banks (Murphy 2011: 274ff) and for the European Investment bank to fund infrastructure projects (EuroMemo Group 2010: 4, 40; EuroMemo Group 2011: 3, 34); state investment banks would be financed directly by central banks, by-passing the hitherto fruitless and dubious route involving liquidity injections into private banks.

- The third key function of the active state is to counteract the pernicious redistribution of income and wealth that has characterised the neoliberal era; this cannot simply involve the secondary transfer of state resources to produce a less inequitable distribution of net incomes, but *must also address the more critical* *and growing disparities of market incomes*; the record of the UK Labour government (1997–2010) demonstrated the haplessness of an anti-poverty strategy that neglected the central function of market distribution, deploying colossal volumes of state transfers merely to prevent a further rise in an already high Gini coefficient (see Leaman 2013). Fiscal transfers play an important but secondary role, compared to statutes of industrial and employment law which allow productivity increases and profit growth to be reflected in the growth of real wages. Ending the destructive tyranny of neoliberalism represents a colossal challenge, not just in the mechanical delivery of a radical new policy-mix, but above all as an intellectual and cultural learning-process. Such change cannot be delivered by an insurrectionist vanguard in individual nation-states, but by a broadly-based, well-informed, dynamic coalition of progressive forces operating at a variety of levels – local, regional, national, global, virtual. We need such a coalition to ensure that we bequeath our grandchildren halfway adequate foundations for decency, justice, sustainability and coexistence.

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Chapter 2

Legitimacy intermediation in the multilevel European polity and its collapse in the eurocrisis

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Introduction

European integration has created a multilevel polity in which governing powers are exercised at the European, national, subnational and local levels. But whereas in EU member states there is generally a clear hierarchical relationship in which the political and legal bases of legitimate authority at the national level dominate those at the regional and local levels, the relationship between the EU and its member states is much more ambivalent. European law, it is true, claims supremacy over all national law, but EU political legiti-

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macy seems to be highly problematic: failed constitutional referenda, low and falling voter turnout at European elections, an absence of public debates about European policy choices, but also increasing resentment of EU interference in national policies and institutions and continuing worries about a 'European democratic deficit'. These issues are coming to a head in the present eurocrisis, which seems to challenge not only the viability but also the legitimacy of the existing architecture of governing in the multilevel European polity. This chapter attempts to respond by confronting the dual traditions of legitimacy discourses in Western political theory with the governing structures of the existing European polity, and with their incipient transformation under the challenges of the present crisis.

Legitimacy discourses

Legitimacy is a normative and highly contested concept. Its pragmatic importance in political systems is best clarified from a functional perspective (Scharpf 1999): in exercising their powers, governments must claim resources and constrain actions in ways that will often conflict with the interests and political preferences of their subjects. As a consequence, compliance must be an underlying problem in all political systems. It may be brought about through coercion, based on credible threats, effective surveillance and punishment; or it may be brought about through inducements, based on credible promises and attractive rewards. Coerced and induced compliance do indeed play a role in all political systems. But government will be oppressive, ineffective and wasteful where these mechanisms play more than a supportive role in stabilising a general pattern of voluntary compliance that is not based on the explicit cost-benefit calculations of self-interested subjects.

Most of the time, of course, law abidance is habitual. But when the discrepancy between required behaviour and personal interests and preferences increases, and when low-risk opportunities for evasion exist, legitimacy beliefs may become a crucial factor contributing to the voluntary compliance with undesired rules or decisions of governing authority (Easton 1965: 278–319; Kielmansegg 1971; Beetham 1991; Scharpf 1999, 2007; Höffe 2002: 40). Such beliefs, however, are not primarily a matter of individual consciences. To create a sense of moral obligation and to provide justification for the 'losers' consent' (Anderson *et al.* 2005), they need to be socially shared and reinforced through justifying narratives and discourses. Where they are effective, they will reduce the need for and the cost of controls and of negative or positive sanctions that would otherwise be needed to ensure compliance. In other words, socially supported legitimacy beliefs should be seen as a functional prerequisite for the existence of governments which are, at the same time, effective, efficient and liberal.

But before turning to the substantive discourses supporting legitimating beliefs in Western political systems, I need to introduce three conceptual presuppositions which I will use in subsequent discussions without being able to fully develop and justify them in this paper. The first concerns David Easton's (1965: ch. 10) *hierarchy of legitimating references*. Support for a political system may relate to the characteristics of the *authorities* exercising acts of government, to the characteristics of the political *regime* that empowers these authorities, or to the characteristics of the political *community* that is governed through this regime. The implication is that potential noncompliance may be countered not only by arguments justifying the specific *policy* in question but also by arguments asserting the legitimacy of higher levels of the political system in question. But there is also a reverse implication which will play a role in my discussion of legitimacy in the multilevel European polity.

Second, if the function of legitimacy is to ensure the acceptance of unwelcome acts of government, it also follows that the *need for legitimation* increases with the severity of the sacrifices imposed and/or the political salience of the issues at stake. If policies match my interests and preferences, my compliance does not depend on legitimating arguments. On the other hand, normative appeals will also vary in their *legitimating capacity*. Thus, where vital interests and deeply held normative convictions are at stake, very powerful arguments may need to be invoked if potential defectors are to be persuaded to refrain from noncompliance, civil disobedience or violent protest. In other words, legitimacy should be understood as a *relational concept*, rather than as an invariant characteristic of policies or polities. This will also play a role in the later discussion of the alleged European democratic deficit.

Finally, I will also refer to the distinction between *input-oriented and output-oriented* legitimating arguments (Scharpf 1970, 1999; M.G. Schmidt 2008; Ruffing 2011). These concepts resonate with discussions of 'representative and responsible government' (Birch 1964; Mair 2008, 2009) or of governments as 'agents' and as 'trustees' of the people (Alter 2008). What matters, in other words, is the *responsiveness* of governors to the collective preferences of their constituencies and their capacity to serve the *common interest* of the political community in accordance with its norms and values. From a historical and intercultural perspective, the arguments invoked in legitimating discourses vary widely. In the specific context of constitutional democracies in the European Union, however, their premises and implications may be elaborated and clarified through reference to the core arguments of two distinct traditions in Western political philosophy – for which I will use the labels 'republican' and 'liberal'.[1] Whereas the former emphasizes the common good of the polity and the collective self-determination of its citizens, the latter highlights the protection of individual rights and the need to base the exercise of governing powers on the consent of those who are affected.

The republican discourse

Republicanism is rooted in the Aristotelian tradition – whose contemporary vitality is manifest in the communitarianism of Alasdair MacIntyre (1984, 1988) or Charles Taylor (1992) and others.[2] Here, man is understood as a *zoon politikon* who could not exist in isolation and who can only grow to realise his own intrinsic *telos* within a *politeia* that provides the preconditions for the *eudaimonia* of its members. In that sense, the polity is prior to the individual (Aristotle 350 B.C. [2007]: Book 1, 1253a). In order to realize the common good – which is the precondition for the good life of its members – the polity needs to be governed, and it needs to be governed well. In principle, good government may be achieved in monarchic, aristocratic or democratic constitutions – but each of these is also vulnerable to characteristic perversions if the powers of

[1] In the literature, these labels are not used consistently, and contemporary discussions of democratic legitimacy tend to combine arguments derived from both traditions. I hope to show, however, that it is theoretically and pragmatically useful to identify the distinct logics of these discourses.

[2] This is not meant to deny differences within the tradition. Lovett and Pettit (2009), for instance, take pains to differentiate their own 'neo-republicanism' from the communitarian literature – and within the former camp, 'neo-Athenian' and 'neo-Roman' positions will also differ on some points (Schäfer 2011).

government are employed to serve private or partisan advantages. Given the overriding importance of the common good, however, the remedy could not be constraints on the powers of government. Instead, Aristotle's focus is on the need for virtuous governors and on conditions and institutional arrangements that would favour their selection and continuing commitment to the common good of the polity (Aristotle 350 B.C. [2007]: Book 3).

From his output-oriented focus on the common good, Aristotle, who like Plato was unimpressed by the performance of Athenian direct democracy during the Peloponnesian War (M. G. Schmidt 2008: 41–43), saw little reason to place higher trust in the continuing virtuousness of citizens (in the role of democratic governors) than in that of aristocrats or monarchs. On balance, he thought that orientation to the common good might be most secure in a mixed constitution that combined elements of democracy and aristocracy. But if there was to be democracy, the common good would require the free and equal participation of all citizens (among whom women and slaves were not included) in public debates over the laws through which they would mutually govern each other (Aristotle 350 B.C. [2007]: Book 3; Book 6, 1317b).

The concern for the common good of the polity, the virtuousness of governors, and its institutional preconditions had also shaped the political philosophy of republican Rome. Going beyond Aristotle's institutional relativism, however, Roman republicanism rejected the option of monocratic power and insisted on civic participation in the mixed constitution of a self-governing *res publica* (Cicero 51 B.C.). A millennium later, the Roman aspirations reappeared in the Florentine Republic, where Machiavelli's *Discorsi* (1531[1966]) also reflected on the frailty of the virtues that were required for maintaining a *civitas libera* (Pocock 1975). From there, one branch in the history of political ideas leads to James Harrington (1656[1977]) and other 'neo-Roman' theorists of an egalitarian 'free commonwealth' during the short-lived English republic (Skinner 1998, 2008) who, in turn, had a powerful influence on the political thought of the American Revolution and on Jeffersonian and Jacksonian democracy in the early history of the Union (Pocock 1975; Dahl 1989: ch. 2; Pettit 1997). In contemporary Anglo-American political philosophy, these emphases on republican liberty, democratic self-determination and political community are of vital importance in 'neo-republican' as well as 'communitarian' discourses.[3]

The other branch in the history of republican thought leads to the democratic radicalism of Rousseau's *Contrat Social* (1762[2011]), which shaped the political thought of the French Revolution and continues to have a powerful influence on Continental democratic theory. With the classical heritage, Rousseau shares the primacy of the political community, the output-oriented emphasis on the common good, and the absence of institutional limitations on the powers of government (M. G. Schmidt 2008: 94). At the same time, however, he radicalises the aspirations of republican liberty, and his institutional preferences are shaped by the input-oriented practices of Athenian democracy. Liberty for all, in his view, could only be achieved through general laws which are determined by the equal participation of all in collective choices (*Contrat Social*, Book 1, ch. 6; Book 2, chs. 1, 4). His assumption was that such laws would be adopted by majority vote.[4] But then, as it had for Aristotle, the 'virtuousness' of citizens in the role of the collective legislators became the critical problem. For Rousseau this meant that the aggregate concerns of self-interested individuals (*volonté des tous*) needed to be transformed into common-interest oriented collective choices (*volonté générale*). Since – unlike the English and American 'aristocratic republicans' (Dahl 1989: 25–26) – he was unwilling to consider a non-egalitarian mixed constitution,[5] he had to restrict the potential application of his normative postulates to relatively small communities with a high degree of pre-existing social homogeneity (*Contrat Social*, Book 2, Chs. 8–10).

[3] Cf. Michelman (1989), Pettit (1997), Skinner (1998), Kramer (2004), Bellamy (2007), Lovett and Pettit (2009) on the one hand, and Walzer (1983), MacIntyre (1984), Taylor (1992), Sandel (1982, 1996) on the other.

[4] In fact, Rousseau anticipated the analytical argument of the 'Condorcet jury theorem' several decades before its publication: assuming that the common interest was objectively given, its identification may be equated to a search for truth. Since individual perceptions of truth may vary somewhat, the larger number of (sincere and independent) votes should identify the best approximation (Berg 1996; Grofman and Feld 2006).

[5] Equality, for Rousseau, was only required for the legislative function. The executive might well be monarchic or aristocratic.

That precondition, however, was obviously lacking when, after 1789, Rousseau's political philosophy came to shape the ideals of the democratic revolution in France. Nevertheless, in the subsequent evolution of representative democracy, the theoretical difficulty was pragmatically resolved by an institutional architecture which combined the medieval representation of estates (which Rousseau had rejected as unequal) with the egalitarian aspirations of democratic self-government (Pitkin 1972; Dahl 1989: 28–30), and could thus claim to satisfy the output- and input-oriented criteria of republicanism at the same time. Here, legislation was delegated to representatives who were expected to exercise their mandates as 'trustees' for the common interest of the community. But these mandates would be established and withdrawn through periodic general elections based on universal and equal suffrage – with the consequence that representatives could be held accountable for their exercise of governing powers by the electorate at large. Moreover, to ensure the common-interest orientation of legislative and electoral choices alike, policy-making and politics were to be shaped by continuous discussions in the public space of the political community (Habermas 1962; Elster 1998).

The liberal discourse

Republican liberty insists on the prevention of arbitrary or partisan rule, and basic individual rights and civil liberties are necessary preconditions for political participation and self-determination. Beyond that, however, the extent to which individual interest positions are to be protected is to be determined in the political processes that will define the common good of the community as well as the standards of justice and the reach of individual rights. In liberal political philosophy, by contrast, the normative order is reversed.[6] Here, the individual is prior to the political community, individual self-determination limits the domain of legitimate collective action,

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[6] In the words of Michelman (1989: 446–447): 'In a republican view, a community's objective, common good substantially consists in the success of its political endeavour to define, establish, effectuate, and sustain the set of rights (less tendentiously, laws) best suited to the conditions and mores of that community. Whereas in a contrasting liberal view, the higher-law rights provide the transactional structures and the curbs on power required so that pluralistic pursuit of diverse and conflicting interests may proceed as satisfactorily as possible'.

and the protection of individual interests takes the place of the republican commitment to a holistically defined common good.

These, at any rate, are the premises of the Anglo-American tradition of liberal political philosophy. Its roots do not go back to antiquity but, paradoxically, to Thomas Hobbes' efforts to justify the restoration of monarchical prerogatives after the English Revolution. To achieve this purpose, Hobbes had to attack the republican concept of liberty as freedom from domination (because it implied collective self-government) and replace it with the individualistic concept of liberty as freedom from interference (Skinner 2008). In a hypothetical state of nature, so the basic argument of the Leviathan (1651[1986]), this liberty was continuously threatened by the *bellum omnium contra omnes*. To escape from it, individual self-interest would dictate submission to a sovereign authority with unconstrained power to ensure the security of life, liberty and property of its subjects. From this remarkably unpromising start, however, liberal political philosophy – from John Locke (1690[1952]), Adam Smith (1776) and Jeremy Bentham (1789[1996]) to Friedrich A. Hayek (1960), Milton Friedman (1962) or Richard Nozick (1974) – has developed normative precepts which would continuously extend the domains of individual liberty and justify ever tighter constraints on the governing powers of the political community.

The intellectual and political success of liberal political philosophy was due, to a large extent, to its symbiotic co-evolution with classical, neo-classical and institutional economics. Sharing individual self-interest as their normative and methodological premise, liberal political theory and classical economic theory also converged in their conclusions: the republican concept of a holistically defined 'common good' was, of course, rejected. And while utilitarian welfare economics proposed to replace it by the maximisation of aggregate individual interests (Kaldor 1939), that solution is regarded as unacceptably collectivistic by libertarian political philosophers (e.g., Hayek 1976), who would only consider Pareto efficiency as a liberty-preserving criterion of legitimate political action. Moreover, where the republican tradition had considered virtuous government as a necessary precondition of societal and individual well-being, classical economic theory claimed to show that the 'wealth of nations' was brought about by the uncoerced (and morally unencumbered[7]) interactions of self-interested private individuals guided by the 'invisible hand' of free markets. And if individual interests in material well-being could be realised by the market, it was also possible to reduce the threatening omnipotence of the Hobbesian sovereign to those governing functions that were essential for the maintenance of external and internal security, the establishment and protection of property rights, and the enforcement of contracts. In other words, it was the symbiosis with classical economic theory that allowed liberal political philosophy to shift its focus from the republican concern with the preconditions of 'virtuous' government to institutional solutions that would reduce the domain of governing powers and constrain their exercise.

But that was not the only effect of the symbiosis. Given the Hobbesian switch to 'negative liberty' – understood as the 'freedom of pursuing our own good in our own way' (Berlin 1958: 11) – restraints imposed by governing authorities needed to be justified in all spheres. And since market interactions are considered to be voluntary by definition, and hence compatible with negative liberty, the sphere of legitimate government action is reduced to functions that could not be performed by the market. In other words, the correction of analytically defined 'market failures' is seen as circumscribing the domain of permissible public purposes. Even within this domain (which is generally circumscribed by welfare economics), however, the legitimacy of political choice is further challenged by the 'Public Choice' variant of libertarian political theory.

Just as the 'private vices – public benefits' logic of classical economic theory did not postulate virtuous economic actors, the Public-Choice theory of politics also does not base its expectations on the republican postulate of common-interest oriented governors. In the absence of an 'invisible hand', therefore, models assuming purely self-interested politicians, bureaucrats and citizens inevitably came to expect massive 'government failures' (Niskanen 1971; Buchanan 1986;

[7] Adam Smith, it is true, had introduced a moral philosophy based on 'sympathy' among the members of a community in his *Theory of Moral Sentiments* (1759[1976]). But the economics of his *Wealth of Nations* (1776[1999]) presuppose rational egotism and provide theoretical respectability for the 'private vices – public benefits' hyperbole of Mandeville's *Fable of the Bees* (1714[1957]).

Mueller 1989). And compared to these, even the market failures identified by welfare economics would often appear as the lesser evil. On the basis of these models, the normative political theory of modern liberalism generally supports the deregulation and privatisation of a wide range of state functions that had formerly been considered necessary remedies for market failures. Beyond that, radical libertarian theorists like Nozick (1974) and Hayek (1960, 1976) also challenge the legitimacy of redistributive government functions. They do not deny that even ideal markets may generate massive inequalities of wealth, incomes and life chances. But since (economic) theory cannot derive 'objective' standards of distributional justice from its models, all political attempts to correct market outcomes would be qualified as arbitrary and hence illegitimate interferences with negative liberty.

In institutional terms, therefore, the foremost concern of liberal political theory is to limit the potential reach of governing authority through the constitutional protection of individual rights. And where the need for governing powers cannot be generally denied, the liberal ideal is government by a consensus of the affected interests. Ideally, therefore, the decision rule ought to be unanimity (Buchanan and Tullock 1962). But since that is not usually practicable, liberalism's main concern is to prevent the 'tyranny of the majority' through the checks and balances postulated by James Madison in the *Federalist No. 51* (Madison *et al.* 1788[1961]), through super-majoritarian decision rules, multiple veto positions and pluralist patterns of interest intermediation (Truman 1951; Dahl 1967).

The ideological triumph of market liberalism has overshadowed a second tradition of liberal political philosophy, originating in the Continental rather than the English and Scottish Age of Enlightenment. Immanuel Kant's premises were as individualistic – and hence as anti-republican – as those of Hobbes, Locke and Adam Smith. But Kant's starting point in his *Grundlegung* (1785[1961]) was the moral autonomy of the rational individual, rather than the sanctity of individual self-interest. Finding himself (women were still not considered) with the capacity of reason, man must become aware of his own freedom and the concomitant duty to act on the basis of his own cognitive and normative judgments. But reason will also tell him that the same conditions apply to all other human actors as well, and that the exercise of his own freedom must be limited by the equal freedom of all others. As for Hobbes, therefore, the basic problem is the potential incompatibility of individual actions. For Kant, however, the solution cannot be the sacrifice of individual autonomy to the hierarchical authority of a sovereign. Instead, voluntary self-coordination can be achieved by reason itself – which, guided by the 'categorical imperative', will only allow the choice of actions whose maxims the rational actor could want to see established as a general law.

Assuming what game theorists call 'complete information', and allowing the even more heroic assumption that different actors will converge in their assessment of the normative appropriateness of particular rules of conduct, self-coordination through the categorical imperative might indeed work in a model world. But Kant is too realistic to ignore the 'crooked timber' of human nature – meaning the fact that individual action may also be driven by passions and self-interest, rather than being guided by pure reason. Hence the moral imperative by itself would not ensure the practical compatibility of autonomous actions. In practice, therefore, individual choices need to be constrained by binding laws which are so effectively sanctioned that they would work even for a 'society of devils'. But if these laws are to nevertheless approximate a state of universal freedom, they must be laws of general application and they must prescribe rules of conduct to which all who are affected should and could freely agree in their capacity as morally autonomous and rational actors. In other words, Kant moves the coordination problem from the level of individual action to the level of general rules, and he deals with the problem of normative convergence by moving from the un-coerced agreement of real actors to a criterion of virtual consensus.

In contrast to its Anglo-American sibling, Kantian liberalism did not develop in symbiosis with classical and neo-classical economic theory.[8] And since its basic criterion of legitimacy was the generality and consensual acceptability of binding rules, it also did not postulate

[8] It is true, however, that ordoliberal economists and lawyers, whose work was influential in shaping the normative foundations of a 'social market economy' in postwar Germany, did draw on Kantian philosophy for some of their precepts – for instance, for insisting on general competition rules rather than discretionary state interventions in the economy. See, e.g., Böhm (1950); Eucken (1960, 1969); Mestmäcker (1994); Schlecht (2000).

the existence of inviolable individual interests or impose dogmatic limits on the potential domain of governing functions. Thus John Rawls' (1971) search for criteria of distributive justice would be fully compatible with Kantian liberalism – but incompatible with Hayek's or Nozick's libertarian principles. Moreover, if my freedom excludes all choices that could violate the equal freedom of others, the categorical imperative could also justify very stringent restrictions on negative liberty. And as Isaiah Berlin (1958: 29–39) pointed out, the virtual-consensus test through which its meaning is to be ascertained may well depend on information and analyses for which ordinary citizens or democratic majorities seem poorly qualified and which might thus be best left to the vicarious judgment of experts. In other words, like Rousseau's republicanism, Kantian liberalism also has an authoritarian dimension and it may be invoked to legitimate laws that depart widely from the empirical preferences of ordinary citizens (Somek 2008).

But then, Kant was a well-established professor writing under a regime of enlightened absolutism in eighteenth-century Prussia, and he had no intention of designing either the constitution of a liberal democracy or the ground rules of a liberal market economy. Nevertheless, his insistence on government through laws of general application continues to have a powerful influence on the constitutional theory of liberal democracies, and there is at least a formal correspondence between Kant's criterion of virtual consensus and the liberal preference for unanimous or super-majoritarian decisions, checks and balances, pluralism and stakeholder democracy. At the same time, however, Jürgen Habermas' (1992) influential concept of 'deliberative democracy' – which could not be farther removed from the normative models of market-liberal political theory – also has obvious Kantian roots, and may in fact be seen as an attempt to provide a republican solution to a problem that Kant had failed to resolve.

Kant expected individual reason to ensure the compatibility of individual actions if these are guided by the generalising logic of the categorical imperative. Conflicts, in other words, could only arise from the non-rational and selfish impulses of human nature. Since these ought to have no influence on legislation, the criterion of reason-based consensus, which would legitimate state-imposed general laws, could be seen as a matter of objective determination.

Habermas starts from a similar position when he insists that deliberative democracy should only admit arguments representing 'generalizable interests'. In contrast to Kant, however, he allows for an initial plurality of bona fide generalised preferences. As a consequence, the determination of legitimate laws cannot be the object of vicarious analyses. It requires a participatory solution where policy choices should emerge from processes of uncoerced and consensus-seeking public debates in a shared political space. In other words, though starting from Kant's idealistic individualism, the aspirations of deliberative democracy have less in common with liberal political theory than with the republican ideal of collective self-determination.[9]

Differences

It has become clear that both republican and liberal political philosophy rely on *output-oriented* as well as *input-oriented* legitimating arguments – but that they use these with different references. In the republican tradition, output-oriented arguments emphasise a holistic notion of the common good of the polity. Its substantive content, however, cannot be derived from normative theory but must be defined by virtuous governors (and, in a democracy, virtuous citizens) in the governing process itself. Liberal theory, by contrast, offers positive as well as negative specifications of output legitimacy. Positively, the basic function of government is to protect the security of life, liberty and property against external and internal threats. Beyond that, however, output-oriented liberal arguments have a negative thrust, emphasising normative constraints on exercises of public authority that would interfere with individual liberty. More specifically, market liberalism denies legitimacy to all state functions that could potentially be substituted by free markets or that interfere with the free operation of markets.

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[9] There is a caveat, however. The absence of theoretically specified institutional preconditions and the emphasis on consensus-oriented deliberation have contributed to the attractiveness of the Habermasian approach for students affirming the democratic legitimacy of present governing institutions 'beyond the state'. There is a temptation to ignore the postulates of egalitarian participation and publicness and to treat the mere discovery of deliberation (or 'arguing') among participants in international or supranational decision processes as evidence of a democratically legitimating practice (Joerges and Neyer 1997; Schmalz-Bruns 1999; Dryzek 2002).

These choices on the output side will also shape, or at least constrain, the dominant input-oriented legitimating arguments of both traditions. For liberalism, the choice seems straightforward: the function of ensuring external security and internal law and order is best entrusted to a Hobbesian executive power whose decisions are placed beyond the reach of partisan politics. Moreover, the function of protecting individual liberties against the 'tyranny of the majority' is best ensured by delegating potentially divisive governing functions to the non-political trusteeship of independent (ordinary and constitutional) courts, independent central banks and independent regulatory agencies. With the domain of 'political' choices thus drastically narrowed, liberal political philosophy is free to define individual autonomy as the supreme value and government by consensus as its institutional ideal. It is approximated in institutions with super-majoritarian decision rules, multiple veto positions and free access for the widest range of 'civil society' groups and organisations. If the consequence is a structural bias favouring the defenders of the status quo and handicapping the proponents of political change, this is welcomed as a protection of negative liberty – except, of course, in situations where the status quo is defined by state-imposed rules that interfere with the exercise of individual liberties (Ganghof 2009). As a consequence, liberalism has a 'thin' concept of 'citizenship' which, essentially, ensures protection for a range of individual rights that is wider and more secure than the set of universally recognised human rights. And it provides no explicit normative reasons for an obligation to comply with acts of government imposing sacrifices to which one has not consented.

In republicanism, by contrast, 'citizenship' implies not only the rights, but also the obligations of membership in a self-governing political community (Karolewski 2010). Civic rights need to be protected to ensure the capacity, the equal standing and the freedom of citizens to participate in political processes; and civic obligations include the moral duty to exercise rights of participation with a view to the common interest of the community (Schäfer 2011)[10], and to accept the burdens and sacrifices imposed by legitimated political processes. Hence input-oriented legitimacy has to bear heavier

[10] Kimpell (2009) argues that nineteenth-century republican theorists replaced 'civic virtue' with 'enlightened self-interest'. In my view, this should be seen as a move from republicanism to liberalism.

burdens than is true in liberalism. The 'no-domination' principle of republican liberty rules out Hobbesian executive powers, and it puts limits on the delegation of governing powers to non-accountable courts and agencies. Instead, the principles of collective self-determination and equal participation would allow majority rule within the constraints of constitutionally protected civic rights. At the same time, however, input-oriented republican legitimacy is constrained by the output-oriented criterion of '*buon governo*' (D. Schmidt 2003), requiring virtuous governors to practice justice and pursue the common good of the polity. In principle, therefore, legislators and governments in representative democracies are confronted with conflicting requirements – they are oath-bound to act as trustees of the common interest and, at the same time, they are treated as accountable agents of constituents who are free to grant or withdraw governing mandates in general and periodic elections.

The solution to this dilemma of democratic republicanism is John Stuart Mill's ideal of 'government by public debate' (Habermas 1962, 1992): public affairs should neither be managed by non-accountable trustees nor by agents guided solely by the fear of sanctions imposed by self-interested and poorly informed electorates. Instead, governors and citizens should be engaged in debates and controversies in a shared public space where proponents and opponents will justify and criticise specific choices through reference to the common good and the common norms and values of the political community. Under these conditions, republicans expect that voters will also respond as public-interest oriented citizens – which then allows them to accept majority rule without provoking the liberal fears of 'tyranny' or 'populism' (Riker 1982).

Clearly, the requirements for input-oriented legitimacy are more demanding in republican theory than they are in liberalism. And so they should be, given the different dividing line between what must be left to private autonomy and what may potentially become the subject of public affairs. Republican self-government may legitimately attempt to shape socioeconomic and sociocultural conditions that liberalism would place beyond public interference. And whereas liberalism, even of the Kantian variety, faces great theoretical difficulties in justifying corrections of market-allocated life chances (Rawls 1971), solidaristic redistribution among the members of the political community has become a core issue of twentieth-century republican politics. It follows that republicanism must be more concerned with the quality of the inputs and politics that shape the exercise of such far reaching potential powers.

In the context of discussions about a European democratic deficit, however, the most important difference concerns the place of '*political community*' in liberal and republican legitimating arguments. Referring back to David Easton's (1965) hierarchy, it appears that liberal arguments focus on the quality of *policies* and on institutional safeguards at the level of governing *authorities* and constitutional *regimes*. But given their individualistic premises, the reference to *political community* has no legitimating function in liberal discourses. Human rights and individual interests may be effectively protected within any aggregate of persons that happens to be assembled under a 'decent' (Rawls 1999) constitution. If properly constrained governing action should nevertheless violate individual preferences, 'exit' rather than 'loyalty' and 'voice' (Hirschman 1970), and 'voting with the feet' (Tiebout 1956) are seen as appropriate remedies. In that sense, liberalism appears as a truly universalistic or cosmopolitan political philosophy whose insistence on the security of life, liberty and property rights, tightly circumscribed political functions and consensual decision-making could define 'good governance' within any aggregate of individuals anywhere and at any time.

By contrast, republicanism (and even more so, its 'communitarian' variant) must appear inherently particularistic. From its Aristotelian origins onward, the focus has been on specific political communities with a remembered past and an anticipated future, and with a commitment to shaping the common good of these communities with the support of and in response to their citizens.[11] And 'republican liberty', understood as a principle of 'non-domination', is meant to ensure the collective self-determination of citizens, rather than the negative liberty of individuals. Hence the polity as a political

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[11] In Easton's (1965) terminology, what matters here is not merely the existence of a political community defined by frequent political interactions (*ibid*.: 177), but a 'sense of political community' (*ibid*.: 184–189) – defined as '[…] the feeling of belonging together as a group which, because it shares a political structure, also shares a political fate […] [T]o the extent there is a *feeling* of political community, the members will possess mutual sympathy and loyalty with respect to their participation in a common political unit' (*ibid*.: 185, emphasis in original).

community of self-governing citizens with a specific collective identity has remained the ultimate referent of republican legitimating arguments (Miller 2000). And the more the functions of government are extended, and the more they may interfere with individual preferences, the more the relational character of legitimating arguments comes into play. It increases the relative importance of appeals to the 'we-identity' and the solidarity of citizens and it emphasises the orientation of public debates to a common interest and shared norms of justice that may legitimate the sacrifice of self-interested concerns. That is why republican perspectives on European integration must pay attention to information about the historical factors facilitating state and nation building (Rokkan and Eisenstadt 1975) or about the breakup of established states like the former Yugoslavia or Czechoslovakia and the current difficulties of majoritarian democracy in polities with conflicting collective identities like Belgium (Billiet *et al.* 2006; Swenden and Jans 2006), Canada, Spain or Northern Ireland, for that matter. By the same token, the erosion of national boundaries and the difficulties of recreating conditions of 'boundedness' on a European scale (Bartolini 2005; Ferrera 2005) will be of concern only in the context of republican legitimating discourses (Karolewski 2010).

Constitutional democracies – and the European Union?

The discussion above has accentuated the differences between the dual traditions of Western political philosophy. But conceptual distinctions do not rule out either pragmatic coexistence or normative complementarity. On the contrary: the institutions and practices of Western constitutional democracies and their normative beliefs are based on the combination of principles that have been asserted separately in the republican and in the liberal traditions. They are all liberal polities in the sense that the state is responsible for external and internal security and the protection of property rights, that governing powers are distributed and constitutionally constrained, that individual rights are protected by an independent judiciary, and that plural interests have access to the policy-making processes by which they are affected. At the same time, however, Western constitutional democracies are all republican in the sense that they are representative democracies where governing authority is directly or indirectly obtained and withdrawn through regular, universal, free and equal elections, where policy choices are shaped through public debates and the competition of office-seeking political parties, and where institutions that are exempt from electoral accountability will still operate in the shadow of democratic majorities or, at least, of a democratic *pouvoir constituant*. Moreover, public policy everywhere is heavily involved in replacing or correcting market outcomes by providing education, health care, social services and social transfers either directly or through redistributive regulations and subsidies. And interventions in the market are more frequent everywhere than market-liberal doctrines would allow.

In other words, republican and liberal principles coexist, and they constrain, complement and reinforce each other in the constitutions and political practices of all Western democracies (Michelman 1999; Habermas 2001; Bellamy 2007). Nevertheless, the actual institutions vary in the extent to which they facilitate liberal or republican practices – and these practices will, in turn, shape the emphases of the prevailing discourses on political legitimacy (Lijphart 1999; V.A. Schmidt 2006). But these differences seem to fade in importance if we now turn our attention from the world of democratic nation-states to the European Union. When seen by itself and judged by the standards discussed here, the Union appears as the extreme case of a polity conforming to liberal principles but which, at the same time, lacks practically all republican credentials.

The EU's liberalism is most obvious in the priority it accords to the protection of (certain) individual rights and the tight institutional constraints on majoritarian political action: the European Court of Justice (ECJ) is more removed from correction by politically accountable actors than the constitutional court of any democratic state. From early on, it has interpreted the Treaty commitment to establish a Europe-wide market and the free movement of goods, persons, services and capital not as a programmatic goal to be realised through political legislation, but as a set of directly enforceable individual rights that will override all laws and institutional arrangements of EU member states. Moreover, the ECJ has also begun to protect non-economic human rights (Weiler 1999), and it is now dynamically extending their reach (Wollenschläger 2007; Scharpf 2010, 2012).

At the same time, the European polity's capacity for effective political action is impeded by the existence of multiple veto positions in European legislation; and the input side of its political processes could not be more pluralist and less majoritarian in character. The Commission itself, which has a near monopoly of legislative initiatives, relies on an extended infrastructure of committees and expert groups allowing access to a wide range of interest associations and 'civil society' organisations. Moreover, through the Council of Ministers, whose agreement by at least a qualified-majority vote is required for all legislation, all interests that have access to the national ministries in charge will also have access to the European level. Finally, the European Parliament, whose role in legislation has been considerably expanded in recent Treaty revisions, also prides itself on giving voice to interests and concerns that might possibly have been ignored in the Commission and the Council. In short, it is extremely unlikely that significant stakeholder interests could be victimised by a 'tyranny of the majority' at the European level.

But if the EU does qualify by liberal standards, it definitely fails by the criteria of republican democracy. On the output side, the Union's capacity to promote the common good is constrained by the consensus requirements of a multiple-veto system (Scharpf 1988; Falkner 2011). These requirements prevent effective collective action in response to many problems that member states could not deal with nationally. The EU's notorious difficulties in developing a common foreign and security policy and its inability to regulate competition over taxes on company profits and capital incomes are just the most glaring examples (Howorth 2007; Ganghof and Genschel 2008a, 2008b). Moreover, these same decision rules are responsible for an extreme conservative bias in EU policy. While new legislation must have broad political support, once it is adopted, it cannot be abolished or amended in response to changed circumstances or changed preferences as long as either the Commission refuses to present an initiative or a few member states object. Beyond that, all rules derived from the judicial interpretation of the Treaties can only be corrected through Treaty amendments, which must be adopted unanimously by member governments and ratified by parliaments or popular referenda in all member states. In other words, once EU law is in place, the *acquis* is nearly irreversible, and its correspondence with the common good of the Union (or contemporary political preferences) becomes progressively more tenuous as time goes on (Scharpf 2009).

From an output-oriented republican perspective, therefore, the European polity suffers from a problem-solving gap where member states find their policy space constrained by European law, while the capacity for political action at the European level is constrained by very high consensus requirements. In theory, of course, the multiple-veto constraints could be relaxed through a move to majoritarian decision rules for European legislation. But from a republican perspective, this remedy could only deepen the European legitimacy deficit.

In the absence of a strong collective identity, the peoples of the 27 member states do not constitute a political community that could legitimate a regime of Europe-wide majority rule on politically salient issues. And if it were installed nevertheless, political interactions would not meet republican standards: there are as yet no Europe-wide media of political communication and debates, no Europe-wide political parties to articulate and aggregate citizen interests and preferences, no Europe-wide party competition focused on highly salient European policy choices – and thus no way in which the citizens of European member states could respond collectively to proposed or actually adopted policy choices at the European level or to their effects. Regardless of the increasing powers of the European Parliament, therefore, there are no European governors (or governing parties[12]) that must anticipate and respond to the egalitarian control of Europe-wide election returns (Greven 2000; Harlow 2002; Føllesdal and Hix 2006; Hix 2008). While some republican authors hope that these deficiencies might be overcome through institutional reforms facilitating the politicisation of European policy choices, they seem to pay insufficient attention to the EU's lack of 'political-community' foundations[13] – which republican theory must treat as a crucial

[12] In multi-party or 'consociational' polities, voters may not be able to oust a government, but they may be able to punish individual governing parties.

[13] More optimistic authors should at least pause to reflect on the present state of Belgian politics, where political mobilisation in the Flemish and Walloon communities seems to commit political leaders to policies maximising the perceived interests of each community – and to drastically reduce their freedom to agree to

precondition for collective self-determination by majority rule (Karolewski 2010). And for the time being, at any rate, even optimistic empirical assessments will only assert the existence of a 'thin' and unevenly shared European collective identity that will not support the majoritarian resolution of highly salient and divisive issues at the European level (Risse 2010).

Legitimacy intermediation in the multilevel European polity

From a republican perspective, therefore, challenges to European acts of government cannot be met at the higher levels of David Easton's (1965) hierarchy of legitimating arguments. As a political community, the European Union has at best very weak claims on the loyalty of disaffected citizens; as a political regime, it does not conform to democratic standards of political interaction; and while the legality of EU authorities is not in question, they lack the legitimating essential of electoral accountability. Nevertheless, academic concerns over the alleged European democratic deficit have only recently begun to provoke political discussions outside of the European Parliament. And in light of the rapidly increasing volume of European policy output, observers assuming republican criteria of political legitimacy might truly wonder why political protests and demonstrations against EU policies were extremely rare before the present crisis, and why open noncompliance, civil disobedience and active resistance were practically unheard of.

From a republican perspective, this puzzle could be resolved by two connected hypotheses. The first one starts from the relational concept mentioned above, which suggests that the supply of legitimacy need not be greater than the demand for it. Thus, European policy-makers, being aware of the weakness of EU legitimacy at the 'community' and 'regime' levels, may have avoided highly intrusive and politically controversial policy choices. At the same time, and perhaps more plausibly, the multiple-veto constraints of EU policy processes may have prevented the adoption of policies that would violate the highly salient concerns of member-state constituencies. In

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compromises at the national level (Berge and Grasse 2003; Billiet *et al.* 2006; Swenden and Jans 2006; Bursens and Sinardet 2009).

either case, EU policies would avoid manifest challenges testing the legitimacy of European governing powers.

In spite of its surface plausibility, however, this hypothesis does not seem to address the fact that even before the onset of the euro crisis, there were European policies which had a massive impact on the economies, institutions and policy legacies of EU member states, and which have been analysed – and sometimes celebrated – in the literature on 'Europeanization' (see, e.g., Cowles *et al.* 2001; Münch 2008; Höpner and Schäfer 2008; Graziono *et al.* 2011; Kelemen 2011). While the overall transformation of European economies, societies and polities must surely be the cumulative effect of a multitude of proactive and reactive interactions of public and private agents, many of the most salient changes can be traced directly to specific policy choices at the European level. Hence the puzzle remains; and in order to account for the absence of manifest legitimacy crises, a second hypothesis and a more complex normative model need to be considered.

This hypothesis starts from the recognition that the EU is not a free-standing, single-level state, but part of the two-level constellation of the European polity. In it, the member states are indeed expected to conform to the full range of liberal as well as republican criteria of legitimacy – and it is their legitimacy which, until very recently, has protected the Union against direct challenges to its policies (Scharpf 2007, 2009). To clarify this argument, it is useful to distinguish between an enforcement–compliance relationship and a legitimating relationship between governments and citizens. They are congruent in unitary states and in states corresponding to the model of 'dual federalism' (where central and regional governments are responsible for different policy areas and rely on their own, separate enforcement structures). Even in German 'unitary federalism', where compliance with federal law is enforced by *Länder* authorities, congruence is ensured by the fact that the dominant legitimating relationship runs between citizens and the national government, and that *Länder* elections are generally treated by political parties and the media as 'second order national elections' in which the performance of the federal government is treated as a salient issue (Burkhart 2008; Moore *et al.* 2008).

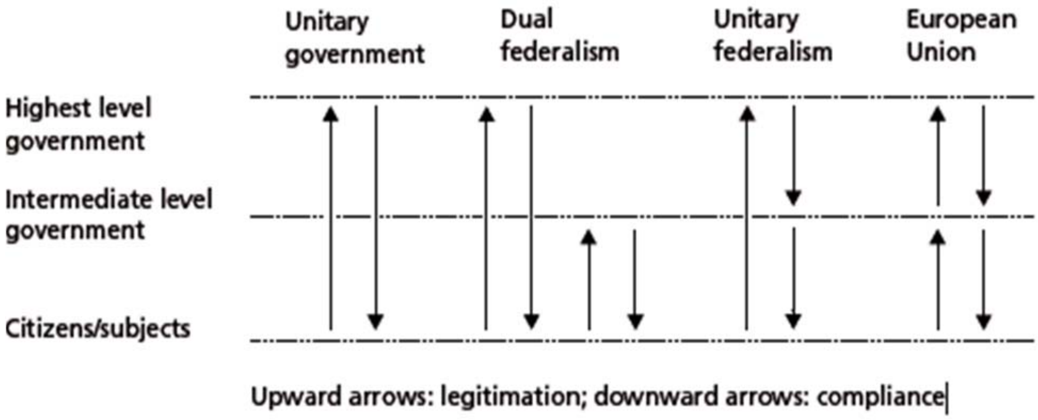

Figure 2.1 Compliance and legitimation in multilevel governments.

The two-level polity comprising the European Union and its member states shares some important structural characteristics with German federalism (Scharpf 1988). As in Germany, citizens do not confront the higher-level government directly. From their perspective, compliance is demanded almost exclusively by the administrative agencies, tax authorities and courts of their national polities. And from the Union's perspective, what matters is the willingness and ability of its member governments to ensure the implementation of European law. This is the compliance which the Commission keeps monitoring, and which is also the subject of a growing body of compliance research (Falkner *et al.* 2005; Zürn and Joerges 2005; Börzel at al. 2007).

In contrast to Germany, however, we also see a two-step legitimating relationship in the European polity. Whereas in German federalism, public debates and party competition focus on national policies and politics, and citizens are used to addressing their demands and their electoral responses to the higher (national) level of government, the higher level of the European polity is generally beyond the horizon of citizens' expectations and political demands; it is not the target of public debates and party competition, and most importantly, it is not vulnerable to electoral sanctions (Mair 2008). Citizens will not usually know the origin of the rules with which they are asked to comply, but they know that the only government which they might hold politically accountable is their own. In effect, therefore, national governments must generally bear the full burden of political accountability for unwelcome exercises of governing authority, regardless of how much European law may have contributed to these.

In a republican framework insisting on collective self-determination and democratic accountability, therefore, the EU must be legitimated not as a government of citizens, but as a government of governments.[14] What matters first and foremost is the willingness and ability of member states to implement EU law and to assume political responsibility for doing so. But if that is the case, normative discussions of EU legitimacy also need to reflect the limits of their capacity to justify the European policies they must implement. At a superficial level, the answer to the first question is easy. Democratically accountable governments unanimously agreed to create the European Union with its competences, institutions and decision rules – or they joined it later in full knowledge of the *acquis* and its obligations. They did so to realise purposes and to deal with problems that are beyond the reach of national policy choices. At the same time, however, these benefits of membership – and ultimately European integration itself – are highly vulnerable to the temptations of free riding. Hence, there are very good normative arguments obliging member states to comply with European law (Garrett 1992, 1995).

In relation to their own citizens, however, governments remain responsible for protecting and advancing the common good. If they find it necessary to participate in international or supranational institutions in order to deal with problems that could not be resolved in the national domain, there ought to be good output-oriented arguments supporting integration. Where that is so, governments should be able to justify European policies in 'communicative discourses' (V.A. Schmidt 2006) if these are challenged in national politics. And if they do not succeed, they will have to bear the political cost.[15] In any case, however, they will remain accountable to

[14] This is not meant to say that a purely 'intergovernmentalist' model would be either empirically or normatively sufficient (Eriksen/Fossum 2009). Much of what the EU is in fact doing cannot be explained as the outcome of pure intergovernmental bargaining (Falkner 2011). And for much of what the EU is in fact doing, it makes no sense to postulate a meaningful legitimating chain linking European policy choices to governments, governments to national parliaments, and these to national elections (Hix 2008). What I am saying is that in the absence of a direct legitimating relationship with its citizens, the EU must rely not only on the compliance of its member governments, but also on their legitimacy.

[15] Since voters and political opponents are not obliged to be fair, blaming the EU and confessing their own impotence is unlikely to be a useful strategy for embattled governments.

their citizens for the policies they implement. From the perspective of republican legitimacy, that is as it should be. The electoral responsibility of national governments could only end – as is true in unitary German federalism – if and when the higher-level government becomes politically accountable for its own policy choices.

Since this is not yet so in the European Union, governments are likely to use their roles in EU legislation to avoid European policies whose immediate impact would provoke politically salient opposition at the national level. Nevertheless, input-legitimacy will be weakened by the need to find compromise solutions that will deviate from pre-existing domestic preferences in order to accommodate the positions of other member states as well (Scharpf 2000). Moreover, the multiple-veto system that limits the political salience of individual EU decisions will also prevent national governments from intervening against their cumulative impact if negative effects of 'Europeanization' should become politically salient in national constituencies.

There is no question, then, that legitimacy intermediation in the two-level European polity is no equivalent for the legitimating potential of democratic self-government in the unitary or federal nation-state. But since the preconditions of republican legitimacy do not (yet) exist at the European level, it is the best we can rely on for the time being. And until recently, at any rate, the moderating influence of national governments on EU legislation, and their continuing accountability for its implementation, has shielded the Union against the legitimacy crises which authors and politicians castigating its democratic deficit should have expected. In the present eurocrisis, however, the shield of legitimacy intermediation has been pushed aside as citizens are directly confronted with the massive impact of European policies – and with their manifest lack of democratic legitimacy.

The end of legitimacy intermediation in the eurocrisis

By its own logic, legitimacy intermediation cannot support those 'supranational' European governing functions in whose exercise member-state governments (or the European Parliament, for that matter) are not involved. Most prominent among these[16] is the power of judicial legislation exercised by the European Court of Justice and the European Central Bank's power over monetary and exchange rate policies in the Monetary Union. In the literature, their legitimacy is often taken for granted, since national constitutional democracies are also respecting the political independence of constitutional courts, central banks and some regulatory agencies (e.g., Majone 1996; Moravcsik 2002). But the analogy is misleading. At the national level, the independence of central banks and regulatory agencies is supported and could be modified by democratically accountable governments and parliaments, and even the independence of judicial review is exercised in the context of common public space as a horizontal dialogue among (in the language of American constitutional law) 'co-equal branches of government' (Bickel 1962). In the EU, by contrast, the horizontal dialogue is transformed into a vertical, hierarchical relationship between supranational authorities and national agents.[17] And efforts to correct the ECB's policy or the rule announced in a Treaty-based ECJ decision would require Treaty amendments that must be ratified by parliaments or referenda in all 27 EU member states. In other words, the ECJ and the ECB are much further removed from the influence of democratically accountable governors than is true of their formally 'independent' counterparts in constitutional democracies.

As a consequence, supranational EU government cannot be legitimated, even indirectly, by input-oriented arguments. Its justification can only be derived from output-oriented arguments. In other words, it must depend on the belief that the common good of the community is better served by authorities that are not under the direct control of parliaments and governments exposed to electoral accountability and the temptations of partisan politics. Thus, the independence of judicial review, in particular, is supported by the deeply entrenched (liberal as well as republican) conviction that the democratic process itself depends on the protection of civic rights. By contrast, broad support for politically independent central banks is a more recent

[16] The Commission's power to define and apply competition rules for the private and public sector should also be included here.
[17] Some observers might detect traces of a virtual dialogue between some judgments in Luxembourg and in Karlsruhe. But how could the ECJ interact with similar interlocutors in all 27 member states?

achievement, owed to the intellectual ascendancy of monetarist economics. When invoked at the European level, however, both justifications appear deficient.

The ECJ has had little or no opportunity to protect civic rights and the institutional foundations of democratic processes. Instead, its authority did benefit from a general respect for the rule of law and a more specific admiration for its role as the 'motor of European integration'. At the same time, however, its vigorous protection and extension of individual (and mainly economic) rights has been the major force in a liberal transformation of the political economies of EU member states. Whether the overall impact of the ECJ's judicial legislation has been to serve the common good of the European polity is certainly not obvious. But since I have explored these issues elsewhere, I will relegate them here to a footnote.[18]

While the ECJ's judicial legislation may arguably have exceeded its intended mandate, this was certainly not true of the ECB. The institutional structure of the Monetary Union, the ECB's mandate and the constraints on member-state autonomy were unanimously adopted by governments and ratified after much public debate by parliaments or referenda in all EU member states. And the ECB was perfectly complying with its mandate to ensure price stability in the eurozone. If

[18] Initially, 'integration through law' (Cappelletti *et al.* 1985) was widely applauded as an effective way of removing political blockades at the end of the 1970s. Empowered by its early and largely uncontested assertion of the supremacy and the direct effect of European law, the ECJ was in fact able to go beyond the original intent of member governments by advancing the 'negative integration' of European economies through its very extensive interpretation of individual economic liberties (Alter 2001, 2009; Stone Sweet 2004; Scharpf 1999, 2011a; Höpner and Schäfer 2008; S. K. Schmidt 2011). As a consequence, ECJ decisions have progressively reduced the domain of allowable national policy choices (Kelemen 2011). And since 'positive integration' through European legislation was and is still impeded by high consensus requirements (Falkner 2011), judicial legislation has been a major factor in the liberal transformation of political cultures in EU member states (Scharpf 2010). Promoted in individual cases of very low political salience, this transformation has largely proceeded below the threshold of public attention. It was only when a series of ECJ decisions seemed to upset national rules of industrial relations (Joerges and Rödl 2008; Rödl 2009) that some political actors began to take notice – but apparently with little effect (Blauberger 2012). So even though integration through law imposes increasingly tight constraints on democratic policy choices at the national level, its own legitimacy has not (or not yet) become a politically salient issue.

the outcome is nevertheless a eurocrisis that seems to be threatening European integration itself, its cause was neither 'agency drift' nor even the noncompliance of member governments, but deficient theoretical assumptions that had supported the legitimating belief that creating the Monetary Union would serve the common interest.[19]

Monetary Union and the failure of output legitimacy

These beliefs could be described as a 'monetarist fallacy'. For national economies, monetarist economic theory predicts inflation-free economic growth if the stability-oriented monetary policy of an independent central bank assumes the leading role in macroeconomic management and if governments avoid inflationary budget deficits. That assumes, of course, that the bank's policy will be targeted on the actual conditions of the national economy. With regard to a European Monetary Union, however, monetary economists (mainly American) pointed out that monetarist assignment of governing functions presupposes an 'optimal currency area' (Mundell 1961), and that the monetarist model could not work in a eurozone comprising extremely heterogeneous national economies (Eichengreen 1990; Feldstein 1997). But in the political drive for more European integration, these warnings were disregarded. Instead, it was believed that more intense interaction in the Monetary Union itself would also ensure the convergence of economic conditions (Dyson and Featherstone 1999; Issing 2002; Marsh 2009; Heipertz and Verdun 2010). On theoretical grounds, however, one should instead have expected a reinforcement of divergent dynamics (Enderlein 2004).

As it turned out, theory was the better predictor: uniform ECB interest rates pushed low-inflation economies like Germany into a prolonged recession while stimulating the former soft-currency economies of Greece, Ireland, Portugal, Spain and Italy (the GIPSI countries) into credit-financed overexpansion and real estate bubbles. In its first decade, therefore, the Monetary Union generated an increasing divergence of unit labour costs, current-account balances and compensating capital flows between surplus and deficit economies. Thus, when the global economy was shaken by the international financial crisis following the collapse of the Lehman

[19] My account is based on the research presented in Scharpf (2011b) and a number of later but unpublished papers and presentations.

bank in 2008, the credit squeeze was most disastrous in the GIPSI economies that had come to depend on the availability of massive capital imports. And as domestic demand fell and unemployment increased steeply, governments intervened and public-sector deficits escalated, as they did everywhere. However, in the GIPSI countries, some of which had reduced public-sector debt to extremely low levels before the crisis, the rise was steeper than elsewhere. At this point, finally, investors began to worry about the ability-to-pay of euro states whose economies depended on capital imports to compensate negative current accounts. And as the risk premia of government bonds increased and debt refinancing became more expensive, the danger of state insolvency – first in Greece and then in other GIPSI states – has turned into a crisis of the euro itself.

What we have, then, is a major step in European economic integration which deprived democratic member states of macroeconomic controls over their national economic fates by establishing a strictly non-democratic supranational regime whose claim to output legitimacy depended on the 'monetarist fallacy'. Since this belief was mistaken, uniform supranational monetary policy was wrong for Germany, where it caused a deep recession between 2001 and 2005, and it was wrong for the GIPSI economies, where it generated the preconditions of the present crises. Initially, however, political blame was allocated at the national level. Since the effects of misspecified monetary impulses are indirect, and were politically invisible while the ECB was ostensibly following its mandate, and since voters are not obliged to be fair, national governments had to pay for the massive failure of European policy – first in Germany in 2005, and then in Greece, Ireland, Portugal, Spain and Italy as well. But that has not been the end of the story, and in the process, the role of European policy has become much more visible and problematic.

Rescuing the euro through supranational intervention

The threat of state insolvency first arose in Greece at the beginning of 2010, and for a few months it seemed possible that its government would be left to cope with it. But it soon became clear that Greek bankruptcy might undermine the solvency of creditor banks in France and Germany, that it might trigger domino effects in other GIPSI states, and that a Greek exit from the Monetary Union might provoke currency fluctuations that could reduce the competitive advantage that German exports enjoyed in the Monetary Union. By

May 2010, therefore, the German government had come to see the Greek government-debt crisis as a threat to the euro, and a collapse of the euro as a threat to European integration. And in the same spirit, all eurozone governments were ready to ignore the 'no-bail-out clause' and other constraints of the Maastricht Treaty in order to save the euro at any cost. In the process, however, they also have destroyed the precarious preconditions of legitimacy intermediation in the European polity.

There is no point in detailing here the sequence of rescue operations, the still ongoing efforts of institutional reform and the economic effects these have brought about by the time of this writing (July 2012). From a democratic theory perspective, what matters most are two basic characteristics:

First, the rescue operations themselves have been exclusively targeted at the state-credit crises, rather than at the crises of the real economies of the GIPSI states. Their focus is on the insolvency threat caused by escalating costs of (re)financing public debt in international credit markets. And apart from interventions by the ECB in secondary markets, relief is provided through the reduced-rate credits from rescue funds which are supported by direct contributions and guarantees burdening the budgets of all eurozone states.

Second, these rescue credits are associated with 'conditionalities' whose ostensible purpose is to reduce or eliminate the need for state credit in the short term, and to prevent its recurrence in the future. Thus the 'memoranda of understanding' defined by the Commission, controlled by the 'Troika' and sanctioned by the Ecofin Council have imposed severe budget cuts, public-sector layoffs, and increased consumption taxes – which further reduced aggregate demand, employment and tax revenues in depressed real economies.

Since these effects could have been easily foreseen, one must assume the influence of counterfactually stabilised cognitive and normative 'frames'. One reason must have been the fact that the rescue credits must ultimately be backed by the commitments of taxpayers in the creditor states (rather than by enabling the ECB to play the role of 'creditor of last resort' for all euro states). Thus, creditor governments accountable to their taxpayers surely had reason to insist on conditions, controls and sanctions.

Even more important, however, seems to have been the persistent intellectual and political influence of the monetarist fallacy: if stability-oriented monetary policy in national economies works best when excessive public-sector deficits are avoided, the failure of stability-oriented ECB policy must have been caused by excessive national deficits. And since the Greek case seemed to fit the pattern (at least to some extent), the dogma was reinforced, even though Germany had also found itself compelled to violate the Maastricht criteria during its deep recession, and even though Ireland and Spain had reduced their public debt far below the Maastricht requirements. In this spirit, austerity dictates could not be relaxed even though real economies continued to shrink while mass unemployment escalated to levels unheard of since the Great Depression of the 1930s.

Moreover, at German insistence, most EU governments have now agreed to a 'Fiscal Pact'[20] that is meant to permanently enforce fiscal discipline by requiring the adoption of balanced-budget rules in all national constitutions. At the same time, some of the EU's 'Six-Pack Regulations'[21] have tightened the Excessive Deficit Procedures of the Stability Pact by introducing stringent European supervision and quasi-automatic sanctioning mechanisms in case of noncompliance, and they have also extended supervision, direction and sanctioning in a new Excessive Imbalances Procedure that will allow the Commission to control a wide range of national economic and social policy choices.

More generally, the lessons which European policy-makers have drawn from the eurocrisis did not include a re-examination of the economics of monetary centralisation or a reflection on the monetarist fallacy (De Grauwe 2009; Feldstein 2011). They continue to ignore the disastrous role of one-size-fits-all monetary policy, and they insist on blaming the crisis on national policy failures. In effect, they seem to have convinced themselves that democratically accountable national governments and parliaments simply cannot be trusted to adopt and implement the kind of policies that would make the euro work.

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[20] Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (signed on March 2, 2012).

[21] Council Directive 2011/85/EU; Regulation (EU) No 1173/2011; Regulation (EU) No 1174/2011; Regulation (EU) No 1175/2011; Regulation (EU) No 1176/2011; Regulation (EU) No 1177/2011.

From this, it might also follow that creating the supranational Monetary Union was a case of premature and excessive institutional integration. But given the unconditional political commitment to save the euro, that conclusion would not be policy relevant. Instead, the dominant view has come to the belief that the Monetary Union was insufficiently supranational and lacked the powers to create the preconditions for the success of the monetarist model at the level of the eurozone.

In hindsight, therefore, it is seen as a fatal mistake that the deficit rules of the Stability Pact were not rigorously enforced against Germany and France. And if heterogeneous national economies failed to converge as expected, governments should have been forced to adopt policies that would have ensured convergence. The primary goal should have been major increases in economic flexibility – even if these would have required major economic, institutional and social transformations. In most member states, this would have included politically controversial measures to increase the profitability of private investment, to eliminate rigidities of the labour and service markets, to privatise public enterprises, and to generally reduce the burdens of the welfare state on the economy.

This, at any rate, was the logic of the 'supply-side' reforms adopted by Margaret Thatcher and Ronald Reagan after their conversion to monetarism in the 1980s. It was also the logic of the somewhat milder Hartz IV programme which Germany, under the constraints of euro-monetarism, adopted in response to the long recession of 2001–2005. And much harsher versions of such supply-side reforms have, in fact, been defined and enforced through the 'conditionalities' imposed on the GIPSI governments that had to apply for rescue credits in the eurocrisis.

From an economic perspective, the elective affinity between monetarism and supply-side policies seems quite plausible. And if the monetarist model should ever be made to work in the eurozone, it would indeed depend on a much greater degree of convergence among the heterogeneous member economies. It also seems plausible that greater convergence would require much greater degrees of economic flexibility, which could not be achieved without major supply-side adjustments in most or all euro states. In other words, if the euro is to be defended at all costs, economic logic does seem to suggest that the combination of fiscal discipline and liberalising 'structural' reforms may be the price that must be paid.

Whether the present strategy is likely to succeed in rescuing the euro, and whether its potential success would outweigh its costs in terms of mass unemployment, social inequality and societal disintegration, are not issues that I will explore here. Instead, I wish to discuss its implications for political legitimacy in the European polity. What matters here is the fact that, practically for the first time in the history of European integration, European policies have a direct and massive impact on the lives and concerns of citizens or on their highly salient political preferences, while European policy-makers are perfectly visible as the authors of these policies.

In this regard, the situation in countries where fiscal discipline and supply-side reforms were externally imposed and controlled differs from constellations where similarly unwelcome policies were chosen and defended in national elections by the politically accountable Thatcher, Reagan or Schröder governments. Quite obviously, national democratic processes were disabled as ever more detailed and highly publicised instructions on welfare cutbacks and labour market deregulation had to be implemented by successive Greek governments and parliaments without even the opportunity for face-saving gestures – let alone the permission to call a referendum. Or take the Portuguese experience, where in May 2011 all potential governing parties were required to promise that they would carry out the 'memorandum of understanding' regardless of the outcome of the upcoming national election. Moreover, from the citizens' perspective, the authors of these dictates are not anonymous market forces; they have the faces of Merkel, Schäuble, Sarkozy, Barroso and Trichet – none of whom, however, can be taken to account by Greek or Portuguese voters.

But if the loss of autonomy is obvious for debtor states, it is no less true for the parliaments of creditor countries, which are asked to accept ever more staggering commitments to cover the ever increasing financial risks associated with a succession of rescue funds. And in spite of negative majorities in opinion surveys, spectacular gains by anti-European parties, the collapse of coalition governments or the injunctions of constitutional courts, it is clear that agreement will ultimately be '*alternativlos*': summit resolutions and

Ecofin agreements on the rescue of the euro have the character of take-it-or-leave-it offers that no member-state parliament could afford to reject.[22]

In other words, the European responses to the euro crisis have disabled national democratic legitimacy, and at the same time, they have destroyed the possibility of legitimacy intermediation on which the European polity so far had depended. For the first time, therefore, the exercise of European governing functions must depend on its own legitimacy.

Legitimate supranational government?

But on which arguments could it be based?

Output-oriented justifications of present rescue measures have lost most of their plausibility after having failed over the course of more than two years. And even the optimistic expectations associated with supply-side reforms could only envisage a long and difficult road to the eventual recovery of the GIPSI economies. At the same time, there is also no chance that claims to output legitimacy could support radical alternatives suggesting the exit of Greece and perhaps other GIPSI states, or even a return from the Monetary Union to the more flexible European Monetary System of 1979–1999. Exits might nevertheless happen, and they would restore political autonomy at the national level. But their economic, social and political effects are still shrouded in radical uncertainty. And if they were now proposed as European policy choices, they could not generate the trust in responsible government on which output legitimacy must depend. The same could be said of the vision that would try to use the eurocrisis as an opportunity to achieve a breakthrough to a European federal state. On the one hand, it is unclear how such efforts might contribute to a resolution of present economic crises, and on the other hand it seems entirely unrealistic that political integration, in contrast to the economic integration of the last century, could now be promoted as progress to an uncontroversial 'common good'.

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[22] This may be different in countries like Germany and Finland whose governments have either taken a leading role in shaping European agreements or have succeeded in gaining special arrangements protecting salient national interests. Under either condition, national accountability may still have some substantive meaning. But neither of them could possibly be generalized.

So if 'rescuing-the-euro' policies are not supported by output-oriented legitimating arguments, could they be justified by input-oriented criteria?

Input-oriented European legitimacy?

'Rescuing-the-euro' policies had – and still have – major impacts on citizens' personal interests and highly salient preferences in debtor and creditor countries alike, and if they should have to be justified in input-oriented terms, it is necessary to specify the type of policies and the institutions and processes in which these are determined.

The Monetary Union has totally removed the competences of monetary and exchange rate policies from its member states, and it has tried to constrain their fiscal competences. In the eurocrisis, debtor states have completely lost fiscal autonomy, and the exercise of wide ranges of their economic, social and labour-market competences has been subjected to direct European control. Creditor states, on their part, have been required to carry the main burden of rescue credits through direct contributions and financial guarantees from their own budgets and at the expense of their own taxpayers. Moreover, with the recent adoption of the Six-Pack Regulations and of the Fiscal Pact, European control over fiscal policy and over an indefinite range of other national competences is being generalised to apply to all member states, regardless of any applications for rescue credits. What needs to be legitimated, therefore, are European controls over national policy choices and national resources, rather than choices about common European policies and the allocation of European resources.

In order to appreciate the implications, it seems useful to consider the 'Excessive Imbalance Procedure' that was adopted as a directly applicable EU regulation by the Council and Parliament in November 2011 (EU 1176, 2011). In contrast to the dominant obsession with past budget deficits, the regulation does perceive the eurocrisis as a consequence of the extreme divergence of macroeconomic balances that had developed among the economies of the eurozone. But avoiding any reference to the negative impact of uniform monetary policy on heterogeneous economies, the regulation focuses entirely on the need to control national policies. To this effect, the Commission has defined a 'scoreboard' of internal and external statistical 'indicators', ranging from current- account balances, real effective exchange rates and export market shares to house prices, private sector debt and unemployment rates.[23] If Commission-defined upper or lower thresholds are exceeded, the Commission will investigate and, upon finding excessive imbalances, will issue 'recommendations' which may become binding and entail quasi-automatic sanctions in case of noncompliance.

In contrast to rules on budget deficits, however, practically all the balances listed in the scoreboard are not under the direct control of governments. Before entering the Monetary Union, national policy-makers would have influenced them indirectly through the monetary, fiscal and exchange-rate instruments available for macroeconomic management. Since these instruments are no longer available at the national level (and since their use by the ECB will continue to increase imbalances[24]), it is certainly not obvious what governments should have done to avoid the rise of macroeconomic imbalances in the past.[25] And the regulation does not even try to specify the measures through which they should prevent the rise of house prices or of private sector debt in the future. It merely requests that they should comply with the Commission's recommendations which *'should be addressed to the Member State concerned to provide guidance on appropriate policy responses. The policy response of the Member State should use all available policy instruments under the control of public authorities'* (EU 1176/2011 at § 20).

Remarkably, the most troubling constitutional implications of this regime seem to have been totally ignored: regardless of the Treaty's allocation of governing functions between the Union and its member states, the Commission will be free to specify any and all national measures which it may consider economically useful – and it may do so without reference to any predefined rules nor even a shared theoretical paradigm of the kind that Keynesian as well as monetarist

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[23] Alert Mechanism Report, COM (2012) 68 final.

[24] At the time of this writing (July 2012), ECB interest rates (and even more so, real interest rates) are too high for the depressed GIPSI economies and too low for Germany.

[25] In the German recession of 2001–2005, union wage restraint and supply-side reforms helped, albeit at the cost of a drastic increase of social inequality (OECD 2011). But it is much more difficult to see what GIPSI governments could have done to prevent the expansion of credit-financed private demand.

macroeconomics had provided. And once the recommendations are effective, it is the Commission who will decide to impose severe penalties for noncompliance – unless a qualified majority of governments in the Council can be mobilised to reject these.

What has been established here is not an improved system of Keynesian or monetarist macroeconomic management (that would operate in the context of established economic theory, research and public criticism) but a discretionary regime of supranational intervention in the management of national economies and societies. While the EU regulation was – albeit on a disputable Treaty base (Höpner and Rödl 2012) – adopted by the community method of EU legislation, it does not and could not by itself specify any general rules that member states should follow. Instead, it leaves it to the Commission to define not only performance criteria for national economies but also the specific measures that governments should adopt to correct imbalances. And given the extremely diverse and contingent conditions to which economic interventions must respond, it would indeed be counterproductive from a problem-solving perspective if governments, or the Commission for that matter, were required to apply predefined rules. But under the criteria of liberal as well as republican constitutionalism, discretionary authority must either be narrowly circumscribed or subject to democratic accountability.

Since the Commission itself lacks any kind of input-oriented legitimacy, the regulation did assign formal authority to the eurozone Ecofin Council, even though its actual influence is minimised by the 'reverse-qualified-majority' rule for the adoption of recommendations and the imposition of sanctions.[26] But even if a positive Council vote were required, that would not suffice to create intergovernmental input legitimacy.[27] The decisions in question do not (and could not) adopt common rules for all member states. Instead, they impose directions and sanctions on individual member states in matters which are generally within their constitutional domains. Concededly,

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[26] Regulations EU 1176/2011 at Art. 10(4) and EU 1174/2011 at Art. 3(3). The European Parliament would even have preferred automatic sanctions.

[27] The problem, at this point, is not simply the domination of 'executives' in all processes of rescuing the euro – which is condemned by Habermas (2011) and other promoters of European democracy. It would persist if all Council decisions were ratified by national parliaments.

the governments represented in the Council may be constitutionally and democratically legitimated to agree to common rules binding, and obligations burdening, their own polities. But there is no way in which German or Finnish voters and parliaments, or the voters and parliaments of most member states,[28] could authorise their governments to impose special sacrifices on the citizens of Greece or Portugal or of any other member state. In other words, intergovernmental input legitimacy may sustain general rules applying to all member states, but it cannot legitimate discretionary interventions in individual member states.

This is different in unitary states organised by the principle of 'democratic centralism', where legitimate authority is concentrated at the top and may legitimately intervene in any and all matters at regional or local levels. In federal nation-states with democratically legitimate federal and regional governments, by contrast, the instances of allowable federal intervention in matters reserved to the regions are rare and carefully circumscribed by the Constitution. The European Union, however – let alone the eurozone – is still far from being a federal state with a democratically legitimated central authority. If that is so, the discretionary authority claimed by the Commission in the Six-Pack Regulations is neither legitimated by intergovernmental agreement nor could it be supported by arguments invoking the legitimacy of democratic centralism.

In short, the Monetary Union, the eurocrisis and the policies defending the euro have created an institutional constellation in which the control of democratic member states over their economic fate has been largely destroyed. Since the effective instruments have been removed, the loss cannot be compensated by ever more intense European controls of the remaining national options. Instead, effective macroeconomic control at the European level would require the capacities of a federal state with a large central budget, centralised capital taxation and social and employment policies – and with the capacity for democratically legitimated majoritarian policy-making.

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[28] Like the defendant in a criminal trial, the government of the 'member states concerned' will of course have no vote in the decision: EU 1174/2011, Art. 5; EU 1176/2011, Art. 12.

Some pro-European theorists, publicists and politicians seem to hope that the eurocrisis itself might provide the push for overcoming the resistance of self-interested governments to political integration (Habermas 2011). But even if, under the pressure of an escalating crisis, governments should agree not only to further transfers of sovereignty, but also to the direct election of the Commission President, or if the European party families should present candidates for that office in European Parliament elections, that would not yet create the political community which, from a republican perspective, would allow for legitimate majority rule. On the contrary: the eurocrisis, its dominant framing as a consequence of fiscal irresponsibility, and the disastrous impact of rescue policies designed by creditor governments on the basis of this frame have provoked conflicts of interest and identity, mutual distrust and recrimination, and widely diverging public discourses in national polities. These effects are counteracting the evolution of a 'sense of political community' that could sustain advances of European political integration and democratic legitimation. There is a risk, therefore, that attempts at institutional reforms that would respond to the failure of the supranational Monetary Union by attempting to create the political infrastructure for a much wider extension of supranational governing powers may provoke political reactions that could, in the end, destroy the past achievements of European integration as well.

Reducing the burden on European legitimacy

Now if present policies to rescue the euro and the more permanent regime that is being established to prevent future crises of the Monetary Union lack democratic legitimacy – what is to be done? The obvious solution would be to stop defending the euro, to acknowledge the common responsibility for having created a dysfunctional supranational regime, and to seek agreement on a common, organised and orderly return to the more flexible regime of an (improved) European Monetary System, which had worked reasonably well between 1979 and 1999. Unfortunately, however, all European policymakers have categorically ruled out this option, so we have neither plausible scenarios of how it might be implemented nor plausible estimates of the inevitably high costs of a possible transition.

But if we are stuck with the Monetary Union and with European institutions whose weak claim to political legitimacy does not match the need for legitimating highly visible European interventions in matters that have great political salience in debtor and creditor countries alike, a continuation of present policies could indeed provoke a manifest legitimacy crisis in the multilevel European polity. At this point, however, the logic of the theoretical concept of relational legitimacy introduced above may contribute a somewhat cynical suggestion to the search for pragmatic coping strategies: if the capacity for legitimation cannot be increased, the imbalance might still be avoided if the demand for legitimacy could be reduced by lowering the political salience of European policies. These, after all, were the conditions under which the European Union was able to avoid manifest challenges to its legitimacy before the present eurocrisis.

Theoretical logic, of course, can only suggest directions for the search. It cannot define economically effective and politically feasible pragmatic solutions. But just assume that direct ECB credits, or a banking license of the ESM, would eliminate the need to combat the state-credit crisis of the GIPSI countries through budgetary commitments at the expense of taxpayers in creditor states. This would, of course, require a departure from the Maastricht prohibition of monetary state financing. At the same time, however, it would drastically reduce the political salience of rescue credits in the public opinion of creditor states – and it would, by the same token, defuse the populist pressures insisting on dictates of drastic fiscal retrenchment in return for the rescue credits. As a consequence, conditionalities could be relaxed somewhat, and some commitments to present rescue funds might be converted into transfers to stabilise the atrophied social systems of the GIPSI states.

If something like that were indeed to happen, the eurocrisis would not be over, and the basic contradiction between monetary centralisation in a heterogeneous eurozone would still persist. But the intensity of the acute crisis would be reduced, and European policy would contribute to its resolution, rather than merely increasing its non-legitimated demands and constraints on member-state polities. In other words, interactions in the multilevel European polity might again return to lower levels of political salience – which would grant European and national policy-makers, policy intellectuals and policy researchers the time to explore more sustainable long-term solutions.

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Comment

The eurocrisis as a victory of neoliberalism?

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The Monetary Union: Another instance of the EU's neoliberal bias?

The EU's Single-Market legislation, the Commission's competition policy, and the ECJ's progressive extension of the domain of economic liberties have had a liberalising and deregulatory impact on the economies, societies and institutions of EU member states. And the 'conditionalities' imposed in response to the eurocrisis on the recipients of rescue credits are even more direct in their liberalising impact. Like the supply-side programs which Margaret Thatcher and Ronald Reagan had adopted in the 1980s, they insist not only on fiscal austerity but also on a wide range of 'structural reforms' requiring liberalisation, deregulation, privatisation, tax cuts, welfare cutbacks, wage cuts and union busting. It seems reasonable to ask, therefore, whether the Monetary Union itself should also be seen as part and

[*] My paper which was discussed at the Oslo conference had been prepared for another occasion. Hence the conveners asked me to elaborate, among other issues, on the relationship between policies adopted in response to the euro crisis and an alleged general bias of European integration in favor of neoliberal policies. After further reflection, my comments represent a more radical version of my remarks at the conference.

parcel of a general neoliberal thrust of European economic integration. On a superficial level, one might even consider conspiracy-theoretic explanations suggesting that the anticipation of this outcome should also have motivated the policy makers that brought it about. In fact, however, the story is more interesting.

The Bundesbank model did not fit.

In the political sphere, the creation of the Monetary Union was strongly influenced by the perceived success of the Bundesbank's monetarist policies in achieving price stability and economic growth in the German economy in the turbulent 1970s and in the 1980s. The European Monetary System (EMS) of 1979 had been an attempt to share this success and to avoid currency fluctuations through a commitment to monetary coordination. In effect, this placed the Bundesbank in a position of hegemonic leadership: In order to maintain agreed-upon exchange rates, other central banks had to mirror German monetary policies. This worked smoothly for the structurally similar political economies of the 'DM block', but it strained the political and institutional capabilities of 'soft-currency countries'. From time to time, these had to accept politically painful devaluations – which were also reflected in the higher interest rates they had to pay. For their governments, therefore, it seemed plausible to demand an end to German hegemony by re-creating a Bundesbank-like regime at the European level whose policies would fit the general state of all economies in the eurozone. And the geopolitical constellation of German unification provided the window of opportunity in which these demands were accepted by a reluctant German government.

What the political proponents of Monetary Union had not taken into account, however, were the essential preconditions of the Bundesbank's success story which did not exist in the eurozone:

- Bundesbank policies were precisely targeted on the current inflationary pressures and growth potential of an individual economy.
- These policies were broadly accepted and respected as a beneficial constraint on government fiscal policy and on the wage-setting strategies of Germany's large, powerful and economically sophisticated industrial unions.

- The redistributive German welfare state and fiscal equalisation rules were generous and effective enough to keep inter-regional disparities of economic growth, employment and incomes at low levels.

Under these conditions, 'monetarist coordination' could in fact ensure inflation-free economic growth and relatively low unemployment without a need for neoliberal supply-side policies. Similar institutional conditions also existed in the quasi 'corporatist' Austrian, Dutch, Belgian or Finnish political economies – which had facilitated monetary coordination among the hard-currency or 'DM-block' countries in the EMS. But they did not exist in the future eurozone.

Several of the former soft-currency states had been able to meet the quantitative accession criteria of the Monetary Union through heroic political efforts. But their economic, institutional and political structures continued to generate inflationary dynamics that were stronger than those in former hard-currency countries. Hence centralised monetary policies of the European Central Bank (ECB), which had to target average economic conditions in the eurozone, could not fit the economic conditions of all member states. Moreover, national economic and political actors would also differ in their responses to monetary impulses. In other words, the Monetary Union was far from constituting an 'optimal currency area' (OCA) in which central-bank policies would 'transmit' basically similar monetary impulses to all member economies. On theoretical grounds, this suggested that uniform monetary policies were likely to generate macroeconomic divergence among the members of the eurozone – and these implications had been clearly spelled out in a series of publications by (mainly American and Keynesian) macroeconomists.

Why were the theoretical warnings ignored?

In the run-up to the Maastricht Treaty, the preconditions of the Bundesbank's success and their theoretical implications were ignored. On the political level, the larger Germany was willing to demonstrate its continuing loyalty to European integration by sacrificing the Deutsche Mark, while others were eager to end the Bundesbank's hegemony. But the warnings derived from OCA theory were also disregarded by the central bankers in the Delors Committee who had proposed Monetary Union in 1989, by the Commission economists celebrating the single currency as the culmination of market integration in their 1990 report entitled 'One Market – One Money', and by the majority of Continental academic economists. It is at this point that the influence of neoliberal theory seems to have made a difference.

The monetarist mainstream of the 1990s had moved beyond the Bundesbank's pragmatic approach in the 1970s or the monetarism of Milton Friedman (who, incidentally, was among the critics of the Economic and Monetary Union, EMU). Under the influence of 'rational-expectations' models, the 'new classical macroeconomics' denied the capacity of monetary and fiscal policy to affect real economic growth and employment even over the medium term. Since rational economic actors would anticipate and discount the effects of macroeconomic interventions, these could only affect the rate of inflation. As a logical consequence, therefore, the unconditional commitment of monetary policy to price stability became a free good, and so did the commitment of fiscal policy to balanced budgets.

From this perspective, the theory of optimal currency areas and the warnings derived from it appeared as a throwback to the Keynesian illusions of the 1960s and the pretensions of macroeconomic steering which had failed in the 1970s. And while the heterogeneity of eurozone economies could not be denied, the market-driven responses of rational actors to the common currency would ensure economic convergence without government intervention. Hence the Commission was confident that the eurozone, though it was not initially an OCA, would soon become one since liberalised capital markets and the removal of exchange-rate risks would facilitate the optimal allocation of capital and thus accelerate the catch-up development of less advanced member economies. In short, all that was needed to make the EMU a success was a firm commitment of the ECB to price stability, and rigid rules on public-sector deficits that would prevent national governments from creating inflationary pressures affecting the eurozone as a whole.

While both of these requirements were installed as binding rules in the Maastricht Treaty and the Stability Pact, there was no reference to the coordination of wage setting – which had played a crucial role in the Bundesbank model. In the paradigm of the new classical macroeconomics, wage setting was not a policy variable. The theory assumed wage flexibility, rather than an institutional capacity of industrial-relations systems to achieve wage coordination. Hence if wages were mentioned at all in the analyses promoting and defending the Monetary Union, it was only to emphasise flexibility. How this was to be achieved, and what governments could do about it, was left unexplored.

But neoliberal beliefs collapsed in the eurocrisis

By now there is no question that the warnings derived from OCA-theory had been well founded. Nevertheless, the early years of the Monetary Union had seemed to confirm optimistic expectations. The ECB succeeded in keeping average euro inflation rates below the level that the Bundesbank had once achieved, and nominal interest rates fell everywhere to German levels. As a consequence, however, real interest rates were relatively high in Germany and other low-inflation countries. The ensuing depression of domestic demand pushed the German economy into a long recession with rising unemployment. It was eventually overcome through union wage restraint and supply-side reforms of the labour market which favoured an export-led recovery – and hence rising current-account surpluses. In the former soft-currency countries with higher inflation rates, by contrast, real interest rates were extremely low, fuelling a credit-financed surge of domestic demand. It generated economic growth with rising employment and real wages (much of it in the real-estate sector). And it also caused imports to rise much faster than exports – which were handicapped by the rise of unit labour costs. As a result, current-account deficits and thus the need for capital imports, increased steadily.

During the first decade of the Monetary Union, the imbalances between the surplus and the deficit members of the eurozone were not treated as a cause for concern by national or European authorities. Since the deficits were easily financed through capital flows from surplus economies, the divergence was actually welcomed as an indication of successful capital-market integration and catch-up development. And even the dramatic rise of real-estate prices in Ireland and Spain did not worry the ECB which saw itself responsible only for consumer price inflation and, in any case, would not want to outguess the market valuation of assets. On the tenth anniversary of the Monetary Union, therefore, public celebrations of the resounding success of the euro were unaffected by worries over dynamically increasing external imbalances in the eurozone.

These beliefs collapsed, however, when the international (Lehman Brothers) financial crisis of 2008 caused a world-wide credit squeeze and a particularly deep economic crisis in those states that had become most dependent on capital imports. Private debt was transformed into public debt as governments were forced to save their overextended banks. And in the case of EMU member states with high current-account deficits, financial markets came to doubt their solvency – which then turned the economic crisis of deficit countries into a eurocrisis.

The eurocrisis and structural neoliberalism

The decision to save the euro and the subsequent series of euro-rescuing operations have led to far-reaching changes in the governance of the Monetary Union which have created a regime in which neoliberal policies became structurally entrenched. They no longer depend on actors' neoliberal convictions and are thus largely immune to theoretical challenges and political opposition.

The interest-based commitment to save the euro

When the possibility of Greek insolvency first arose at the end of 2009, a neoliberal response, which had quite a few supporters in Germany and other surplus countries, would have let the market take its toll. Moreover, rescuing the euro required the violation of the no-bail-out clause and the prohibition of monetary state financing – i.e., of two 'ordoliberal' principles that had been included in the Maastricht Treaty at German insistence. As a consequence, the decision to save the euro was and is still being opposed as a violation of liberal economic doctrines and of European and national constitutional law, whereas normative defences appealed to a basic commitment to European integration. What mattered in fact, however, were straightforward interest-based considerations.

From the perspective of Germany and other surplus countries, the accumulated export surpluses of their economies amounted to a huge creditor position which could collapse with disastrous consequences for banks and private savings if the euro were allowed to fail. At the same time, their exports and employment had come to benefit from greatly undervalued real exchange rates – which could not persist if the deficit countries were allowed to exit the Monetary Union. As a consequence, governments committed to save the euro at any cost had the full support of private financial institutions, of industry and of organised labour, all of whom had reason to fear the potentially disastrous consequences of a euro collapse.

In short, the basic decision to defend the euro had no neoliberal underpinnings. But once that decision was in place, it implied that the challenges of the eurocrisis must be met under the structural constraints of the Monetary Union. It is these constraints, rather than any (probably persisting) neoliberal beliefs in Brussels and Berlin, that explain the liberalising impact of euro-rescue policies.

The new euro regime and its challenges

The eurocrisis had begun as a state-credit crisis that could have caused the insolvency of some EMU states. Ignoring the Maastricht rules on fiscal bail-outs and monetary state financing, these threats have so far been averted by rescue credits and unconventional ECB operations. At the same time, moreover, a new euro-governance regime is emerging that is meant to address and remove the causes of the crisis in order to ensure the future viability of the Monetary Union.

The analysis on which the new regime is based was presented by the Commission at the onset of the eurocrisis in its report on 'Competitiveness and Imbalances' which finally acknowledged that the Monetary Union, far from ensuring market-led convergence, had led to massive external imbalances and a dramatic divergence of economic competitiveness among its member states. These dismal outcomes, however, were not attributed to the disincentives of centralised macroeconomic policy in a non-optimal currency area, but rather to policy failures at the national level: Governments should have prevented the rise of external indebtedness through banking and credit regulation, and they should somehow have prevented the loss of international competitiveness through measures preventing above-average increases of unit labour costs. Since these imbalances are now seen to threaten the viability of the euro, they must be corrected under Commission guidance by the governments of the member states affected.

In essence, this analysis has shaped the 'conditionalities' imposed on the recipients of euro-rescue credits that are defined by the Commission, controlled by the Troika and sanctioned by the threat of state insolvency. And it has also informed the institutions and the policy instruments of a new governance regime of the Monetary

Union that applies to all EMU member states. Apart from the ECB's role as an unacknowledged lender of last resort for embattled eurozone governments and the centralised system of banking regulation that is still to be set up, the new regime has reinforced and tightened the constraints on national budgetary policies through the revised Excessive Deficit Procedure of the Six-Pack and Two-Pack regulations, the Fiscal Pact and the European Semester.

In a long-term perspective, these instruments of fiscal control might help to reduce the dependence of the democratic state on international capital markets – surely a worthwhile goal in principle. In the context of the acute economic crises of the deficit countries, however, short-term fiscal retrenchment did in fact increase public-sector deficits by reducing business activity, employment and public-sector revenues. Since these effects were so predictable, one must assume that the continuing insistence of euro-rescue policies on fiscal austerity is not primarily motivated by an interest in reducing the credit needs of crisis states. Instead, fiscal cutbacks appear to serve the same purpose as the 'structural reforms' that are imposed on the recipients of euro-rescue credits and that have been generally institutionalised through new 'Excessive Imbalance Procedure' included in the Six-Pack legislation. They are meant to deal with the divergence of competitiveness and external balances that the Commission's 2010 report had identified as a fundamental threat to the viability of the euro.

Even though the Commission-defined 'scoreboard' seems to treat surpluses and deficits symmetrically, the emphasis is clearly on external deficits: Current-account deficits imply a dependence on capital imports, and the loss of international competitiveness implies that the economy will not be able to reduce it through its export performance. And as deficit economies will depend on the ebb and flow of international capital markets, deficit states will remain vulnerable to speculative attacks on their solvency – which implies a permanent threat to the stability of the euro. Since these vulnerabilities do not exist in economies with current-account surpluses (even though these are also involved indirectly), the new euro regime is asymmetrically focused on the prevention and correction of external deficits.

Nominal vs. real devaluation

Before entry into the Monetary Union, deficits could have been directly addressed through a devaluation of the *nominal exchange rate* which would have reduced imports and increased export competitiveness. But since that remedy is no longer available, external balances can only be improved through measures reducing the demand for imports and the price of exports.

What is required, in other words, is an *internal* devaluation of the *real exchange rate* that requires domestic demand and wages to fall. Compared to nominal devaluation, this remedy is more difficult to achieve, and its distributive impacts are much more negative. That is not meant to suggest that nominal devaluation would be either painless or automatically effective. In the traded sector, it may increase price-sensitive demand for domestic products, but it will also increase the prices of imports and hence increase average inflation rates for everybody. And if unions should try to protect their real-income position by insisting on compensatory wage increases, the export advantages will be lost as the country gets caught in a devaluation-inflation spiral. In other words, to be economically effective, nominal devaluation does depend on unions that are able and willing to forego real-wage increases in order to improve employment in the traded sectors.

Internal or real devaluation by contrast must try to reduce domestic demand and to improve international competitiveness by reducing prices in the traded sector. Governments cannot achieve that directly, but they may reduce mass incomes through welfare cutbacks. They may try to increase price competition through privatisation and the deregulation of services. And they may reduce unit labour costs by lowering minimum wages and by increasing wage competition between job holders and unemployed job seekers. To that end, they may deregulate employment-protection rules, they may use welfare cutbacks to reduce reservation wages, and they may deny legal effect to collective-bargaining agreements.

All of these measures have in fact been included among the 'structural reforms' which the Commission defined in its 'Memoranda of Understanding' for Greece, Ireland and Portugal and in the recommendations addressed to the Spanish, Italian and recently also the French government. They resemble the supply-side and union-busting policies pursued in the 1980s by the Thatcher government in the UK and by the Reagan administration in the United States, and similar measures were also part of the Hartz-IV reforms adopted by the Red-Green government in Germany in 2004. It is clear that they resonate with the policy precepts derived from the neoliberal paradigm. But that, by itself, does not yet explain the seeming inevitability with which they are now adopted and maintained by governments of all political persuasions.

Supply-side policies in the eurozone: inevitable and effective

In the crises of the early 1980s, the ascendancy of monetarism and supply-side theory was supported by the belief that Keynesian demand management had manifestly failed in the 'stagflation' period of the 1970s. In its policy implications, the new paradigm insisted that price stability must be ensured through monetary and fiscal restraint, while economic recovery should be achieved through wage cuts that will reduce consumer prices and thus increase the real purchasing power of domestic demand. Put into actual practice in the UK and the US, these policies did in fact achieve price stability whereas their expected effects on growth and employment were mostly counteracted by rising exchange rates. At the same time, however, the supply-side policies of the 1980s had a lasting negative impact on real wages and social inequality. In contrast to the 1980s, however, similar policies dealing with present crises in the eurozone are no longer a matter of political choice, driven by neoliberal convictions and perhaps also by the redistributive political influence of capital owners. They have become structurally entrenched.

In the Monetary Union, priority of price stability is enshrined in the Treaty. And the disregard of demand-side policies is no longer a matter of theoretical convictions denying their effectiveness: When faced with a recession or depression, governments can no longer resort to monetary and fiscal reflation or to devaluation. The only options that are still available to them are supply-side policies to reduce wages and prices. But if these policies appear similar to those adopted by Margaret Thatcher and Ronald Reagan in the 1980s, their economic effects in the Monetary Union are different from those predicted by supply-side theory, and they are also stronger than those that could actually be achieved in the UK and the US in the 1980s.

The supply-side theory of the 1980s had expected economic gains to be achieved through increases in the real purchasing power of domestic demand – and in the UK and the US, these gains were largely counteracted by currency revaluation. In the eurozone, however, exchange-rate movements are eliminated. And in the case of the German supply-side reforms of 2004, economic and employment gains were in fact achieved. But they were not achieved through a rise of effective domestic demand. Instead, union wage restraint and 'reforms' reducing reservation wages constrained domestic demand, including the demand for imports, whereas stagnant or falling unit labour costs increased the price-competitiveness of the traded sector. In effect, therefore, it was an export-led economic recovery through which Germany was able to overcome the EMU-induced recession of 2001-2005. But the price to be paid for recovery was a steep increase of social inequality.

The German experience seems to fit a theoretically plausible pattern: By preventing exchange-rate adjustments, the Monetary Union increases the effectiveness of supply-side responses to economic recessions. But these effects will not be achieved by the rise of real domestic demand. Instead, they will constrain the demand for imports and, depending on the state of export markets, they may also increase external demand. And as rising exports will not be impeded by rising nominal exchange rates, persistent supply-side policies will eventually result in increasing current-account surpluses – and in persistent internal devaluation which will be reflected the increasing under-valuation of real exchange rates.

Conclusion: Euro-rescue policies as a race to the bottom

For eurozone states caught in a recession, therefore, supply-side policies and internal devaluation are the only allowable national responses, and they are also likely to be more effective than they would be outside of the Monetary Union. But the rise of external surpluses must be matched by deficits elsewhere, and one country's gain of competitiveness implies corresponding losses among its trading partners. In other words, by removing the exchange-rate buffer the Monetary Union has dramatically increased the interdependence between national economic policies. And it has created structural constraints under which the only permissible and potentially effective responses to an economic recession have the effect of 'beggar-my-neighbour' strategies directed at other members of the eurozone.

Worse yet, if these strategies are effective, their trading partners are also constrained to use supply-side 'structural reforms' in order to defend or restore their international competitiveness and to prevent the dangerous rise of external indebtedness. And so on, and so forth. In principle, therefore, the Monetary Union has created a vicious cycle of supply-side reforms and a constellation in which the alleged temptations of competitive nominal devaluation have been replaced with an institutionalised compulsion to engage in competitive real devaluation. The systemic effect is a 'race to the bottom' in which the member states of the eurozone are forcing each other to reduce unit labour costs by increasing the competition among jobseekers – through the deregulation of labour law, the dismantling of collective-bargaining institutions and the reduction of minimum wages and of social benefits for the unemployed.

All these are of course measures corresponding to the precepts of neoliberal economic theory, and the outcomes will also favour the incomes of capital owners and their agents over the incomes from work and the need of groups depending on public-sector services and transfers. But unlike similar policies adopted in the UK and the US in the 1980s, they do not depend on the neoliberal convictions of policy makers or on the political influence of capital interests, and they cannot be reversed by political changes to a Labour government or a Democratic administration. As long as the Monetary Union is maintained, supply-side reforms and competitive internal devaluation are institutionally entrenched.

Part II

Looking back, looking forward

History matters

Chapter 3

When the *peloton* hit the mud
Displacement struggles and the EU crisis

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A muddy tale

Let us imagine a group of cyclists, say six in number, all members of the same club, wearing tee-shirts with the same starry design. When we first encounter them they are enjoying a long, invigorating and amiable tour through familiar, undulating hills. These cyclists have broadly similar backgrounds and live in fairly close proximity, cheek by jowl. Their families and communities have not always been nice to each other in the past. There has been shouting, even shooting, and worse. But now all that is behind them. They have put aside their weapons and picked up their bikes. Now they are discovering a new togetherness, cultivating shared interests and activities, building ever-closer solidarity.

On the road, the cyclists are all bunched together in a tight *peloton*, competing with each other in a friendly way, enjoying the summer sunshine.[1] At the front of the group some well-muscled fitness

[1] Peloton is a French word originally meaning a platoon or a little ball but more recently used to refer to the main group of riders in a bicycle race who typically form a closely bunched group. The word conveys not just forward movement but also a

fanatics are setting the pace, while others are enjoying an easier ride in the slipstream. Life on the road is good and everyone is making the best of it in their own way. The birds are singing.

As they pedal through the countryside, neighbours give them friendly waves, and some ask to join them. Soon the number of cyclists has doubled. Some of the newcomers have signed up so they do not miss out on any advantages club members might get (cheaper inner tubes? advice on gear ratios?). Others want, above all, to put on the club's tee-shirt which has become a sign of being 'cool', 'ok', and definitely not nasty or disreputable.

So now the *peloton* contains a more complex mix of people. The spirit of the *peloton* begins to change, comprising different styles and attitudes. As it gets bigger the cycling pack starts to lengthen out along the road, reducing the intimacy of the early kilometres. But good will remains high as liquid refreshments and energy-giving biscuits are passed back along the moving line to the stragglers.

Just as everyone is adapting to this new more elongated formation, a dramatic event occurs. One of the two front riders suddenly jumps off his bike, and swaps it for a tandem bicycle made for two riders, one that is super-tough and super-light. He rejoins the group with his smaller brother behind him. This causes some mutterings, as people realise that they will soon all be trailing behind this supercharged vehicle with its extra muscle-power unless they can keep it with them in the middle of the pack.

During an overnight sojourn at a friendly wayside tavern, discussions begin about how to refresh and reinforce the bonds of solidarity within the *peloton*, which is the on-road expression of the cycling club's togetherness. Perhaps a joint savings scheme to cover bike repairs? Other ideas are also floated but meanwhile a line of hopeful people from far and wide is forming by the tavern bar.

Candidates for club membership make claims about their cycling fitness and how much they share the 'spirit of the club', its ethos of

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mixture of competition and cooperation since riders in the rear of the peloton save energy by positioning themselves in the slipstream of those in front.

competition mixed with comradeship. Many of them are welcomed in, and there is also a waiting list. It is tremendously flattering for the club to be in such demand and the travel talk gets more ambitious. In the spirit of Star Trek, they vow to boldly go where no cycling club has gone before. They will find a promised land where cyclists can be free, strong, secure and happy. So now the object is more than togetherness-instead-of-fighting. It is togetherness-to-reach-the-promised-land. Some have doubts and reservations, or do not take this mission too seriously. But there are already so many benefits to being in the club (like knowing the right people, and being part of a big enterprise) that they continue to string along.

When they all set off on the road next day, their leaders leave the comfortable contours of their early rides and point their wheels towards steeper, unknown hills. From now on the ride is more exhilarating but also more challenging. The 'tail' of the expanded *peloton* is now so long that cyclists find it difficult to keep in close touch as they ride. Many of the messages they shout to each other get carried away in the breeze. Everyone is enjoying the ride in their own way. However, thanks to a strong following wind, they keep the show on the road, maintaining forward momentum.

But suddenly disaster strikes. It happens as the cyclists glide down an unfamiliar country lane with a sharp incline. They go round a bend and discover their nice smooth road is leading them – *quelle horreur!* – straight into a very muddy field which has recently been occupied by a herd of cows.

As they hit the mud the leading pack of cyclists begins to break up and slow down, coming to a stop. Meanwhile, those behind crash into the leading group. Several riders fall over and get covered with malodorous muck. There is much lamentation. It is not clear how the ride can be continued. For what seems like ages, everyone tramps through the mud, unable to mount their bicycles, unsure what to do, trying to work out how to get out of this mess and carry on with their journey.

The point is that the club has committed itself to the destination, not just to the cycling. 'Getting there' has become more important than enjoying a peaceful comradely ride.

If the cycles cannot take the club where it wants to go, then some more powerful means must be found. Eventually, a large bus smelling of new paint is delivered to the scene. It looks unfinished, only half-made. It rattles a bit. But perhaps, even in this incomplete state, it will deliver more effective traction through the mud than bicycle wheels. No one is sure if the bus will take them to the promised land but at least it might get them out of the mud. Will it do both these things: get them out of the mud *and* take them to the promised land?

Now there follows a vigorous argument. Who will drive the bus? Who deserves to have a seat on board? How much should the fare be? What if some people cannot afford the fare? Can some people be thrown off the bus? Can the bus be successfully driven to the promised land? If not, what has to be changed? Does the bus have to be made more robust and powerful? Does the vision of the promised land have to change? Or will the bus only reach that destination if its passengers show they are sufficiently 'worthy' by obeying the 'rules of the bus'?

These are not easy questions. People lose their temper. Some dislike the change from 'the spirit of the club' to 'the rules of the bus.' They begin to accuse each other of bullying, hypocrisy, and freeloading. Finally, the cyclist with the titanium tandem bike seizes the driving wheel and fires up the bus engine with the help of a few close friends. The bus begins to plough its way across the mud but nobody is content, no-one is happy in their skin. Mechanics are still working on the bus, modifying its features, shifting people from seat to seat, and installing CCTV cameras. At the back of the bus, some angry passengers are ripping up the seats.

The meaning of this muddy tale: For cycling club read European Union (EU). The muddy field is the credit crunch and sovereign debt crisis. The couple on the bicycle made for two are, of course, the two parts of Germany reunited after 1989. The cycling club's promised land refers to the European Dream embodied in the Maastricht Treaty, especially its social charter and the creation of European citizenship. The unfinished vehicle brought into the muddy field is the EU's increasingly centralised governance structure.

This new governance structure includes not just the European Financial Stability Facility (May 2010), the Fiscal Stability Treaty (March 2012), and the European Stability Mechanism (October 2012) but also the so-called 'six pack' and 'two pack' and the Macroeconomic Imbalances Procedure (MIP). [2] Monitoring and disciplinary supervision of national economic policies are to be carried out by the European Commission and European Central Bank (ECB) through the European Semester.[3] Not least, work is under way to establish a banking union.

The European Union has become a virtual construction site, more so than ever before. During the past few years the sounds of drilling, hammering, sawing and welding have competed with squeals of anguish and the noise of rioting. The birds are still singing but no one can hear them.

How did the EU get into that muddy field? How has life amidst the mud changed it? What are the prospects for life beyond the mud?

Before the mud

Bicycle theory: This tale is a salutary warning to those who rely on the so-called 'bicycle theory' of institutional development.[4] Bicycle theory begins by noting that if you are sitting on your bicycle while it is stationary with both feet on the floor this is a stable situation. But if you push down on one pedal – in other words, change the existing pattern of balances – then the only way to avoid falling over is by pushing down on the other pedal. In fact, you have to continue pedalling and now, lo and behold, you are moving forward. You may, perhaps, be going further and faster than you originally intended but you are likely to see the negative benefits of not colliding with the ground and even the positive benefits of the progress you are making. Of course, if a muddy field brings your bicycle to a standstill, then you fall over anyway. But before exploring that issue let us apply bicycle theory to a familiar domestic setting.

[2] The 'six pack' and 'two pack' are measures that strengthen surveillance, partly by giving quantitative values to guidelines and targets. The MIP is intended to identify potential risks, and deal with imbalances as they arise.

[3] The European Semester is a yearly cycle of economic policy coordination.

[4] Fred Bergsten of the Peterson Institute has been credited with formulating the bicycle theory in the context of trade liberalisation. See also Rodrik, D. 'Trade policy as riding bicycles', *Dani Rodrik's weblog*, 20 July 2007, retrieved from: <http://rodrik.typepad.com/dani_rodriks_weblog/2007/07/trade-policy-as.html> (last accessed 6 August 2013).

Suppose a number of flat mates decide to share the tasks of meal preparation. This has consequences or 'knock-on effects', impacting on other activities that also need coordinating for everybody's good: for example, buying food. Further chores and, indeed, pleasures are likely to come onto the agenda. Balance and harmony are maintained by consensus-promoting dialogue combined with incremental innovation and all this takes the flat mates into new territory. In fact, some of the flat mates who share the cooking and shopping may even end up married or in civil partnerships. Popular sit-coms such as *Friends* have been based upon exploring these matters, and their intriguing outcomes.

A refinement of bicycle theory is an approach that may be labelled 'managed displacement.' The objective in such a case is to dislocate long-established arrangements in a relatively minor way that can be made acceptable to those directly involved, knowing that this will trigger a cascade of further changes. Suppose that in, say, 1950, the 'lady of the house' in a large city mansion decides to upgrade her catering arrangements. Suppose she decides to put a big new freezer in her kitchen, which has been run in an old-fashioned way since her grandmother's time. The butler gets a representative from the freezer company to visit the kitchen, explain the potential benefits of the freezer to the staff, and discuss their initial anxieties. Then the kitchen workers are left to make the best of it, reporting back to 'the lady upstairs' at intervals. We would not be surprised to learn that the installation of the freezer prompts change in patterns of food buying and use, alerts the kitchen staff to the possibilities of other new technology (e.g. food mixers), and ends up by stimulating a complete redesign of kitchen practice.

In other words, the initial innovation disrupts the old pattern and points towards a new one – but leaves that new pattern far from complete. To get the full benefit of the initial innovation other long-standing arrangements also have to be disrupted, but with the promise that life will be better for all concerned. A wholesale transformation is achieved but in small stages and with the active complicity of those who are affected.

Managed displacement in Europe, round one: Jean Monnet, one of the European movement's main founders and early activists, was the impresario of managed displacement.[5] He worked hard with his political friends to put this approach into practice.[6] He correctly foresaw that creating the European Coal and Steel Community in 1951 would impact on a wide range of business and governmental activities and interests. This fact gave 'the Six' a strong push down the road towards the creation of the European Economic Community (or 'Common Market') in 1957. The working of the common market was disrupted by various transaction costs including border controls and inconsistencies between the national legal frameworks within which commerce was carried out. Some of these inconvenient irrationalities were removed with the creation of the Schengen area (1985). Others were abolished by the Single European Act (1986), which established a single market in goods and a framework for greater political cooperation between member states.

Not that things went completely smoothly. There were economic downturns in the early 1970s and early 1980s. In 1985, Herbert Giersch (1985) complained about 'eurosclerosis' – slow growth and high unemployment. Three years later Mrs Thatcher raised her flag in Bruges against the threat of 'a European superstate exercising a new dominance from Brussels.'[7] The handbag waved, menacingly. However, these early decades gave Europe's politicians plenty to crow about. Of course, managed displacement cannot be given all the credit. There were other factors such as the prolonged postwar boom, and the massive public and private investment coming across the Atlantic during the Cold War years.

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[5] Jean Monnet used to talk about making Europe more united through a strategy of 'dynamic disequilibrium'. 'Dynamic disequilibrium' is the motive force that makes 'managed displacement' work; it is the pedals going round, pushing the bicycle forward. According to the theory of dynamic disequilibrium, cooperation between partners increases trust between them and builds up their organisational means to carry out shared tasks. This is likely to enhance both the capacity and the willingness to extend organised cooperation. It also increases the functional importance of the shared bureaucracy and the political power of those who control it (Duchene 1994: 376).

[6] The French foreign minister Robert Schuman was the key player.

[7] See Thatcher, M. (1988) 'Speech to the College of Europe (The Bruges Speech)', retrieved from: <http://www.margaretthatcher.org/document/107332> (last accessed 7 August 2013).

If the Cold War had not ended in 1989, the process of Europe-making might well have drawn to a close in the late 1980s with the creation of an integrated trading block in Western Europe. But that was not to be. The Iron Curtain was destroyed and Germany was reunified. This was a massive and unexpected displacement of the Cold War political order. It meant that Germany would carry much greater political and economic weight in Europe. Everybody feared this, including Germany's politicians who did not want to be depicted as leaders of a re-born would-be 'master race' intent on humiliating their neighbours. There was some danger of a 'displacement struggle' breaking out, aggravated by political cheerleaders in Britain and France, perhaps encouraged by Russia, stoking up fears that a big new bully boy had arrived on the block.

Managed displacement in Europe, round two: In order to avoid a prolonged and bitter struggle over the position of Germany after 1989 another carefully handled process of managed displacement was needed in Europe. How was this to be done? The answer was to set about building a stronger political framework for the European Union. This was very challenging, and there was a clear risk of failure, but the alternative risk – deep division between those welcoming and those hostile to a reunified Germany – was more immediate, very pressing, and potentially transatlantic in scope; it had to be avoided at all costs.

The case for a more united and more centralised 'political' Europe was that the newly enlarged German state could be contained and harnessed – and also accepted, legitimised and protected – within such a framework. This prospect was consistent with the European vision of a promised land dreamed up during that sojourn at the wayside tavern described in our muddy tale. The promised land would find a place at its heart for a European Germany that was democratic, pacific, and friendly.

In fact, taken together, the Maastricht social charter with its blueprint for European social rights, and the Copenhagen criteria for membership of the EU provided a vision of the European Union as a Post-Humiliation Polity, one that offered a dignified life to all citizens. This was an important advance on the early days when the main object of 'the Six' was mainly to prevent states, especially France and Germany, from trying to humiliate each other. During the 1990s citizens were also brought more fully into the equation. They could expect to have an existence from which all avoidable humiliations – such as poverty, deprivation, insecurity and subjection to state brutality – were to be removed. They could expect to have their interests cared for.

So Germany was not the only beneficiary of this deal. Indeed, Germany made a sacrifice, or so it appeared at the time. Its leaders agreed to merge the strong German Deutschmark within a common European currency, the euro (see for example Bertelsmann Institute 2013). This new currency was issued by a new European Central Bank (created in 1998) and introduced gradually between 1999 and 2002.[8]

However, when it began, the euro was not backed up by a eurozone-wide finance ministry, nor by a European federal government able to establish a Europe-wide economic policy subject to democratic controls. As is well known, a 'political Europe' remained abhorrent to several member states. The idea of a common currency was much easier to sell. It could be presented as a sensible extension of the strategy of reducing transaction costs within the common market. This 'Euro-lite' approach was all that was politically manageable during the late 1990s and early 2000s.

The euro's promoters hoped that during the currency's early years Europeans would begin to realise, through experience, that a more highly developed governance framework was needed. They would see just how inconvenient life was when that framework did not exist or remained inadequate. At that point, perhaps, member states would agree to construct the more centralised and overtly politicised structures that were required. They would include a substantial European-level apparatus for monitoring, supervising, and regulating the economic policies and budgetary strategies of member states. An increasing number of people would realise that a United States of Europe was a functional necessity.

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[8] As long ago as 1957, Jean Monnet was promoting schemes for trans-European coordination in financial matters. At that time he had in mind a European stabilisation fund but the basic strategy of promoting dynamic disequilibrium was the same as for the common currency. Monnet commented privately, to a colleague, that 'Via money, Europe could become political in five years' (Duchene 1994: 312).

In other words, the introduction of the euro was supposed to be the opening move in a second round of managed displacement. It was an attempt to repeat on a larger scale the process that Robert Schuman, Jean Monnet and others had helped to set in motion during the 1950s. In the event, this process ran out of control. As our 'muddy tale' relates, the starry-shirted cyclists found themselves in humiliating circumstances: upside down and covered in cow muck. Displacement processes turned out to be much more difficult to 'manage' than might have been thought, given the success of the 'first round.' Why?

The untangling of managed displacement: First, a brief word on the concept of displacement: it sometimes means physical movement (migrants and expatriates are everywhere) but in other cases does not take that form. Commonly, displacement is structural, organisational, cultural and social-psychological rather than geographical. Often it is resisted, for a while at least. Those who cannot resist often try to escape, even, perhaps, committing suicide. Those who cannot escape submit (on displacement and humiliation, see Smith 2006, 2008, 2012, 2013).

At one extreme, a powerful overlord may enforce displacement from above. This, of course, is an instance of *managed displacement*. An example occurred when Stalin demanded collectivisation of the Russian peasantry in the 1930s. It was a brutal programme, enacted through deliberate humiliation of the so-called *kulaks*, or rich peasants. Hitler's 'final solution' for the 'Jewish problem' is another notorious case.

At the other extreme, displacement may be a disordered existential condition in which almost everyone's life is being dislocated, so that no one is in charge and everyone is competing to survive as best they can. This was Europe during the Second World War, and this situation may be described in terms of *displacement struggles*. In such cases, the main object of participants is normally either to impose humiliation on others (for example, through death and/or defeat) or avoid being humiliated themselves.

In between these two cases, we may imagine the following case: a network of neighbouring groups or nations, all displaced in various ways, faced with the challenge of bringing order to their situation without experiencing or imposing humiliation amongst themselves. This was West Europe in the postwar period although for the first few years the US played the role of the 'lady upstairs,' perhaps with

Jean Monnet as the butler. This is a further instance of managed displacement. The idea was that dialogue and willing cooperation would lead to a situation of increased harmony, a condition that does not imply total agreement but, rather, continuing discussion to resolve differences as they arise.

It is important to stress that the EU (or, rather, the European Economic Community [EEC]) began life as a small collection of humiliated states. Germany and Italy had been comprehensively defeated in war. France and Britain were in process of losing their empires. The Benelux countries were recovering from Nazi occupation. They were all 'in recovery', trying to face up to their transformed situations in the shadow of Washington.

The story of the European Union is this: for about three decades a relatively balanced arrangement allowed managed displacement to work reasonably successfully but then it began to untangle for two reasons. Firstly, the prestige and authority of Washington was seriously damaged by the outcome of the Vietnam War. Secondly, the balance of power within the EU was upset by the reunification of Germany, and, more generally, by the process of enlargement towards the east and south-east. The result of these two transformations was to turn the EU from an arena of managed displacement into an arena of displacement struggles.

These tensions had always been there but they became more intense. One struggle set advocates of big government and big business against each other. Each wanted control over the distribution of income and wealth, and the shaping of public opinion. Whenever either tendency became too powerful, spokespeople for the other tried hard to beat it back down, usually treating it as a bitter enemy with whom no compromise was possible. In fact, this struggle took several forms within Europe, as will be seen.

The other struggle was the contest between the United States and the European Union for political influence within the West and beyond. In the period from 1951 to 1989, in other words during the EU's first period of managed displacement, the American state was, in effect, monarch of the West. The European Economic Community served as its royal court, strategically important because of the Cold War. By the mid-1950s, all the West European courtiers were bound together by the fact that they had been comprehensively humiliated and 'put in their place' by Washington, either in 1945 or in 1956 (after the Suez adventure. On Suez see Kyle 2011). Despite these indignities, the European project benefited from being nurtured within the protective politico-military cocoon provided by the transatlantic alliance under the leadership of Washington.

As has been noted, the political atmosphere changed profoundly after the US suffered its own humiliation in Vietnam between 1968 and 1973. West European governments were able to take a more independent line. Washington hit back by devaluing the US dollar, cutting defence spending, and forcing Europe to stand on its own feet a little more. This was a small rehearsal for the challenges faced by the EU after 1989 when the US increasingly turned its attention away from Europe and towards the Middle East and Asia.

After 1989, a vacuum was left by the sharp reduction of America's overpowering but supportive presence. This was partly filled by a vast reservoir of private and public borrowing capacity, a commercial facility that fuelled and funded the ambitions of politicians and consumers. A key moment was the 'big bang' (1986), which opened up the City of London to American finance houses, making available a large amount of credit across Europe and beyond.[9]

All this liquidity helped to overcome the drag factor of 'eurosclerosis' while feeding the EU's ambition. Its leaders were quite prepared to combine three enormous tasks: (1) introducing the euro; (2) taking in several new member states inherited from the defunct Soviet and Yugoslav regimes; and (3) building up the powers and capacities of Brussels.

By the 1990s, as already noted, the EU had largely freed itself from its old dependence on Washington.[10] However, an internal division that had always been present in the EU became much more pronounced. The original European marriage between France and West Germany contained a creative tension between the state-focused *dirigisme* of Paris and the greater willingness of Germany, especially under

[9] For a recent account see 'Big Bang gave London top tier status', *Financial Times,* 8 April 2013, retrieved from: <http://www.ft.com/intl/cms/s/0/bd6ec894-a074-11e2-a6e1-00144feabdc0.html#axzz2bAaqMN3i> (last accessed 6 August 2013).

[10] However, the relative weakness of Brussels during the Balkan war was a nasty shock.

Ludwig Erhard, to let business, and finance have their head, albeit in a socially responsible way.[11]

As the number of member states increased the tension become less creative since it became easier for politicians on either side of the dichotomy to find like-minded people to associate with. In fact, by the 2000s, if not earlier, it became possible to discern two cross-cutting dichotomies.

First of all, a sharp distinction has appeared between two types of political economy, both of which are heavily represented in the EU. On one side of the dichotomy are states in which the voice of 'the market' is held to be the main arbiter of politico-economic behaviour. On the other side there are states in which political leaders and government officials emphasise that their main duty is to serve 'the people' and protect the interests of citizens rather than meet the demands of financiers. Crudely, we may identify these two types according to whether they give priority to big business ('the market') or big government ('the people').

However, on each side of this dichotomy a further distinction may be made. On the one hand, there are political leaders and business elites who take pride in the stern manner with which they stick to clear principles and formal rules. On the other hand, there are politicians and business folk who take a more flamboyant and adventurous approach, with greater tolerance towards rule-bending while, of course, staying inside the law. So we have the stern rule-enforcers and the adventurous rule-benders.

In fact, we can discern four tendencies, although these do not produce four exclusive and permanent groups since there are always marginal cases and countries in which different tendencies compete. We can label these four tendencies and give examples, as follows (see Table 3.1).

First there are the *high priests*. For example, a sternly rule-enforcing governmental approach can be found in Brussels, where the European Commission's bureaucracy is very keen to maintain a high reputation

[11] Ludwig Erhard was West German Chancellor 1963–1966, having been Vice Chancellor 1957–1963 and Minister for Economics from 1949 to 1963.

for competence and probity.[12] Then there are the political *cavaliers*, virtuosos of crowd-pleasing adventurism. In this field we may look to Italy, Romania and Hungary, all prominent examples of political clientelism. On the other side of the dichotomy, we also have two tendencies. One of these consists of the rigorously punctilious *puritans*, prominently represented by the ordoliberals in Frankfurt and Berlin. Finally, profit-seeking big business and finance also has its *buccaneers* and for an example there is no need to look further than London where Boris Johnson is a doughty champion of the capital's neoliberal financial interests.

Table 3.1: Divergent tendencies within the EU

	Big Government	**Big Business**
Stern Rule-Enforcers	*The High Priests* European Commission	*The Puritans* Ordoliberalism
Adventurous Rule-Benders	*The Cavaliers* Political Clientelism	*The Buccaneers* Neoliberalism

With hindsight, it is possible to recognise that all four of these interests – the high priests, the puritans, the cavaliers and the buccaneers – were quite happy to ride along in loose association with each other in the enlarged *peloton* that was the EU 'cycling club' in the early 2000s. Meanwhile, debt levels were high in the private and public sectors. Deficit targets were not being met. The euro was not being supported by the disciplined budgetary practices that were officially required. The ready availability of credit sapped the will of politicians to take the difficult decisions needed to enforce those practices.

In other words, the eurozone 'needed' a 'good' crisis[13] to prepare the

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[12] A recent blog noted 'that the entrance exams for EU officials are tougher than those for most national civil servants. The language skills required also deserve a premium wage. And the level of complexity in crafting policies palatable to all 27 member states is quite unique'. However, high pay and a reputation for arrogance make the bureaucracy vulnerable to criticism. 'The EU gravy "gravy train" in Brussels – fact or fiction?', *Public Service Europe*, 5 June 2013, retrieved from: <http://www.publicserviceeurope.com/editor-blog/211/the-eu-gravy-train-in-brussels-fact-or-fiction> (last accessed 6 August 2013).

[13] See Hilary Clinton's address at the European Parliament in March 2009: 'Clinton: Never waste a good crisis', *The Independent*, 6 March 2009, retrieved from:

ground for pushing forward the project of giving the EU more centralised control over member states. A crisis duly arrived. The credit crunch drained a great deal of liquidity out of the system, bankrupted some prominent finance houses, and turned a number of governments into beggars.

But was it a ‘good’ crisis or a ‘bad’ crisis? Did it prepare the way for a completion of the managed displacement that had begun in the early 1990s? Or did it set the scene for a round of destructive displacement struggles within the EU?

Amidst the mud

Arguably, the collapse of confidence that burst the enormous debt bubble late in 2008 was itself the product of a displacement struggle: the so-called war on terror. Following 9/11, President Bush had committed Washington to wiping the Taliban and Al Qaeda off the face of the earth. That was the big mission of his presidency, the justification for two costly wars. By September 2008, a few weeks before the presidential election it was clear Bush had completely failed to accomplish his mission and was planning to withdraw American troops from Afghanistan and Iraq. Meanwhile, Obama and McCain, two unknown quantities, were neck and neck in the opinion polls.

At a time of maximum political uncertainty the American state’s capacity to enforce its will was thrown into doubt. Surely in some minds the following questions surfaced: since Washington has failed to carry out its threat to destroy its enemies, how strong is the US state in 2008? Does it have the strength it used to have? Does it have the will? Can it even back up its own banking and financial sector? For example, what kind of cover could Washington offer if the huge debt overhang went sour, if institutions starting calling in their loans?

Whatever its origins, when the crisis hit Europe during 2009–2010, it caused the muddy catastrophe depicted earlier. For the first time the EU’s structures were severely tested without the back-up they had previously received from three uplifting and propelling forces: the postwar boom, American investment during the Cold War, and, most

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<http://www.independent.co.uk/news/world/americas/clinton-never-waste-a-good-crisis-1638844.html> (last accessed 6 August 2013).

recently, deregulated finance. When easy credit, the last of these supports, was pulled away the EU came down to earth and hit the ground with an enormous bump.

As is well known, an informal coalition consisting of the European Commission (EC), the European Central Bank (ECB), and the International Monetary Fund (IMF) (the so-called *troika*) gave emergency first aid. They arranged bailouts for some heavily-indebted countries (notably Ireland and Greece) in return for austerity measures; imposed temporary 'technocratic' governments upon Greece and Italy; reassured investors (in July 2012) that the ECB would underwrite large-scale refinancing of national central banks to whatever extent was necessary; and made initial steps towards a European banking union.

The troika's bed-side manner was ghastly, and its triage added to victims' suffering, partly due to the emergency team's miscalculations.[14] Their repertoire of therapies was meagre and miserly. What did Brussels prescribe? Three things, according to Martin Wolf in May 2013: writing off the worst debts; financing existing imbalances; and making each country (i.e. its citizens) bear alone the costs of rebalancing its national economy through lower wages, higher unemployment, reduced services and the like.

This means that for the next few years most of Europe's national economies will be contracting simultaneously, all trying to cope with the attendant social and political shocks. Many people across the EU will suffer and, crucially, they will all be suffering at the same time. This will reduce opportunities for neighbourly cooperation, allowing those who have clambered out of the mud to pull out those still floundering or gathering their strength. It also increases the aggregate level of debt and the overall cost of debt write-offs within the EU.

Wolf believes that 'prospects for desirable longer-term reforms – a banking union and enhanced risk-sharing – look quite remote.' The net result is that the EU's member states will only achieve 'stabilisation' at the cost of growth, losing all economic dynamism. That, we can add, is the price of low trust and unwillingness to cooperate.

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[14] See 'IMF concedes major missteps in bailout of Greece,' *New York Times*, 5 June 2013, retrieved from: <http://www.nytimes.com/2013/06/06/business/global/imf-concedes-major-missteps-in-bailout-of-greece.html?_r=0> (last accessed 6 August 2013).

Defenders of the current approach point to recent reductions in unit labour costs as proof that they are making sick economies more efficient or productive. However, the way this is being done shows that the EU has lost, or is losing, two of its most important characteristics: a strong sense that all member states are equal in dignity and worthiness; and a determination to stop governments humiliating each other and their own people.

A post-humiliation polity offering equality, dignity, and a place at the council table: that was what made countries like Ireland, Greece, Spain, Portugal and ex-members of the 'Eastern Bloc' in Europe look with envy towards Brussels long before they were able to join. But during the half decade since 2008 a small clique of 'northern' governments, under the leadership of Berlin in alliance with Brussels, has seized control of the EU's agenda and institutions and is ruling in quite a different spirit.

A hierarchy of relative worthiness and competence has been asserted with Germany at the top and the 'pigs' (Portugal, Italy, Ireland and Spain) at the bottom. The very acronym PIIGS conveys the humiliation and contempt being poured upon those who had paid the price of, so to speak, being in the wrong place when the music stopped. There is no space here to repeat the familiar story of indignant protest and misery in the countries most affected. Instead, we may simply note that the suicide rate in Greece, traditionally one of the lowest in Europe, is now one of the highest.[15]

Meanwhile, four displacement struggles are under way within the EU (see figure 3.1). The one that has received the most attention is between the puritans (the German ordoliberals) and the cavaliers

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[15] 'The rate of increase in suicides in Greece was the highest in Europe in the first half of 2011, according to figures from the country's health ministry. Experts attribute the rise to the country's economic crisis. Painful austerity measures and a seemingly endless economic drama is exacting a deadly toll on the nation. Statistics released by the Greek ministry of health show a 40 per cent rise in those taking their own lives between January and May this year compared to the same period in 2010. Before the financial crisis first began to bite three years ago, Greece had the lowest suicide rate in Europe at 2.8 per 100,000 inhabitants. It now has almost double that number. Attempted suicides have also increased'. 'Greek woes drive up suicide rates,' *The Guardian*, 18 December 2011, retrieved from: <http://www.guardian.co.uk/world/2011/dec/18/greek-woes-suicide-rate-highest> (last accessed 6 August 2013).

(most notably, the Greeks). However, cutting across this is a confrontation between the City of London, head-quarters of Europe's financial buccaneering tendency, and the high priests who manage the European Commission.

HIGH PRIESTS (European Commission)	→ collaboration ←	PURITANS (ordoliberals)
↓ rivalry ↑	↘ ↙ hostility and alienation ↗ ↖	↓ rivalry ↑
CAVALIERS (Political clientelism)	→ collaboration ←	BUCCANEERS (Neoliberals)

Figure 3.1: Displacement struggles and collaborative relationships in the EU

Both these axes of tension are between interests that know each other very well and have done much business with each other. But in both cases there are vocal pressure groups with intense ideological commitments that find many people and institutions 'on the other side' almost viscerally offensive. So it is with some ordoliberals confronted with 'lazy' and 'immoral' Greeks. So it is with some free-market prophets in London who see Brussels as a dangerous den of red-tape mongers keen to stifle all enterprise. In times of crisis these ideological voices, with analyses long prepared, seize the chance to make their case. If given their head and left unchecked they point the way towards alienation reinforced by hostility.

Two other struggles are under way, less ideological, more pragmatic. One is the rivalry between the buccaneering neoliberal tendency and the puritan ordoliberals: many traders in Frankfurt would like to win business from the UK and subject the City of London to greater European regulation. Meanwhile, cavalier prime ministers such as Victor Orbán of Hungary and Victor Ponta of Romania are in conflict with the high priests in Brussels. The European Commission is trying to overrule their attempts to remodel their countries' national constitutions to give long-lasting political advantages to their parties and themselves. Both sides are talking tough.

It is notable how images from the past are being resurrected in this cauldron of conflict. We have all recently seen doctored images of Angela Merkel wearing a Nazi uniform taken from the Greek press. For his part, Viktor Orbán told a crowd of nearly a quarter of a million Hungarians celebrating the 1848 revolution that Hungary was not going to be a 'colony.' He drew a pointed comparison between Brussels officials with their 'finely tailored suits' and Soviet generals with their 'shoulder patches.'[16] It is striking how the EU, previously focused so optimistically on its future, has become pessimistically preoccupied with a past that its peoples fear might return.

It is not possible to reduce these interwoven conflicts to a dispute between the Teutonic North and the Mediterranean South or a confrontation between government and business. Where would Ireland and Slovenia (respectively, neighbours of Britain and Austria) fit into such an analysis? And how would we account for the current alliance between bureaucratic high priests in Brussels and market-oriented puritans in Berlin, joint architects of current attempts to dig the EU's bus out of the mud? Or how explain the mutually convenient arrangements between buccaneering marketeers and ambitious political cavaliers that have allowed oligarchs to thrive, as in the Czech Republic, and privatisation to flourish, as in Hungary.[17]

After the mud

Before looking at possible futures, let us briefly return to our story about the starry-shirted cycling club with which we began. Remember the club members' heady talk in the wayside tavern about a post-humiliation society, a vision that appealed to many would-be members. Recall the exciting journey of that rather fragmented throng of bikers as they adventured up and down hilly contours,

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[16] In practice, Hungarian government ministers have been more conciliatory, on other matters at least. They invited the so-called Venice Commission (the European Commission for Democracy through Law, an arm of the Council of Europe, established in May 1990) to examine Hungary's recent legislation on judicial reform, oversight of the media and relations between churches and the state. See 'Hungary and Europe – Salami tactics', *The Economist*, 24 March 2012, retrieved from: <http://www.economist.com/node/21551100> (last accessed 6 August 2013).

[17] See 'Blog: Five families that rule Czech Republic', *Akttualne.cz*, 23 May 2012, retrived from <http://aktualne.centrum.cz/czechnews/clanek.phtml?id=746021> (last accessed 6 August 2013); Blinken, D. (2011) 'Privatization helps', *Huffington Post*, 31 July 2011, retrieved from: <http://www.huffingtonpost.com/donald-blinken/privatization-helps-the-h_b_914383.html> (last accessed 6 August 2013).

holding it all together somehow. Recollect the bitter arguments that resounded across the gruesome mud and continued aboard the bus. Now the bus is moving but in which direction? What will be the guiding spirit? Will it be the vision of post-humiliation? Perhaps the lure of picaresque adventurism will prevail, offering careers built through making lucrative deals, cultivating rich friends and building up political empires? Or will we see a resurgence of *nostalgie de la boue*, an atavistic wish to carry on the fights that broke out in the mud? Let us consider these three possibilities, and the futures they might herald.

Possible future I – Europe as an arena of resentment and revenge: Could war possibly return to Europe? This question was asked aloud by Mrs Merkel recently when she was trying to muster all the votes she could for a bailout fund.[18] Scaremongering is a useful political trick, of course – but she is not the only one. In a recent interview, Jean-Claude Juncker, prime minister of Luxembourg and till recently head of the Euro Group said that:

> [A]nyone who believes that the eternal issue of war and peace in Europe has been permanently laid to rest could be making a monumental error. The demons haven't been banished; they are merely sleeping, as the wars in Bosnia and Kosovo have shown us. I am chilled by the realization of how similar circumstances in Europe in 2013 are to those of 100 years ago.[19]

He added that the greatest danger was not armed conflict among EU member states but political fragmentation. This mattered because

> [b]y the middle of this century, Europe will comprise only a good 7 percent of the world's population. Already today, over 80 percent of economic growth comes from other regions of the

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[18] 'Collapse of euro could pose threat to peace, says Angela Merkel', *The Daily Telegraph*, 26 October 2011, retrieved from: <http://www.telegraph.co.uk/news/worldnews/europe/germany/8851912/Merkel-wins-rescue-fund-vote-after-raising-spectre-of-war.html> (last accessed 6 August 2013).

[19] 'Jean-Claude Juncker Interview: "The Demons Haven't Been Banished"', *Der Spiegel*, 11 March 2013, retrieved from: <http://www.spiegel.de/international/europe/spiegel-interview-with-luxembourg-prime-minister-juncker-a-888021.html> (last accessed 6 August 2013).

> globe. A united Europe is our Continent's only chance to avoid falling off the world's radar.[20]

Juncker's argument is a strong one. It directs attention to the two most serious axes of hostility in recent years: between Germany and Greece, and between the City of London and the European Commission. They are serious because they have raised the real possibility that either Greece or the UK may leave the EU. Pressure from inside the EU to force a Greek exit from the eurozone has died away but unpredictable political forces have been released within Greece. At some point it may suit the purposes of Greek political opportunists to break free from 'Northern' tormenters. If that happens, an unstable state would be stepping out of the EU into a potentially volatile region.

Meanwhile, uncertainty about the UK position has increased following Mr Cameron's promise to hold an 'in-out' referendum in Britain if he wins the next general election. The geo-political position of the EU would be weakened by the exit of either Greece, strategically located on the world's east/west and north/south boundaries, or the UK, still one of the world's richest countries. However, such defections need not be fatal as long as they do not start a trend of dissatisfied voters in other countries demanding exit. That seems unlikely, although not entirely impossible if popular hostility to immigrants – a theme common to Greece's Golden Dawn and Britain's UKIP party – became so great that throughout Europe voters were to demand a return to strong national border controls.

In practice, however, the most serious and widespread form of alienation and fragmentation is occurring in the relationship between national political leaderships and their citizens.[21] Many voters do not

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[20] *Ibid.*

[21] It was noteworthy that both Katrina Barysch of the Centre for European Reform and Mats Persson of Open Europe have supported the idea of getting national parliaments more involved in the legislative processes of the European Union. They both gave evidence before the House of Lords EU Sub-committee (on economic and financial affairs), session on 'Genuine Economic and Monetary Union and its Implications for the UK' on 21 May 2013. Transcript not available at time this chapter was written. See <http://www.parliament.uk/business/committees/committees-a-z/lords-select/eu-economic-and-financial-affairs-and-international-trade-sub-committee-a/inquiries/parliament-2010/genuine-economic-monetary-union/> (last accessed 6 August 2013).

expect their politicians to be honest, trustworthy or committed to the good of the electorate. However, few voters organise politically to look after their own interests. Instead, given the chance, a rising number cast anti-votes for anti-politicians, especially charming entertainers such as Beppe Grillo and Nigel Farage. Some serious politicians such as Boris Johnson, defender of London's finance houses, have learned that it pays dividends to mimic this style, and be even funnier. The current plague of political apathy suggests that the EU's structures are relatively safe from attack either on the streets or in the voting booth. The real danger lies elsewhere.

Possible future II – Europe as a corporate milch-cow: The credit crunch has hit citizens, governments and some finance houses in a highly publicised way. Less well advertised are the negative impact upon cash-rich business corporations and the zombie-like condition of Europe's high streets. Citizens are evidently spending at a lower rate and in smaller volumes. While householders cut up their credit cards and concentrate on paying back their mortgages, corporate investors are wondering where the next dividend is coming from. It seems likely that a large part of the answer is by selling services traditionally provided through taxation income in the public sector. This is the sphere that turns citizens' social rights into actual hospital beds, schools, geriatric nurses and so on.

Austerity is sharply reducing government spending in all such areas. Those who can afford it are turning towards private providers, including insurance companies. Health services, education and social care (old peoples' homes and so on) provide potentially lucrative opportunities for corporations with spare funds they want to turn over (see, for example, Albeht 2009; Dan *et al.* 2012; Deloitte 2008).[22]
Alongside endemic voter apathy, and the systematic reduction of the public sector through austerity measures (a truly humiliating form of

[22] See also 'Private healthcare market in Central Europe 2012', *PR Newswire*, 2 October 2012, retrieved from: <http://www.prnewswire.com/news-releases/private-healthcare-market-in-central-europe-2012-172254241.html> (last accessed 6 August 2013); The Economist Intelligence Unit Limited (2011) 'The future of healthcare in Europe', Report from *Economist Intelligence Unit* 2011 sponsored by Jannsen, retrieved from: <http://www.managementthinking.eiu.com/sites/default/files/downloads/EIU-Janssen%20Healthcare_Web%20version.pdf> (last accessed 6 August 2013).

managed displacement), consider a third factor: the great power of business lobbyists in national capitals and in Brussels. One of the tasks of such lobbyists, apart from winning contracts, is to influence policy including the specification of standards (e.g. how many hours may para-medics work or how many children may be looked after by a registered child-minder). Lower standards mean higher profits but worse services, a dilution of social rights. Another lobbyists' tactic is to express resentment ('on behalf of the public') against close monitoring of services by public officials whose task is to ensure that standards of provision are maintained.

The main point is that corporate profits may be secured for future years by privatising services freed up for exploitation by the rolling back of the state. Ironically, this means that in spite of anti-Brussels bile spat out from London there are very powerful business interests – not just European but transatlantic and global – that will use all their muscle power to resist the break-up of the EU. As far as these interests are concerned, Europe is a vast and seamless market, a happy hunting ground. For the large corporations and their lobbyists, the years after 2008 are a bit like the aftermath of 1989. Now, as then, they can eat from the larder of opportunities being released from the grip of governments as politicians cease to take responsibility for the welfare of their citizens.

Possible future III – Europe as a post-humiliation polity: Turning to the third, and most optimistic, vision of the future, it is useful to review what is at stake. The EU now fills the substantial territorial and socio-political space left by the receding tide of American prestige and influence, and the collapse of the Soviet empire and Yugoslavia. The EU's potential global influence is enormous but so are the challenges it faces. Its primary objective should be to protect and sustain the European standard of living and way of life, what Steven Hill has labelled 'Europe's promise' (Hill 2003) and to enable others beyond Europe to achieve those standards and way of life as far as possible.

This European way of life depends on maintaining the shifting and perpetually contentious balance between market and state. This balance makes the EU distinct both from the state-heavy regimes of China or Russia and the market-heavy regime of the United States. In Europe business and government remain in perpetual, though covert and usually polite, struggle, each trying to gain benefits from the other without giving too much away in return. The EU has to remain on the centre ground between two poles: globally, these two poles are well represented by, on one side, the arch-cavalier Mr Putin of Russia, who has tamed his oligarchs, and, on the other side, the arch-buccaneer Mr Murdoch, prince of neo-cons and a highly influential lobbyist in Washington.

An urgent task is to reverse the degradation of citizens' social rights (reduced pension entitlements, diminished child support provision, and so on) and regain ground lost during the austerity blizzard. Where is the money to come from? The obvious answer is that it can only come from those who have it. It is relevant that when challenged, tax-avoiding companies insist they will pay all taxes legally required.[23] They should be taken at their word. They should be asked to make a greater contribution towards the costs of maintaining the 'human capital,' the infrastructures, and other social goods from which they benefit.

Table 3.2: Share of World GDP 2010

EU-27	25.8%
United States	22.9%
China	9.1%
Japan	8.7%
Brazil	3.3%
India	2.7%
Remaining G20 countries*	14.2%
Rest of the world	13.3%

Source: Eurostat and UN Statistics Division

Bear in mind the strong gravitational pull of the European market, even in the near-inert state into which it lapsed following the credit crunch. The EU's aggregate GDP makes it the largest market in the world (see Table 3.2). It is both possible and necessary to extract a greater tax take from businesses throughout the EU. In this way, cash-rich companies can and should make a major contribution towards alleviating the pain of austerity.

[23] See, for example, 'Google boss: We follow the law on tax', *Sky News*, 23 May 2013, retrieved from: <http://news.sky.com/story/1094264/google-boss-we-follow-the-law-on-tax> (last accessed 6 August 2013).

The London Stock Exchange could lend a hand. Doing so might well be a shrewd move on its part. There have been efforts within the EU to reduce the influence and independence of London as a financial centre: for example, proposals to shift control of Libor regulation to Paris, and cap bankers' bonuses. Politically speaking, if the banks and finance houses in the City of London wish to strengthen their position it would be sensible to throw their considerable weight fully behind the campaign to regulate tax havens that Mr Cameron inaugurated when presiding over the G8 in 2013.

How can the rest of us help to ensure the EU retains its distinctive framework of social citizenship and fulfils its ambition to reduce inequality and injustice? One requirement is vigilance in drawing attention to proposed legislative innovations that will undermine these things. For example, in June 2013 Pia Eberhardt of Corporate Europe warned that the EU-US trade deal currently being negotiated contains what is, in effect, she says, a 'transatlantic corporate bill of rights'.[24]

Leaked documents detailing the European Commission's negotiating mandate refer to a 'proposal for investor-state dispute settlement' that would 'enable American companies […] to skirt European courts and directly challenge EU governments at international tribunals, whenever they find that laws in the area of public health, environmental or social protection interfere with their profits.'[25]

Eberhardt lists several corporate lobbyists – including BusinessEurope, the US Chamber of Commerce, AmCham EU, the Transatlantic Business Council – who 'all advocate the inclusion of investor-state arbitration in the proposed free trade deal.'

These lobbyists 'have made clear that industry would oppose any deal in which investment protection was traded off against public policy objectives, including human rights and labour protections.' One example: energy companies such as Chevron would be able, she suggests, to challenge European governments who want to slow down shale gas development on health or environmental grounds and

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[24] Corporate Europe Observatory, 'A transatlantic corporate bill of rights', report, June 2013, retrieved from: <http://corporateeurope.org/trade/2013/06/transatlantic-corporate-bill-rights> (last accessed 15 August 2013).

[25] European companies investing abroad would have the same privilege in the US.

'oblige them "to refrain from undermining legitimate investment-backed expectations".'[26]

Meanwhile, a good motto is: don't panic, especially now the European Commission is beginning to admit that austerity went too far, too fast, and the IMF is also acknowledging that mistakes were made. Given time, and a gradual recovery, Greeks and Germans will hopefully look back with shame on the names they called each other. The heated press coverage has already died down. The historical ghosts raised recently should be dispelled. History is not a guide to our present or future in this case.

Even the very recent past can be thoroughly misleading. Katinka Barysch, deputy director of the Centre for European Reform got it more or less right when giving evidence before a House of Lords sub-committee on 21 May 2013. She pointed out that although 'it is the euro that caused the crisis […] we will not introduce the euro again. We will not have German unification again. And we are learning the lessons from the impact of very fast market liberalization.' [27] In other words:

> If we build a massive edifice right now on the basis of the lessons that we are learning just right now from this […] crisis, and a crisis that perhaps won't return, we might not prevent future crises because they might not be the right measures.[28]

Ms Barysch showed that she did not accept the cliché that we now have a 'German Europe.' Current conditions were temporary and would probably change. As she put it:

> The euro crisis has skewed the political situation in Europe in a way that exacerbates the dominance of Germany. Expect that to be mitigated once the other European economies recover. So if you build something quickly now it will be too rule based, it will be too German, it won't suit the other Europeans, and, very

[26] Corporate Europe Observatory, 'A transatlantic corporate bill of rights', report, June 2013, retrieved from: <http://corporateeurope.org/trade/2013/06/transatlantic-corporate-bill-rights> (last accessed 15 August 2013).
[27] The quotations were taken directly from the television coverage. The official version will presumably be available in Hansard by the time this chapter appears in print.
[28] *Ibid.*

> importantly, if we move too fast in the direction of the European political union right now we leave the people of Europe behind because we have unprecedented low trust in the European project. So I would say we need to make changes but we need to take our time. [29]

Neither Berlin nor Athens should be made a scapegoat for our present troubles. The main obstacle on the road to the EU becoming a post-humiliation polity is neither Germany nor Greece. It is something else. It is the fact that throughout much of Europe business has displaced the citizen as the main voice speaking in the ear of government. This is, indeed, a humiliating piece of managed displacement. It will not be put into reverse without a long and deliberate struggle. The voice of the ordinary citizen voice needs to be heard as well.

In parliamentary democracies such as ours governments ultimately act 'in the name of the people.' It is the voters who produce political legitimacy when they express their will, in elections and sometimes on the streets. As the creators of that legitimacy, the people have a very powerful 'producer interest,' one that abides even when industries collapse and trade unions decay. Politicians like Grillo and Farage are rediscovering the art of mobilising the involvement of voters, and their principal message is that ordinary people must recover their rights and their dignity.

Now this seam of gold has been uncovered, it can be mined by others, but not to reinforce and ride a sense of alienation and hostility against 'outsiders.' The message of renewing citizens' rights and dignity can be fashioned in much more positive ways, especially when linked to the demand that big business must 'step up to the plate' and pay its dues to government. If that is done we have some hope of restoring the proper balance between market and state that has been the basis of Europe's success in the past.

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[29] *Ibid*.

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Chapter 4

The EU crisis in historical perspective

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This paper's argument is structured around three central points. First, postwar European history has been a period of genuine progress. The economic and political integration of Europe, moreover, has played a large role in the achievement of the peaceful, prosperous, and mostly tolerant Europe that we know today. When we narrate European integration history, we are writing a success story – albeit one that is now looking somewhat tarnished.

Second, the historiography, especially the official historiography, of the European Union (EU) has been too prone to recount this successful period of European history from a 'Whig' perspective whereby certain policies and personalities – i.e. those who are closely associated with the project of European integration – are regarded as 'progressives', while their opponents and critics are condemned as reactionaries. All 'advances' in the process of integration are attributed to the progressives; all lulls to the actions of the process' critics. In fact, the opposite has often been true. If we keep an open mind, we see that European integration, leaving aside structural causes, and looking solely at the role of political agents, has several times been brought close to disaster by the actions of its most fervent supporters; by the same token, it has been shaped profoundly by the actions of leaders whose main concern was to protect the interests of the nation states that they represented.

The EU that we see today, in short, is the outcome of a prolonged and recurrent battle of ideas and wills, not the gradual unfolding and prevailing of an ideal.

Third, I have recently begun wondering whether this technical historiographer's work on narrative structure helps us to understand some of the failings of political analysis that have been common during the crisis of the EU of the past few years. What I tentatively suggest in this paper is that the tendency, very evident in the historiography, to polarise the narrative between 'those building Europe' and 'those opposing the European project' is a frequent practice in political analysis, too. Reasoned and reasonable opposition to what is, at any given moment, the emerging consensus is often portrayed as 'eurosceptic' hostility to the European project.

Contemporary European history as an era of progress

I have always been very impressed by Sir Louis Namier's belief that when writing general history,

> the function of a historian is akin to that of the painter and not of the photographic camera; to discover and set forth, to single out and stress that which is the nature of the thing, and not to reproduce indiscriminately all that meets the eye.
>
> (Namier 1972: 379)

Quaint though this phrase may sound in the age of tablets and I-Pads, Namier's insistence that a good historian will try and isolate that which is significant and structure his narrative around it is surely right.

Now, if we are writing a general history of postwar Europe, the crucial starting point is that progress has occurred, if the yardstick for progress is the common-sense one of the happiness and prosperity of peoples, the spread and consolidation of democracy between and within Europe's nation states, and the degree of tolerance and mutual understanding present in our societies.

As individuals, we are fitter, healthier, live longer, have more leisure and more interests. We are more open-minded morally: women work, marriages that fail can be dissolved, people of different skin colour and sexual orientation can marry without social or legal disapprobation. We don't, for the most part, loath other people just because they are Jews, or Catholics, or disabled, or black. Despite some recent alarming instances of intolerance in some European countries, Europeans probably hate less than they ever have done. Those political parties that do try to mobilise emotional opposition to cultural diversity and tolerance are despised by most Europeans – sometimes to the point that we think that they have nothing to tell us, which is often not actually true.

The process of European integration has been a major contributor to this exceptional era of progress in European life. Without European integration, postwar Europe in all probability would have been less peaceful, less prosperous and less democratic.

European Integration has provided a way for France and Germany (and now Poland and Germany) to live together peacefully. It is an exaggeration to say that European integration has brought peace to Europe (NATO and sheer revulsion from war were surely more important), but it is clear that the construction of Europe has provided a way of resolving the main cause of war in the twentieth century, namely the German question. West Germany found a home in the West largely through European integration and the unification of the two Germanies was greatly facilitated by the fact of European integration and the political tensions that might have ensued from the incorporation of East Germany into the West could be peacefully domesticated beneath the 'European roof' evoked by Helmut Kohl in January 1990.

Europe is today a more democratic part of the world than it has ever been: in 1940, nations such as Belgium, Luxembourg, Denmark and the Netherlands were sovereign states in name only, as thinkers like Edward Hallett Carr or Harold J. Laski were at pains to point out (on this point, see Gilbert 2009; Gilbert 2012). European integration has allowed the peoples of the so-called 'small countries' to have a voice in the decision-making of their larger neighbours. This is one of the most important achievements of European integration, although it is one that is often forgotten, perhaps because nation states have primarily benefited from it. In any event, there is less 'autistic realism', to use Christopher Hill's frank term, in Europe today than there has ever been (Hill 2003: 243). It is no longer possible simply to bully small nations into submission – the Greek, Cypriot, Irish and Portuguese bail-outs notwithstanding (and it may be said here that the unease felt by many in Europe at the harshness of the terms imposed upon these countries stems from the fact that we have become unused, *thanks to the process of European integration*, to the spectacle of big countries dictating terms to smaller ones). To this extent, the EU is the institutional incarnation of the ideas of liberal internationalists throughout the twentieth century.

European integration has strengthened democracy in another way: had Greece, Portugal, Spain and several of the countries of the former communist bloc not been allowed to join the EC[1]–EU club, one can be sure that their democratic transitions would have failed, or run into much greater difficulties. This is *not* counter-factual history, merely a thought experiment that enables one to recognise the key significance of the variable of European integration in the overall broader process of European democratisation (although one should also recognise that the converse is true: European integration on its present scale would have been unimaginable without democratisation; indeed, I would argue that European integration is an off-shoot or function of the wider historical process of democratisation in Europe, which is a major reason why historians of contemporary Europe should place a greater weight in their narratives on southern and central Europe than they typically have).

European integration has furthermore helped preserve democracy in the more unstable of the nations that became democratic after World War Two. In the case of Italy, being a founder member of the process of European integration is unquestionably one of the principal causes of the country's postwar success. In his recent book, *La Cenerentola d'Europa* (2010), Antonio Varsori argues that Italians' often uncritical support for European integration derives from its critical role in the country's development. In the 1950s, there were plenty of clerical reactionaries in Christian Democracy who might have been tempted to flirt with Salazarism had De Gasperi not led Italy into Europe: the subsequent economic miracle established the equation 'Europe=

[1] European Communities (EC).

Prosperity' in Italian minds. One cause of the Communist Party's increasing moderation from the late 1960s onwards was its belated realisation that greater European unity was not a cunning American plot, but a project that was bringing concrete rewards to Italian workers; before the Italian Communist Party (PCI) definitively embraced democratic pluralism, support for European unity, along with anticommunism, was one of the few things that Italy's democratic parties shared and gave them a basis for common political action. In the 1990s, as Italian democracy collapsed, the perceived need to qualify for the euro gave incoherent Italian politics a coherent goal to aim for. Italy is hardly a political model for others to copy (Varsori 2010, see especially pages 410–416). Nevertheless, absent its participation in the European construction, Italy would almost certainly have endured catastrophic political upheaval, as opposed to permanent political tension. You can live with the latter, but the former is better avoided.

The example of Italy also underlines the contribution made by European integration to the standard of living of many of its member states. Freer trade between Europe's nations has enormously raised the overall standard of living of Europe's peoples, especially southern Europeans and, since 1989, the peoples of Central Europe; by promoting freer trade in everything but agriculture Europe has also stimulated economic growth around the world and played a major part in generating wider global prosperity.[2]

The fact of European postwar progress is, incidentally, the underlying reason why revisionist works of European integration history, of which

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[2] To anticipate my argument somewhat, the Common Agricultural Policy (CAP) provides a very good example of how the official historiography of the Community, by regarding any policy that strengthened European integration as an 'advance' can be insensitive to other interpretations of the impact that the process of integration has had. Thus Jan van der Harst, in his chapter on the CAP in Michel Dumoulin (ed.) (2007), argues that the 'creation of the CAP was a major contribution through which the divergent interests of the Member States became to a great extent, and almost miraculously, mutually complementary. It is worth underlining that the spillover effect from the agricultural policy helped to bring about European integration' (van der Harst 2007: 336). Van der Harst's argument, in short, is a form of one-eyed utilitarianism. In so far as the CAP generated political unity between the Six it was a 'Good Thing', the havoc it played with world trade flows and the huge costs it has imposed upon European consumers notwithstanding. Ranchers in Argentina, grain producers in Iowa and breadline banana growers in Ecuador might reasonably beg to differ.

John Gillingham's (2003) *European Integration 1950–2003: Superstate or New Market Economy* is perhaps the best known, have been largely unsuccessful. By focusing relentlessly on the EU's evolution into a bureaucratic obstacle to the market economy, Gillingham violently caricatures the EU rather than portrays it, though we should remember that caricatures always capture and exaggerate flaws and imperfections that truly exist. His Namierite camera focused on an important detail and blew it absurdly out of proportion (Gillingham 2003).

Whig history and the interpretation of European integration

So, if the history of postwar Europe is a history of progress in which European integration looms large, how do we tell that story? There is no doubt that the standard narrative, certainly in the more 'official' literature, or the literature written by scholars emotionally committed to the success of European integration, is a quasi-triumphalist one which pictures the European Project as a postwar attempt to overcome the catastrophic legacy of nationalism in Europe. As Jean-Baptiste Duroselle wrote, in his Commission-sponsored history of Europe,

> [the] forty years that have passed since the end of the second World War represent an essential difference with respect to the preceding millennia […] For the first time in history, the governments of European countries have officially committed themselves to a 'process of unification' by means of a policy of mutual accord, rather than conquest and hegemony[…].[3]
>
> (Duroselle 1990: 409)

It has been all too easy to assume that this 'process of unification' was bound to succeed: two Scandinavian scholars, Hagen Schulz-Forberg and Bo Stråth, have recently argued that European integration historiography (and Brussels itself) has been in thrall to teleology and path dependency and has portrayed the EU as a 'goal-driven project that is taking, as if by nature, automatic steps towards ever tighter integration and ever-higher Europeanness' (Schulz-Forberg and Stråth 2010: xi).

3 My translation of the Italian edition. The book was published in French, with English, German and Italian editions.

Certainly many scholars write as if there were a struggle after 1945 between progressive supporters of a federal Europe, or at least of greater economic integration, and national governments, especially those of Britain and France, who fought to preserve national sovereignty and loose intergovernmental structures. Fortunately, thanks to the actions of Schuman and Monnet, De Gasperi and Adenauer, the principle of supranational institutions won out. The European Coal and Steel Community (ECSC) and the European Defence Community (EDC) were approved, outright federalism seemed possible, only for the project to be endangered in August 1954 by the chauvinism of the French national assembly and the craftiness of Pierre Mendes-France, which led to the EDC Treaty, and the allied plans for a European Political Community (EPC) to be hamstrung (for a very good book that nevertheless strongly takes this line, see Preda 1990).

The 'setback' – a favourite word, and what a significant one it is – to the project, however, was soon overcome thanks to a gallant Belgian, Paul-Henri Spaak, who 're-launched' the project at Messina in June 1955. Spaak's initiative survived a concerted attempt by the British to sabotage it (Plan G), and the outmoded Colbertism of the French government, and issued in the March 1957 Rome Treaties. They themselves were only a staging post before the next battle began between tenacious national governments reluctant to accept that great gain for European unity, the CAP, which is the legacy of another 'child of the light', namely Sicco Mansholt.

At this point, the project ran into its most redoubtable opponent, Charles de Gaulle. I have read thousands of reverent mentions to the 'Monnet method' of incremental increases in supranationalism in my time, but never one to the 'Gaullist method' of European integration, which is odd when one reflects that the Luxembourg compromise, which led to thirty years of unanimous voting in the Council of Ministers and created the strong preference for unanimity that exists to this day, and the European Council, which since its beginning in 1974 has been the de facto Cabinet of the EC-EU, are both creations that can be traced back directly to De Gaulle's actions or ideas.

If one looks at the historiography of the Luxembourg compromise, for instance, one will struggle very hard indeed to find an account that does not describe the General as an aggressor, sometimes in very emotional language. Yet what actually happened? Hallstein, the

President of the Commission, in order to get more budgetary power for the Community's supranational institutions, and specifically for the Commission, campaigned for a revision of the EEC Treaty (the treaty establishing the European Economic Community) and secretly instigated the other member states to renege on their longstanding commitments to France over agriculture in order to put pressure on the French government.

De Gaulle found this behaviour despicable and concluded in July 1965 that he could not trust the Commission with the powers it was seeking, nor concede France's veto after 1966. De Gaulle believed that Hallstein and Mansholt, in particular, had 'disqualified themselves as neutral senior officials' by their behaviour. Academic accounts of the 'Empty Chair Crisis' never depict Hallstein as a reckless and untrustworthy bureaucratic empire builder – although the memoirs of the French Commissioner at the time, Robert Marjolin, hint at such an interpretation (Marjolin 1981: 356–365). Wilfrid Loth, in the chapter I'm citing here attacks de Gaulle for having 'vilified' Hallstein as a 'power-hungry technocrat'(Loth 2007: 85, 100) Certainly, serious historians could make the case for seeing the Luxembourg compromise, which eventually resolved the Empty Chair Crisis, as a creative policy choice which enabled the EC to overcome the foolish self-imposed hurdle of qualified majority voting and for seeing the Commission's behaviour as highly dangerous for the survival of the European project as a whole. But if one did that, one would leave the realm of politically acceptable narrative judgment.

Schulz-Forberg and Stråth (2010) actually are wrong, I think, to characterise the EU's self-conception of the progress of European integration as an automatic, teleological forward movement.[4] It is more correct, I think, to see the prevailing narrative as 'Whig history'.

What do we mean by 'Whig history'? The reference is to a small, rather repetitive and in places maddeningly vague essay published in

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[4] In their view, the EU has diverged from its early mission to create a European polity and has become a market-driven, neoliberal project with no authentic dimension of Europeanness. This disjuncture between rhetoric and reality is covered by the 'hypocrisy' mentioned in the title of their book, namely the rhetoric of ever closer union. In effect, Schulz-Forberg and Stråth (2010) regard the post-Maastricht EU as something of a fraud.

1931 by the British historian and historiographer Herbert Butterfield, called *The Whig Interpretation of History*. Butterfield's principal target was the narrative history tradition of British political and constitutional history of the Victorian and Edwardian periods, which depicted the rise of British liberal democracy as a culmination of a centuries-long process whereby greater equality, justice and political freedom had been established as a result of gradual policy choices enacted by Britain's enlightened élites. The important thing to notice is that the subject matter of this interpretation was not false. As a matter of fact, Great Britain had since the seventeenth century gradually suborned the Crown and the aristocracy to the rule of law, had balanced the interests of town and country, and had incorporated the new manufacturing and working classes produced by the Industrial Revolution into the political process. By 1931 women had been given the vote, self-determination had been extended to the Irish and the government was negotiating greater self-government for India. All of this had been achieved, by the standards of continental Europe, with astonishingly little violence (Ireland obviously excepted). If one reads *Whig Interpretation* closely, you see that Butterfield was not disputing the fact of British constitutional and political progress (indeed, during World War Two Butterfield wrote what his biographer C.T. McIntire calls 'a piece of historical scholarship in the service of English patriotism', called *The Englishman and his History*), but rather certain narrative devices that marred the general historiography of the subject (McIntire 2004: 115).

What were these narrative devices? In essence, Butterfield condemns the error of organising general history 'by reference to the present'. Whig historians ask 'how did our (excellent) current state of affairs come about?' instead of doing what historians should do, which is 'the analysis of all the mediations by which the past was turned into our present'. This might sound like a very fine distinction, but in practice it is not, or so Butterfield contends. Historians who prefer the first method, he thinks, tend to assume that at every stage in the historical process there were those whose actions promoted the eventually successful outcome (the 'Whigs') and those who consciously or unconsciously obstructed the unravelling of history's plan (the Tories). As a result:

> if we see in each generation the conflict of the future against the past, the fight of what may be called progressive against reactionary, we shall find ourselves organizing the historical story upon what is really an unfolding principle of progress, and our eyes will be fixed upon certain people who appear as the special agencies of that progress.
>
> (Butterfield 1963[1931]: 45–46)

For Butterfield, this approach is simply mistaken:

> Instead of seeing the modern world emerge as the victory of the children of light over the children of darkness in any generation, it is at least better to see it emerge as a result of a clash of wills, a result which often neither side wanted or even dreamed of […] if we see each generation as a clash of wills out of which there emerged something that probably no man ever willed, our minds become more concentrated upon the process that produced such an unpredictable issue […].
>
> (Butterfield 1973[1931: 54)

In short, we immerse ourselves in a narrative in which we 'recapture the richness of the moments, the humanity of the men, the setting of the external circumstances, and the implications of events […]' (Butterfield 1963[1931]: 69) which is to say that we show history in its full complexity, rather than focus on the struggle between those who were on the right side of history and those whose actions held it back.

To illustrate how applying Butterfield's methodology can lead us to think outside the box of standard EU historiography, let's take two glaring examples of the progressive/reactionary depiction in the historiography, namely Altiero Spinelli and Ernesto Rossi's *Manifesto di Ventotene* (1941), one of the canonical texts of the European movement, and Mrs Thatcher's opposition to Jacques Delors' rapid acceleration of integration after the Single European Act through the so-called 'Bruges Speech'.

Spinelli (Rossi, a very interesting intellectual figure, has subsequently been forgotten outside of Italy) is universally regarded as one of the founding fathers of the EU. A building is named after him at Brussels; his role as a proponent of a federal political union in 1953 and 1983–1984 is venerated; he served as a European Commissioner and wrote many books pressing the cause of a Federal Europe. More to the point, the ideas put forward in the *Manifesto* are regarded as part of the intellectual basis for European integration. The notion that cooperation of Europe's peoples in a federal state was a necessary reaction to the catastrophe undergone by Europe in the first half of the twentieth century at the hands of nationalist regimes is very widely regarded as the pure font from which European integration sprang. Yes, as Alan Milward (1999) contended in *The European Rescue of the Nation State*, the first stages of European integration were driven by the need to provide welfare for Europe's masses, but the ideal of creating the conditions of peace between Europe's nations was ever-present, as even a quick glance at the Schuman Declaration, with its openly stated objective of making future war between Germany and France impossible, illustrates. When scholars label the *Manifesto* a 'federalist' document and Spinelli as a 'federalist' thinker, this is what they mean.

Spinelli and Rossi understood something quite different. Federalism was for them a phase in European history in which nationalism took the place of capitalism as a necessary and in some ways progressive phase in the development of human history.

What Spinelli and Rossi contended in the *Manifesto* is that the age of totalitarianism had been an outcome of the *grandioso processo storico* of liberalisation (since the desire of peoples for self-determination had been transformed by nationalism into imperialism), but that the age of totalitarianism would be a mere parenthesis if the progressives of Europe exploited the military defeat of Nazi Germany and its allies to establish revolutionary socialist regimes willing to take the leap to a *reorganizzazione federale dell'Europa*. What this federalist reorganisation would look like was sketched very vaguely. The *Manifesto* simply says that it will be the 'greatest and most innovative creation to emerge in Europe for centuries', will possess its own armed forces, will 'decisively sweep away economic autarchies' and yet will allow its member states to keep the 'autonomy' that permits 'a flexible expression and development of political life in keeping with the particular characteristics of the various peoples'[5].

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[5] All quotations from Spinelli, A. and Rossi, E. (1941) *Il Manifesto di Ventotene,* retrieved from: <http://www.altierospinelli.org/manifesto/it/manifesto1943it_it.html> (last accessed 7 August 2013). Most scholars of European integration have read

In the case of Italy, as Part Three – *I compiti del dopoguerra e la riforma della società* – makes clear, political development would have been anything but 'flexible'. Italy would need a Republican constitution, 'nationalizations on a massive scale', the abolition of the fascist corporations, an agrarian reform to give land to the peasants, access to education according to merit, the abolition of the *Concordato* between the Vatican and the state and a revival of the state's role in nurturing a 'critical spirit' towards religion.

According to the *Manifesto*, the defeat of Nazi-fascism would be the midwife for such vast changes, in Italy as elsewhere. Europe's nation states were shattered, traditional élites were damaged or destroyed. The myth that nations could remain independent, retaining their sovereignty by means of neutrality or non-aggression pacts, had been disproved by events. The internationalism of the League of Nations had been discredited, as had the principal ruling dynasties of Europe. In this situation, the essential future political conflict was bound to be the battle between the progressive forces intent on superseding the traditional nation state model (which even if it was re-established on socialist lines, inevitably would relapse into war) and reactionary forces, who would try to re-light the flame of patriotism and hence re-establish the old order. The great question would be who would win over the 'popular masses', who would be *materia fusa* 'susceptible to being moulded into new forms' by political actors who had the will to take power and use it.

This would not be done by voting and parliamentary democracy. The *Manifesto* argued explicitly that 'democratic methods will be a dead weight in the revolutionary crisis' since they would only reproduce the abject confusion of the masses about what to do. What was necessary was a committed revolutionary party, composed of the politically enlightened working class and guided by the intellectuals that would act in the name not of 'a still non-existent popular will' but in full consciousness 'of representing the deepest needs of modern society' to establish a 'dictatorship of the revolutionary party' and to construct the new state and create around it a "new democracy'.

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the *Manifesto*, if they have read it at all, in English translation. But the phrases about 'dictatorship of the revolutionary party' are omitted in some English versions.

The logic of the *Manifesto* in short recalls that of the *Social Contract*: In so far as the revolutionary party represented what was good for European society it would be enacting Europe's General Will, i.e. what Europeans ought to want, whether actual Europeans knew it or not. Hence – so long as the Communists didn't get their hands on the revolution and turn Europe into a copy of the bureaucratic despotism in Russia – there was no need to be too alarmed about the word dictatorship. So long as the revolutionary élite from the beginning introduced 'with a firm wrist' the conditions for a free society, political democracy would gradually assert itself as citizens participated in the life of the state and understood and accepted the benefits of the (unfortunately dubbed) 'new order'.

An intelligent ignoramus, unaware of Spinelli's subsequent career and the subsequent history of European integration, would certainly be tempted to use labels other than 'federalist' to characterise the *Manifesto*: these might range from 'utopian socialist', to 'naïve historicist' (for there is certainly much to criticise in the Manifesto's account of the rise of fascism, not least that its broad structural thesis exculpates the German and Italian political cultures of responsibility) to less edifying terms such as 'Jacobin'. The point, however, is that it is not clear how this militant tract, whose vague federalist prescriptions actually occupy only a few brief paragraphs, has any connection whatever with the process of European integration as it was implemented by mostly Catholic, centrist, democratic politicians in the early 1950s, or how it can be regarded, as it certainly is, as a visionary understanding of the significance of supranationalism for Europe. A historian motivated by Butterfield's prescriptions on writing history, and hence less willing to take on trust the notion that he was a 'child of the light', would try to trace the process by which Rossi and Spinelli's ideas permeated the European center-left and perhaps would wonder whether the *Manifesto*'s procedural preference for constructing Europe over the establishment of representative democracy explains anything important about the subsequent evolution of the European project. For myself, I think it does – a history of the early years of European integration that underlines the various strands of elitist thinking that were woven into the project is long overdue.

The case of Mrs Thatcher's Bruges speech is an equally striking illustration of Butterfield's approach. For one can actually make a very strong case for suggesting that Mrs Thatcher was intent on defending the *raison d'être* of the European Community from those, like Jacques Delors, who sought to turn the Community into – the quotation from the Bruges speech is obligatory: 'a European super-state exercising a new dominance from Brussels'[6]. Let's look closely at what the Bruges speech says. Thatcher states quite clearly that:

> Britain does not dream of some cosy, isolated existence on the fringes of the European Community […] Our destiny is in Europe, as part of the Community […] The European Community is the practical means by which Europe can ensure the future prosperity and security of its people in a world in which there are many other powerful nations and groups of nations.

This is a eurosceptic rant? However, Mrs Thatcher argued that the Community should reflect several 'guiding principles'. What were these principles? (1) 'willing and active cooperation between member states is the best way to build a successful European Community'. Thatcher, in short, was in favour of continued and indeed strengthened intergovernmentalism (2) 'Community policies must tackle present problems in a *practical* way, however difficult that may be'. That meant, in particular, dealing with the abuses of the CAP, which had become, in her view, 'unwieldy, inefficient and grossly expensive'. (3) 'My third guiding principle is the need for Community policies which encourage enterprise […] the aim of a Europe open to enterprise is the moving force behind the creation of the single European market by 1992.' Thatcher goes on to argue that more supply-side measures to deregulate protected sectors such as banking, insurance and civil aviation were necessary. (4) 'Europe should not be protectionist […] We must ensure that our approach to world trade is consistent with the liberalization we preach at home'. Thatcher, in short, was arguing for an EC that took an active liberalising role in the Uruguay trade round. Guiding principle (5) was the 'most fundamental issue'. 'Europe must continue to maintain a sure defence through NATO […] We must strive to maintain the United States' commitment to Europe's defence'. The European

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[6] All quotations are from Thatcher, M. (1988) 'Speech to the College of Europe (The Bruges Speech)', retrieved from: <http://www.margaretthatcher.org/document/107332> (last accessed 7 August 2013).

Community, in short, was part of a wider 'Atlantic Community' since 'Europe' was to be found on 'both sides of the Atlantic'.

Thatcher thus thought that it was vital to have a free-trading, liberalising economic community that looked to Washington for defence leadership, focussed upon concrete economic questions rather than lofty visions of culture and identity, and which made key decisions on an intergovernmental basis ('to suppress nationhood and concentrate power at the centre of a European conglomerate would be highly damaging and would jeopardise the objectives we seek to achieve'). Certainly, as Sir Stephen Wall, a senior British diplomat who was at the heart of Britain's European policy under Thatcher, Major and Blair has pointed out,

> [despite] all the heat generated by the speech, it was a statement of British European policy which could have been made by almost all of Mrs Thatcher's predecessors from Macmillan onwards and which has been made, albeit less trenchantly, by every one of them since.[7]
>
> (Wall 2013)

Even more to the point, hers was an understanding of the function and goals of the EC that would have seemed totally unexceptional to Paul-Henri Spaak, Leo Tindemans, Ludwig Erhard, Amintore Fanfani and Helmut Schmidt, not to mention almost every postwar Dutch leader. So why is the speech so often characterised as being hostile to the very notion of European integration? As the 'eurosceptic' document *par excellence*?

The answer is timing, pure and simple. The Bruges speech is made in September 1988, just as the 1992 Initiative began to pick up speed and as the Hannover European Council made the important, though not yet decisive, choice to empower a committee of central bankers to discuss how monetary union could be implemented. There is a distinct shift of gear in the EC's own rhetoric after Hannover. Its self-esteem was on the rise. In 1988, moreover, Jacques Delors began to be the subject of flattering articles in the international press and the

[7] Wall is the author of (2008) *A Stranger in Europe: Britain and the EU from Thatcher to Blair*, Oxford: Oxford University Press.

Community was portrayed more and more often as a wakening giant by U.S. journalists making anthropological forays to Brussels.[8] European analysts, enthusiastically interpreting the *Zeitgeist*, argued that the 1992 Initiative would represent much more than a protracted process of reducing non-tariff barriers and establishing a Community-wide level playing field. They asserted that what was happening was a sign of renewal, after a long period of stall, of the drive towards European unity. European integration, as in the 1950s, was once again invested with an aura of world historical significance (for a particularly forthright example of this literature, see Ludlow 1989).

Mrs Thatcher was hence rowing energetically against the tide, which academic interpreters of European integration have found incomprehensible and perhaps even morally wrong. My point, however, is that if words have meanings it is hard to regard the Bruges speech as eurosceptic, if that word means, as it surely should, outright opposition to the very notion of European institutions and pooled national sovereignty on ethical or political grounds. I suppose one might with justice use labels like 'cautious vision of the Community's role' or 'discordant view of the Community's future policy' to characterise Thatcher's approach, because her speech certainly clashed with the direction being taken by the EC in the late 1980s. But saying more than that seems to me to be unjustified and, to be honest, not necessarily more appropriate than writing 'Mrs Thatcher's clarion call for the Community to respect its traditional priorities'.

My point is that rightly judged, there are no triumphs or setbacks for the process of European integration, only political leaders, or national electorates, disagreeing – often sharply – over what to do. Delors had

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[8] 'Having set a deadline for lifting all economic barriers by the end of 1992, the European Community has raced ahead in recent weeks to eliminate a large number of obstacles […] The Community hopes to remove all border posts so that people can drive from Munich to Malaga without stopping at Customs. And this is only the beginning. Predictions that an all-powerful European president could emerge and hold his or her own against the United States and the Soviet Union are exaggerated, or at least premature. Still, the implications of the economic integration of the 12 nations are immense […]. Although the unification plan was established with economics in mind, it will inevitably have vast political repercussions […] Individually, the nations of Europe find it hard to be seen as equals by the superpowers. It might be a different story with a united Europe of 320 million people.' 'The World Watches Europe, the Power That Will Be', *New York Times*, 31 July 1988.

one vision of the Community's future; Thatcher another. The consequent 'clash of wills' led to Thatcher's isolation and defeat (although this does not mean that her views were without resonance and influence). The historian's job is to study the process of what happened and how it happened, not tell a morality tale. If we take off the distorting lens of the Whig perspective, we see that European integration has on occasion been greatly strengthened as the result of the efforts of proponents of greater intergovernmentalism – the creation of the European Council in 1974, which was anathema to many supporters of European integration – being the classic case. The integration process has also several times been brought close to ruin by the keenest advocates of greater supranationalism, or even outright federalism (witness the saga of the European Defence community, 1952–1954, Hallstein's clash with De Gaulle in 1965, the 'Year of Europe' debate in 1973–1974, and the multiple perpetrators of the would-be Constitution in 2002–2004).

Historians of European integration need, in my view, to adopt a cast of mind whereby the Dutch 'No' Vote in 2005 is understood to be as much part of the evolution of the EU as the signature of the Constitutional Treaty.[9] Recalcitrant voters in Ireland, Denmark, Sweden, France and the Netherlands, not to mention *det norske folk* who obstinately prefer their independence to a place in the European Community of destiny, have dissented from the mainstream view of what the process of integration required, but they did so, usually, for reasons that they considered to be good, not because they were necessarily 'eurosceptic' or 'populist'. Their rejections of one EU proposal or another, moreover, had an effect on how the process of European integration subsequently evolved – which is what, pace Butterfield, historians should be interested in.

Historical analysis as a guide to political understanding

In the last section of this paper, I wish to suggest that Butterfield's understanding of politics as a 'clash of wills' can assist us with political

[9] See Fossum and Menéndez (2011), especially chapter 4, for a rare example of EU scholarship that grasps that the rejection of the Constitution by Dutch and French voters was as much part of the process of European integration (they would say of Constitution-making), as was the Laeken Convention.

analysis of the EU today. Rather than seeing the EU as an institutional arrangement – which is what most political scientists think it is, although they disagree over how it should be categorised, I think the EU can creatively be portrayed as a freewheeling *conversation* to which the institutions have given formal structure. The great achievement of European integration since 1945 is precisely that European nations have stopped barking threats at one another and engaged in mutual debate about where common interests lie. Like any conversation, the EU depends for its continuance on the willingness of its participants to keep talking, and is prone to going off at a tangent as individual participants ride personal hobby horses or refuse to talk about subjects they dislike or fear. When, moreover, the talk stops, and decisions have to be taken, a 'clash of wills' is inevitable, since talking can take us only so far. At every major juncture in its history, the principal participants in the European conversation – the member states, though they are obviously not the only ones – have been faced with the dilemma of whether staying in the conversation was worth their while.

There are good reasons for thinking that the conversation is headed for a genuine quarrel; something that goes beyond the verbal spats that have been a commonplace in the EU's history. If we ask ourselves, 'will the EU survive the crisis of the Euro?', which is the sort of question that many people are quite legitimately asking nowadays, we are faced with a host of shouted, excitable and violently conflicting points of view. Different participants, be they governments, members of the Commission or the European Central Bank (ECB), intellectuals or prize-winning economists are vociferating:

- 'It will if the Commission is given greater power to monitor member state deficit spending and admonish countries that do not abide by the rules';
- 'It will if we create a full banking union regulated by the ECB';
- 'It will if we achieve a full political union, in which an elected executive responding to the European Parliament takes the place of the European Council as the Union's chief decision maker';
- 'It will if the member states squeeze annual deficits on public spending to under 3 per cent of GDP and introduce German-style

reforms to deregulate labour markets and enhance competitiveness';

- 'It will if we create a transfer union to redistribute the gains from the rich North and West to the South and East of the Union';
- 'It will if the EU launches coordinated action among its member states to boost growth, which is the only way to avoid the large-scale social conflict that continued austerity will bring';
- 'It will if we strengthen European identity and construct a sense of European cohesion'.

Other solutions could easily be added – the list is practically endless. Market gurus like Nouriel Roubini can rattle off a dozen policy choices that the EU 'must' make in a single half-page newspaper interview.[10] The two things that all these solutions have in common, however, is that they imply a transfer of yet more authority and political power to the institutions of the EU and that they posit institutional or regulatory fixes to problems that are bound to be politically controversial and hence reduce, at a stroke, the complexity of the answer to the original question by turning them into a question of *technique*, not politics.

Such solutions are, in short, a set of vivid examples of what Michael Oakeshott (1967), in a once-famous but now sadly neglected essay, called 'Rationalism in Politics', namely the belief that politics is the application of technical knowledge, the 'politics of the book', rather than a craft that is acquired through performance and which provides the statesman with practical knowledge, in any given context, of what is politically feasible and what is not. The introduction of the euro itself, in fact, is an even more blatant instance of the 'habit of mind' that Oakeshott was condemning and it may be that the current proliferation of schemes to fix the Euro's shortcomings simply underlines the sagacity of his conviction that 'all that the Rationalist can do when left to himself is to replace one rationalist project in which he has failed by another in which he hopes to succeed' (Oakeshott 1967: 32).

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[10] See, for example, 'ECB must cut rates or risk crisis again - Roubini' *CNN Money*, 11 March 2013, retrieved from: <http://money.cnn.com/2013/03/11/news/economy/europe-ecb-roubini/index.html> (last accessed 7 August 2013).

The heart of the conversation within the EU in the coming years will be the tensions induced by the proposal of technocratic solutions to what are, for individual countries, deeply political questions. This means that for the next few years the EU will be the *site* of a *protean clash of wills*, as political leaders try, for many entirely comprehensible reasons, to support or oppose, or strengthen or dilute, the propositions outlined above (not to mention other questions ignored here, such as social issues like gay marriage). The outcome is entirely uncertain, just as the outcome has always been uncertain at decisive moments throughout the whole history of European integration. To complicate the picture further, the British government is openly campaigning for an EU that does less, and that allows the UK even more opt outs from the Lisbon Treaty than it already possesses, while the Dutch government, traditionally a strong advocate of ever closer union, has weighed in to the conversation by announcing that there are no fewer than 54 core competencies which it believes should remain extraneous from the Brussels policy process (Dutch Government 2013).

In such a political climate, the relevance of studying 'Whig history' is obvious. Is someone who opposes more Commission control over national accounts, the introduction of a banking union, political union, labour market deregulation, transfer union, coordinated growth strategies and artificial attempts to make us more conscious of being 'European', or indeed any single one of these, *necessarily* a 'child of the dark' rather than a 'child of the light'? Is this what being 'eurosceptic' ultimately means? The British government is familiar with being typecast as 'eurosceptic' even when, as in the case of Britain's refusal to join the 'fiscal compact', or indeed to join the euro itself, it was merely doubting that the latest fashionable scheme to solve the EU's problems, or to drive ahead the 'European Project', coincided with its country's long-term economic interests and its own immediate political survival. Will the Dutch now join Britain in the dock of federalist public opinion?

If they do, it will be a pity. European integration, as I have tried to make clear, has not followed a linear progress and many of its most creative policies and institutional solutions can be attributed to the process's critics – to the Tories, not just to the Whigs. The EU that we have today does not even begin to correspond to what the early exponents of unity would have wanted and it is an intellectual error to act as if it is. It is not a democratic federation (and nor is it likely to become one), nor is it a purely intergovernmental 'Union of States', nor, perhaps above all, is it a 'European Dream' providing an alternative model to the U.S. and exporting the 'normative power' of its political and social model to newly developing countries.[11] Rather, it is a mishmash of all these things; the residue of bargains hard-fought, of four generations of statesmen trying to cope with rapidly changing circumstances in creative (or unimaginative) ways, and of policy entrepreneurship by national politicians, European Court of Justice (ECJ) justices, Commission presidents, activist bureaucrats and even civil society, newspaper columnists and intellectuals. The EU in 2023 – assuming, what cannot be assumed, that the inevitable 'clash of wills' is not so shattering as to break the whole edifice asunder – will likewise be an unplottable evolution of the present-day institutional order.[12] Moreover, if history is any guide (and it is), some of the institutional innovations that are most prized and efficacious ten years from now will in all probability have been the brainchildren of statesmen and nations that opposed the conventional wisdom and that were even characterised in the heat of the moment as 'eurosceptic'.

Future historians will have the enjoyable task of pointing such anomalies out. But a positive future outcome – defined as one in which European integration continues to play a crucial role in perpetuating democratic liberal progress in Europe – is only likely to occur if the EU's practitioners and academic cheerleaders are less blithely 'rationalist' in their policy making, and if the 'conversation' of European integration is carried on in civilised tones. The rising tide of euroscepticism, especially in Britain, is universally agreed to be a consequence of Brussels' technocratic distance from EU citizens, of the

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[11] This, of course, was the thesis of arguably the most starry-eyed book on the EU published in the early 21st century (no small claim), Jeremy Rifkin's (2004) *The European Dream: How Europe's Vision of the Future is Quietly Eclipsing the American Dream*. Rifkin's claim that 'Europe has become a giant, freewheeling experimental laboratory for rethinking the human condition and reconfiguring human institutions in the global era' (Rifkin 2004: 83), seems dated in the extreme; like reading a eulogy to the early League of Nations.

[12] I would like to express my debt here to Sir Michael Leigh, until recently Director General for Enlargement at the European Commission. I attended a seminar he gave on the 'EU in 2020' at the Bologna Center of the Johns Hopkins University on 29 November 2012 and the metaphor of the EU 'conversation', which I've developed in this last section of the paper, occurred to me as a result of listening to his lucid, balanced, and thoughtful exposition of why the EU was unlikely to fall apart. A summary of Sir Michael's talk, and three-question video interview, can be found at <http://www.jhubc.it/BIPR/seminarreportsall.cfm> (last accessed 7 August 2013).

EU's failure to preserve European prosperity, and of the tendency to play Goliath to the smaller states in economic difficulties – a tendency that undermines one of the core reasons for the process of European integration's postwar success. In the collective imaginary of several European states, especially in the Mediterranean, Mrs Thatcher's nightmare of a 'super-state' crushing the liberties of the member states has become a reality. The powerbrokers of the EU, both in the major national capitals and in Brussels, need to realise that an essential aspect of any good conversationalist is an ability to listen.

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Chapter 5

The general crisis of the European Union
A genetic approach

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Introduction

In a paper published in 1927 Otto Toeplitz, a distinguished German mathematician, characterised his method of introducing young students to the differential and integral calculus as a genetic, rather than historical, approach. The historian, and also the mathematical historian, Toeplitz argued, must record all that has been done, while he intended to select and utilise from the history of mathematics only those ideas, principles or methods which were at the root of important developments. It is not history for its own sake in which I am interested, he concluded, but the genesis, at crucial points, of problems, principles, and proofs. I find Toeplitz's distinction quite useful also outside the domain of mathematics, and particularly useful for identifying the deeper roots of a complex problem like today's general crisis of the European Union.

The starting point must be the recognition that the present crisis of monetary union is only one aspect, or dimension, of a more general predicament which also involves a worsening legitimacy problem, dysfunctional institutions, the limits of collective leadership and, not least, a decision-making system still largely based on the principle of 'one-decision-fits-all' – a principle inherited from the time when the aim was to establish a common market among the six rather homogeneous founding members of the European Economic Community (Piris 2011). That what the EU is facing today is a general crisis – rather than a specific episode like, say, the *Empty Chair Crisis*, the conflict between France and its five European partners in the 1960s – is not a new insight. Thus Chiti, Menéndez and Teixera (2012), are well aware of the multidimensionality of the present crisis, and include in their analysis broad and to some extent exogenous factors like the American subprime mortgage crisis and even the crisis of neoliberalism. This chapter focuses on endogenous factors. It aims at identifying the principles, assumptions, and operational rules behind, not only the crisis of monetary union, but also the partial or complete failure of other ambitious projects such as the 'Europe '92' Single Market programme; the Lisbon Strategy for Growth and Jobs of the year 2000 – with its promise of making the EU 'the most competitive, knowledge-based economy in the world' by the year 2010; or the 1970 Werner Plan to achieve Economic and Monetary Union (EMU) by 1980.

Since the crisis of the EU is general, it follows that attempts to deal with one particular dimension may affect also other dimensions, perhaps unfavourably. As we shall see later on, for example, the attempt to solve the crisis of the euro by greater centralization of economic, fiscal, and even social policy only aggravates an already serious legitimacy problem – to the point of transforming the EU's democratic deficit into a democratic default. Although the various dimensions of the crisis interact, I submit that the best way to understand the origins of the general crisis, is to start from the crisis of the euro. This is because monetary union, with all its gaps and fragilities, is a kind of metaphor of the entire process of European integration as it has developed so far. The essence of metaphor is 'understanding and experiencing one kind of thing in terms of another' (Lakoff and Johnson 1980: 5). In particular, structural metaphors 'allow us […] to use one highly structured and clearly delineated concept to structure another' (*ibid*.: 61). Precisely because monetary union is a highly structured and clearly delineated concept it allows us to better understand important features of the traditional methods of integration. In short, my argument is that the problems of monetary union reflect the weaknesses and structural flaws of the process of European integration started with the 1957 Treaty of Rome. The reason EMU is so revealing is that, unlike other major EU projects, monetary union inevitably produces results which the average citizen is in a position to assess. The importance of this distinction between EMU and other European projects, including the Single Market, will be stressed in the next section.

One should always keep in mind, however, that the present crisis of the EU is not the crisis of European integration, *tout court*, but only of a particular approach to it – what used to be known as the Community Method, and its functional analogues such as the method followed in establishing monetary union. It would be unnecessary to make such an obvious remark were it not for the widespread tendency, in discussing the EU, to use a synecdoche, i.e., a rhetorical figure of speech in which a part represents the whole as in the expressions 'hired hands' for workers, 'good brains' for intelligent people, or 'Brussels' for the EU institutions. A synecdoche can provide understanding by picking out from the many parts that may be taken to stand for the whole that part which is judged to best illuminate a particular aspect of the whole; but it can be seriously misleading if the judgment is incorrect or unduly biased. Since the autumn 2011, if not sooner, the German chancellor has been repeating that 'if the euro fails then Europe fails'. Europe is larger than the EU and there are many other problems besides the eurocrisis, but presumably the phrase is meant to call attention to the broader implications of the collapse of the common currency by focusing attention on this particular problem: a synecdoche. At the same time, however, the identification of 'Europe' with one particular method of integration suggests that there is only one road to the integration of the old continent, thereby implicitly rejecting other possible approaches.

Functional vs. territorial integration

The point is that if we wish to understand the nature of the present crisis, we must seriously consider alternative modes of integration – alternatives that should be reasonably robust with respect to the two main problems the EU is facing today: excessive centralization in some key domains, and a level of internal diversity that is changing the very nature of the enterprise. Given the present level of socioeconomic heterogeneity in the EU, the model of integration *à la carte* advocated in the past by Ralph Dahrendorf (and before him by David Mitrany) is more flexible, hence more robust, than the two- or multi-speed approach to integration introduced by Tinfemans in the 1970s and recently rediscovered by Jean-Claude Piris and by other authors, including Habermas. While still a member of the European Commission, Dahrendorf wrote a series of newspaper articles, published in 1973 under a *nom de plume*, in which he severely criticised the European institutions and their strategy of integration by stealth. The first of the four principles he advocated as a means of accelerating the integration process was that it is more important to solve problems than to create institutions. This was a clear, if implicit, criticism of integrationist leaders such as Paul-Henri Spaak and Jean Monnet, for whom what mattered most were not concrete results but the creation of European institutions – regardless of what these institutions might do. It was Dahrendorf's third principle that expressed the idea of integration *à la carte*, meaning that 'everyone does what he wants and […] no one must participate in everything', a situation that 'though far from ideal is surely much better than avoiding anything that cannot be cooked in a single pot' (cited in Gillingham 2003: 91–92). This meant that there would be common European policies in areas where the member states have a common interest, but not otherwise. In other words, European integration should be based on functional more than on territorial criteria. This, said Dahrendorf, must become the general rule rather than the exception if we wish to prevent continuous demands for special treatment, destroying in the long run the coherence of the entire system – a prescient anticipation of the present practice of moving ahead by granting opt-outs from treaty obligations.

Unfortunately, none of the forms of differentiated integration discussed by Dahrendorf, by Tindemans, and by other writers in the 1970s were based on, or inspired by, any formal social-scientific theory. This is true also of more recent proposals, such as the ideas advanced by Joschka Fischer in his Humboldt University speech of May 2000, or by the new advocates of multi-speed integration. As far as functional integration is concerned, a sound conceptual basis is provided by the economic theory of clubs, originally developed by James Buchanan (1965), and later applied by Alessandra Casella (1996) to study the interaction between expanding markets and the provision of product standards. She argues, *inter alia*, that if we think of standards as being developed by communities of users, then 'opening trade will modify not only the standards but also the coalitions that express them. As markets […] expand and become more heterogeneous, different coalitions will form across national borders, and their number will rise' (*ibid*.: 149). The relevance of these arguments extends well beyond the narrow area of standard-setting. In fact, Casella's emphasis on heterogeneity among traders as the main force against harmonization and for the multiplication of 'clubs' provides a good theoretical basis for the mode of integration advocated by Dahrendorf (Majone 2009: 215–222).

We can now start to analyse the general crisis of the EU from the 'genetic' viewpoint, i.e., in terms of the ideas, processes, and decisions that are at the root of the current predicament. A natural starting point is the prevailing confusion between two quite different criteria for evaluating the results of European integration achieved so far: by process or in terms of outcomes.

The primacy of process

A basic feature of the traditional approach to integration is the much greater importance attached to process – decision-making methods, institution building, allocation of powers, etc. – rather than to concrete results which citizens can understand and evaluate. The primacy of process over results was affirmed especially by Paul-Henry Spaak, according to whom 'everything which tends toward European organizations' was good. In 1949 he commended a proposal for common European postage stamps as having equal value with any other proposal. In the words of historian Alan Milward: 'Any form of integration, any form of common authority in Europe, had become the indispensable guarantee for postwar security, and he [Spaak] became increasingly indifferent to what that authority might be or do' (Milward 1992: 324). Even today the primacy of process is evident in the criteria generally used to assess the success of strategic decisions taken at European level. Thus an agreement to proceed in a certain direction may be advertised as an achievement of historic significance, though many important issues remain unresolved, and ultimate success is far from being certain. What really counts is having reached a collective agreement, even if the agreement is of the least-common-denominator type.

Agreement on EMU, for example, was celebrated as a turning point in European integration, in spite of the fact that the Maastricht Treaty left a number of fundamental policy questions unanswered. In order to make political agreement possible, questions concerning measures to coordinate economic policies, or to provide compensatory budgetary transfers, were simply sidestepped. Also issues of external monetary policy, unitary external representation of the monetary union, exchange-rate policy, and political accountability were left unsettled. Even the basic question: whether it made economic sense to adopt a one-size-fits-all monetary policy for such structurally different national economies, was never properly discussed. As a result, EMU turned out to be a high-risk project with no easy exit option if things went wrong. The chosen strategy simply assumed an irrevocable commitment to the single currency and accorded no place to failure (Tsoukalis 1993).

The absence of contingency plans – another typical feature of policymaking at EU level – is a direct consequence of the primacy of process over results: given suitable process criteria, 'success' is practically guaranteed. Thus the fact that 'it took only a few weeks for the euro to become the single European currency used in daily transactions from Finland to Portugal and from Ireland to Greece' has been taken as proof of the success of the single currency: 'The success of the launch of the euro is not only technical and economic, it is also and foremost political. The euro is the most visible and practical symbol of the progress towards a political union in Europe' (De Grauwe 2004: 363). What makes this premature celebration notable is less the enthusiastic tone than the fact that the writer is not a pro-integration political leader or a self-interested Brussels bureaucrat but a distinguished monetary economist. One is more prepared to discount the rhetoric of official documents, such as the Commission's White Paper on *European Governance*, or to understand the optimism of EU leaders celebrating the fiftieth anniversary of the signing of the Treaty of Rome (Majone 2009: 81–87).

The reliance on process criteria, with the resulting presumption of 'success', also explains the willingness of EU leaders to compromise their collective credibility by committing themselves to overoptimistic goals. The way monetary union was designed and implemented provides the clearest illustration of the complete disregard, not only of expert opinion, but also of such basic principles of crisis management as the timely preparation of contingency plans and careful attention to signs that may foretell a crisis. The problems with which we are confronted today are not isolated and more or less random accidents, but structural flaws of policymaking in the EU. Monetary union has made these flaws so visible precisely because it has revealed the political and normative limits of evaluation by process.

The principle of *fait accompli*

This principle, which instructs European policymakers to push ahead with integration projects, even the most ambitious ones, without worrying too much about either feasibility or democratic legitimacy, is the foundation of the so-called Monnet method. The most penetrating characterization of this method has been provided by Pascal Lamy, former European Commissioner and erstwhile lieutenant of Commission President Jacques Delors: 'Europe was built in a St. Simonian [i.e., technocratic] way from the beginning, this was Monnet's approach: The people weren't ready to agree to integration, so you had to get on without telling them too much about what was happening'. However, Lamy was honest enough to add: 'Now St. Simonianism is finished. It can't work when you have to face democratic opinion' (cited in Ross 1995: 194). Actually, 'technocratic' – the adjective often used with reference to Monnet's approach – is the wrong label for such an attitude, since the first task of a true expert consists in analysing the conditions under which a given task is at all feasible, and then determining whether the eventual constraints – economic, political, or technological – may be removed, at acceptable costs, before the decision is implemented (Majone 1989: 70-81).

This approach to European integration implies that the success of a collective decision is determined by the decision makers themselves – by the very fact that they agreed on the decision. As already noted, this emphasis on the process of decision-making rather than on actual results excludes *a priori* the possibility of failure. For this reason questions of feasibility are systematically ignored by integrationist leaders, as will be seen in a later section. For example, the feasibility of the goal of the 1970 Werner Plan, monetary union by 1980, was never questioned. The so-called 'bicycle theory' of European integration – according to which integration must keep moving forward, especially in a crisis, for the bicycle (that the EU is seen to be) not to fall – provides a suitable rationalization of *fait accompli*. Over the years systematic application of this principle has generated what I have called a political culture of total optimism (Majone, forthcoming). The basic features of this peculiar political culture emerged in the 1960s and early 1970s – the age of 'permissive consensus', when the integration project was taken for granted by European publics, as part of the political landscape, and did not seem to require any kind of accountability by results. Such a benign attitude was facilitated by the fact that most European policies were too remote from the daily problems of the people to seriously concern public opinion. True, policies such as the Common Agricultural Policy or particular regulatory measures have been questioned and criticised often enough; but controversies and contestations always remained confined within fairly narrow political and academic circles, or within particular interest groups.

Monetary union has completely changed the situation. The risks inherent in the Monnet-Spaak approach to European integration – the principle of *fait accompli* and the primacy of process – can no longer be overlooked: the eurocrisis is making the economic costs of a premature and poorly designed monetary union too obvious to be ignored. The political costs may in the end be even more significant. All the possible solutions of the crisis discussed in Brussels and in the national capitals so far, prescribe greater centralization of fiscal, social, and countercyclical policies, and the establishment of supranational authorities with the requisite powers – all of this without prior political integration and at a time when popular hostility towards 'Europe' is reaching unprecedented levels of intensity. It should be noted that European leaders had enough time to assess both the economic and the political costs of EMU: the relation between monetary union and political integration was a much debated issue during the process of negotiation and ratification of the 1993 Treaty on European Union. Few people remember, or even know, that the move to EMU was supposed to be accompanied by a parallel move to EPU (European Political Union). One of the arguments used by chancellor Kohl to persuade German voters to give up their beloved Deutschemark in favour of a common European currency was that EMU would be the final step before political union. The decision to proceed with monetary union was taken despite the fact that no agreement could be reached on EPU or at least on an effective coordination of national fiscal policies. Thus EMU became the prime example of *fait accompli*, while the relation of monetary to political union continued to be ignored.

When the euro was introduced an American political economist wrote: 'Prudence might have counselled that the European Union take certain steps well before the creation of the euro area' (Henning 2000: 41). He was referring to the many policy questions concerning monetary union left unanswered by the Maastricht Treaty. In spite of such obvious flaws, Wim Duisenberg – who as the then president of the European Central Bank (ECB) should have been better informed about both the shortcomings of the system and the financial conditions of would-be members of the monetary union – was absolutely delighted when, in January 2001, Greece adopted the euro. Like many other Euro-enthusiasts the Dutch central banker was convinced that for the sake of European union it was important to have as many countries as possible in the monetary union, including Greece. Possible risks were totally ignored. Henning, like the majority of American experts, counselled prudence, but the truth is that prudential reasoning is foreign to the principle of *fait accompli*.

The disruptive consequences of the decision to proceed with monetary union regardless of economic and political risks became evident some fifteen years later, with the near bankruptcy of Greece, Portugal and Ireland, and a crisis of the eurozone which not only speculators but also a growing number of experts and policymakers see as threatening the collapse of monetary union, perhaps of the EU itself. Experience has confirmed what economists and economic historians have known for a long time; namely, that monetary union without political union is, if not impossible, at least fragile – as shown, for example, by the short life of the Latin Monetary Union. Founded in 1865 by France, Italy, Belgium, and Switzerland; joined by Greece and Romania two years later; this monetary union ended with the Franco-German war of 1870–71, by which time the system had been already undermined by the monetary manipulations of some member states. What we understand more clearly today is that membership in a monetary union without political union makes a country fiscally fragile. This fragility, as Martin Wolf wrote in the *Financial Times* of 3 May 2011:

> is inherent in the construction: members are neither sovereign states nor components of a federation. The big challenge for the euro zone is to resolve this contradiction. Given the state of public opinion today, as revealed by electoral results and surveys, from Finland to Hungary, and from Sweden to Portugal, a federal solution is impossible. Does this mean that the members of the euro zone can resolve the contradiction only by recovering their sovereignty?

Despite the severity of the crisis, EU leaders continue to display optimism concerning the outcomes of the collective decisions taken in Brussels. This is because they have a vested interest in the preservation of a system that, among other things, allows them to take unpopular measures *in camera* rather than in a direct confrontation with the opposition parties at home. A display of optimism, regardless of actual results, is facilitated by the fact that most decisions taken in Brussels must satisfy different, even conflicting, interests. Thus the decision to proceed with monetary union was supported by leaders who saw EMU as a necessary step towards political union; by those who wished to terminate the 'tyranny of the German Mark'; and by national politicians who correctly assumed that membership in the eurozone would immediately improve the credit rating of their countries, allowing their government to borrow at significantly lower rates of interest. A decision that has to satisfy many different interests must necessarily be ambiguous or incomplete or, most likely, both. In December 2011 Werner Mussler, the Brussels correspondent of the *Frankfurter Allgemeine Zeitung*, summarised in the following terms his experience of sixteen summits in two years to discuss the eurocrisis:

> It is one of the peculiar features of decision making in the EU that the compromises reached at the summits leave much room for different interpretations, so that afterwards everybody can claim victory. But this only means that many questions remain unresolved.
>
> (citation in Sarrazin 2012: 213).

The *acquis communautaire*

Since the beginnings of European integration in the 1950s the key problem facing national leaders and supranational institutions has been how to induce sovereign states to credibly commit themselves to a project which, if successful, would necessarily entail the acceptance of limits on national sovereignty. How to achieve such credible commitments is another example of a general problem most clearly perceived in the case of monetary union. European treaties, like all international treaties and national constitutions, are 'incomplete contracts' to use the language of transaction-cost economics. This means that the parties are unable to foresee accurately all the relevant contingencies that might arise in the implementation of the treaties, and are also unable or unwilling to determine and agree upon a course of action for each possible contingency. Contractual incompleteness can lead to problems of imperfect commitment, such as various forms of pre- and post-contractual opportunism. The founding fathers of the EEC attempted to meet the problems of contractual incompleteness by delegating to the European Commission and Court of Justice the task of filling the gaps in the Rome Treaty. This solution created its own problems, however (Majone 2009). Another device for eliciting credible commitments to the unfolding integration process consisted in making the so-called *acquis communautaire* binding for all present and future member states. The European Commission has defined the *acquis communautaire* as 'the rights and obligations, actual and potential, of the Community system and its institutional framework'. This means that in principle a member state has to accept, *en masse*, the provisions of the treaties, the decisions taken by the institutions pursuant to the treaties, and the case law of the European Court of Justice. At first sight the requirement seems reasonable: after all, anybody wishing to join a club must accept to follow its rules. As a commitment device, however, the *acquis* is problematic, not least because the rules developed by the European Community/Union over half a century are many, complex, and often ambiguous. They have to be interpreted, and considerable discretion is thus involved in their application. For example, the UK and Denmark were officially exempted from the duty of joining the monetary union, while Sweden obtained a *de facto* opt-out when it joined the EU in 1995. On the other hand there is no *de jure* or *de facto* opt-out for countries that joined the Union in 2004 and 2007; the new members, as well as future members, must (in theory) introduce the common currency as part of the *acquis communautaire*. They must first satisfy the convergence criteria, of course, but the collective judgment concerning the satisfaction of the admission criteria is a political decision, as was already the case with Greece and other older members of the EU at the beginning of monetary union.

Moreover, the criteria for admission to the monetary union are purely financial, hence they do not reflect the socioeconomic conditions of a country. This can produce rather paradoxical results. For instance, according to some projections of the European Commission only one member of the EU-27 was expected to satisfy all the criteria of the Stability Pact in 2010: Bulgaria. This country, one of the poorest members of the EU, had the lowest budget deficit of all the member states in 2009, and expected its budget to be balanced in 2010. For Bulgaria, as for many other new member states, the only problematic parameter had been inflation, but because of the global economic crisis also inflation had sharply declined. Thus, the Bulgarian government hoped that the national currency, the lev, would enter the Exchange Rate Mechanism II (a sort of waiting room for countries planning to introduce the euro) already in the Spring of 2010, and to adopt the common currency by 2013 or 2014, ahead of economically more advanced countries (Martens 2009).

The imposition of the *acquis communautaire* on new member states has already produced some unexpected consequences. The accession negotiations for each Central and Eastern European country were structured through bilateral Accession Partnerships setting timetables for harmonization ('alignment') in various areas, and closely monitored by the Commission. This approach left little scope for the candidates to set their own pace and priorities, and caused considerable criticism about the language of 'partnership' being a euphemism for the imposition of EU priorities. In some cases the minimum social standards set by the European directives turned out to be lower than the national standards of the new members, giving their governments an excuse for lowering the level of social protection. Thus, it has been observed that the transposition of the Information and Consultation Directive has been used by the Polish, Slovak, and Estonian governments to weaken the national standards in this area. Also the 1993 Working Time Directive was used by some governments to reduce the cost of overtime, and to support management's demands of more flexible working times (Meardi 2007). In these and other cases, social standards in the new member states have been reduced, rather than raised, by the transposition of EU directives. Thus, acceptance of the *acquis communautaire* has undermined the *acquis national* of the new members, just as policy harmonization in the older member states has often undermined the priorities set by the democratic process at national level.

At the same time, formal acceptance of the *acquis* by older member states has not eliminated such consequences of incomplete commitment as adverse selection and moral hazard. Adverse selection refers to the kind of pre-contractual opportunism that arises when one party to a bargain has private information that can be used to reduce the net benefits of the other contracting partner(s); while moral hazard is a form of post-contractual opportunism that arises when actions required under the contract are not easily observable by the other contracting partners. It is by now more or less openly acknowledged that these two types of opportunism have played a major role in the sovereign-debt crisis of the eurozone. The crisis of monetary union has made the traditional opportunism of the member states too visible to be denied or ignored, as so often in the past. Thus it was always suspected that Greece, as well as other countries with large public debts, engaged in various forms of pre-contractual opportunism in order to be admitted to monetary union as soon as possible. Early admission was considered important for reasons of national prestige, but even more in the hope that transferring power over monetary policy to a central bank supposedly modelled on the Bundesbank, would allow the national governments to import, or free-ride on, Germany's reputation for fiscal discipline. Thus, perverse incentives to conceal information on the true condition of public finances were present from the very beginning of monetary union. What made the temptation irresistible for some countries was the fact that most national governments supported a 'political' decision concerning the flexible application of the Maastricht parameters. They did this in order to start the monetary union with as large a group of participants as possible. As a consequence, countries like Belgium and Italy, with public debts well over 100 per cent of GDP were allowed to join EMU from the beginning, while the financial data presented by Greece and other countries were accepted without any serious scrutiny.

The political decision to adopt a common currency for a group of countries with different economic structures and different approaches to public finance was bound to generate perverse incentives for at least some of the contractual partners. Before the final decision on EMU was taken, the then president of the Bundesbank tried in vain to convince European leaders that

> [m]ore than a single currency, the emerging single European market needs converging policies, which are still not in place in all participating countries. The repeated references to alleged huge savings in transaction costs for the countries of a single currency area are not in the least convincing.
>
> (Poehl 1990: 36)

The truth is that for most political leaders the warnings of the experts about a premature monetary union counted very little when compared with the immediate advantages of monetary union. As soon as a country adopted the euro, its public debt received the highest grade by the international rating agencies, and consequently its government could borrow at about the same interest rate as the most virtuous members of the bloc. This meant that countries like Greece, Portugal, or Spain could borrow at rates well below the double-digit rates they had to pay before adopting the euro.

In particular, the possibility of borrowing at low cost in the international financial market is what made possible the Spanish real-estate boom. As a result of the euro-induced boom, wages and inflation grew much faster in Spain than in Germany or France. At the same time, the ECB, being mainly concerned with the level of inflation in the largest economies of the eurozone – Germany, France, and Italy – allowed the interest rate to remain low: too low for the conditions prevailing in Spain. This is also what happened in the case of Ireland. For a number of years, inflation in this country had been considerably higher than the average inflation in the eurozone. The ECB, however, was mainly concerned with average level of inflation in the eurozone, which average depended heavily on the price level in the larger economies. As a consequence, it kept the interest level much too low with respect to what would have been appropriate for the booming Irish economy. Naturally enough, Irish families took advantage of what were, in real terms, *negative* interest rates to engage in their favourite activity, buying property, until the real estate bubble exploded.

Ignoring feasibility

A political culture of total optimism implies a total disregard of the many constraints – technical, economic, political, institutional, cultural – that severely limit the range of feasible choice of democratically accountable governments. One of the most important tasks of policy analysis, as practiced at the national level, is to identify all the important constraints, evaluate their significance for different implementation strategies, and estimate the costs and benefits of relaxing those constraints that are not absolutely binding. In decision-making at EU level, on the other hand, feasibility analysis is replaced by goal setting and wishful thinking. The examples mentioned in the preceding pages may provide sufficient empirical support for this statement, but a few more instances may be added to show how deep-rooted and general is this insouciant attitude.

At the Hague summit in December 1969, the heads of state and government of the EEC decided to reduce exchange rate flexibility and to move towards economic and monetary union. EMU was to replace the customs union as the main goal of the new decade. A high-level group, chaired by the prime minister of Luxembourg Pierre Werner, was entrusted with the preparation of a report on the establishment of monetary union. In October 1970 Werner presented an ambitious seven-stage plan to achieve this goal within ten years (!) by means of institutional reforms and closer political cooperation. The plan glossed over serious differences of opinion concerning the strategy to be adopted during the transitional period in order to achieve a sufficient harmonization of national economic policies. The crucial difference was whether the Community would move towards monetary alignment – irrevocably fixed parities and the elimination of margins of fluctuation – before the effectiveness of the system of policy coordination had been demonstrated. The countries of the so-called 'monetarist' bloc (led by France and including also Belgium and Luxembourg, with widespread support in the European Commission) held the view that the EEC should move towards monetary alignment even before the system of economic policy coordination had proved its effectiveness. Hence, they were in favour of early steps to fix the exchange rates, as a prelude to full monetary union. While agreeing that imbalances in balance of payments were a sign of financial disequilibrium, the 'monetarists' believed that responsibility for correcting such imbalances lay equally with surplus and with deficit countries. In practice this meant that strong-currency countries with balance of payments surpluses (Germany and the Netherlands, forming the 'economist' group) should support economically weaker countries (such as France and Italy) through currency intervention and the pooling of foreign exchange reserves. The Werner plan attempted to minimise the differences between 'monetarist' and 'economist' positions by proposing parallel progress in both monetary integration and economic policy coordination. The final report of the Werner Group was based on a consensus among its members concerning the ultimate objective of monetary union, and a rather vague compromise between 'economists' and 'monetarists' about the intermediate stages. Paradoxically, but characteristic of planning at the European level, the main conflict within the Werner

Group concerned, not the feasibility of EMU within the short time-scale envisaged, but the strategy to be adopted during the transitional period. The consensus on the assumed feasibility of the goal and the unresolved disagreements about the means turned the realization of EMU into a question of political desirability.

Here is another, more recent, example of complete unconcern for feasibility. At the summit held in the Portuguese capital in March 2000 the EU Council launched the so-called Lisbon Strategy for Growth and Jobs. As already mentioned in the introduction, the European leaders promised that by the year 2010 the Union would become 'the most competitive, knowledge-based economy in the world', thus leaving the United States lagging behind. In order to justify such an ambitious goal it was assumed that the EU would grow at an annual average rate of 3 per cent, so as to create 20 million new jobs; while maintaining a commitment to solidarity and equality and, of course, respecting the environment. The 2010 target had been set by the EU leaders in the heady days of the new century when the European economy was booming – while its basic structural problems remained largely unresolved. The experts knew all along that the goal was in fact unfeasible: it would have required an annual growth rate of productivity of about 4 per cent. Instead, in recent years productivity in Europe had been growing at about 0.5 to 1 per cent, while in the U.S. productivity growth had been about 2 per cent per annum. As in the case of EMU so in the case of the Lisbon strategy the warnings of the experts were simply ignored. Eventually, disappointing economic developments convinced EU leaders that it was wiser to drop the target date of 2010, which they did on the occasion of the 2005 Spring European Council. Surprisingly, the press releases following the Spring 2007 meeting of the same body reported that the heads of state or government of all 27 member states 'acknowledged the success of the Lisbon Strategy for Growth and Jobs, reflected in higher growth and falling unemployment figures'. As it turned out, what the Council celebrated so enthusiastically was a cyclical upswing, not structural growth, as was shown by the data released by the European Statistical Office in August 2007: the Union was still dragging behind the U.S. on practically all indicators (Majone 2009: 195–196). Eventually, the Lisbon Strategy was declared dead in 2011 by Commission President Barroso who, instead of explaining the reasons of the failure, used the occasion to announce the launching of a new 'Europe 2020' project.

Lack of concern about future problems entails, not only a lack of preparations to meet the new situation, but also a sense of shocked surprise when problems arise. Consider the surprise caused in 2005 by the rejection of the draft Constitutional Treaty by impressive majorities of French and Dutch voters – 55 and 65.1 per cent, respectively. In an extraordinary meeting in Brussels in early June 2005 the Presidents of the Commission, of the European Parliament, and of the EU Council at first tried to minimise what had happened. They insisted that the ratification process continue, so that at the end of 2006, when it was scheduled to be completed, a general reassessment of the situation could be made. Their hopes were dashed by the British decision to postpone indefinitely the referendum originally planned for the first half of 2006. Denmark, the Czech Republic, and Poland soon followed the British example, reinforcing the general impression that the Constitutional Treaty was effectively dead. According to informed observers, moreover, the draft Constitution would not have passed popular consultations, not only in 'Eurosceptic' countries like the UK, Denmark, or the Czech Republic, but even in Germany. Yet, the possibility of a rejection of the draft Constitution had never been seriously considered in Brussels: by explicit admission of the president of the European Commission, no 'Plan B' existed.

Integration vs. democracy: the Community method

The nature of the European polity as a system based on the representation of corporate, rather than individual, interests (what in pre-democratic times used to be known as 'mixed government', see Majone 2005: 46–49) appears most clearly in the so-called Community Method. Euro-leaders are still divided on the merits of the method, and especially over whether or not it should be generalised, i.e. extended to all areas of activity of the EU, including foreign policy and defence. Also the popular view of the EU as a polity run by unaccountable bureaucrats rests, in the final analysis, on a simplistic, though not wholly mistaken, understanding of the ways this method operates in practice.

Some authors have proposed to distinguish between a 'classic' Community method derived from the treaties, as interpreted by the Court of Justice of the EU, and some updated version of it. The updated version would include such recent reforms as the non-binding Open Method of Coordination (OMC), and more efficient decision-making rules in the Council – primarily the replacement of unanimity by qualified majority even in areas close to the core of national sovereignty. The validity and/or usefulness of such innovations have been questioned by a number of analysts, however. There seems to be a growing consensus in the literature that OMC has fallen far short of expectations. It has also been argued that OMC and other informal and non-binding new modes of governance, far from enhancing the legitimacy of EU policymaking, threaten to do precisely the opposite. This is because they lack the certainty, transparency, and legal protection that are provided by the classic Community method (see Idema and Kelemen 2006 for a good survey of the relevant literature).

Proposals to make the Community method more efficient by generalizing qualified majority voting raise also serious normative problems. The reformers point out that in a EU with twenty-seven (now twenty-eight) members, governance will be practically impossible without extending QMV to all areas of EU policymaking. The rule of unanimity, they say, is both inefficient and unjust since it gives the possibility to any country, even a very small one, of imposing the *status quo* on the other members of the Union. As I have shown elsewhere, the proposed reforms, if implemented, would actually undermine the very approach they are supposed to improve (Majone 2005: 53–59). An essential feature of the Community mode of governance is that the nature of the prevailing interests determines the method of decision-making. This means that each subject-matter has its own decision-making procedure according to the nature of the interest receiving special protection under the treaties: a unanimous vote in the Council in policy areas of particular relevance to national sovereignty; qualified majority voting in matters where national interests have to be reconciled with the common interest; autonomous powers of decision to the Commission where supranational interests should prevail. This being the case, the proposal to extend QMV to all areas of EU policymaking, far from strengthening the traditional method, would actually subvert it.

The principle that decision rules should be tailored to the nature of the various interests deserving protection is one of the main results of the theory of collective choice as developed by James Buchanan and Gordon Tullock in *The Calculus Of Consent* (1962). The reason why collective activities should *not* be organised through the operation of the same decision rule for all subject-matters is that the costs of collective decision-making to the individual members of the group vary considerably from issue to issue. In general, the more important the issue, the greater the majority required for a collective decision. When basic interests of individual members of the group have to be protected against the potentially negative consequences of a decision, unanimity – or something close to it – is the optimal decision rule.

In the EU context, two more observations are relevant. First, if efficiency in decision-making were the only relevant criterion, then it would be necessary to get rid also of the co-decision procedure, under which the European Parliament enjoys the same status as the Council in the lawmaking process. In fact, it has been demonstrated that in areas where the QMV rule applies, decision-making speed did not accelerate, but actually deteriorated, largely because of the delays stemming from the complex procedures required by co-decision. Second, it is ironic that the Commission, which is among the strongest advocates of generalised QMV, should oppose the veto power that the unanimity rule, where it applies, gives to each member state: with its monopoly of legislative initiative, the Commission also enjoys a power of veto (or at least of 'pre-veto') over legislative ideas it dislikes. In sum, recent proposals to extend the Community method in various directions are hardly convincing, either empirically, theoretically, or normatively. In the following analysis, which is concerned with this method as one of the roots of the EU's democratic deficit, it appears therefore preferable to stick to the traditional view, as it is stated, for instance, in the Commission's White Paper on *European Governance* (Commission 2001: 12).

According to this document, the Community Method rests on three principles:

1. The Commission is independent of the other European institutions; it alone makes legislative and policy proposals. Its independence is meant to strengthen the ability to execute policy, act as guardian of the treaties, and represent the Community in international negotiations.

2. Legislative and budgetary acts are adopted by the Council of Ministers and the European Parliament, always on a proposal made by the Commission.

3. The European Court of Justice guarantees the maintenance of the balance among European institutions, and respect for the rule of law.

It is especially important to understand what is implied by the Commission's monopoly of agenda-setting. First, other European institutions cannot legislate in the absence of a prior proposal from the Commission. It is up to the latter to decide whether the Community should act and, if so, in what legal form, what should the content be, and which implementing procedures should be followed. Second, the Commission can amend its proposal at any time while it is under discussion, but the Council can amend the proposal only by unanimity. On the other hand, if the Council unanimously wishes to adopt a measure that differs from the Commission's proposal, the latter can deprive the main Community legislator of its power of decision by withdrawing its own proposal. Such a sweeping delegation of legislative powers to a non-elected body was a response to the crisis of the mid-1950s. After the collapse of the plans for a democratic, pre-federal European Political Community, the architects of the EEC faced a situation never contemplated by the federalists of the first postwar decade: the existence of a tradeoff between democracy and integration. The fathers of communitarian Europe consistently resolved this tradeoff in favour of integration. The implications of this choice did not appear as serious to them as they appear to us today because it was expected that the competence of the EEC would remain so narrow that the indirect legitimacy provided by the democratic character of the member states would suffice. Even Robert Schuman, father of the Coal and Steel Community and 'European saint' (Milward 1992), thought that the competence of the supranational institutions should be limited to technical problems, and should not extend to functions involving the sovereignty of the member states. Also at the national level, after all, certain technical tasks are delegated to non-majoritarian institutions, such as independent central banks and regulatory bodies. The relatively limited scope of the original plans explains why the debate about the democratic deficit started only after the Single European Act expanded significantly both Community competences and the domain of application of majority voting. What was originally a marginal trade-off – a small sacrifice of democracy for the sake of greater efficiency in limited areas of economic integration – became a surrender of basic principles of representative democracy as the competences of the EU kept growing.

It is indeed hard to imagine how the Community method – designed for a small group of fairly homogeneous West-European countries, mostly averse to nationalism and willing to sacrifice important elements of national sovereignty for the sake of closer integration – could survive more or less intact in a completely different political environment. It seems much more likely that the EU of the future will be characterised by flexible institutional arrangements like those variously described in the literature as 'variable geometry', 'Europe à la carte', 'multi-speed Europe', or by even more radical institutional designs. In this scenario the scope of the Community method would have to be restricted – rather than extended or even generalised, as optimists in Brussels were still advocating a few years ago – and some of its key principles either abandoned or extensively reformed. Only those who continue to believe that the integration process must move in a single direction can imagine that a radical reform of the method must spell the end of the idea of European unity. Even a convinced federalist like Joschka Fischer was prepared to give up the received integration methods in favour of a different, more democratic, approach to political integration. It will be recalled that the project presented by the former German foreign minister in his Berlin speech of May 2000 assumed that the irrevocable commitment to a full-fledged federal union would be preceded by a period of intense *intergovernmental* cooperation, during which supranational institutions would no longer play a significant role. More logically consistent, or perhaps more intellectually honest, than other federalists, Fischer openly expressed his doubts that a democratic federation of democratic states could be established on the foundations of democratically unaccountable institutions.

On the occasion of the celebrations for the fiftieth anniversary of the Rome Treaty some official speakers attributed the accomplishments of half a century of integration to the invention by the Founding Fathers of an original institutional setting, having in the Community method its most significant expression. In choosing a high level of institutionalization as their approach to integration, however, the Founders overlooked the fact that '[i]t is not institutions that create a sense of belonging, but a sense of belonging which makes institutional constraints acceptable' (Guéhenno 1993: 79). Acceptance of institutional constraints is particularly problematic when the effectiveness of the institutions begins to be questioned, or is at any rate less evident than official claims pretend. The effectiveness of the Community method should be most visible in the area of economic integration, and yet according to most economists and economic historians, the contribution of the EEC institutions to the growth of the European economy during the three 'glorious decades' 1945–1975 has been quite limited (Majone 2009: 81–87). After the early phase of rapid catch-up with the United States, development stagnated and even regressed, so that the desire to improve poor economic performance has guided EU policy over the last thirty years. In spite of ambitious projects such as EMU and the Single Market, the Community method has thus proved unable to reverse, and even to stop, the steady deterioration of the relative position of the EU as a whole with respect to its major international competitors.

Moreover, if it is true that the Community method puts the European Commission 'at the heart of the Union' as some authors have asserted, then it follows that the political weakness of this institution since the end of the Delors era could not but reduce the effectiveness of the method. Centrally positioned in the institutional architecture of the EC/EU, the Commission has been able to play a number of roles not explicitly envisaged by the treaties. For instance, it has often been a broker and mediator of interests at several points of the policy process; in particular, in Council of Ministers meetings, which it attends at all levels – working parties, Permanent Representatives, and Ministers – as a nonvoting but nonetheless traditionally influential participant. Closely related to, and partly overlapping with, its role as 'honest broker', the Commission has been a facilitator of EU decision-making by presenting itself as the body best able to provide the necessary information. But even aside from the Commission's present political weakness and the growing distrust of the member states, its role as honest broker, mediator, and facilitator was bound to decrease in time, the reason being that the significance of such functions is inversely related to the level of available information.

In an information-poor environment productive interchange is made possible by the presence of persons or institutions in a position to know the resources, constraints, and preferences of the potential transactors. In an information-rich environment, on the other hand, transactions can be carried out directly by the interested parties. This is the gist of the arc-of-information hypothesis advanced by Miles Kahler in an important study of international institutions and economic integration (Kahler 1995). According to this hypothesis, when information about national preferences is scarce and expensive, a substantial degree of information-gathering is required before strong, centralised institutions can emerge; but when information is plentiful and cheap, decentralization is likely to be more efficient in transaction-costs terms. In other words: 'when levels of information are very low, formal and centralised institutions cannot be constructed; when they are high, such institutions are unnecessary' (Keohane 1995: 142). With specific reference to the EU, Kahler conjectured that 'Europe's highly centralised institutions may seem less necessary as economic integration and political understanding produce an increasingly information-rich environment' (Kahler 1995: 123). He cited mutual recognition and the debate on the principle of subsidiarity since the Maastricht Treaty as evidence supporting his hypothesis of growing decentralization. True, neither subsidiarity nor mutual recognition have proved sufficiently robust in practice to directly affect the institutional evolution of the EU. The prediction of eventual institutional decentralization is likely to prove correct, however.

From the democratic deficit to a democratic default?

In January 2011 the magazine *Der Spiegel* revealed that the German chancellor was working out plans for an 'economic government' of the eurozone. The first step in the new strategy to further integrate the EU on economic issues was to be the 'Pact for Competitiveness' – a long-term plan intended to provide a permanent solution for the ongoing eurocrisis. The Pact would obligate all eurozone members to adhere to sound fiscal *and* social policies, including reform of the national pension systems to reflect demographic developments, and modest wage increases that should no longer be adapted automatically to rising prices. In short, Frau Merkel proposed that the countries of the eurozone, and perhaps later all EU member states, should 'dovetail' (*verzahnen*) their economic and social policies. Biting criticism of the Pact for Competitiveness came from across the EU: from long-time members of the Union and from the new members of Central and Eastern Europe; from small and large countries; from debt-ridden southern countries and fiscally virtuous northern countries; even from the head of the European Commission. The Belgian Prime Minister Yves Laterme pointed out that coupling wages to price trends has been part of his country's social model for decades. Werner Faymann, the Austrian chancellor, opposed Merkel's pension plans saying: 'I am not willing to tell my countrymen that they have to work longer'. Luxembourg Prime Minister and then chairman of the group of finance ministers of the eurozone, Jean-Claude Juncker, found the idea of eliminating wage increases pegged to inflation no more promising than an earlier proposal to suspend voting rights in the European Council for the countries that violated EU budget deficit rules. Commission President Barroso expressed fears that the Competitiveness Pact would undermine the single market, a concern shared by British Prime Minister David Cameron (*Spiegel On Line International,* 14 February 2011). Because of such widespread reactions to attempts to use the crisis of the euro to bend the social policies of the member states to the needs of monetary union, Frau Merkel's Pact for Competitiveness had to be shelved, but not the goal of greater centralization, or tighter harmonization, of national economic, fiscal, and social policies.

The fact that only one year later most national leaders were prepared to accept even more stringent conditions than those foreseen by the Pact is a clear indication of the steady worsening of the crisis. A new, much stricter, regime of regulation and control of national budgetary and economic policymaking was established in 2012 by the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union ('Stability Treaty', signed as an international treaty by all EU member states other than the United Kingdom and the Czech Republic), together with a group of regulations, issued in 2011, concerning enforcement of budgetary surveillance in the eurozone; enforcement measures to correct excessive macroeconomic imbalances; strengthening of the surveillance and coordination of economic policies; the prevention and correction of macroeconomic imbalances. The aim of the new regime is to ensure that the members of the eurozone fulfil three main duties: to achieve a balanced budget; to avoid an excessive government deficit; and to prevent or correct macroeconomic imbalances – the latter duty being in fact a general obligation of all member states, since it concerns general economic policy rather than monetary and fiscal policy. Under the first duty each eurozone member state must submit a stability programme to the Council of Economic and Financial Affairs (ECOFIN) and the Commission, setting out, among other things, the budgetary and economic policy measures being taken; government liabilities; and the assumptions made about economic developments. However, the central task of each national government is to set a medium-term budgetary objective (MTBO), with a realistic target and a plan to realise it. This will be assessed by the Council which can 'invite' the government to adjust its programme if it is unhappy with it. The Stability Treaty states that the budget of all signatories of the treaty must be balanced or in surplus. The balanced budget rule is considered so central that it is to be set in a binding and permanent national law, preferably of a constitutional character. Hence, the MTBO is the central norm for all states. Countries that do not have a balanced budget must set out adjustment plans towards reaching their MTBO, and make sufficient progress towards achieving this goal each year. The adjustment plan will set out what needs to be done each year in a very exacting way: 'it is the adjustment plan which moves States into a regime where their budgetary planning is co-governed by the EU institutions' (Chalmers 2012: 679).

The second duty of the member states – to avoid an excessive public deficit, i.e., a situation where there is a planned or actual budget deficit of more than three per cent of GDP or total government debt of more than sixty per cent of GDP – requires debt reductions for the majority of eurozone states that do not satisfy these parameters. For states with large public debts this may amount to repaying several percentage points of GDP each year. The Stability Treaty requires each member state found to have an excessive deficit to put in place a 'budget and economic partnership'– to be approved by the Council and the Commission – setting out structural reforms to ensure a durable correction of its deficit. Hence,

> Co-government is not simply […] about debt reduction but about extensive reform which will limit the State's need to borrow, either because it has smaller expenditure requirements (i.e., a smaller welfare state) or has secured higher tax receipts. The partnership will, therefore, go to the structure and rationale of a State's fiscal and welfare systems.
>
> (Chalmers 2012: 680)

Concerning the final duty of member states – to correct macroeconomic imbalances, defined as developments which may potentially affect the proper functioning of the economy of a member state, of the eurozone, or of the entire EU – an alert mechanism is established to facilitate early identification and monitoring of such conditions. States identified as experiencing excessive imbalances have to agree a corrective action plan with the Council, spelling out detailed policies, provisions for surveillance, and a time table: again, a regime of co-management between national governments and European institutions, notably the Commission and ECOFIN. The Commission assesses the possibility of an excessive imbalance (or of an excessive deficit) and ECOFIN then decides about the presence of these conditions. During these procedures the state under investigation is subject to monitoring by the Commission, and is expected to provide regular reports on its progress in correcting the imbalances. To be noted that ECOFIN includes the finance ministers of both debtor and creditor countries, the latter being consistently in favour of a strict disciplinary approach, so as to minimise the risk of having to offer more financial support to the countries in financial difficulties.

The traditional role of the national parliaments is significantly constrained by these new regimes. Thus member states are supposed to present their budgetary plans to the Commission and to the group of Finance Ministers of the eurozone no later than October 15, with the Commission giving its opinion before the 30th of November; the opinion is then discussed by the Eurogroup. In other words, the Commission, not the national parliament, is the first institution where the proposed budget of a country in financial difficulties is examined. Moreover, the national legislature has only one month to adopt the budgetary law after the Commission opinion. This is because budgetary laws are supposed to be synchronised across the eurozone so that they are adopted no later than 31 December. The final outcome may well be that:

> [a] zone of influence dominated by the Commission and ECOFIN is established, with political conflicts taking place within these, but the atrophying of local democracy leads to a hollowing out of domestic processes so that these become little more than administrative containers.
>
> (Chalmers 2012: 693)

At that point the democratic deficit of the EU would turn into a democratic default.

Even under present arrangements the political costs of financial aid for debtor countries are extremely high. The detailed conditions which must be satisfied by a country receiving financial aid are specified in a 'Memorandum of Understanding', which is usually updated quarterly. These Memoranda and their updates cut ever more deeply into details of national legislation. Fritz Scharpf (2011: 19) gives the example of the 2010 Memorandum for Greece. The second update of 22 November 2010 included a commitment to 'comprehensive reform of the health care system', which in the third update of 23 February 2011 was further specified to include detailed targets for the pricing of generics and for the methods by which social security funds pay doctors. In the Irish case the Memorandum of Understanding of 8 December 2010 'was more detailed on reforms of the banking system but also included precise commitments on labour market and pension reforms, on cuts in public-sector employment and pay, in cuts in social programs and reductions of the statutory minimum wage' (*ibid*.). If national authorities wish to adopt policies that are not consistent with the Memorandum, they must consult with the European Commission, the ECB and the International Monetary Fund (IMF). The Irish Memorandum goes on to state that the authorities 'will also provide the European Commission, the ECB and the IMF with all information requested. […] Prior to the release of the instalments, the authorities shall provide a compliance report on the fulfilment of the conditionality'. Scharpf concludes: 'once an EMU member state has applied for the protection of the European rescue funds, its government will be operating under a form of "receivership"'. This explains the reluctance of countries like Spain and Italy to apply for such funds, despite the insistence of the ECB and the Commission.

Actually, 'receivership' might even be too mild a term for the conditions imposed on the borrowers. Max Keiser, a British TV presenter and former Wall Street broker, spoke instead of an 'occupation regime' imposed by the troika (cited in Scharpf 2011: 20), and if some recent reports are correct, the reference to the consequence of military defeat is not inappropriate. For example, in 2011 the Irish budget was sent first to Germany for approval before it was even seen by the Irish parliament. According to usually well-informed observers, the 40-page document detailing Ireland's budget plans for 2012 and 2013, and the covering letters of intent from Minister of Finance Michael Noonan were sent to the European

Commission by the troika following its third quarterly review of the implementation of the austerity measures prescribed by the Memorandum of Understanding. This material was then made available to the finance committee of the German parliament where it was discussed – presumably to satisfy the requirement of the German Constitutional Court that the Bundestag must be aware of Germany's financial commitments and risks. The paradox is that in order to satisfy its constitutional obligations the German parliament had to infringe a basic right of the equally sovereign parliament of a fellow member state. It hard to find a better illustration of the normative costs entailed by the current attempts to resolve the crisis of the eurozone without facing the deeper problems of a premature and poorly designed monetary union. As the crisis intensifies, all the proposed ad hoc solutions tend to aggravate the democratic deficit of the EU. It is not only the citizens that are being excluded from the debate about the future European integration, but also most national governments that are forced to accept the solutions proposed by a few national leaders representing the major stockholders of the ECB.

Unsurprisingly, by the summer 2012 the distance between European citizens and EU institutions had reached a level unimaginable only a few years before, as made evident by massive anti-EU demonstrations in Athens, Lisbon, Madrid, and Barcelona. In Hungary burning the EU flag became a proper way of expressing deep dissatisfaction with the perceived indifference of 'Europe' to the severe financial crisis of the country. According to Làzlò Lengyel, a Hungarian economist and publicist, what is happening in East Europe today is in many respects similar to the disenchantment with socialism of the 1970s and 1980s. Hungary was the first country to which were applied the sanctions foreseen by the new regime of supranational regulation and control of national budgetary and economic policymaking. This led not only to demonstrations in Budapest of 200,000 people, but also to prime minister Victor Orbàn denouncing EU's 'colonialism' (*BBC News*, 16 March 2012). Cristian Parvulescu, a Rumanian political scientist, explains that the great expectations which East Europeans had linked to the membership of their country in the EU have been largely disappointed. The consequence is what we observe today: a return to populism and nationalism. The developments in Hungary, he concludes, should be an alarm signal. The politics of Hungarian prime minister Viktor Orbàn are seen as serious attempts to find nationalist solutions to the problems of the country also by the Bulgarian political scientist Iwan Krastew, who warns about the risks of dismissing Orbàn as a nut. The EU's would be faced with a serious situation if the Hungarian model started to have followers in four or five East European countries. The EU is no longer perceived as a factor of stability in East Europe; from the Baltic republics to Bulgaria, with the only significant exception of Poland, hardly any of the new member states is firmly behind European projects (citations in Versek 2012).

An odd consequence of the crisis in some countries of West Europe has been the revival of the old neofunctionalist faith in the virtues of technocracy. Ernest Haas and his disciples believed that all crucial decisions are made by elites – public-policy makers, economic elites, professional associations, experts, etc. – so that a parliamentary majority is not required to make policy. So far the technocratic revival has not produced the expected results, however. In Greece the technocratic government of prime minister Papademos, a former central banker, did not have sufficient freedom of action because it had to act under the strict bail-out conditions administered by the troika. Hence the experiment was not repeated after the elections of May and June 2012: the Greeks seem to have concluded that under the tight constraints imposed by the EU and the IMF, the distinction between technocrats and politicians supported by highly variegated majorities, becomes elusive.

Implications for the EU

What makes the crisis of the eurozone so important, and so revealing of the more general crisis of the EU, is the fact that the actual consequences of decisions taken at the European level are now so much more visible than they were in earlier stages of the integration process. Buyers are typically interested in the quality and price of a finished product, not in the way it is produced, or in the internal organization of the firm that produces it. Similarly, the 'buyers' of public policy, voters and the citizens at large, are interested in the quality and tax-prices of specific policy outcomes, not in administrative procedures and decision-making processes. Thus, an important, if unanticipated, consequence of monetary union has been to make possible for everybody to question the effectiveness of European policies. Unlike most policy decisions taken in Brussels, the decisions taken by the ECB are widely advertised, and their consequences – whether on home mortgages, on consumer credit, or on the availability of publicly-financed services – have a direct impact on the welfare of all inhabitants of the eurozone, indeed of the entire EU. Also the Bank's non-decisions, e.g., concerning variations in the discount rate, are often discussed in the media. Since the beginning of the crisis of the eurozone, moreover, everybody realises that integration entails costs as well as benefits, and that a positive net balance of benefits over costs can no longer be taken for granted. This new realism is likely to generate a much stronger demand of accountability by results – precisely what is foreign to the political culture of EU leaders. And once results become visible, the normative consequences of failures to deliver the goods can be significant.

Legitimacy, Martin Lipset noted, involves the capacity of a political system to engender and maintain the belief that its institutions are capable of resolving the major problems facing society. He went on to explain that while effectiveness is primarily instrumental, legitimacy is evaluative. Nevertheless, the two concepts are linked:

> After a new social structure is established, if the new system is unable to sustain the expectations of major groups (on the ground of 'effectiveness') for a long enough period to develop legitimacy upon the new basis, a new crisis may develop. […] On the other hand, a breakdown of effectiveness, repeatedly or for a long period, will endanger even a legitimate systems stability.
>
> (Lipset 1963: 65, 67–68)

It is this connection between effectiveness, legitimacy, and systemic stability which makes so worrisome the unsatisfactory economic performance of the last decades, and especially the present crisis of the eurozone. Indeed, the basic reason why today public debate and hostile public reactions have replaced the permissive consensus of the past is precisely the fact that monetary union has put an end to the primacy of process as *the* criterion of policy evaluation in the EU. As long as the permissive consensus lasted, the issue of the democratic deficit did not arise. The consensus began to erode as the EC enlarged and acquired more powers, first with the Single European Act and later with the Maastricht Treaty. Indeed, the ratification crisis of the latter treaty – which led to the opt-outs of Great Britain and Denmark from monetary union – showed that by the early 1990s a permissive consensus no longer existed. This was the time when the democratic deficit became a serious issue.

A number of EU leaders now argue that even if European integration has not delivered all the hoped-for economic benefits, at least it has delivered fifty years of peace and stability in Europe. It is certainly true that since the end of the war Western Europe has enjoyed over half a century of uninterrupted peace. What is doubtful, however, is the causal role of European integration in preserving peace in the old continent: the Nobel Peace Prize is not sufficient evidence! A moment's reflection suggests that it is hardly believable that after the disastrous results of two world wars in fifty years, Europeans had either the resources or the will to use again military means to resolve their conflicts – a conclusion which the distinguished Princeton economist, Albert Hirschman, had already reached three decades ago:

> [T]he European Community arrived a bit late in history for its widely proclaimed mission, which was to avert further wars *between* the major Western European nations; even without the Community the time for such wars was past after the two exhausting world wars of the first half of the twentieth century.
> (Hirschman 1981: 281; emphasis in the original)

Aspirations to enduring peace and the 'repudiation of war' expressed in the post-1945 constitutions of countries like Germany and Italy explain the reluctance of the members of the EU to engage in military actions – not only in distant theatres, but even in Europe's backyard. When the Yugoslav crisis broke out in June 1991, Jacques Poos, the foreign minister of Luxembourg and President of the European Council for the first six months of that year, declared: 'This is the hour of Europe, not the hour of the Americans'. Unfortunately, the EU proved unable to enforce stability and peaceful coexistence among the peoples of the former federation, and had to appeal to the United States for help. The civil war in Bosnia was ended by the intervention of the American superpower, which then mediated and guaranteed the Dayton Agreement of November 1995 between Serbs, Croatians, and Moslems. Four years later, this time in Kosovo, the EU displayed again its inability to ensure peace and respect of basic human rights even in areas of clear European interest.

In sum, a most important, if unintended, consequence of monetary union has been the injection of a good dose of realism in the discourse about European integration. The implications of this change are vast. On the one hand, a culture of total optimism cannot survive once the benefits and costs of European integration are assessed more realistically; on the other hand, this new realism means that it is no longer possible to de-politicise the integration process in the sense of disregarding the opinion of voters. If the picture sketched in the preceding pages is even approximately correct the only reasonable conclusion can be: back to the drawing board! Keeping in mind, however, that what has failed in so many respects is not European integration tout court, as so many EU leaders would have us believe, but a particularly unimaginative and inadequate approach to integration: unimaginative because it followed too closely the model it wanted to make obsolete: the national state; inadequate, because it failed even to approximate the level of popular support enjoyed by the same national state.

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Chapter 6

Crisis and change in Greece
What price democracy?

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Greece has been in crisis mode for five years now. The roots of Greece's financial woes have been analysed quite extensively, and the consensus is that the country's core state functions are badly in need of reform. At the same time, the austerity 'therapy' that the country is currently following at the behest of its EU partners and principal lenders has come under scrutiny and fire for going about the needed reforms the wrong way. Many predict that Greece is doomed to fail, pointing at the country's poor track record of economic reform, or to its gargantuan debt and severe social problems that both the crisis itself and the counter-crisis measures have brought about. This chapter argues that, indeed, reform as is currently being attempted is unlikely to succeed, but that the reasons listed above are proxy causes of reform failure. What determines the success of counter-crisis reforms in a democratic state is the extent to which these can stand up to democratic scrutiny – a prerequisite for their long-term (democratic) legitimacy.

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For the purposes of my analysis here, I identify two core components of democracy, which underpin, in one form or another, all models of democratic governance in theory and practice: a) *autonomy* (citizens are politically autonomous, in that they are not only subjects but also authors of their laws); and b) *accountability* (citizens are able to hold their representatives accountable) (see, for example, Barber 2003 [1984]; Fraser 1990; Saward 1998; United Nations General Assembly 2005). In times of crisis, it may be seemingly impossible to reconcile effective crisis management, which relies on quick executive decisions, with the democratic control mechanisms designed to preserve and enforce autonomy and accountability. This apparent conflict of interests between crisis management and democratic governance is amplified exponentially when both governance and crisis unfold in an internationalised context. On the one hand, internationalisation appears to be not fully compatible with democratic governance (e.g. Wolf 1999; Papadopoulos 2007). On the other hand, internationalisation makes effective crisis management more difficult, if not elusive. This is because it increases the likelihood of a crisis 'spill-over' from the originally affected polity into those interconnected with it, thus lengthening the chain of institutions or executive bodies tasked with crisis management and critically slowing down response times. Nowhere is this more evident than in the case of 'multilevel governance' European Union (EU), whose extensively analysed (and long-disputed) democratic deficit and decision-making (in)effectiveness have come under more intense scrutiny during the ongoing Eurocrisis (see Fossum and Menendez in this volume; also Crum and Fossum 2013; Hodson and Puetter 2013).

The first point I argue in this chapter is that this dual incompatibility of effective crisis management with democratic and internationalised governance is superficial. For a crisis to be successfully contained and overcome, adherence to democratic standards is a prerequisite. In the case of Greece, even with the added complication layer of 'multilevel' democracy (Crum and Fossum 2009), the issue at stake remains: Do the current counter-crisis reforms in Greece satisfy the core criteria of democratic governance, i.e. the conditions for long-term democratic legitimacy? To answer this, I look at the democratic credibility not only of the counter-crisis measures taken, but also of their public justification. In the last part of the chapter I conclude that, in light of this brief democratic evaluation, the current reform path followed in the case of Greece leads to the normalisation of non-democratic governance both at national and EU levels, which in turn has a cumulative effect on the transformation (or mutation) of democracy in substantive terms.

Democratic crisis reform: an oxymoron?

Crises cause four things to happen: Firstly, they violate expectations of what is understood as 'normal' or 'how things should be' and thus create the need and demand for 'relatively rapid response to contain or mitigate the harm' (Hermann 1963; Seeger *et al.* 2003). Secondly, they are disruptive: they interrupt the function of an organisation thus posing a threat to the achievement of commonly agreed goals and/or affecting the performance of common problem-solving mechanisms, hence the need for rapid response. Thirdly, as threatening situations that belie expectations of normality and have widespread negative repercussions, they inevitably create high levels of uncertainty, focus the attention of the media and increase the public's demand for information (Seeger *et al.* 2003; Gonzalez-Herrero and Pratt 1995).

Fourthly, and in contrast with the first three negative effects, crises create ideal conditions for reform. An emergency generates favourable conditions of consensus – social and political – to proceed in a swift fashion with changes in structures and institutions which may have been malfunctioning for years or decades prior to the outbreak of the crisis. It is arguably easier to introduce such structural reforms during a crisis because a certain degree of leadership autonomy and rule-bending are accepted, if not expected. We can thus expect that even the mildest, briefest crisis brings about some system change. At the very least, a set of measures are added to the routine procedures for aversion of similar crises in the future. More substantial reform is especially likely to take place if the following factors (maxims) are present (Boin *et al.* 2005: 128–129):

- *Perceived inevitability of the crisis*: leaders are more likely to adopt a reformist strategy if they attribute the cause of the crisis to external factors;

- *Annoyance*: policy-makers are more likely to implement lessons learnt from a crisis if they see the crisis as an opportunity to solve long-standing irritations and problems;

- *Political survival*: leaders are more likely to proceed with reforms if they perceive that there is a minimum winning coalition favouring reform in the political venues that are essential to their own survival in office;

- *Structural opportunities*: reform strategies are more likely to be adopted if leaders can operate within the framework of an ad hoc centralisation of initiative and authority.

The basic expectations, therefore, of any leadership is that a) they will (try to) stop the crisis as quickly as possible; and b) they will attempt a certain set of reforms. How these two expectations materialise determines the democratic credibility of a crisis management strategy. As Arjen Boin *et al*. (2005: 8) put it, 'Many crises could be terminated relatively quickly when governments can simply "write off" certain people, groups, or territories, or when they can deal with threats regardless of the human costs or moral implications of their actions. *In countries with a free press, a rule of law, political opposition and a solid accountability structure this is not possible* [emphasis added]'. This is because even if one of these democratic components is disregarded or violated, the rest will act as control barriers that will cancel out the attempted counter-crisis measures or reforms.

A hasty 'wrap-up' of a crisis, for example, without any attempt to correct the weaknesses in the institutional/governance structure that led to the crisis in the first place, falls short of the accountability principle (not enough time to properly explore who, how and why is responsible for the crisis and proceed to the necessary reforms, thus failing to safeguard the citizenry from a future similar crisis). Even if the accountability structure of the polity is too weak to stop such a hasty crisis closure in its tracks, the political opposition and/or the media will act as barriers (at the very least, the crisis 'blame game' brings gains to the opposition and 'sells' well as media content). Similarly, we can almost certainly expect a strong backlash from society in the case of abuse of power during crisis in order to push through counter-crisis measures or reforms (restriction of the autonomy element during the process of counter-crisis decision-making); and/or failure to effectively communicate and persuade citizens about the need for these measures (violation of the accountability element at the crisis communication stage) (Boin *et al.* 2005: 129–134; Seeger *et al.* 2003: 219–238; Coombs 2010). In sum, violation of the core functions of democracy at any of the three crisis-management stages (decision-making process; measures; communication), will trigger democratic control mechanisms that will either alter the course of the crisis-management strategy or signal its failure altogether.

What happens, however, in the case where counter-crisis measures and reforms violate the core democratic functions at all stages of the crisis management process and, worse even, this violation does not trigger off democratic control mechanisms? Could we then have a failure of democracy rather than failure of the crisis-management strategy? In the following, I show how in Greece's case, the Eurocrisis has created favourable conditions for in-depth reform but the strategy followed is consistently and continuously removed from democratic standards in all its three dimensions (process of decision making; reforms; communication). This puts the attempted reforms on shaky ground, but at the same time contributes to the normalisation of non-democratic governance through the prolongation of crisis conditions.

My focus here is primarily on the national dimension of the crisis management and the extent to which the Greek governments of the last six years have adhered to the core democratic principles during their attempt to bring Greece out of the crisis. Nevertheless, the role of the EU institutions and other EU member states is also discussed-albeit briefly – both in terms of the framework and rules they have set which underpin the counter-crisis actions at national level; and in terms of whether that counter-crisis framework compares to democratic standards.

Greece and the eurozone crisis: a disaster waiting to happen or a golden opportunity for reform?

Recipe for disaster

Historically, democratic governance in the modern Greek state has been weak: Internally, the Greek state apparatus has been plagued by nepotism, corruption and clientelism for nearly two hundred years now (e.g. Mouzelis 1978). Externally, the Greek government and parliament have rarely had a strong voice, independent of Greece's ally or 'protector' (in the earlier days) countries.

Since the outbreak of the eurozone crisis, media and scholarly analysis have painted a realistic – though often exaggerated and biased – picture of the components that make up Greece's current financial and economic woes. At the epicentre is the Greek political system: Two parties (Panhellenic Socialist Movement, PASOK, and New Democracy, ND) and three families (the Papandreou, the Karamanlis and the Mitsotakis) have dominated the political scene not just since the fall of the junta but nearly since the beginning of the last century (although ND and PASOK were new parties in the post-junta period, their first leaders and other key members had considerable links with the pre-junta political system).[1] And nepotism never appears alone: Clientelism, fiscal profligacy and populism are expected accompanying phenomena, along with state inefficiency and corruption, to which all the above inevitably lead. Christos Lyrintzis (2011) succinctly describes the Greek political establishment as based on 'partitocrazia' and 'bureaucratic clientelism', while Jason Manolopoulos (2011) refers to the '"seven-headed hydra" of cronyism, statism, nepotism, clientelism, corruption, closed shops and waste' that plagues the Greek society and economy. The ways in which the two parties have exploited their power over the last 30 years in order to reinforce and expand their influence and patronage networks have been well-documented (Pappas and Asimakopoulou 2011). Their tactics invariably include the creation of new public structures on the basis of electoral rather than rational economic/functional criteria, providing assistance from state and party mechanisms to private entrepreneurs in order for the latter to secure loans, business licenses and lucrative deals in return for political support (Pelagides and Mitsopoulos 2010) and using appointments in public sector positions as a means to return or gain favour with voters.

The pace of European integration reforms has also been slow; unsurprisingly perhaps given the resistance to change that clientelist, nepotistic and corrupt systems usually display. Even key sectors of the Greek economy (agriculture, tourism) have remained largely

[1] See Tzogopoulos (2013) for a more detailed account of Greece's political dynasties and career politicians who started out as Youth Party members and have been in the political arena for years or decades.

underdeveloped, with Greece struggling to absorb available EU structural funds to support change and growth (Spanou 1998).

And then came the euro. The underdeveloped, largely agricultural Greek economy was shoehorned (or for others, cheated its way) in a strong-currency zone together with the heavily industrialised and far more advanced economies of the North. Joining the euro brought a short-lived flood of cheap money and an illusion of growth and prosperity, but in effect locked the country in a currency that its economy could not match in strength. When the global financial crisis broke out in 2008, the country was ill-prepared to face it, not only because of the large public debt it had accumulated but also because certain corrective actions like currency devaluation were no longer available to it. Added to these came the near complete loss of Greece's credibility during 2009 and 2010 because of the instability of the domestic political scene and of the 'revelation'[2] that Greece had misled its EU partners regarding its state of finances back in 2000 in order to enter the eurozone.

The eurozone and the EU were also ill-prepared: There were no provisions for support mechanisms or response strategies in the event of such a crisis. After the first shock of Greece announcing a state of fiscal emergency and then getting 'rescued' by the ad hoc mechanism of the Troika (European Central Bank, European Commission, International Monetary Fund), several analysts were quick to point out that the euro too was an imperfect currency, poorly designed from the start. The Stability and Growth Pact, which several eurozone members have broken (Germany and France actually lead by example), has been described as largely a list of desirable outcomes that a common currency area should enjoy, not a list of measures participant countries should have in place in order to obtain optimum currency (Manolopoulos 2011). Pegging Greece's currency and subsequently economy to a strong currency without making the required structural reforms first was a decision taken by Greek and EU officials on the wishful thinking that economic and financial convergence would take place once Greece and other weak EU economies were in the eurozone.

[2] As discussed later in the chapter, the state of Greece's finances and economic development was no secret when the decision was taken to admit the country in the eurozone.

In sum, Greece has nearly always suffered from a system of weak democratic governance or 'executive politics',[3] which the current EU state of crisis has exposed and exacerbated (Benz 2013 on 'executive politics' and the eurocrisis; Panagiotarea 2013 on the 'system failure' of the eurozone). Is it possible, then, to expect any reforms to take place, and democratically legitimate as such? Certainly, and in spite of Greece entering the current period of crisis on a weak democratic footing, the country appears to have a golden opportunity for reform ahead.

Recipe for reform

As discussed earlier in this chapter, a crisis generates especially favourable conditions for radical break from past practices and systems if the following factors or maxims are present: perceived inevitability; annoyance; high chances of political survival for the reformists; favourable structural opportunities. Are these conditions met in the case of crisis-struck Greece? First, the condition of inevitability: Given its lock-in in an incomplete currency union and the enormous pressures from global markets, Greece had arguably little chance of successfully withstanding the impact of the global financial crisis. A key component here linked to the inevitability maxim is the element of uniqueness. Given Greece's political and financial state of affairs, it was simply a matter of time before a crisis broke out. Since the Greek case presents many unique points or peculiarities, it follows that any measures taken need to be equally 'unique'. Then we have the condition of annoyance: This is the opportunity to eliminate the 'seven-headed Hydra' of a state and all its malfunctions that have been plaguing Greek citizens for decades and are largely responsible for their current dire situation.

And thus, the third condition for reform emerges: optimum circumstances of political survival for those who will attempt the

[3] Here, I borrow the term 'executive politics' from Benz, who includes this as one of the several possible constellations (and the least desirable, in my reading, at least) of an EU democracy, i.e. a multilevel system of governance where both the European Parliament and the national parliament have weak control or influence over the executive and interparliamentary relations are also weak (Benz 2011 and 2013). In the case of Greece in the pre-EU era, 'executive politics' aptly describes the inability of the Greek parliament to control the national executive, as well as the constant interference (overt and covert) of other national executives in the Greek decision-making process (e.g. Carabott and Sfikas 2004; Featherstone and Katsoudas 1987).

reforms. Because Greece's crisis has come through as the ultimate emergency (unbearable external pressures, domestic structures too weak to simply repair), political and public support for coalition governments soared in 2012–2013.[4] This has given a solid political alibi to national political parties to form alliances with their ideological opponents, something previously unthinkable. Such coalition governments allow for the political cost of the reforms to be shared across several political formations and remove a significant proportion of possible opposition obstacles reforms could meet in the parliament. Consequently, the way opens for the fourth condition to be met, namely structural opportunities for reform. Emergency powers are afforded to the reformist government and since this is a coalition, the possibility that these emergency powers will be blocked is reduced.

The crucial question, however, is not whether the eurozone crisis has created favourable conditions for reform, but rather, a) what kind of reforms are attempted; and b) whether these reforms and their public justifications meet the democratic standards of autonomy and accountability. As I show in the following, the current counter-crisis reform path followed further weakens Greece's democracy, all the while putting very few of the above-outlined 'wrongs' right.

The Economic Adjustment Programme: adjusting democracy?

For the last four years, Greece has been operating under the rules of the Economic Adjustment Programme (EAP), more widely known as Memorandum or Mnimonio (in Greek) or 'bailouts' (in media talk). This is a set of agreements signed between the Greek government, the Bank of Greece, on the one hand, and the Troika, on the other. These agreements provide loans to the Greek government in order for the latter to pay off previous accumulated debt, in exchange for a set of

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[4] Indicatively, see MRB Hellas S.A., 'Πρόθεση ψήφου Εκλογών, Πανελλαδική Τηλεφωνική Έρευνα για τη Real News', May 2012, retrieved from: <http://www.mrb.gr/Mrb/media/RN-16-17-05-2012.pdf> (last accessed 18 October 2013); καπαresearch, 'Nationwide Survey on political developments on behalf of To Vima', July 2013, retrieved from: <http://kaparesearch.com/index.php?option=com_k2&view=item&task=download&id=29_90e874b62f2dacc1c91e5d5dee24fa08&Itemid=137&lang=en> (last accessed 18 October 2013).

harsh economic and financial reforms, aptly labelled 'austerity' (See Annex for a detailed explanation of the Economic Adjustment Programme). In total, € 240 billion worth of loans have been committed by the IMF (€ 49.8 billion) and the eurozone countries (€ 190.2 billion). The money is released to Greece in instalments, following satisfactory reports by the Troika's Task Force, i.e. the European Commission, the European Central Bank and the IMF staff that are tasked with monitoring the country's progress in implementing the Memorandum.

At first glance, the reforms that the Memorandum mandates (sharp reduction of government spending, increase of state revenues, reduction of bureaucracy, tackling of corruption, increase of efficiency) seem as obvious solutions to some of Greece's chronic problems. Nevertheless, the overall feasibility of the crisis reforms has been intensely questioned by economists, political actors and even critical voices within the IMF and EU Commission (IMF 2013a; 2013b; 't Veld 2013), not only because of the dubious effectiveness of the imposed 'austerity logic' (Bitzenis *et al.* 2013),[5] but also because of the inability of the Greek governments to effectively implement core measures.

Autonomy, accountability and the EAP process

The Memorandum agreements have removed the ability of the Greek governments, current and future, to dispute or breech any aspect of the agreement and have also removed the possibility that such disputes are examined by Greek courts of law. Indicatively, the Amendment Agreement relating to the Master Financial Assistance Facility Agreement between the European Financial Stability Facility (EFSF), the Hellenic Republic as Beneficiary Member State, the Hellenic Financial Stability Fund and the Bank of Greece is governed

[5] See the following: Kevin Featherstone 'Are the European banks saving Greece or saving themselves?, *The Guardian,* 22 March 2012, retrieved from: <http://www.theguardian.com/commentisfree/2012/mar/22/greece-european-banks-eurozone> (last accessed 20 January 2014); 'IMF Document Excerpts: Disagreements Revealed', *The Wall Street* Journal, Real Time Economics, 7 October 2013, retrieved from: http://blogs.wsj.com/economics/2013/10/07/imf-document-excerpts-disagreements-revealed/ (last accessed 24 October 2013); Stevis, M. and Talley, I. 'IMF concedes it made mistakes on Greece' (article based on strictly confidential IMF internal document), *The Wall Street Journal*, 5 June 2013, retrieved from: <http://online.wsj.com/news/articles/SB10001424127887324299104578527202781667088> (last accessed 24 October 2013).

by English law and stipulates that all legal disputes concerning the Memorandum (or were Greece to break the agreement) will be handled by the courts of the Grand Duchy of Luxembourg (Gazette of the Government of the Hellenic Republic 2012b: 5772–5773). These and other similar provisions in the EAP agreements led to the constitutionality of the Memorandum itself being challenged in Greece's supreme administrative court (StE). Although the StE deemed the Memorandum compatible with the Constitution, the decision (Council of State Plenary 2012) is still causing controversy (Manitakis 2011, Antoniou 2012). In 2011, after then-premier George Papandreou quit, an interim government was formed in Greece, until elections would be held. Typically, such governments have an administrative and time-limited role only. But in an unprecedented display of disregard for democratic standards both by national and EU leaders, the government that was installed under the technocrat Loukas Papadimos was given the support of three political parties (ND, PASOK and LAOS) and an extended mandate. Its main role was to sign EPA-related reforms and measures and to ensure their implementation by passing relevant legislation.[6] Further reducing the entire representation process to window-dressing, in the months before the 2012 national elections current Prime Minister Antonis Samaras was put under enormous and humiliating pressure by the Troika and EU member state leaders to confirm in writing that he would implement the EPA to the letter were he to win the elections. Evaggelos Venizelos, of PASOK, had to do the same.[7]

[6] At the time of his appointment, Papadimos was shown in polls to enjoy the approval of as much as 78 per cent of the electorate. This was interpreted as unequivocal endorsement of Papadimos by the Greek public, even though he had not been elected. Only a month, however, after his appointment, polls were already showing a sharp decline in his popularity as well as disappointment with his government's work, see 'MRB political survey on behalf of real.gr', December 2011, retrieved from: <http://www.real.gr/DefaultArthro.aspx?page=arthro&id=111550&catID=11> (last accessed 24 October 2013). This helped to fix the date for the 2012 elections and put an end to the attempt to maintain the unelected government in place long-term (Hare 2012).

[7] To get an idea of the international political 'drama' that preceded the 2012 national elections, see G. Wearden 'Eurozone crisis live: Greek president attacks Germany as bailout looks shakier', *the Guardian*, Business Blog, 15 February 2012, retrieved from: <http://www.theguardian.com/business/2012/feb/15/eurozone-debt-crisis-greece-eurozone-gdp> (last accessed 24 October 2013).

A string of EU legal documents have further inflicted a lethal blow on the possibility of the Greek people to hold accountable those who represent and legislate on their behalf. Firstly, the Treaty on Stability, Coordination and Governance or 'fiscal compact' (European Council 2012) makes it obligatory for national budgets to be balanced or in surplus, otherwise an automatic surveillance mechanism will kick in. The 'Six-Pack' set of measures on macroeconomic surveillance of the member states further defines the sanctions that member states will face, should they breech the 'fiscal compact'; while the 'Two-Pack' set of measures specifically identifies the monitoring and sanctioning measures of eurozone member states that fail to comply with the 'Six-Pack'.[8] On top of all these, Greece's economy and fiscal policy are further subject to 'post-programme surveillance' by the Commission, according to Article 14, of EU 'Regulation No. 472/2013 (European Parliament and the Council 2013) which is specific to member states that have sought or will seek support from the European Financial Stability Facility. What this 'post-programme' surveillance actually means is that 'the Commission shall conduct, in liaison with the ECB, regular review missions in the Member State under post-programme surveillance to assess its economic, fiscal and financial situation. Every six months, it shall communicate its assessment to the competent committee of the European Parliament, to the EFC and to the parliament of the Member State concerned and shall assess, in particular, whether corrective measures are needed.' These provisions place Greece under surveillance for at least another 25 years. As the conservative and largely pro-Memorandum' newspaper Kathimerini succinctly put it, 'Greece can choose its government, but not its economic policy'.[9]

The inefficiency trap

Further compounding the democratic deficit of the process through which the EAP is enforced, Greek policy makers invariably opt for shortcuts in the national legislating process, either bypassing the

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[8] European Commission, 'EU economic governance', Economic and Financial Affairs webpage, available a:t <http://ec.europa.eu/economy_finance/economic_governance/index_en.htm> (last accessed 3 April 2014).

[9] N. Chrysoloras, 'Greece can choose its government, but not its economic policy', *Kathimerini online*, 24 October 2013, English version available at <http://www.ekathimerini.com/4dcgi/_w_articles_wsite3_1_24/10/2013_524640> (last accessed 24 October 2013).

parliament completely (use of Presidential Decrees or Acts of Legislative Content, which do not require a vote in the parliament) or using 'express' procedures to pass legislation (introducing several legislative acts under one article only and/or classifying a legislative proposal as 'urgent' which reduces the debate time in parliament to a minimum). The Constitution certainly allows for all these tools to be used in exceptional circumstances, meaning that these methods are not an invention of these specific crisis-period governments. However, the conditions under which these processes can be followed are explicitly defined in the Constitution, but are not always met in the case of the Memorandum reforms.

A case in point is the closure of the public broadcaster ERT, which was shut down in scandalous fashion in June 2013. The Memorandum dictates that 15 000 public sector employees be dismissed by the end of 2014, of whom 4 000 must be fired by the end of 2013. Of those latter ones, 2000 had to be dismissed by the end of June 2013 in order for Greece to receive the next disbursements from the Second Economic Adjustment Programme. By mid-June 2013, the government had proceeded with exactly zero dismissals and there was no specific plan in place on how to reach that target on an objective, needs-and-performance basis. Thus the ERT became an obvious, seemingly easy solution. By shutting it down overnight, and firing all of its 2 656 reporters, journalists, TV and radio technicians and support staff, it could then show the Troika, whose inspection visit was looming, that the government had the will and ability to meet agreed targets. The public outcry within Greece and from abroad at shutting down the public broadcaster had not been factored in,[10] nor

[10] Indicatively, see the following: 'Greek Government barely avoids collapse', *Spiegel Online International*, 18 June 2013, retrieved from: <http://www.spiegel.de/international/europe/samaras-government-in-greece-survives-broadcaster-battle-a-906466.html> (last accessed 18 October 2013); 'L'État grec a fermé brutalement l'intégralité de son audiovisuel public' [The Greek government has abruptly closed all of its public broadcasting], *Le Figaro*, 11 June 2013, retrieved from: <http://www.lefigaro.fr/medias/2013/06/11/20004-20130611ARTFIG00592-l-etat-grec-a-ferme-brutalement-l-integralite-de-son-audiovisuel-public.php> (last accessed 18 October 2013). In an equally unprecedented move, for the Greek media sphere anyway, ERT's personnel continued broadcasting illegally, through the radio and web TV frequencies of other Greek media platforms, displaying not only defiant attitude but also exemplary 'independent', collective

had the political friction that was caused among the members of the tri-partite government. Eventually, Democratic Left (DIMAR), the smallest party in the coalition, decided to withdraw from the government over the ERT affair, bringing the government's power in parliament down to just above the required majority threshold.

The decision of the government to shut the ERT down through the use of an Act of Legislative Content was challenged in Greece's supreme administrative court (StE), not because there was opposition to the ERT's reform per se, but because the public broadcast was interrupted. StE stipulated that there can be no termination of one public broadcaster without its simultaneous replacement by a new one and therefore the government ought to take action in order to establish an interim public broadcaster until the new, reformed one is ready in September 2013 (Council of State 2013). Analysts have also pointed to the superfluous use of the Act of Legislative Content (which allows cabinet ministers to proceed without consent of the parliament) in this case, as a law already exists (Law no. 4002/2011), which stipulates precisely the closure of the ERT and its replacement by a smaller, reformed broadcaster. The government has subsequently had to announce a total of approximately 2 000(!) positions in order to staff the interim public broadcaster, so that it can go on air.

Another example is tax reforms, a major and potentially beneficial provision of the Memorandum. Despite the regular promises for a fair and transparent tax system, attempted reforms have thus far been producing meagre revenue, because of the state's inability and/or unwillingness to recoup lost tax income from large-scale tax evaders. Reductions in public sector personnel have taken place hastily and with short-term fiscal gains in mind. As a result, state services crucial for the implementation of anti-tax evasion policies remain (or are left) with too few employees to perform even basic duties, let alone to carry out in-depth tax-evasion investigations and prosecutions. [11] Instead, the increase in value-added tax (VAT) and new property and

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news-making (as opposed to the typically hierarchical and heavily government-biased news structure ERT broadcasts had before).

[11] See, for example, the recent developments concerning the notorious Lagarde list here: 'Investigation into suspected tax dodgers on Lagarde list shelved?' *EnetEnglish*, 9 October 2013, retrieved from: <http://www.enetenglish.gr/?i=news.en.article&id=1525> (last accessed 24 October 2013).

emergency taxes has hit payroll-employees, pensioners, and in some cases even the unemployed, the hardest. One example is property tax: Due to its inability to check wealth, the state has opted for horizontal taxation of any type of building or land, including chicken sheds (!), arable areas, forested land and land used for animal grazing. There are no exemptions or tax-free threshold, not even for those who only own one property (the one where they live), those who are unemployed, those who live in low estate-value areas or have low income. By next year, property taxation will have increased by 684.4 per cent since 2009 with taxes burdening equally the haves and the have-nots.

Violating autonomy and accountability: the EAP measures

The austerity trap

Greece is trapped in what for the moment seems an endless cycle of debt, recession and austerity. At the beginning of the crisis, in 2009, Greek public debt stood at 129 per cent of GDP (€ 299 billion) and public deficit at 15.6 per cent of GDP. It was hoped that the first Memorandum (€ 110 billion loan at 5.5.per cent interest rate plus the accompanying austerity measures) would bring Greece's public deficit below 3 per cent by 2014 and would enable the country to re-access private capital markets by the end of 2012. In 2014 public debt is estimated to reach 177 per cent of GDP or € 320 billion; higher than when the crisis broke out (Preliminary Draft Budget for 2014, see Ministry of Finance of the Hellenic Republic 2013a). This is in spite of the must-trumpeted fact that the public deficit is expected to drop to 2.6 per cent, with the budget showing a primary surplus of € 3.4 billion.[12] Despite the assurances and confidence of the Greek

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[12] The restructuring of privately-held Greek public debt in 2012 was dubbed the 'world's biggest debt restructuring deal', see L. Baker and S. Sassard 'Insight: How the Greek debt puzzle was solved', *Reuters*, 29 February 2012, retrieved from: <http://www.reuters.com/article/2012/02/29/us-europe-greece-idUSTRE81S0NP20120229 (last accessed 24 October 2013). It converted high rate bonds with short maturity to low rate bonds with long maturity (which significantly lowered the debt costs), and also introduced a direct 53.5 per cent haircut to the nominal value of the privately held debt. The triumphant announcements of the Greek government about the near-total participation of private Greek-debt holders in the PSI were short-lived. Only hours after the conclusion of the PSI, analysts and journalists questioned the benefits of the 'haircut'. Nouriel Roubini called it a 'sweet

government and the European Commission that this 'primary surplus' prediction has brought about, the consensus among economic analysts is that in Greece and all other EU member states currently in crisis, current levels of austerity are only going to increase public debt ad infinitum. As de Grauwe and Ji put it:

> Even when these countries manage to maintain a high primary surplus of 4% for many […] it will still take between 12 to 22 years to halve the debt. […] *The issue is whether their political systems will have enough resilience to maintain such "temporary" austerity programmes in order to slowly and painfully draw down the levels of debt*.
>
> De Grauwe and Ji (2013: 5), emphasis added

Interesting detail: During this 'early' crisis period (2009–2013), central government expenditure for servicing the debt amounts to € 144.6 (in loan interest repayments and annuities) and government expenditure on short-term securities and Treasury bills to € 176.5 billion (Government Budget 2013, see Ministry of Finance of the Hellenic Republic 2013b); in total the equivalent of the public debt at the start of the crisis.

Without doubt, the social cost of the austerity measures is unprecedented: Unemployment is currently at almost 27 per cent (approaching 60 per cent for those under 25) and the economy in deep recession (GDP has shrunk by nearly 50 per cent since 2009).

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deal' for private investors, see (http://www.cnbc.com/id/46651030), while the Wall Street Journal Greece wrote of a 'historic' default that was unlikely to 'end the debt-strapped country's epic financial problems', sited from C. Forelle 'Greece defaults and tries to move on', *Wall Street Journal*, 10 March 2012, retrieved from: <http://online.wsj.com/news/articles/SB10001424052970204603004577270542625035960>, last accessed 24 October 2014). A sober look at what the PSI actually achieved shows that the haircut alone 'lowered the debt-to-GDP ratio by 55 percentage points, but as Greek banks at the same time were holding almost 1/3 of the restructured debt, this also created the need for the Troika to pay for a bank recapitalisation in 2012, which added back an additional 25 percentage points to the debt-to-GDP ratio. So all in all the net impact of the debt restructure in 2012 was that it lowered the debt-to-GDP ratio with 30 percentage points, meaning that it would have been up at 207 per cent by the end of 2012 if it had never been performed'. See 'Greek Government-Debt crisis', *Wikipedia*, retrieved from: <http://en.wikipedia.org/wiki/Greek_government-debt_crisis#cite_ref-164> (last accessed 24 October 2013).

One in five Greeks are at risk of poverty according to the recent data released by Eurostat (Eurostat 2012) but a careful reading of the report reveals that 'at risk of poverty' is a person in a household whose disposable income is already *below* the 'at risk of poverty' line. At the same time, there is hardly any welfare 'safety net' left for those in need, as public spending on social services has been slashed to a meagre 29.4 per cent of total government spending (Preliminary Draft Budget 2014; Eurostat 2012).

Despite high unemployment and recession, Greece still has to fulfil the Memorandum target of laying off 15000 public sector employees by the end of 2014. The fewer people in employment, the less revenue flows in the state tax, pension and healthcare coffers, which are already on the brink of collapse. For those who are still employed, the country is under pressure to further reduce the minimum national salary, even though this currently stands at € 585 before tax and contributions (lower still for unskilled workers and those under 25 years of age).[13] Lowering the minimum salary is deemed *conditio sine qua non* for investors to start flocking in the country and for employment to rise again. Besides the lack of evidence to substantiate a positive link between low minimum salaries and increase in employment (see Schmitt 2013), further decreasing wages – or pensions – also reduces already-strained household disposable income and thus triggers even deeper recession of the economy (IMF 2013a).[14] Similarly, drastic cuts in healthcare funding (not to be confused with sorely-needed management reform in order to stop waste and corruption in the sector) may reduce the government's expenditure in the short term but leave a significant proportion of the population without access to basic services, particularly in rural areas. This, in medium-to-long-term can only mean decrease in the

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[13] For a single employee under 25, the minimum monthly salary (calculated on the basis of 40 hours per week) is set at € 510. An unskilled worker can expect a minimum of € 26 for a day's work (set at six hours and 40 minutes) if they are over 25, or € 21 if they are under 25 (Gazette of the Government of the Hellenic Republic 2012a). For the calculation of salaries see here: 'ΕΓΣΣΕ [National General Collective Employment Act]', *Ergatika Website*, retrieved from: <http://ergatika.gr/sse/egsse> (last accessed 18 October 2013).

[14] See also R. Wilder 'Unfounded Obsession With the Greek Minimum Wage' *The Wilder View*, EconoMonitor, 8 February 2012, retrieved from: <http://www.economonitor.com/rebeccawilder/2012/02/08/the-unfounded-obsession-with-greek-minimum-wages/> (last accessed 5 April 2013).

quality of public health, thus further costs for the state (see Kentikelenis and Papanikolas 2012, Stuckler and Basu 2013).

The democratic deficit of austerity

If the primary duty of a democratic government is to safeguard the welfare of its constituents and uphold social fairness, then imposing crisis reforms that have a devastating effect on society and are of dubious effectiveness clearly goes against democratic principles. But looking at specific Memorandum-imposed crisis reforms more closely, what also becomes clear is that the relevant national legislation is at best constitutionally controversial and at worst confirmed as unconstitutional. One example is the legislation concerning reductions in state pensions. Stipulated by the Memorandum as a condition for future loan disbursements, reduction of pensions has taken place three times so far. The most recent law (Law 4093/2012) concerning reductions in pensions was challenged in Greece's Supreme Court of Audit, which ruled that certain provisions of this law are unconstitutional, because they conflict with the constitutional obligation to respect and protect human dignity, the principles of equality and proportionality and the protection of labour (Court of Audit 2012). Specifically, the Court, meeting in plenary sitting, ruled virtually unanimously that the following provisions are unconstitutional:

- The raising of retirement age from 65 to 67 years ('contrary to the principle of legitimate trust');

- The introduction of measures which reduced state pensions – for the fifth time since 2010 – by 5–15 per cent;

- The abolishment of 'Christmas and Easter allowances, as well as leave bonuses indiscriminately, without taking in consideration those on small state pensions'; and

- The raising of the age limit for those entitled to the Social Solidarity Allowance (EKAS) from 60 to 65 years.

More recently the Court of Audit ruled that the Memorandum-imposed retrospective reduction of pensions under special salary agreements (judges, military personnel among others) is unconstitutional and contrary to Article 1 of the Additional Protocol to the European Convention on Human Rights (ECHR) (Court of Audit 2013).

The Memorandum laws (3833/2010 and 3845/2012) that impose reductions in salaries, benefits, etc. of the state sector employees have also been found unconstitutional and inconsistent with the European Convention on Human Rights and the applicable law regarding International Employment Contracts by the County Court of Athens (County Court of Athens 2012), while four First Instance Courts (in Chios, Xanthi, Messologgi and Rethymnon) have ruled that the 'availability status' for public sector employees violates not only the Constitution but also the European Social Charter (in order to meet Memorandum targets, the government has to put 12 500 public sector employees in a state of availability by the end of the year, whereby they will continue to work full time but for 75 per cent of their salary and not necessarily in the same position or subject as before).[15]

Crisis communication and democratic standards: defending the indefensible?

If the democratic credentials of the EPA measures and the way they are imposed are shaky at least, perhaps some democratic credibility is to be gained through the process of public communication and justification. This can happen in two ways: Firstly, that the information provided to the public about the EPA process is clear, accurate and consistent, thus enabling Greek citizens to give their consent to the crisis reforms on the basis of knowledge rather than propaganda or fear. Secondly, even if decision makers are not forthcoming with the necessary crisis information, we can expect that a healthy democratic public sphere will facilitate public scrutiny of the implemented crisis reforms and thus allow for decision makers to be held accountable. One question, then, is how do Greek leaders publicly justify the EAP and related crisis reforms? The other question is what is the role of the media, national and international, in the public communication process of the Greek crisis?

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[15] These decisions prompted MEP Nikolaos Chountis to bring two questions to the Commission concerning the latter's obligation to ensure that any agreements between Greece and the Troika (and therefore, the Commission) are not unconstitutional. The Commission responded both times that it is the responsibility of the Greek authorities to ensure that any measures taken comply with the country's Constitution. See Official Journal of the European Union 2013 and 2014.

As regards the former, Greek leadership of the past six years appears convinced that there is no other way; or rather, that the alternative (unilateral debt write-down and exit from the eurozone) would be far more painful and destructive for Greek society. To a certain extent, Greek citizens appear to share this notion of inevitability, particularly the aspect of uniqueness of their case, i.e. Greece is in crisis because it is Greece, therefore the measures are such because they have to address a unique case.

For one, a significant proportion has voted for pro-Memorandum parties at the latest elections (significant enough to allow the pro-Memorandum parties to form a coalition government). Public opinion is more supportive of coalition governments, which in itself is unprecedented. Most of Greeks also support the dismissal of public sector employees and a reformed ERT.[16] Moreover, when polled at times when a new package of austerity measures was about to be voted through in parliament, the majority of Greek respondents have consistently expressed the preference that the government exhausts its four years in office (the 'let government govern' component of crisis reform).

In light of these attitudes, surely Greek policy makers are legitimised to proceed with the reform in any way they deem necessary? The answer can only be negative to this, for the following reasons. To begin with, polls consistently show that none of the current political parties gather more than 20 per cent of voters' preference, and none of the current party leaders are viewed particularly favourably.[17] So, when some of these parties gather enough votes to form a coalition, they do not automatically carry enough legitimacy to proceed with life-changing reforms in the manner and speed that is required by the Memorandum.

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[16] Indicatively, see the following public opinion survey: Rass (2013) 'Πανελλαδική Έρευνα Γνώμης', retrieved from: <http://www.rass.gr/surveys/ELTYPOS_publ_230613.pdf> (last accessed 24 October 2013).

[17] For the most recent public opinion survey see MRB Hellas S.A. (2014) 'Έρευνα καταγραφής των πολιτικών εξελίξεων σε σχέση με την πολιτική επικαιρότητα', opinion poll conducted on behalf og Realnews.gr, April 2014, retrieved from: <http://www.mrb.gr/Mrb/media/RN-08-11-04-2014.pdf> (last accessed 5 May 2014).

Crucially, from a public communication perspective, there are gaping inconsistencies between pre-election promises and post-election deeds. In other words, Greek leaders get elected on the premise of 'there is plenty of money, it's a matter of fair redistribution' (Papandreou in 2009) or 'the Memorandum terms must be renegotiated; we will prioritize growth and development' (Samaras in 2011) and then backtrack on their pre-election commitments.[18] Therefore, they are not elected for what they actually do but for what they promised they would do. Going back on their pre-election commitments forfeits what limited legitimation for drastic reforms they may receive by being elected.

Momentum for reforms is at its strongest when and for as long as policy makers remain ahead of the crisis developments and are not perceived as part of the problem. But in Greece's case, one set of policy makers (the national lot) were very quickly identified as a major cause of the problem, hence the low confidence of the voters in the Greek leadership's ability to get the country out of the crisis. The other set of policy makers (the Troika) has also lost public legitimation, but at a slower pace. The loss of legitimation is directly linked to a steady stream of critical voices in the public sphere that have called in question the effectiveness of the EPA and provided information and analysis that undermine the qualities attributed to the Greek crisis (inevitability, uniqueness).

For example, the harshness of the Greek reform programme has been typically justified on the basis that Greece cheated its way into the eurozone and now the rest of the eurozone countries have to pay the price. However, it quickly transpired that Greece was already known to have serious problems in getting 'their numbers right', well before it joined the EMU. In its 2010 report to the Council of Ministers, the European Commission (2010: 6) admitted: 'The October reporting by the Greek Authorities is exceptional in terms of procedure, but it is neither without precedents nor an isolated episode'. Crucially, the information did not, on its own, trigger Greece's debt crisis. As Erik Jones points out:

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[18] See Tzogopoulos (2013: 135–136), for a list of instances when crisis-period leaders and policy makers have backtracked on their promises.

> […] when Greek officials made their "shock" announcement in October 2009, bond yields on ten-year Greek sovereign debt remained flat. Indeed, analysis of cross-border capital flows shows that international investors actually moved into the country rather than moving out (Merler and Pisani-Ferry 2012: 6). This suggests there was no new information in that announcement that the markets had not already discounted. On the contrary, the incoming Greek government only quantified something that was already well known.
>
> (Jones 2013: 297)

Crucially, several other countries, which share only some or do not share any of Greece's 'unique' characteristics and problems, have nevertheless ended up in similar crises, including Iceland, Hungary, the Baltic states, Cyprus and Portugal (Jones 2013). The Greek case is in this sense not unique. Instead possible explanatory factor for the crisis in several European countries is their 'peripherality'. In Jones's words:

> […] the Greeks may have been incompetent insofar as they made bad strategic choices, they may have been unfortunate in the sense that global forces moved against them, but they also may have experienced the unintended consequences of the same dynamics that brought about the economic and financial crisis in the first place. […] this third possibility is disturbing because it suggests that Greek performance was not exogenous to the crisis; on the contrary, both the crisis and Greek performance were determined by the same set of causal factors. To the extent that this is true, changing Greece – or trying to avoid being like Greece – is not the answer. Instead, the key is to change those factors that brought us to Greece in the first place.
>
> (Jones 2013: 295)

As more information enters the public sphere about the unsustainability of the Greek public debt; of the devastating effects that the crisis reforms are having on Greek people; and of the fact that the Troika was aware of the faults in the imposed reforms, the ability of policy-makers to reassure voters 'that they know a way out' – a vital component for successful reform (Boin *et al.* 2005: 131) – is further undermined. A close look at opinion polls clearly shows that voters' choices are driven to a large extent by the inevitability of the situation alone, meaning that they do not think their personal circumstances, or those of the country and the EU, are going to improve in the future; nor do they trust any political institution or leader in particular to deal with the crisis effectively.[19] They do not fully share the leadership's vision of the future; the vast majority agree reforms are needed, but prioritise growth and development instead of austerity. Crucially, the current reforms are perceived as vastly unfair, which further diminishes the latter's likelihood for success.

As leaders at national and EU level fail to convince multiple audiences that the reform they are attempting is not only inevitable, but also good and realistic, the only key communication tool left to them is intimidation (i.e. we go through with the inevitable or else). To this end, national and international media have played a vital role (Tzogopoulos 2013; Mylonas 2012). This usually translates in dramatic media coverage of the government's negotiations with the Troika, including predictions of bankruptcy and chaos unless Greece manages to extract its next loan disbursement, as well as scenarios of early elections and/or Greece getting expelled from the eurozone. Another consensus-extracting technique is to lay the blame with the citizens, thus cancelling the validity of any protests. Papandreou led the media chorus (domestic and international) in appointing collective blame when he declared that the Greeks are lazy and corrupt (never mind that this is unfounded; the accusation was dramatic, simple and made for good headlines, so it stuck).[20] Former government Vice-President, Theodoros Paggalos, has dedicated one of his books and accompanying website to proving that all Greeks share responsibility for the money-wasting, tax-evading, corruption-breeding party of the past three decades; and should therefore now

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[19] See Standard Eurobarometer 79 (2013) 'The factsheet on Greece', retrieved from: <http://ec.europa.eu/public_opinion/archives/eb/eb79/eb79_fact_el_en.pdf> (last accessed 26 August 2013).

[20] For concise presentations of relevant statistics, see Tzogopoulos (2013), and also D. Thompson 'Why Does the Laziest Country in Europe Work the Most?', blog *The Greek Crisis,* 29 May 2012, retrieved from: <http://www.greekcrisis.net/2012/05/why-does-laziest-country-in-europe-work.html> (last accessed 26 August 2013); and 'Are Greeks Lazy?', *Slate*, 19 December 2011, retrieved from: <http://www.slate.com/articles/business/moneybox/2011/12/european_financial_crisis_is_europe_a_mess_because_germans_work_hard_and_greeks_are_lazy_.html> (last accessed 26 August 2013).

share all the burden of putting things right.[21]

This strategy of consensus via intimidation may or may not be effective. This is not the point here. For a crisis reform strategy to meet the minimum democratic standard, the possibility of choice – and, therefore, of pluralism – has to be maintained. When reforms rely on intimidation to gain public legitimacy, then the possibility of choice has already been removed. And this is where the cumulative effect of persistent disregard for the minimum democratic standard becomes critical for the survival of democracy. Trapped in what they think is an inevitable and inescapable situation, demoralised and defamed, citizens resign to their fate, accepting reforms that are unconstitutional in form and substance, as well as detrimental to their quality of life. Democratic governance becomes a secondary concern (if at all), as the struggle for every day survival takes over. It is through this process that non-democratic governance becomes normalised, dealing a fatal blow on democracy. But all may not be lost yet: Earlier this year, a public survey actually thought to ask respondents on their views on the Constitution. Three out of four respondents thought it needs to change so that citizens' role in democracy is enhanced against the parliament, the government and political parties.[22] And nearly all agreed that democracy is a very positive word indeed. It remains to be seen whether democracy will survive the crisis and if so, what kind of democracy that will be.

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[21] 'Pangalos stands by we-all-ate-together statement', *Ekathimerini.com*, 18 April 2012, retrieved from: <http://www.ekathimerini.com/4dcgi/_w_articles_wsite1_1_18/04/2012_438123> (last accessed 24 April 2014).

[22] Metron Analysis (2013) 'Public Opinion Survey on Current Affairs, on behalf of the newspaper Eleftherotypia', February 2013, retrieved from: <http://www.metronanalysis.gr/web/html/index.asp?language=greek&page=surveys> (last accessed 24 October 2013).

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Annex: The Economic Adjustment Programme

The first time Greece officially requested economic assistance was on 3 May 2010. In its application, it requested € 80bn from the rest (15) of the eurozone countries and € 30bn from the International Monetary Fund (IMF). The aims and measures of the three-year programme that Greece would implement in return for the requested loans were laid out in a Memorandum of Understanding, which comprised the following:

- Memorandum of Economic and Financial Policies;
- Technical Memorandum of Understanding; and
- Memorandum of Understanding on Specific Economic Policy Conditionality

Signatories to the Greek side were the then Finance Minister, George Papaconstantinou (currently facing charges of breach of faith, tampering with an official document and abuse of office in relation to the so-called 'Lagarde list' scandal) [23] and the President of the Bank of Greece, George Provopoulos. The Commission signed on behalf of the eurozone member-states. Subsequently, the actual loan agreements were signed on May 8 2010: the *Loan Facility Agreement* with the countries of the Euro; and the *Stand-by Arrangement* with the IMF. The sum of these agreements is often called for short 'Memorandum' or 'Mnimonio', but its official title is 'Economic

[23] When George Papaconstantinou was still in office, the French government (in which current IMF managing director Christine Lagarde was Finance Minister at that time, hence the name 'Lagarde list') forwarded to its Greek counterpart a computer disk containing the names of 2000 Greeks with accounts totaling about € 6bn at an HSBC branch in Geneva, for investigation of possible tax evasion. The disk remained in ministerial drawers for some time, until the Greek press got hold of the case last year. The list was eventually leaked to journalist Kostas Vaxevanis, who published it in its entirety in his magazine Hot Doc- and was subsequently arrested for this. A parliamentary inquiry that lasted six months concluded, by an overwhelming majority, on July 16 2013 that there is sufficient evidence to bring Papaconstantinou to trial for allegedly having removed the names of three of his relatives from the original list, before handing a copy of it over to the tax authorities. A panel of Supreme Court judges will confirm the charges and arrange for Papaconstantinou to be tried by a special court. The only other time in Greece's recent history when a special court took place was back in 1989, when key PASOK members, including its founder and then prime minister Andreas Papandreou, were referred to trial by special court for alleged involvement in a money-laundering scandal.

Adjustment Programme'.[24] The money is released to Greece in instalments, following satisfactory reports by the Troika (or Task Force), i.e. the European Commission, the European Central Bank and the IMF staff that are tasked with monitoring the country's progress in implementing the Memorandum.

It is an understatement to say that the implementation of that first Memorandum did not go very well. The slow pace of reforms in combination with the recession-inducing measures quickly made it clear that the targets of the imposed austerity programme would not be met. Two rounds of austerity measures approved by the Greek parliament; one Interim National Reform Programme (Ministry of Finance of the Hellenic Republic 2011); and several rounds of mass public protests and union strikes later, Greece was moved on to its Second Economic Adjustment Programme (approved on 14 March 2012 by the eurozone finance ministers). This provided € 130 billion for the years 2012–2014 plus any undisbursed amounts of the first programme, at a total of € 164.5 billion of which € 144.7 billion is committed by the eurozone. The remaining € 19.8 billion that the IMF contributes is part of a four-year € 28 billion arrangement under the Extended Fund Facility for Greece that the IMF approved in March 2012. Moreover, Memorandum II, unlike the first programme which was based on bilateral loans, is financed by the European Financial Stability Facility (EFSF) on the side of eurozone member states. Crucially, it was accompanied by private sector involvement (PSI), more widely reported as 'haircut', whereby € 199.2 billion, or 96.9 per cent of eligible principal, was written down, resulting in a pay-out of € 29.7 in short-term EFSF notes and € 62.4 in new long sovereign bonds. Hence, the face value of Greece's debt declined by about € 107 billion as the result of the exchange, or 52 per cent of the eligible debt.

In November of last year (26–27 November 2012), eurozone finance ministers and the IMF agreed to extend the fiscal adjustment period by two years. The Greek government is now expected to achieve a primary surplus (comprised of current government spending less current income from taxes, and excluding interest paid on

[24] European Commission, DG Economic and Financial Affairs, 'Financial assistance to Greece', retrieved from:
<http://ec.europa.eu/economy_finance/assistance_eu_ms/greek_loan_facility/>
(last accessed 22 August 2013).

government debt) equivalent of 1.5 per cent of GDP in 2014, instead of the original target of 4.5 per cent – which is now the target for 2016 instead. They also agreed on a package of measures aimed at reducing Greece's debt to 124 per cent of GDP by 2020. In addition to the government bonds' buy-back that the Greek government proposed (at a proposed €10 billion for privately-held bonds worth €30 billion), the eurozone member states agreed to the following initiatives:

- A reduction in Greece's interest rate charged on the loans provided in the context of the Greek Loan Facility by 100 basis points (bps).

- A reduction in the guarantee fee costs paid by Greece on the EFSF loans by 10 bps.

- An extension of the maturities of the bilateral and EFSF loans by 15 years and a deferral of interest payments of Greece on EFSF loans by 10 years.

- A commitment by member states to pass on to Greece's segregated account an amount equivalent to the income on the Securities Markets Programme (SMP) portfolio accruing to their national central bank as from budget year 2013.

Part III

Disintegration through non-law?

Law matters

Chapter 7

Europe's economic constitution in crisis And the emergence of a new constitutional constellation

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A preliminary note on the course of the argument

Europe is in troubled waters. Constructive suggestions like the federal finality that Joschka Fischer sought to promote in his legendary lecture at the Humboldt University in Berlin[1] more than

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* Earlier versions of this chapter have been presented on 22 March 2012 at the Centre for Transnational Studies at the University of Bremen, on 8 November 2012, at the *Trentième anniversaire de l'Association internationale de droit économique* in Wroclaw, Poland, and on 15 January 2013 at the Centre for European Law and Governance at the University of Amsterdam. The argument developed further with each presentation. The present text has been elaborated subsequent to the citizenship conference in Uppsala on 21–22 March 2013. I am indebted to the discussants at these occasions, not exclusively, but, in particular, to Jonathan Zeitlin and Patricia Mindus. A first elaboration of the argument ('*Europas Wirtschaftsverfassung in der Krise*') was published in 2012 *Der Staat*, 51(3): 357–38 and the translaton by Sandra H. Lustig, and Matthew G. Harris was published as a working paper no. 6/2012 in *ZenTra Working Papers in Transnational Studies*. In the course of these revisions the text has not only increased in size but also been elaborated considerably. I wish to thank Chris Engert, Florence, for his linguistic assistance and editorial help.

1 '*Vom Staatenverbund zur Föderation – Gedanken über die Finalität der europäischen Integration* [From Confederacy to Federation: Thoughts on the Finality of European Integration], 12 May 2000, retrieved from: <http://whi-berlin.de/documents/fischer.pdf> (last accessed 24 January 2014). How widely the lecture was noted is illustrated by the comments in Joerges, Mény and Weiler (2000).

ten years ago no longer sounds credible and contrast, ever more unhappily, with the endless and frenzied crisis management which has placed its stamp of rigid austerity policy on the 'periphery' of what was to evolve into an 'ever closer Union'. What is at stake is the rule of law and the project of 'integration through law', which characterised and connected European law scholarship transnationally,[2] in the formative phase of the integration project and a good while thereafter. Europe is far from hosting 'the most competitive, knowledge-based economy in the world' as the Lisbon Council proclaimed in the year 2000; its economy is at the core of the present crisis. European constitutionalism, which dominated academic discussion for a decade, and which, in all its endeavours, thoroughly neglected the inherently political dimensions of 'the Economic,' has been silenced.

Seemingly paradoxically, the same holds true for Germany's ordoliberalism and its project of an 'economic constitution'. According to this school of thought, the legitimacy of the European project was, to rest upon the legal ordering of the economy:[3] the economic freedoms of the EEC Treaty (Treaty Establishing the European community), a system of undistorted competition, and an economic policy 'complying with justiciable criteria' (Mestmäcker 1973: 106) were the cornerstones of this order; they were to orient the integration process in a way that the European polity would be legitimated by – and reduced to – an economic *ordo* whose validity did *not* depend upon democratic credentials, let alone upon the transformation of Europe into a fully-fledged federal state.[4]

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[2] A chapter from Joseph H.H. Weiler's Ph.D thesis, 'The Community system: the dual character of supranationalism' was groundbreaking, see Weiler (1981), and then the seminal work he orchestrated: Cappelletti, Seccombe and Weiler (1987).

[3] See, for a critical account, Joerges (2005: 465 *et seq.*, 2010).

[4] See, for a particularly thorough re-construction, Milène Wegmann (2002). Her work corresponds instructively to Wolfgang Fikentscher's earlier *magnum opus* on *Wirtschaftsrecht* (economic law). Decades before the studies on global governance, European governance, the relation between the levels and the impact of transnational governance on national statehood became *en vogue* in political science, and 'constitutionalism beyond the state' became everybody's concern in legal scholarship, Wolfgang Fikentscher (1983a, 1983b) had conceptualised *Wirtschaftsrecht* in truly transnational and constitutional perspectives, and composed the two monumental volumes accordingly: The first volume is dedicated to *Weltwirtschaftsrecht* (world economic law) and *Europäisches Wirtschaftsrecht* (European economic law); national economic law (*Deutsches Wirtschaftsrecht*) is presented upon

This idea guided and accompanied ordoliberalism's path to Europe. Nobody championed or developed it more consistently than Ernst-Joachim Mestmäcker. One of his seminal essays is the lecture '*Macht-Recht-Wirtschaftsverfassung*' (Power-Law-Economic Constitution), which he gave at the *Verein für Socialpolitik* conference in 1972 in Bonn. There he explained that the pressure to harmonise, stemming from integration, would become stronger. A Common Monetary Policy would mean 'ultimately giving up' the opportunity to maintain far-reaching differences between the economic orders (Mestmäcker 1973: 109).

The Community for which the original ordoliberal concepts were conceived and to which Mestmäcker referred seems nothing less than idyllic from today's perspective; it was, of course, both smaller and more homogeneous than the current Union. For this reason alone, it is anything but surprising that the incorporation of the project of integration into law, in particular, its commitments to a legal ordering of economic policy (*Ordnungspolitik*), no longer seem viable. By now, the symptoms of a deep crisis are evident and the necessity to develop new perspectives for the European project seems irrefutable. To be sure, the course of history cannot be reversed. But it is all the more important to analyse it and to try to understand how and why, in particular, the configuration of the relationship between law and politics in the integration project has contributed to the 'integration failure' which we are witnessing in the current crisis. This essay will proceed in five steps:

The first step, taken in some haste, is about the Weberian notion of the nation-state and its pursuit of power through economic strength. The second involves the taming of the selfsame nation-state by law, and, then, the de-coupling of the European economic constitution from the labour and social constitutions of the nation-states, which presents itself to the one – ordoliberal – side as nothing but a logical implication of the establishment of a European economic order, while other political quarters perceive this disconnection as a threat to the legacy of the welfare state. This is followed by an analysis of the various dimensions of the problems of the integration project, which

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this basis. This conceptualisation documents the truly universalist commitments of the ordoliberal tradition which Wegmann emphasises.

will refer to Karl Polanyi's economic sociology. The next section is an elaboration of these remarks. It deals with the establishment and the crisis of Europe's Economic and Monetary Union (EMU); it includes an overview over Europe's new 'crisis law' and its assessment by the German Federal Constitutional Court (GCC) and the Court of Justice of the European Union (CJEU). The dramatic nature of our current situation will then be illustrated by means of a fictitious dispute between Carl Schmitt and Jürgen Habermas in the following section. In the analysis of this dispute, Carl Schmitt's theorems will prove to be frighteningly realistic. 'But where danger threatens, that which saves from it also grows' (Hölderlin 1994[1954]: 243). What kind of regime did Europe impose on itself, and what does this mean for European citizenship? These challenges will be addressed in an Epilogue, which will also tentatively consider an alternative vision to both the frightening as well as the possibly merely voluntarist scenarios on the future of the European integration project.

Max Weber's Nationalstaat

The steps towards European integration after World War II document, above all, how our bellicose past was overcome. At the same time, the project was meant to rein in the economic militancy of the nation state as well. Max Weber formulated his perception of that nation state in his 1895 inaugural Freiburg address as follows:

> Our successors will not hold us responsible before history for the kind of economic organization we hand over to them, but rather for the amount of elbow-room we conquer for them in the world and leave behind us. Processes of economic development are in the final analysis also power struggles, and the ultimate and decisive interests at whose service economic policy must place itself are the interests of national power, where these interests are in question. The science of political economy is a political science. It is a servant of politics, not the day-to-day politics of the individuals and classes who happen to be ruling at a particular time, but the lasting power-political interests of the nation. And for us the national state is not, as some people believe, an indeterminate entity raised higher and higher into the clouds in proportion as one clothes its nature in mystical darkness, but the temporal power-organization of the nation, and in this national state the ultimate standard of value for economic policy is 'reason of state'. There is a strange

> misinterpretation of this view current to the effect that we advocate 'state assistance' instead of 'self-help', state regulation of economic life instead of the free play of economic forces. We do not. Rather we wish under this slogan of 'reason of state' to raise the demand that for questions of German economic policy – including the question of whether, and how far, the state should intervene in economic life, and when it should rather untie the economic forces of the nation and tear down the barriers in the way of their free development – the ultimate and decisive voice should be that of the economic and political interests of our nation's power, and the vehicle of that power, the German national state.
>
> (Weber 1980[1895]: 438 *et seq.*)

'It was not the agreement of many audience members with the following remarks, but their dissent that prompted me to publish them', Weber wrote in the preliminary notes to the publication of his lecture. His lecture has weathered these concerns well. It is profoundly thought through in terms of economic theory, sociology, and history, and, despite all its jingoistic pronouncements, is also a critique of the lack of political capacity of the German political class (see Aldenhoff 1991). At this point, we shall leave it at that. What *is* important, however, is that the martial tone of Weber's lecture very clearly spells out a target of the European project as it was also understood later, in particular, in Freiburg when that city had become the intellectual *Heimat* of the Ordoliberal School.

The civilising accomplishment and asymmetry of the EEC Treaty

> What is historic about the EEC Treaty is that it integrates the internationality of economic relationships into the internationality of law and political institutions. In this sense, the EEC Treaty includes an economic constitution […] Expressed in terms of state and society, the EEC takes as its starting point the law of bourgeois society and its institutions as the first manifestation of the universal in the international realm.
>
> (Mestmäcker 1973: 109–109)

The quotation provides evidence for how ordoliberalism differentiates and liberates itself from Weber's *Nationalstaat*. Now, all this has a price. Liberation came about through the imposition of legal commitments and constraints on the political autonomy of sovereign states. Due to these constraints, it became possible 'to conceptualise an economic policy that can be bound to legal and constitutional norms' (*ibid.*: 102). It is not only the contents of economic policy that are affected by these demands, but also the competencies of legislation and its scope (*ibid.*: 103 *et seq.*) as well as the details of free collective-bargaining and co-determination.

This touches upon a sensitive issue. Even if we assume that the Treaties of Rome have established a European economic constitution, they nonetheless remain silent at least concerning labour and social law. This is why a functional equivalent of the 'social *Rechtsstaat*', in the sense of Article 20(1) German Basic Law or of the 'social market economy', as it was developed programmatically by Alfred Müller-Armack (see Müller-Armack 1966, 1974), could not establish itself at European level. What are the implications of this finding? Fritz W. Scharpf (2010)[5] considers the separation of the economic and social constitutions to be a design-flaw which places Europe's social integration at long-term risk. These statements are, however, sociologically based, and meant in a socio-political way. Explaining how this decision came about is a different question, however; another is whether such explanations are normatively instructive and what legally binding-effect may be granted to this initial situation. The reduction of the European social and labour constitution to the EEC Treaty's principle of non-discrimination is widely viewed as a successful negotiation on the part of Germany, which is supposed to have been worth attaining at the expense of agricultural policy. Now, the *quid pro quo* was agreed upon under the influence of the welfare promises of the Ohlin Report (International Labour Organization 1965), which also impressed the political Left at the time, and took place in the era of 'embedded liberalism' (as used by John G. Ruggie 1982), in which the opening up of national economies seemed compatible with the establishment of welfare-state systems.[6]

[5] In the legal literature, see Rödl (2013).

[6] For a critical discussion of Ruggie's later view, see O'Brien (2011).

But what does all this mean in legal terms? Is this an irreversible 'decision' about the alternatives of a planned economy *versus* a market economy? Or is this a constitutional compromise, as Hermann Heller found the Weimar Constitution to be; that is, permanently binding guidelines for developing the relationship between the economic and labour constitutions in Europe? (see Rödl 2010 and Giubboni 2006: 7 *et seq*.) Both positions suffer from the same difficulty. They treat the results of political negotiations as though these were the results of an assembly convened to draw up a constitution. So, is this merely a piece of history, whose further course is to be accepted as a kind of normative fact that we can no longer influence retroactively?

In the case of European integration, conceived of as a project which is nonetheless at a loss concerning how to determine its *finalité*, it seems to be about adjusting to the dynamics of a development whose decoding is impossible without extra-legal means, but upon whose legal constitution it must, nonetheless, depend.[7] We encounter such undertakings everywhere. Undoubtedly, the encounter with Karl Polanyi, which now follows, is unusual.

Symptoms of crisis in the light of Karl Polanyi's economic sociology

Karl Polanyi is one of the three Viennese *emigrés* who grappled with fascism towards the end of World War II. The other two were Friedrich August von Hayek[8] and Karl Popper.[9] Polanyi took up the issue in his brief and only monograph, which was first published in 1944 (Polanyi 2001[1944]).[10] His analysis is specific, as it is 'embedded' in a re-construction of the core instability of industrial capitalism. This analysis lays heavy emphasis on the role played, within capitalist society, by three 'fictitious commodities': money, labour, and land. These three fictitious commodities denote 'goods' (*Waren*) which nonetheless predate and transcend 'the market', and whose subsequent 'commodification' not only provokes crises both

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[7] In principle, Hans Peter Ipsen's term 'continuous re-configuration' (*Wandelverfassung*) means nothing else; see Ipsen (1987: 201).

[8] *The Road to Serfdom* was first published by Routledge in London in 1944.

[9] *The Open Society and its Enemies* was first published by Routledge in London in 1945.

[10] On Polanyi's topicality, see, for example, Beckert (2007), Streeck (2009: 154–156) and and the *maître penseur* among the Polanyi experts: Fred Block (2003).

within and around capitalism, but also proves to be an impetus for counter-movements to the market (Polanyi 2001[1944]: 69 *et seq)*. In view of the, by now, chronic instability within European EMU, the steady erosion of national labour and social constitutions, as well as continuing conflicts in the area of energy policy, Polanyi's theses and conclusions appear to have gained a depressing degree of general topicality. The following analysis, however, limits itself within this paradigm to the European 'integration through law project', and to the question of what European law has experienced and is experiencing, and what it, itself, has precipitated. Nor is this a matter, for example, of a generalised condemnation of market processes, at least not for strong voices in the Polanyian tradition (Ebner 2007: ch. 2, 2011: 29 *et seq.*). What is dramatic, however, is Polanyi's thesis that treating fictitious goods as marketable products cannot come about smoothly, but will trigger crises and counter-movements. In view of the present state of the European Union, the erosion of the labour and social constitution and the looming conflicts about the future of atomic energy, Polanyi's diagnoses are astonishingly topical (see Joerges forthcoming).

In the present constellation of conflict inter-dependencies, we must remain sensitive towards pertinent problems in their specific contexts. Drawing a line, for example, from Polanyi's fictitious commodities to atomic energy is a stretch, and may be going too far, but it is not absurd to regard atomic energy as a non-marketable good.[11] In any case, the insight that the economic success of this type of energy is due not to natural evolutionary processes, but, instead, to the establishment of markets by political fiat, is irrefutable. European law plays an unfortunate role here. The Euratom Treaty of 1957[12] was in a position to declare atomic energy the technology of the future *par excellence*, but did not Europeanise it, leaving the decision about its use to the nation states instead.[13] The Treaty of Lisbon did not change

[11] In Polanyi (2001[1944]: 73), we read: 'To allow the market mechanism to be the sole director of the fate of human beings and their natural environment, indeed, even of the amount and use of purchasing power, would result in the demolition of society […]. [N]o society could stand the effects of such a system of crude fictions even for the shortest stretch of time unless its human and natural substance as well as its business organization was protected against the ravages of this satanic mill.'

[12] Consolidated version, OJ C 84, 1–112.

[13] The silence of the Euratom Treaty (The Treaty establishing the European Atomic Energy Community, also EAEC) is deafening: the Treaty did not grant the

this in any way[14] – with the consequence that a phasing-out of atomic energy in Europe, which is effective for everybody involved, can only take place if all the member states were to implement it, a scenario which is definitely nowhere in sight.

The consequences of de-coupling the labour and economic constitutions from one another remained unobserved for a long time or were presented time and again as being rectifiable. The notion that a 'European social model' would take the place of the diverse variants of the Western European welfare states was, however, never more than a pale utopian dream. This became apparent after the enlargement towards the East. At that juncture, the socio-economic disparities became so pronounced that a continuation of integration was feasible only in the form of so-called 'negative integration', that is, by reducing the social protection provided by welfare states. This strategy was initiated by the European Commission in collaboration with actors representing relevant interests in both the old and the new member states. The *Viking*, *Laval*, and *Rüffert*[15] decisions are the most striking legal, partial-victories, which, taken together, can be viewed as a confirmation of the decision to treat an economic constitution as a 'pure' market constitution and as the abandonment of the common European constitutional compromise. One must also keep in mind, however, what this means with regard to the acceptance of the project of integration. If Polanyi's diagnoses are correct, then we must anticipate counter-movements seeking to restore perspectives calling for social protection – and after Europe's transformation into an 'austerity union' such signals are becoming ever more visible.

Community the competence to 'authorise the construction or operation of nuclear installations'; see the European Court of Justice (ECJ), Case C-29/99, Judgment of the Court of 10 December 2002, *Commission* v. *Council,* ECR 2002, I-11281, para. 89; on the criticism of this legal situation see Joerges (2012).

[14] Article 194(2) of the Treaty on the Functioning of the European Union (TFEU).

[15] Case C-438/05, International Transport Workers' Federation, Finnish Seamen's Union v Viking Line ABP, OÜ Viking Line Eesti [2007] ECR I-10779; Case C-341/05, Laval un Partneri Ltd v Svenska Byggnadsarbetareförbundet [2007] ECR I-11767; Case C-346/06, *Rechtsanwalt Dr. Dirk Rüffert* v *Land Niedersachsen* [2008] ECR I-01989.

The crisis of Economic and Monetary Union and the European rule of law

These very brief remarks must suffice,[16] so that space remains for the financial crisis which overshadows everything now.

Juridification of Monetary Union

The financial crisis concerns the EMU as it took shape in the 1992 Treaty of Maastricht. The EMU was doubtless a political project, albeit one that was to be shielded strictly from the influence of daily politics, and entrusted to the medium of law instead. It was not '*alternativlos*' (without alternative), as is claimed today. In the 1970s, the Werner-Davignon Plans had attempted to synthesise the economic and social constitutions (Schulz-Forberg and Stråth 2010: 43 *et seq.*) It was precisely during these years, however, that a general turn away from Keynesianism came about; Keynesianism had been legally anchored in Germany in the 1967 Stability Act (*Stabilitätsgesetz*) (Joerges 2011a: 420 *et seq.*) which was to realise the 'magical quadrant' – price stability, high employment, balance of payments, and appropriately increasing economic growth – a balancing act that seemed, at the time, very precarious to many renowned German constitutionalists because it had to be entrusted to the evaluation and discretionary decision-making of the political authorities. While German traditionalists were concerned about rule-guided *Ordnungspolitik*, in Great Britain, the postwar welfare-state *acquis* was revoked. Such a background constellation provided a strong political basis for a new European consensus that was expressed in the project of the single market and the turn to monetarist concepts. Paradigm shifts of this kind do not simply follow theoretical reason, nor should their effective rejection be regarded as evidence of the success of the prevailing paradigm without further ado.[17]

In the case of Europe's economic-policy orientation, two stages of re-orientation can be discerned. Firstly, Commission President Jacques Delors obtained broad support for his project of a single market, which was perceived as an institutionalisation of economic rationality: a commitment to principles which were to guide all

[16] An extensive discussion is to be Joerges (2013).
[17] For the 1970s, see Glasman (2011: 96 *et seq.*), for the present, Crouch (2011).

political action.[18] The Monetary Union and the Stability Pact[19] were understood as complementary projects, as institutionalising an independent central bank outside all political spaces and beyond the institutional structure of the Union was to consummate the new architecture and fossilise a supranational economic constitution.

In a differentiating analysis, Anke Hassel and Waltraud Schelkle argue that EU policy had by no means turned out to be conceptually stringent, but had accomplished and practiced a synthesis of Keynesianism and monetarism incrementally.[20] To lawyers, this is hardly surprising. However, especially in the case of the EU, the jurist must insist on the framing of decision-making processes by mandatory European and nation state legal conditions, which then also determine the institutionalisation of political goals to a significant extent. In the case of the EMU, this reciprocal dependency of law and politics was distinctly perceptible, and this, in turn, determined its unfortunate configuration.

The decision by the GCC on the Treaty of Maastricht had a literally decisive part in making this misfortune come about, when it declared replacing politics by legal rules to be a *sine qua non* for Germany's participation, both in terms of content and institutionally.[21] The reasoning of the Court's 2nd Senate was remarkably complex: it first dealt with the plaintiff's argumentation that the European Union had, under the new provisions, such far-reaching competence that the nation states were no longer in a position to discharge important tasks. This, however, called the continuing existence of *democratic statehood* into question. This argumentation also referred to monetary

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[18] See Lepsius (1997: 57 *et seq.*); regarding application to Europe, see Lepsius (2000: 213-222).

[19] Resolution of the European Council on the Stability and Growth Pact, Amsterdam 17 June 1997, OJ C 236, 1–2; Article 126 TFEU (ex-Article 104 EC Treaty) in conjunction with Protocol No. 12.

[20] See their contribution to the Berliner Dahrendorf Symposium 2011 (Hassel and Schelkle 2011: 4 *et seq.*) The authors thereby oppose Fritz W. Scharpf (2011), who attests to Europe a one-dimensional monetarist orientation in the wake of Germany's shift away from Keynesianism.

[21] *Bundesverfassungsgericht* [BVerfG - Federal Constitutional Court], Cases 2 BvR 2134/92 and 2 BvR 2159/92, *BVerfGE* 89, 155 [*Brunner* v *European Union Treaty*, *CMLR* 57 (1994) 1], 12 October 1993. On the following, see Joerges (1996) and Everson (1998).

policy. But the Court then responded by occupying the spaces for democratically-shaping policy with law. In so doing, it embraced the – in this instance, compatible – ordoliberal and monetarist theorems, and gave them a legal form: Economic integration, the Court said, was an apolitical process that both could and was permitted to take shape autonomously and beyond the member states. Monetary Union was constituted appropriately via a constitutional duty to guarantee price stability and regulations to counter excessive budget deficits. In this way, the objections to the democratic legitimacy of economic integration seemed to resolve themselves.[22] In the public-law divisions of European legal studies in both Germany and in the larger quarters of European constitutionalism, scholars either did not even realise this, or they did not deem it worthy of mention.[23]

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[22] According to Section II 3 a) of the judgment, '[t]he addendum to Article 88 of the German Basic Law, included with a view to the European Union, permits transfer of responsibilities and powers of the *Bundesbank* to a European Central Bank, which meets the strict criteria of the Maastricht Treaty and the European System of Central Banks concerning the independence of the Central Bank and priority of assuring price stability'. I read this conditionality as meaning 'if and because'. Ernst-Wolfgang Böckenförde, who is certainly well informed as he was involved in the decision, refers to a previous passage (II 2 f) in which the Court qualifies the agreement of a 'monetary union in the absence of a political union at the same time or immediately thereafter' as a 'political decision for which the relevant bodies are to be held politically responsible'. He concludes: 'If a Court stays within its remit, it [could] express greater distance only with difficulty' ('Kennt die europäische Not kein Gebot? Die Webfehler der EU und die Notwendigkeit einer neuen politischen Entscheidung', *Neue Züricher Zeitung*, 21 June 2010; also in Böckenförde 2010: 299–303, citation at p. 300. The Constitutional Court even added, in the same section: 'If it transpires that the desired monetary union cannot be made a reality in the absence of a (not yet desired) political union, then a new political decision must be taken about how to proceed.' All this cannot salvage the decision. The 2nd Senate had given its consent to an institutional configuration in which the European law was to dis-empower national politics – and such moves cannot be reversed as both critics and supporters of the EMU have observed; see, on the one hand Majone 2010: 34, 162; on the other, E.-J. Mestmäcker 'Der Schamfleck ist die Geldverachtung. Wer das Ökonomische geringschätzt, weiß gar nicht, welche politische und kulturelle Leistung eine stabile Währung darstellt', *Frankfurter Allgemeine Zeitung*, 18 November 2011, no. 269: 33.

[23] Instead, the Court was confronted with its talk of an 'association of states', its announcement that it would refuse to follow 'diverging legal acts', but above all the statement that it democratic rule presupposes that a 'relatively homogeneous people' has the opportunity 'to give legal expression to what unifies them – intellectually, socially, and politically'. Important benchmarks were set by the criticism of all this in Weiler (1995). Today, in light of the crisis, people frequently detect an 'asymmetry' resulting from the fact that monetary policy was enshrined at supranational level,

Processes of erosion

Mestmäcker commented that, in the light of the 'power struggle between the political and the economic', the question as to 'master and servant' presents itself, and declared the law to be the highest authority. Yet, this authority proved unable to prevail. The situation was far less dramatic than it is today. But the rules agreed upon were flawed in substance, and if they had been enforced, this would have caused harm. In line with this widely-shared view, the very short life of the new legal edifice did not give rise to much concern.[24] When Germany, France, the Netherlands, as well as others, failed to respect the rules of the Stability Pact, the Commission's much vaunted efforts to take action against them dwindled into nothing. Barry Eichengreen, a renowned US observer of European monetary policy ever since the negotiations on the Treaty of Maastricht (see Eichengreen 1992), commented on the breach of the law very frankly. How can one expect compliance with a threshold which has no sound conceptual basis (Eichengreen 2003)? Occasionally, he used even stronger language[25] – and was by no means alone in voicing such principled criticism.[26] Monetary Union was poorly designed, and enforcement of its rules would not have prevented the damage, but increased it, instead.

And things were to become much, much worse during the current crisis. The Union is experiencing a kind of state of emergency in which the law is losing its integrity The all-too-meagre points of reference provided in Article 122(2) TFEU, amended under the simplified revision procedures of Article 48(6) which 'shall not

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while the Member States retained their competence in fiscal and economic policy. In my own account the decoupling of monetary policy from fiscal and economic policy Maastricht has produced 'diagonal conflicts', which are not governed by the 'vertical' supremacy principle and cannot be resolved 'horizontally' among the member states who are all subject to the one size-fits-all policy of the ECB which in turn cannot take their socio-economic diversity into account (on the nation of 'diagonal conflicts', see Joerges 2007: 318 *et seq.*)

[24] For more detail on the following, see Joerges (2005: 204 *et seq*).

[25] As an example: 'The 3% cap is at best ridiculous and at worst perverse', he wrote in a contribution for *DIE ZEIT*, 20 November 2003.

[26] Numerous references are found in Majone (2011a and 2012).

increase the competences conferred on the Union in the Treaties'[27] must justify incalculable solidarity payments;[28] the European Central Bank is disregarding its statutes as they used to be read (Seidel 2010); parliaments are convened to make fast-tracked decisions that cannot be meaningfully discussed; Greece, and other members of the Union, are being told that their sovereignty is now 'limited'; changes of government take place under exceptional circumstances. Polanyi and his analyses of monetary policy are only rarely mentioned during all this. Yet, it is appropriate to bear in mind his qualification of money as a fictitious commodity,[29] and of the risks of destroying the social conditions under which market societies can function (Streeck 2011 and Supiot 2008). Ordoliberal and monetarist standards were Europeanised in the legal constitution of Monetary Union, although it was not possible to Europeanise their societal conditions for functioning, which had developed over time. Majone explains his opinion that the central bank is a 'constitutional monstrosity' by reasoning that the bank is supposed to pursue its stated goal of price stability in a political vacuum, and that it is unable to take the Union's socio-economic disparities into account while doing so.[30] As Scharpf adds, the institutionalised inabilities to do anything other than react to instability and imbalance with intensified austerity programmes, not only threatens the well-being of European citizens, but also endangers the social acceptance of the Union (Scharpf 2011: 5).

Reactions

The pace at which crisis summits are being held and the drafting of more and more new legislation and regulatory complements is breath-taking.[31] It is both important and meritorious to record all this

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[27] Council Decision 2011/199/EU of 25 March 2011 amending Art. 136 TFEU with regard to a stability mechanism for Member States whose currency is the euro, OJ L 91, 1–2, in force since 1 January 2013.

[28] On the Constitutional Court's decision on Greece, see the section 'The rescue package for Greece' below. The reasons provided in plaintiff Peter Gauweiler's constitutional complaint by Dietrich Murswiek are available online at: <http://www.jura.uni-freiburg.de/institute/ioeffr3/forschung/gutachten> (last accessed 24 January 2014).

[29] 'Money […] is merely a token of purchasing power which, as a rule, is not produced at all, but comes into being through the mechanism of banking or state finance' (Polanyi 2001[1994]: 72), see Frerichs (2013).

[30] See Majone (2011 and 2012).

[31] For continuously updated information, see the press releases of the Council on Economic and Financial Affairs at <http://www.consilium.europa.eu/press/press-

precisely,[32] so that we can become aware of the tensions between our inherited concepts and methodological tools, and the present European *praxis.* Here, however, we must limit ourselves to a few highlights:

In March and May 2010, respectively, the Commission developed the 'Europe 2020 Strategy'[33] and the 'European Semester';[34] these were followed, in June 2010, by the European Financial Stability Facility (EFSF) Framework Agreement,[35] and, in March 2011, by the European Council's 'Euro Plus Pact'.[36] Simultaneously, upon the basis of the simplified revision procedures laid down in Article 48(6) TEU, the European Council also decided, on 25 March 2011, to add a new Paragraph 3 to Article 136 TFEU, which permitted the establishment of a stability mechanism and the granting of financial assistance, effective of 1 January 2013.[37] This was followed, in November 2011, by a bundle of legislative measures aimed at re-enforcing budgetary discipline on the part of the member states. The package is supposed to go down in history under the catchy title of the 'Six Pack' and entered into force on 13 December 2011.[38] The high point of all this is the Treaty on Stability, Co-ordination and Governance (TSCG), drafted in December 2011, approved at an informal meeting of the

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releases/economic-and-financial-affairs?lang=en&BID=93> (last accessed 24 January 2014).

[32] Suffice it here to refer to just a few examples from the torrent of literature: Calliess (2011); Ruffert (2011a); Craig (2013a, especially ch. 12 on 'Financial Crisis, Response, and Europe's Future'). See, also Scicluna (2013, and especially ch. 5 with an impressive analysis of Europe's present constitutional constellation [*Vefassungswirklichkeit*]).

[33] European Commission, Communication from the Commission, *EUROPE 2020 A strategy for smart, sustainable and inclusive growth*, COM(2010) 2020 final, 3 March 2010.

[34] European Commission, *Communication from the Commission to the European Parliament, the European Council, the Council, the European Central Bank, the Economic and Social Committee and the Committee of the Regions, Reinforcing economic policy coordination*, COM(2010) 250 final, 12 May 2010.

[35] Confirmed in Conclusions of the European Council, EUCO 13/10, CO EUR 9, CONCL 2, 17 June 2010. The Framework Agreement was concluded by the ECOFIN Council and confirmed by the European Council, Brussels on 17 June 2010.

[36] Conclusions of the European Council, EUCO 10/11, CO EUR 6, CONCL 3, 24–25 March 2011 (Annex I).

[37] See note 27 above.

[38] The five regulations 1173–1177/2011/EU and Directive 2011/85/EU of 8 November 2011, see OJ L306 of 2011.

European Council on 30 January 2012,[39] and signed on 2 March 2012 by 25 out of the then 27 Member States. A debt brake according to the German model has been introduced, and will be subject to judicial review by the CJEU in the form of institutional borrowing, with one member state bringing action against another. Support from the European Stability Mechanism (ESM), a permanent crisis fund, will be available only to countries in the eurozone that have signed the pact. The TSCG has been ratified by the required number of member states and entered into force on 1 January 2013. Two further Regulations submitted back in November 2011 – the 'Two-Pack' – were adopted with parliamentary blessing in March 2013. They provide 'for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area', and 'the strengthening of economic and budgetary surveillance of Member States experiencing or threatened with serious difficulties with respect to their financial stability in the euro area'.[40]

There is much to scrutinise here: the legal problems, their treatment in legal scholarship, the analysis and interpretation of what has been established. The law-politics relationship is particularly challenging. Lawyer, practitioners and academics alike, have all traditionally sought to remain on good terms with political power.[41] When it comes to Articles 122–126 TFEU, our discipline can apparently not resist helping political and institutional actors by taking the letter of the law so lightly as to run afoul of it. But just as legally wayward spirits will sometimes fail to finesse a fine legal point and must withdraw without achieving anything, jurisprudence is facing problems, which seem to lie beyond the reach of its methodological means and conceptual potential. We are not going to re-construct these discussions in any detail here, but merely underline three

[39] See the Treaty on Stability, Co-ordination and Governance in the Economic and Monetary Union in the version of 20 January 2012, available at: <http://european-council.europa.eu/media/639235/st00tscg26_en12.pdf> (last accessed 26 January 2014).

[40] For details see the press release of the European Parliament 'Green light for economic governance "two pack"', retrieved from: <http://www.europarl.europa.eu/pdfs/news/expert/infopress/20130312IPR06439/20130312IPR06439_en.pdf> (last accessed 24 January 2014).

[41] See Stolleis (2003). Michael Stolleis' observations concern primarily, but by no means exclusively, Germany's Nazi period.

particularly disturbing constitutional issues which have reached Europe's most important courts, namely:

1. The establishment of new regimes of economic governance outside the institutional frameworks of the Treaties and of national constitutions, for which two German lawyers[42] have coined the notion of '*völkerrechtliches Ersatzunionsrecht*'.

2. Then, the problem of whether the means with which these regimes have been established may be used to intervene into national constitutions and imposed upon democratically-legitimated governments which require financial support; with this practice, Europe's Crisis management is following international examples.[43] The German Constitutional Court was confronted with the query of whether such practices can be employed among the member states of the Union and/or are even required by Germany's constitution.

3. The substantive issue – often obscured as a simple matter of methodological interpretation – of whether the conceptual basis for EMU must be respected in the interpretation of its provisions: If the EMU suffers from a design defect and the implementation of the law as it stands seems to cause harm, can its rationale be replaced by some alternative, and who is empowered to decide upon such emergencies? The CJEU did not shy away from handing down clear answers to the queries in the *Pringle* case on 27 November 2012.[44]

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[42] Lorz and Saurer (2012), cited in the judgment of the German Constitutional Court of 12 September 2012, BVerfG, 2 BvR 1390/12, discussed below in the next section, at para. 257 of the German version, and para. 226 of the English version.

[43] Pertinent practices have been exercised by central banks and the International Monetary Fund long before the financial crisis. They have been characterised as a feature of the global capital market: 'The new conditionality of the global economic system – the requirements that need to be met for a country to become integrated into the global capital market – […] facilitates the task of instituting a certain kind of monetary policy', wrote Saskia Sassen (2002: 56 *et seq.*).

[44] Case C-370/12 *Pringle* v *Pringle v Government of Ireland, Ireland and the Attorney General*, Judgment of 27 November 2012, *nyr*.

Community method vs. 'Union method' and 'Ersatzunionsrecht'

The special feature of the European system, as Joseph H.H. Weiler explained in his seminal 1981 essay, is the simultaneity and the balance of supranational law and inter-governmental policy (Weiler 1981: 257). He thus characterised a precarious relationship, but certainly did not seek to grant the member state governments *carte blanche* to suspend their commitments to Community (now Union) law whenever they believe that doing so would be irrefutable and expedient. And it is precisely this which is the historical achievement of the Treaties of Rome: that they endeavoured to rein in the power-political actions of the Weberian nation state by legal means. The differences between different modes of interaction in the Union have been quite thoroughly explored (Reh 2012). The move from arguing and deliberative problem-solving to bargaining and the strategic pursuit of so-called national interests and the replacement of the old Community method in which the law provided institutional and procedural protection to the weaker actors make a real difference. Thanks to its domination by the Council, the new 'Union method' faithfully mirrors the power asymmetries in the Union. Should the law care? Mark Dawson and Floris de Witte are among the few[45] who have raised this issue (Dawson and de Witte 2013).[46]

[45] There are more, but they are rare. For another noteworthy exception with a great sensitivity for the hybrid nature of the Union *praxis*, see Edoardo Chiti and Pedro Gustavo Teixeira (2013: 685 *et seq*., 690 *et seq*.), while Chiti and Teixeira, throughout their analyses, assess what they lucidly describe through functional and normative yardsticks and thereby soften their critique, their conclusion is nonetheless uncompromising on this point: The new hybrid method 'tends to set aside the role of EU institutions in exercising their respective competences within a democratic framework based on EU law in favour of power-based intergovernmental relations' (*ibid*., at 708). But this is precisely the reason why not only democracy but also the rule of law in its core transnational function, as we have underlined it in Section II, is at stake.

[46] They (2013: 842) conclude: 'The rise of executive control via the European Council, the increasing ease of making treaty and legislative reforms without consulting smaller member states, and the creation of eternal fiscal rules uncontrollable by national parliaments, unable to be fully discussed and legitimated, is now in danger of desensitising the Union to concerns and interests that need to be accommodated for a stable EU project to continue'. Indeed, and it is true 'that the Union's existing response […] does not bode well for the future' (*ibid*. 844:). What remains to be explained is Europe's apparent political inability to organise a legally robust response to these insights as discussed further below

It is simply amazing that it has become the rule among lawyers not to take these issues seriously. To be sure, the Member States of the Union have conferred their sovereignty only 'in limited fields' and retain political autonomy where this does not occur. But they nonetheless remain bound by their common commitments, in particular, to democracy and the rule of law (Article 2 TEU). This is why the sovereignty that they have retained does not empower them to enter into *qualsiasi* agreement. The Fiscal Compact requires from its signatories[47] changes of fundamental constitutional importance, and the modes of their implementations are anything but consensual.[48] The methodological reasons invoked in various modes replicate what could be observed earlier in European law, namely, a resort to legal formalism which shields law from justifying to what extent it is used (see Joerges 2009): Daniel Thym (2011) argues accordingly that intergovernmental cooperation permits member states to exercise reactive crisis management, where Union law does not provide an instrument for doing so. This move has its methodological precursors in the widely-acclaimed resort to the Open Method of Co-ordination (OMC) in the field of social policy. Its liberation from the straitjacket of the 'Union method' and the replacement of hard law by soft law was explicitly targeted at the attainment of social objectives which

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[47] Least from Germany which has in 2009 constitutionalised the '*Schuldenbremse*' in Article 109 Basic Law. Constitutional provisions, however, are easier to amend than multilateral treaties.

[48] Suffice it here to point to the analysis submitted by political scientist Martin Höpner and lawyer Florian Rödl (2012); similarly Jürgen Bast and Florian Rödl, (2012). The authors demonstrate in detail that the Council's power of surveillance in accordance with Art. 136(1) (b) does not provide for the sanctions which the new regime establishes. Although the coordinating competencies in accordance with Article 121 TFEU (3) and (4) provide for reporting requirements on the part of the Member States as well as recommendations by the Commission, Article 121(6) TFEU does not permit mandatory sanctions. Indeed: The multilateral surveillance in accordance with Article 121(3) and (4) TFEU contains provisions for reports, recommendations, and warnings, but no security deposits (whether or not they bear interest) or fines. Article 121(6) is aimed at removing the right to regulate the details of the procedures in accordance with Article 121(3) and (4) TFEU. The assumption that the Council could reject recommendations from the Commission concerning surveillance only with a qualified majority, but also that such a shift in the institutional structure would be up for negotiation by the Member States, is untenable. This arrangement has created a hybrid of justice and injustice by establishing a regulatory machinery which is not provided for in the Union's legal framework and is to be superimposed on the Member States' institutions and political procedures. See also Fischer-Lescano (2012) and Oberndorfer (2012).

were unattainable under the old regime.[49] The present case, however, is much more dramatic. While the OMC did not accomplish the noble objectives that its proponents had envisaged, the resort to the 'Union method' amounts to a deep transformation of the European constitutional constellation. The stakes are not only higher for this reason, but also because the organisers of the new modes of economic governance fail to provide any theoretical framework within which the means that would be employed to bring the deeply affected member states 'back on track' become visible and comprehensible.[50] It is far from clear how the new regime might accomplish what its organisers envisage and promise. Furthermore, the asymmetry between fully-harmonised monetary policy and nation state competence in economic and fiscal policy diagnosed above remains unaffected. Above all, the stark socio-economic disparities, which have deepened since the Eastern enlargement, remain in place, as do the conflicts resulting from these disparities. As just underlined above, Europe's crisis management operates without conceptual guidance. And this is anything but fortuitous, as this crisis management is intergovernmental and must hence follow the logic of finding compromises between actors with different interests, institutional preferences and political perspectives.[51]

[49] See, famously, Trubek and Trubek (2005), and the critique in Joerges (2008).
[50] By contrast, the proponents of the OMC relied on the well premises of deliberative polyarchy and/or democratic experimentalism: 'In deliberative polyarchy, problem-solving depends not on harmony and spontaneous co-ordination, but on the permanent disequilibrium of incentives and interests imperfectly aligned, and on the disciplined, collaborative exploration of the resulting differences' (Cohen and Sabel 2002: 168). This is a formula which is very close to many methodological pronouncements within the conflicts-law approach and its plea for a proceduralisation (Joerges 2011a). While the proponents of the latter approach diagnose, sadly, that conflicts-law constitutionalism has become a critic which can no longer be presented as a re-constructive approach (see Joerges and Weimer 2013). The most prominent proponents of OMC and democratic experimentalism see, apparently, no reason for such modesty and re-design (see Sabel and Zeitlin 2012).
[51] For a deeper analysis, see Majone (2012: 19 *et seq.*); Scharpf (2011, 2012). What both authors implicitly confirm is the validity of Polanyi's insights in the social embeddedness of the economy; see Block (2003) and Ebner (2007, 2011).

Constitutional guardianship I: Mutual non-recognition of the budgetary power of national parliaments?[52]

The German Federal Constitutional Court is by no means the only forum in which Europe's constitution has been tested (see Piqani 2012). Yet, nowhere else does this occur with such regularity, and although the court has, indeed, gained the reputation of a dog 'that barks but does not bite' (Weiler 2009: 505), the anxieties of the many publics in both the EU and elsewhere awaiting its decisions on the management of the financial crisis are easy to explain: this court supervises the economically most powerful member state whose government underlines again and again how seriously it takes every judicial pronouncement. The GCC is, of course, well aware of all this. The mere fact that it is exposed to political scrutiny from many quarters and that its pronouncements are assessed politically means that it is *de facto* performing a political role. But the source of the court's authority is its legal mandate and the quality of its exercise. It is not just the outcome of a litigation that matters. In this respect Joseph Weiler hit the nail on the head with his respectful ridicule. Indeed, how realistically was it to be expected that the Court would help Mr Brunner and his *DM-Partei* overturn the Treaty of Maastricht in 1993? (see the section on Juridification of Monetary Union above) Would Karlsruhe have been in a position to put a sad end to the Treaty of Lisbon, which had been negotiated with so much effort by so many actors over so many years?[53] And yet, these judgments did matter. In particular, the significance of the Treaty of Maastricht decision, which had, for the first time, raised the previously rather staid discussion about Europe to the level of a true constitutional debate, and which had, albeit only indirectly, imposed Germany's economic philosophy upon the rest of Europe (see the remarks in the section on Juridification of Monetary Union above), can hardly be overstated.

It is, hence, unsurprising that the judgment of 7 September 2011 on the rescue package for Greece,[54] and the decision of 12 September

[52] The following passages on the crisis jurisprudence of the GCC and the CJEU draw on Everson and Joerges (2014).

[53] GCC, Cases 2 BvR 2134/92 and 2 BvR 2159/92, BVerfGE 89, 155, cited in note 21 above.

[54] GCC, Case 2 BvR 987/10 - 2 BvR 1485/10 - 2 BvR 1099/10, 7 September 2011, *BVerfgE* 129, 124, retrieved from:

2012 on the ESM Treaty and the Fiscal Compact[55] were awaited with anxiety in the many European publics and elsewhere, not because anybody had doubts about their outcome, but because it matters how the highest judicial authority of the economically most powerful member state whose government underlines time and again its respect for the GCC would perform the balancing between law and politics, and thereby define its own constitutional guardianship.

The rescue package for Greece

The plaintiffs in this litigation were the usual suspects: a group of professorial economists and Dr. Gauweiler, a member of the *Bundestag*, as representing the Bavarian branch of the Christian Democratic party (CSU). They challenged both German and European legal instruments as well as further measures which are related to attempts to solve the current financial and sovereign debt crisis in the area of the European monetary union.[56]

My reading of the judgment on the Greek rescue package focuses on three concerns. The first is the tension between the financial crisis management and the German constitution. In this regard, the message of the Court is strong in principle, but not so constraining in practice: budgetary powers are a core responsibility of the parliament and a central element of democratic self-rule.[57] This is why the *Bundestag* must remain 'the place in which autonomous decisions on revenue and expenditure are made, even with regard to international and European commitments'.[58] But this is where the law's prerogatives end: parliament enjoys wide latitude in the exercise of

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http://www.bverfg.de/entscheidungen/rs20110907_2bvr098710en.html (last accessed 26 January 2014).

[55] GCC, Case 2 BvR 1390/12, 12 September 2012; an incomplete English translation is available at: http://www.bundesverfassungsgericht.de/entscheidungen/rs20120912_2bvr139012en.html (last accessed 24 January 2014).

[56] Namely, the *Währungsunion-Finanzstabilisierungsgesetz*, (Monetary Union Financial Stabilisation Act), which grants the authorisation to provide aid to Greece, and the *Gesetz zur Übernahme von Gewährleistungen im Rahmen eines europäischen Stabilisierungsmechanismus*, (Act Concerning the Giving of Guarantees in the Framework of a European Stabilisation Mechanism).

[57] GCC, Case 2 BvR 987/10 - 2 BvR 1485/10 - 2 BvR 1099/10, *BVerfGE* 129, 124, paras. 121-123, note 54 above.

[58] *Ibid*., para. 124.

its responsibilities – and this is a political prerogative which the Court will respect.[59] A second concern is compliance with the order of competences. The court recalls its famous dictum from the Maastricht Judgment: legal instruments which disregard the order of competences (*ausbrechende Rechtsakte*) do not apply in Germany.[60] But this *monitum* is actually soft, because it needs to be read in the light of the *Mangold/Honeywell* decision.[61] The court refrained, however, from considering the request for a preliminary ruling under Article 267 TFEU with a view to having the CJEU examine the compatibility of the rescue measure/s with Article 125 TFEU. Instead, it contented itself with assuring that Monetary Union was designed to be a 'stability community' and hence is one.[62] And we, the citizens? We cannot, in a constitutional democracy, be obliged to comply with European commands which exceed the competences conferred to the Union. Hence, we need to accept that our government takes its commitments to our financial interests seriously.[63] 'A crafty and blandishing wink of the eye,' comments Matthias Ruffert (2011b: 844). In fact, the Court is examining only whether Germany has met its 'integration responsibility' (*Integrationsverantwortung*), and then leaves the question of 'under what conditions constitutional complaints against non-treaty changes of primary Union law can be based upon Article 38 Paragraph 1 Sentence 1 German Basic Law' unanswered.[64] The intergovernmental decisions were not 'sovereign acts of German public authorities', 'notwithstanding other possibilities for legal review', which is why they could not be challenged.[65]

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[59] *Ibid.*, paras. 130–132.
[60] *Ibid.*, para. 116 [with reference to the decisions on the Maastricht judgment (note 21 above)] and GCC, Order of 6 July 2010 – 2 BvR 2661/06, *BVerfGE* 126, 282 – Mangold/Honeywell, English version available at; in the Maastricht decision, see, also, paras. 129 and 137 on commitment to the stability concept.
[61] GCC, Order of 6 July 2010, previous note. – 2 BvR 2661/06, *BVerfGE* 126, 282 – Mangold/Honeywell.
[62] GCC, Greece rescue package, note 54 above, para. 129; and the court adds: 'In this connection, particular mention should be made of the prohibition of direct purchase of debt instruments of public institutions by the European Central Bank, the prohibition of accepting liability (bailout clause) and the stability criteria for sound budget management (Articles 123 to 126, Article 136 TFEU).' This remark attracted considerable attention but has not been taken too seriously by the ECB.
[63] GCC, Greece rescue package, note 54 above, para. 98.
[64] *Ibid.*, note 54 above, para. 109.
[65] *Ibid.*, note 54 above, para. 116.

Did the GCC exercise wise judicial self-restraint? This is hardly a proper reading of this rescue package judgment – certainly not if it is read in conjunction with the follow-up ESM decision of 12 September 2012.

The ESM Treaty and the Fiscal Compact

This litigation was more spectacular by far. Not only the usual plaintiffs but also the parliamentary group of *Die Linke* and no less than 37,000 citizens, among them very prominent figures, had filed constitutional complaints with which they requested primarily a temporary injunction, which would inhibit the entering into force of the statutes passed by the *Bundestag* and the *Bundesrat* on 29 June 2012 as measures to deal with the sovereign debt until the decision of the GCC in the principal proceedings.

The outcome was as usual. The government, Brussels, the market were relieved. The resonance in academic quarters was unusually positive. On closer inspection, however, the judgment turns out to be highly problematical. Its ambivalence stems, unfortunately, from the Court's renewed defence of the budgetary power of the German *Bundestag* as a democratic essential. As in the previous judgment, one wonders about the *de facto* importance of this principle. Again, the Court underlined that the *Bundestag* enjoyed wide latitude which the judiciary had to respect.[66] Through this move, the rights of the *Bundestag* were re-defined in a proceduralising mode: the Parliament must be adequately informed, enabled to deliberate, and prevented from delegating its evaluation. It is far from clear, however, to what degree these *caveats* will enable the German Parliament to exercise effective supervision of its government and its transnational activities.[67] Even more important and questionable is the Court's complacency with the rest of the Union. In the pertinent passages, the Court once again strengthened the link between the *Bundestag*'s budgetary responsibility and a distinctly German philosophy of stability (i.e., price stability and the independence of the European Central Bank, ECB, above all).[68] As a consequence, the nature of the

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[66] ESM decision of 12 September 2012, note 55 above, para. 180.

[67] See C. Geyer 'Anatomie einer Hintergehung [Anatomy of a deceit]', *Frankfurter Allgemeine Zeitung*, 21 June 2012, p. 29.

[68] Para 220 in the German version: 'Die haushaltspolitische Gesamtverantwortung des Deutschen Bundestags wird in Ansehung der Übertragung der Währungshoheit

EMU as a stability community (*Stabilitätsgemeinschaft*) is even seen as being protected by the 'eternity clause' of Article 79(3) of the German Basic Law as an unamendable core of Germany's constitutional identity. Thus, the stability principles become the core of a refurbished European economic constitution.[69] All this, the Court hopes, will protect the democratic rights of German citizens. Non-German citizens of the Union, however, should not be amused at all. Why is budgetary autonomy not understood as a *common* European constitutional legacy, respect for which is demanded by Article 4(2) TEU? The one-sidedness of this argument is all the more disappointing as the Court, in an earlier paragraph of its judgment, had opened another and more constructive perspective: the Court explained that 'Article 79(3) seeks to protect those structures and procedures which keep the democratic process open'.[70] The Court did not indicate that it would be prepared to address the tensions between democratic commitments and the integration process, which would include the concerns of all the member states. Instead, the

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auf das Europäische System der Zentralbanken namentlich durch die Unterwerfung der Europäischen Zentralbank under die strengen Kriterien des Vertrages über die Arbeitsweise der Europäischen Union und der Satzung des Europäischen Systems der Zentralbanken hinsichtlich der Unabhängigkeit der Zentralbank und die Priorität der Geldwertstabilität gesichert.' And 'Ein wesentliches Element zur unionsrechtlichen Absicherung der verfassungsrechtlichen Anforderungen aus Art. 20 Abs. 1 und Abs. 2 in Verbindung mit Art. 79 Abs. 3 GG ist insoweit das Verbtot monetärer Haushaltsfinanzierung durch die Europäische Zentralbank.' Para 204 in the translation: In view of the transfer of monetary sovereignty to the European System of Central Banks, the German Bundestag's overall budgetary responsibility is safeguarded particularly by the fact that the European Central Bank subjects itself to the strict criteria of the Treaty on the Functioning of the European Union and of the Statute of the European System of Central Banks with regard to the independence of the Central Bank and to the priority of monetary stability (see *BVerfGE* 89, 155, note 21 above, at pp.204–205, 207 *et seq. BVerfGE* 129, 124, note 54 above, at pp. 181–182). In this context, an essential element of safeguarding the constitutional requirements resulting from Article 20(1) and (2) in conjunction with Article 79(3) of the Basic Law in European Union Law is the prohibition of monetary financing by the European Central Bank (see *BVerf*GE 89, 155, note 21 above, at pp. 204–205; *BVerfGE* 129, 124, note 54, at pp.181–182). Para. 274 is not yet translated. The German original reads: '*Da der Bundestag durch seine Zustimmung zu Stabilitätshilfen den verfassungsrechtlich gebotenen Einfluss ausüben und Höhe, Konditionalität und Dauer der Stabilitätshilfen zugunsten hilfesuchender Mitgliedstaaten mitbestimmen kann, legt er selbst die wichtigste Grundlage für später möglicherweise erfolgende Kapitalabrufe nach Art. 9 Abs. 2 ESMV*.'

[69] See ESM decision, note 55, paras. 219–220, 232–233, 239–279, and 300–319.

[70] ESM decision, note 55, para. 206 in the English extract, para. 222 in the German original.

Court's reasoning leads to a strengthening of the links between economic stability and social austerity. This form of judicial self-restraint seems even more questionable in the light of – or, rather, in the shadow of – the Maastricht Judgment discussed above in the section on juridification of Monetary Union. Once again, the GCC imposes German views on the rest of Europe, albeit in a significantly-modified move. While the Maastricht Judgment assumed that Europe's economic constitution could be an essentially legal project, the new judgment is moving from law to governmental and executive managerialism, with requirements defined mainly by Germany and its Northern allies. To put it slightly differently, we find it deplorable that the GCC acted as (only) the guardian of the German constitution. The qualification of financial assistance as a matter *not* of European monetary but of national economic policy,[71] as well as the somewhat euphemistic statements on the respect of the stability commitments,[72] are anything but robust indicators of truly European commitments. They are embedded in the conditionality of existing crisis management. The GCC talks about democratic essentials, Jürgen Habermas has observed, but has Germany in mind (Habermas 2013: 132–137). The one-sidedness of its decision seems, indeed, obvious – and difficult to overcome. The German Court is not entitled to act as the Guardian of Europe. What we would expect, however, is a readiness to define Germany as a Member of a Union in which the concerns of all the member states and their democratic rights deserve recognition. Only then would the Court document an understanding, or *Integrationsverantwortung*, which might reflect common European commitments.[73]

Constitutional Guardianship II: The methodological failures of the CJEU in the Pringle case

Thomas Pringle, Member of the Irish Parliament, raised a series of objections against the involvement of his government in the ESM Treaty. Of particular interest in the present context is his assertion that the ESM constitutes an autonomous and permanent international institution, designed to evade restrictive provisions in the TFEU in relation to economic and monetary policy, and amounts to an usurpation of competences which were not conferred to the Union.

[71] ESM decision, note 55, para 169.
[72] ESM decision, note 55, paras. 201 *et seq*.
[73] For a similar critique, see Deters (2013).

This argument concerns the factual transformation of the European economic constitution. It is intrinsically-linked to Pringle's concern with the rule of law: the new regime, he argued, has suspended the principle of legal protection. His complaint was rejected in the first instance, but, on appeal, the Irish Supreme Court, in a judgment of 17 July 2012,[74] decided to stay proceeding and submit a reference for a preliminary ruling to the CJEU. The CJEU (Full Court) handed down its judgment on 27 November 2012.[75]

The argument upon which the following analysis focuses, is based upon the court's reading of the bailout prohibition of Article 125 TFEU, and the emergency exception in Article 122 (2) TFEU, through which the unrestrained new mode of economic governance is justified; these are key provisions of the economic constitution established under the Treaty of Maastricht and their re-vision through the judiciary is, hence, about the structuring of a new constitutional constellation. The reasons for this transformation have been addressed throughout the previous sections: it has, by now, become a *communis opinio* that European monetary policy – with its pre-defined objectives and institutional frameworks – cannot operate in tandem with the multitude of national actors that are pursuing economic and fiscal policies under a very loosely-constructed machinery of European supervision. The message of the *Pringle* judgment is in line with what we have observed thus far: the failures of the past justify the efforts of Europe's crisis management which can, therefore, be legalised. The Court's attitude is certainly understandable; its reasoning, however, suffers from serious flaws.

The main flaw is the Court's failure to address the implications of its own explanation of the conceptual background to the 'no-bailout' clause:

> The prohibition laid down in Article 125 TFEU ensures that the Member States remain subject to the logic of the market when they enter into debt, since that ought to prompt them to maintain budgetary discipline. Compliance with such discipline

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[74] Supreme Court of Ireland, *Pringle v The Government of Ireland & Ors*, [2012] IEHC 296, 17 July 2012

[75] Case C-370/12 *Pringle v Government of Ireland, Ireland and the Attorney General*, Judgment of 27 November 2012, nyr.

> contributes, at Union level, to the attainment of a higher objective, namely, maintaining the financial stability of the monetary union.[76]

This is, indeed, a fair re-statement of an ordoliberal legacy which we can still identify within the Maastricht EMU. However, the Court is then silent with regard to the philosophy which underlies our current cure to the failures of the past. This is by no means to suggest that the Court should have advocated an ordoliberal renaissance. Nonetheless, what truly disappoints, in its presentation of the new modes of economic governance, is the lack of any kind of conceptual deliberation about their background and their adequacy. As we have argued in the section on the crisis and Karl Polanyi, the new modes of European economic governance amount to nothing less than a deep transformation of the state of the European Union. To put it slightly differently: Is the CJEU legitimated to depart from the law as it stands and to replace it with a new regime?

The Court finds an easy answer:

> Since Article 122(1) TFEU does not constitute an appropriate legal basis for any financial assistance from the Union to Member States who [sic] are experiencing, or are threatened by, severe financing problems, the establishment of a stability mechanism such as the ESM does not encroach on the powers which that provision confers on the Council.[77]

This is, in itself, a daring assumption. But precisely if one subscribes to the 'bicycle theory' of Europe, and concedes that the constant re-writing of its law is an irrefutable necessity, that one must, all the more, insist both upon an explanation of the new objectives *and* deliberation on the adequacy of the means which they are employing.

Prior to the *Pringle* judgment, Kaarlo Tuori had developed a transformative theory, which sought to anchor the disregard of the economic philosophy underlying the EMU in a 'second order *telos*':[78]

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[76] *Ibid.*, para. 135.
[77] *Ibid.*, para. 116.
[78] See, on the defence of the CJEU, Craig (2013b: 10). Craig characterises the Court's reasoning on Article 15 as 'tenuous' (p. 8) and then uses the two authors cited in the

> [A] teleological interpretation should heed not only the particular *telos* of the no-bailout clause but also the more general objective of the regulative whole Article 125(1) is part of. And this 'second-order' *telos* of the no-bailout clause undoubtedly includes the financial stability of the euro area as a whole. This argument supports the legal impeccability of Member-State assistance, in spite of the no-bailout clause and the inapplicability of the emergency provision in Article 122(2) TFEU. But it also justifies and even presupposes, at least to a certain extent, the 'strict conditionality' of assistance.
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> (Tuori 2012: 34)

Tuori's argument can be read as a search for rationality, an effort to shield the law, its production and its application against its replacement by pure politics. His argument was not available to the Court, and the *Pringle* judgment was obviously not available when Tuori developed it. It is all the more illuminating that the core of his *telos* theory is present in the judgment: in the paragraph already cited, the court invokes 'the logic of the market' as the rationale of the new regime, and underlines that it is precisely this logic which requires strict conditionality.[79]

In an essay which seeks to understand and explain what makes the resorting to *topoi* and theorems from economics so attractive for legal scholarship, jurisprudence and the judiciary in transnational constellations in which the modes of legitimation, as we know them from constitutional democracies, are not available, Michelle Everson has deciphered the 'processes by which law has transformed itself into an economic technology' (Everson 2013: 107). The *Pringle* judgment provides a stunning illustration of her analysis. There is no sinister conspiracy at work in the argumentation of the court and its supporters, but a serious and desperate effort to defend the law's *proprium*. The tragedy of all these moves remains that 'the logic of the market' fails to deliver the kind of objective orientation which the

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text to strengthen the judicial argumentation whereas I feel that they reveal its weaknesses further.

[79] '[T]he activation of financial assistance by means of a stability mechanism such as the ESM is not compatible with Article 125 TFEU unless it is indispensable for the safeguarding of the financial stability of the euro area as a whole and subject to strict conditions', para. 135.

lawyers hope for. The clearest and, at the same time, most disquieting confirmation of that dilemma can be read in AG Kokott's view:

> Given the mutual interdependence of the Member States' individual economic activities which is encouraged and intended under European Union law, substantial damage *could be* caused by the bankruptcy of one Member State to other Member States also. That damage *might possibly be* so extensive that an additional consequence would be to endanger the survival of monetary union, as submitted by a number of parties to the proceedings.
>
> There is no question here of finding that such a danger to the stability of the monetary union exists or *of examining how such a danger should best be combated.* It must only be emphasised that a broad interpretation of Article 125 TFEU would, also in such circumstances, deprive the Member States of the power to avert the bankruptcy of another Member State and of the ability thereby to attempt to avert damage to themselves. In my opinion, such an extensive restriction on the sovereignty of the Member States to adopt measures for their own protection cannot be founded on a broad teleological interpretation of a legal provision the wording of which does not unambiguously state that restriction.[80]

The rescue measures are political decisions; they need no legal justification: *auctoritas, non veritas facit legum*. The replacement of law by discretionary political fiat is Schmittianism pure. It is, therefore, unsurprising that the deeply undemocratic nature of conditionality goes unnoticed or fails to be commented upon.

An interim conclusion

What would have happened to the European Union had its Court of Justice found that Thomas Pringle's concerns about Europe's crisis management were well founded, that the support-mechanisms which the EFSF and the ESM have established interfere with the exclusive European competence for monetary policy, that the amendment of Article 136 TFEU was not possible under the simplified revision

[80] AG Kokott, View of 26 October 2012 in Case C-370/12, paras. 139-140 (my italics).

procedure enshrined in Article 48(6) TEU, that new policies that were being adopted and pursued by the Member States jeopardised the primacy of price stability, that the bail-out provision of Article 125 TFEU prohibited the granting of financial assistance to Member States whose currency is the euro, that the functions assumed by the Commission, the ECB, and the IMF were irreconcilable with the principles on the conferral of powers laid down in Article 13 TFEU, or that the mandate allocated to the CJEU in the ESM Treaty exceeded judicial powers? It is simply impossible to predict the dire consequences. It is equally difficult to find out what the judgment has accomplished, both in terms of its contribution to the taming of the crisis, *and* its effect on Europe's constitutional constellation and the role of law. The situation of the GCC is not much different. The Court could neither clarify the factual uncertainties of the financial crisis, nor was there any normative guidance available that would have helped it to choose between the risks of partisanship for or against the European *praxis*. The German court decided to (re-) delegate the responsibility for what happens and for what is going to happen to the political process. The European court decided to prioritise textual formalism over conceptual reasoning – as though Ernst Steindorff would have never written about the politics of law (Steindorff 1973: 217 *et seq.*, 1974: 621 *et seq.*) and without justifying its departure from the type of teleological interpretation on which it tends to rely so heavily (see Beck 2012). These are but methodological shortcomings. The substantive theoretical default of both courts is their disregard for Europe's commitments to democracy and the rule of law. This unfortunate complacency is inherent in the politics of conditionality to which both courts subscribe. To re-phrase this critique: Do these courts, do the academics supporting them, 'place a thin veneer of legality on the political which allows the executive to do what it wants' (Dyzenhaus 2006: 103), do they consciously, or at least implicitly, re-construct the contemporary conditions in which political guidance and rule has to be provided by the executive rather than representative institutions, and in which law can no longer be understood as a body of rules, but must, instead, content itself with providing standards which are sufficiently vague to empower policy to act according to their understanding of what needs to be done?[81]

[81] Eric Posner and Adrian Vermeule (2011a: 3) have underlined that they seek to reconstruct Schmitt's work in 'generizable social-scientific terms'.

At this point, the critique has to reflect upon its own premises, in particular the assumption that the integrity of law could have been defended. And it is precisely this assumption which may be overly simplistic and naïve. But how can we find out? It may be best to step back and look at the dilemmas that we are facing from some distance.

A fictitious dispute between Carl Schmitt and Jürgen Habermas

The crisis is not an expression of a faulty way of dealing with prevailing law, but an expression of the imperfection of Europe's legal design – including its configuration of the law-politics relationship. A rare, albeit superficial, consensus has emerged regarding this critical evaluation. Beyond this consensus, the crisis has generated challenges for all disciplines engaged in European studies. This is why it would be presumptuous to venture legal and constitutional-policy hypotheses here which would be based upon some definite assessment as to the causes of the crisis as well as forecasts regarding its further course that would be intended to provide a blueprint for Europe's future constitutional architecture. The following deliberations will, as it were, view these ongoing contestations from a distance: in the form of a fictitious debate between Carl Schmitt and Jürgen Habermas. Considering these names, it may be appropriate to begin by stating positions. My theoretical home is the discourse theory of law, both in German and in European law (see Joerges 2000, 2011b). It is all the more disturbing that Carl Schmitt seems to have gained alarming topicality not only with his concept of the state of exception and with his theorem of a commissarial dictatorship (closely linked to that concept), but also with his theory of the *Großraum* and the diagnosis about the 'hour of the executive'.

Carl Schmitt's shadow over Europe

In the context at issue here, it seems best to begin with the theory of the *Großraum*. Carl Schmitt selected a memorable occasion to present it: from 29 March to 1 April 1939, hence still half a year before the war against Poland, but after the *Anschluss* of Austria and the invasion of Bohemia and Moravia (the *Sudetenland*), at the *Reichsgruppe Hochschullehrer des Nationalsozialistischen Rechtswahrer-Bundes* [Reich section of professors in the National Socialist Association of Lawyers] convened in Kiel. At the same time, the Institute for Politics und International Law was celebrating its 25th anniversary. This was the setting in which Carl Schmitt gave his lecture entitled '*Völkerrechtliche Großraumordnung mit Interventionsverbot für raumfremde Mächte. Ein Beitrag zum Reichsbegriff im Völkerrecht*' [The *Großraum* Order of International Law with a Ban on Intervention for Spatially Foreign Powers: A Contribution to the Concept of *Reich* in International Law].[82]

The core argument of his keynote was (for further details, see Joerges 2003) that the *jus publicum europaeum*, which had made the sovereign state its central concept, was no longer in line with the *de facto* spatial order of Europe. Following the model of the Monroe Doctrine, a specific 'space' (the *Raum*) had to become the conceptual basis for international law, with the *Reich* constituting the order of that space. To quote directly: 'The new ordering concept for a new international law is our concept of the *Reich*, with its *Volk*-based, *völkisch Großraum* order.' But what does this mean for the internal order of the *Großraum*? Schmitt refers to the elasticity of the concept of international law, which could also cover the inter-*völkische* relations within a *Großraum* as well. What the *Großraum* requires and constitutes is an 'order that excludes the possibility of intervention on the part of spatially foreign powers and whose guarantor and guardian is a nation that shows itself to be up to this task' (see Schmitt in Nunan 2011: 110).[83]

This claim to leadership was, in Schmitt's words, 'situational',[84] and the concept of the *Großraum* altogether, as he underlined in discussions with his Nazi contemporaries, rivals and critics, was a 'concrete, historical and politically contemporary concept [*konkreter geschichtlich-politischer Gegenwartsbegriff*]' (see Schmitt in Nunan 2011: 107). But in so doing, he emphasised elements which he claimed to be

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[82] The lecture was published as early as April 1939 in the Institute's series; its 4th edition of 1941 refers to translations into 5 languages. The quotations in the following are either our own translations of the extremely carefully annotated reprint in Günter Maschke (1995: 269–320), or, as the title reproduced in this text, from *Carl Schmitt: Writings on War*, edited and translated by Timothy Nunan (Nunan 2011).

[83] Contemporary reactions attested to how the theory of the *Großraum* with its 'German Monroe doctrine' suited Nazi policy; for this reason, the theory is considered Schmitt's way of indicating his return as a leading legal thinker; see Gruchmann (1992: 11 *et seq.*) and. Scheuerman (1965: 161 *et seq.*, 169 *et seq*).

[84] On the theoretical understanding, but also the determination with which Schmitt championed this claim of leadership, see Hofmann (1992:215 *et seq.*) and also Eberl (2008). More complacently, in contrast, see Horst Dreier's appreciation (Dreier 2002).

valid long-term. The obviousness of the *Großraum* concept, he argued, resulted from transformations dominated by technical, industrial, and economic developments. Thus, Schmitt outlined, albeit somewhat apocryphally, an erosion of the territorial state as the harbinger of the necessity to adapt international law to the factual re-structuring of international relations and the replacement of classical international law by norm systems which, today, would affirmatively be called *governance structures*, or, distanced and critically, *managerialism* (Koskenniemi 2007: 16, 2009: 411). He underlined two phenomena in particular, namely, the economic inter-dependencies beyond state frontiers (*Großraumwirtschaft*), and the specific dynamics of technology-driven developments ('technicity' [*Technizität*]).[85] He had already published on both topics prior to 1933 (infamous and important, Schmitt 1933).

Schmitt remained silent on the internal 'order' of the *Großraum* of the war years. In the 1941 edition of the *Großraum*, he remained sibylline,[86] and published his famous '*Nomos der Erde im Völkerrecht des Jus Publicum Europaeum*', which he had written prior to 1945, only in 1950 (Schmitt 2008[1950]). But the topic continued to haunt him.[87] When working with Schmitt's idea in the context of the financial crisis and how it is being handled, it is not just his diagnoses of the loss of sovereignty of nation states and the de-legalisation of their relationships that we must take seriously. This also applies to Schmitt's observations – broadly supported by comparative legal research – on the increase in the powers of the executive (Schmitt 938).[88] But here, we are, above all, concerned with his theorems of the state of emergency (Kennedy 2011; McCormick 1997: 122–156) and

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[85] See Schmitt in Nunan (2011: 111); on the notion of technicity, see (McCormick 1997: 42–46, 92–105).

[86] The preliminary remarks to the 4th edition (Berlin 1941) include the famous motto: 'We are like mariners on a continuing journey, and no book can be more than a log book'.

[87] See Schmitt (1978). In this tribute to the French economic theorist François Perroux, who examined apparently related economic dimensions of space, we read: 'Today, the issue is about the political system for society adequate in relation to scientific-technical-industrial developments. Today, the adage *cujus industria, ejus regio* or *cujus regio, ejus industria* applies', and on the following page he went on: 'The industrialised society is bound to rationalisation, including the transformation of law into legality (Schmitt 1978: 328–329).

[88] On this, of course under the impression of the American understanding of the executive, see Lindseth (2010: *et seq.*).

the (commissarial) dictatorship (Schmitt 1989[1921].[89] Ernst-Wolfgang Böckenförde (2010) was the first to take up the term 'state of exception'. He found successors. 'The European Stability Mechanism', writes Ulrich Hufeld (2011: 122), has 'the format of a constitution-breaching measure along the lines of Carl Schmitt's conceptualisation of contrasts', and adds a quotation from Schmitt's 1928 *Constitutional Theory*:

> Such breakout entities are, by nature, measures, not norms. [...] Their necessity arises from the particular circumstances of an individual case, an unexpected abnormal situation. If, in the interest of the whole, such renegade entities are formed, the superiority of the existential over mere normativity is apparent. Whoever authorised such acts and is capable of acting, is sovereign.
>
> (Schmitt 2010[1928]: 107, own translation)

In a tone of urgency, Frank Schorkopf (2011: 341 *et seq*; 2012) calls the calamity that we are dealing with a 'crisis without an alternative', a constellation in which the actors, including the governments and the executive branches, 'merely have power within the existing conditions, but not over them' (Schorkopf 2012: 225). Anna-Bettina Kaiser (2011) arrives at her position following a precise re-construction of the debates around Article 48(2) of the Weimar Constitution. The handling of this provision and the extensive interpretation of Article 122(2) TFEU really can be placed at the same level (Kaiser 2011: 140). Furthermore, the rules laid down in the Six-Pack, the Two-Pack, and the TSCG must not be sugar-coated. But is the academic community doing justice to its responsibility by merely accepting that the provisions of the EMU are dysfunctional, and abstracting from the dilemma of the political in the EU?

We cannot escape from Carl Schmitt's shadow that easily. What is most plausible to take exception to is the concept of 'commissarial dictatorship'. After all, in the current management of the crisis, the actors are not alone. They must not only come to an arrangement at supranational level, but also between the levels of the multilevel

[89]As examples from the copious literature *cf.*, the explanations in Hofmann (1992: *et seq.* on state of emergency, and 70 *et seq.* on dictatorship).

governance system, as well as internationally – the dictator has been replaced by technicity. But how comforting is this? The fact remains that the new form of European government collides with democratically-legitimised institutions and processes. Thus, it is anything but comforting that the new European practice coincides with ideas of prominent American constitutionalists who draw upon Carl Schmitt in order to turn away from James Madison, and argue the case for a plebiscitary democracy in place of a representative one, and advocate delegating political power to the executive in case of need.[90] And are we, perhaps, exchanging Scylla for Charybdis? Anyone who observes the busy activities of the Commission's Services, their tireless production of more and more new lists of criteria for ever more policy fields in ever more regions will remember Carl Schmitt's words about the 'total', but by no means 'strong' state, which he linked with a polemic against all technocratic efforts that believe that they can decide 'all issues according to technical and economic expert knowledge following supposedly purely substantive, purely technical and purely economic considerations'.[91] Ironically, Schmitt's late essay (Schmitt 1978: 335) quoted above provides a situational-theoretical interpretation of all this. Reading Hans Peter Ipsen's 1,000-page tome on European law, Schmitt confessed, he was 'stricken with deep sorrow', for the following reasons: the approach of European law, which *legalises* a technocratic-functional administration of European associations, has no concept of a *legitimate political* project.[92] Therefore, one cannot speak of the rule of law ('*Rechtsstaatlichkeit*'), much less of democracy. Now, one must take into account what '*Rechtsstaatlichkeit*'[93] and

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[90] Posner and Vermeule (2011: 8): 'When emergencies occur, legislatures acting under real constraints of time, expertise, and institutional energy typically face the choice between doing nothing at all or delegating new powers to the executive to manage the crisis'; the book is riddled with such pronouncements; on this, Urbinati (2014: ch. 4); for a critical discussion of the empirical dimensions and claims of *The Executive Unbound*, see Huq (2012).

[91] '*Die Wendung zum totalen Staat* [The way to the total state]', quoted according to the reprint in Schmitt (1988. On this, see also Schmitt (1931: 78 *et seq.*) and Scheuerman (1965: 85 *et seq.*).

[92] My italics; on the recourse to the duality of legality and legitimacy in the present context, see Mehring (2006: paras. 20–26).

[93] On the theory of the *Rechtsstaat*, see Maus (1986: 40 *et seq.*) Schmitt's differentiation of the categories of 'formal' and 'political' concepts of law and legislation (Schmitt 2010[1928]: 143 *et seq.*), between the generality of laws and the concrete political act of

'democracy' meant to Schmitt. In *Constitutional Theory*, he writes that democracy 'is a state form that is consistent with the principle of identity (i.e., of the concretely existing people identified with itself as a political unit)' – and consequently, it cannot apply to an ethnically diverse Europe (Schmitt 2010[1928]: 223; see also Preuss 1995: 177 *et seq*., and 180 *et seq*). After all this, Jürgen Habermas' reply is all the more important.[94]

The crisis as opportunity according to Jürgen Habermas

In view of the crisis, Jürgen Habermas has brought all his prestige and powerful eloquence to bear. His countless public interventions have been published across Europe in many languages. 'Democracy is at stake', he has warned time and time again,[95] Europe risks establishing a post-democratic regime of 'executive federalism' (Habermas 2011b). These drastic messages, however, are always accompanied by signals of hope and political appeals: he wants us to understand the crisis as a chance, an opportunity to strengthen the European project. The 'strength' which he is advocating is not merely Europe's managerial potential; to him, 'more Europe' also means a deepening of Europe's democratic credentials.

In contrast to so many commentators on the debate on the financial crisis and the future of Europe, Habermas. in his passionate pronouncements, is pursuing a demanding and coherent agenda, which is based upon his long-term explorations of the many facets of the European project. His work upon this theoretical basis started with the essay *Citizenship and National Identity* (Habermas 1999a) just

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will, leads him to executive and governmental law-making in Schmitt (1938); see Hofmann (1992: 83 *et seq*.).

[94] This exploration has not contributed to the '*les-extrêmes-se-touchent*' debate around the relationship of Habermas to Schmitt (for an attempt to update it, see Vollrath 1996; see also Mehring 2006: para. 26 *et seq*.).

[95] Succinctly, for example, in the features' section of the *Frankfurter Allgemeine Zeitung* of 4 November 2011, entitled 'Rettet die Würde der Demokratie [Rescue the dignity of democracy]. A number of these statements are reprinted in Habermas (2011a: 97-129; a more recent example is his essay in *Le Monde*, 27 October 2011. English version 'Jürgen Habermas: democracy is at stake' is available at: <http://www.presseurop.eu/en/content/article/1106741-juergen-habermas-democracy-stake> (last accessed 27 January 2014). Habermas' entire work is comprehensively documented and updated weekly in the Habermas Forum, available at: <http://www.habermasforum.dk> (last accessed 27 January 2014).

prior to the publication of his *magnum opus* on legal theory (Habermas 1999b). Since then, Habermas has occupied himself ceaselessly with the European project, both as a citizen and a theoretician: as a theoretician, he conceives of the process of Europeanisation as a challenge to his theory of the democratically-constituted nation state; from the perspective of the citizen, a response to the catastrophes of the 20th century, for which Germany bears so much responsibility, is manifested in this project, as well as an opportunity to defend democratic welfare-state accomplishments in the processes of globalisation and European integration. As a theoretician on the constitutionalisation of Europe, Habermas seeks to accomplish a type of analysis which is able to grasp the facticity of the processes of Europeanisation, and also to achieve a normative concept that provides both criteria and identifies the institutional conditions for the question of whether the configurations emerging in the process of Europeanisation 'deserve recognition'.[96]

Following his more recent interventions as a citizen, Habermas has approached this aspiration again (Habermas 2012a).[97] He identifies the institutional causes for the crisis and states his polemics against the crisis management in Europe in terminology that critically transforms Schmitt's affirmative observations on the steadily growing power of the executive into critical objections to the present course of the process of Europeanisation: 'Post-democratic executive federalism' (see, for example, Habermas 2012b: 487) is the term he uses to denote – and to criticise – Europe's *praxis*. The European Union must not continue on the path it has taken due to the pressure of the crisis but cease to co-ordinate the relevant policies in the gubernative /governative-bureaucratic style which has been customary until now, but must take the path of adequate democratic legalisation.

The theoretical core of his essay is to be found in the reasons which he gives for this postulate, in which Habermas continues deliberations by Armin von Bogdandy, Claudio Franzius, and Ulrich

[96] For a re-construction of Habermas' works, which, however, seeks to (re-) interpret the author for his own ends, see Joerges (2000).

[97] One can no longer be sure about the seriousness of this distinction. In the preface to his most recent book (Habermas 2013: 8, note 2), Habermas expresses some discontent with the fact that his public interventions did not make it into the general academic discourses.

K. Preuss, in particular (see von Bogdandy 2010: 13, 44; Franzius 2010: 49 *et seq.*; Franzius and Preuss 2012: 33 *et seq.*). He places a dual role for Europe's citizens alongside the recognition that these rights are equally rooted in the democratic constitutional state: they remain citizens of their states but become citizens of the Union as well. With this construct, Europe's ability to be a democracy becomes plausible in theory. In addition, the construct is to provide criteria for democratic constitutionalisation of European governance, and, last, but not least, to satisfy its functional requirements. But it is precisely at this point that it remains under-determined in practical terms as well.[98] In the light of the extreme uncertainty of the current situation, in which precisely the most competent experts are admitting that they are at a loss, in which Europe's publics are falling back into age-old animosities, and populist demands for exclusion are being voiced, in which governments in precisely those countries most deeply affected by the crisis lose their legitimacy, it is neither foreseeable what a European government could accomplish, nor can it be inferred how a political leadership with secure democratic legitimation could be established. 'Until these questions and problems are addressed', American political scientist John McCormick noted in much more tranquil times, 'Schmitt's work and career haunts the study of European integration like a spectre' (McCormick 2003: 141).

Epilogue: From 'one size fits all' to 'unity in diversity'!

The debate on the transformation of Europe's constitutional constellation, its new *Verfassungswirklichkeit*[99] has only started and is bound to move on. Pertinent characterisations oscillate between Executive Federalism (Habermas 2011b), a Distributive Regulatory State or New Sovereignty with Largely Unfettered Power of Rule

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[98] Scicluna (2013: 101): 'So far it has proved difficult, if not impossible, to have a full and inclusive debate on the lofty ideal of "political union" while the Eurozone crisis is still in its emergency phase. As long as this state of emergency persists, European politicians and officials will continue to be heavily focused on the pragmatic, day-to-day steps that (in their opinions) are necessary to save it'; see also Scicluna (2012: 500).

[99] The contrast between *Verfassungsrecht* (constitutional law) and *Verfassungsswirklichkeit* (constitutional reality) is another problematical German legacy – again with root in Carl Schmitt's *Verfassungslehre* (Schmitt (2010[1928]).

(Chalmers 2012, 2013), a *Konsolidierungsstaat* (Consolidating State, see Streeck 2013: ch. 3), Authoritarian Managerialism (Joerges and Weimer 2013), an Unconstrained Expertocracy (Scharpf 2013), an Unbound Executive (Curtin 2014), *Krisenkapitalismus* (Crisis Constitutionalism, see Bieling 2013). None of these characterisations is in line with the ever so positive and optimistic presentation of the integration project which we have been reading over decades. Among the features which are underlined is the lack of any theoretical/conceptual paradigm, a radical disregard of Friedrich A. von Hayek's warnings against the 'pretence of knowledge',[100] a disregard of the rule of law and a thorough de-legalisation of governance.

What does all this mean for European citizenship? What was once a cherished accomplishment is by now characterised by inequalities between the North and the South, the social exclusions of a large part of the European population and political disempowerment. The present calamities are not without precursors (see Everson 2012), but the ambivalences of the vision of transnational, albeit nationally dis-embedded, citizenship have, by now, become ever more apparent and disquieting (see Giubboni 2013). I am not trying to go, in this already overly lengthy chapter, into any detailed analysis. The *problématique*, as it is presented by Everson and Giubboni[101], corresponds precisely to our views on the economic constitution. Just as it is misconceived to subject a socio-economically and politically ever more diverse Union to the discipline of one currency, the construction of a uniform 'European social model' is a misconceived project.

All these depressing diagnoses notwithstanding, this epilogue should not conclude without an outline of what has been announced in the introductory remark: 'But where danger threatens, that which saves from it also grows.'[102] The present state of the Union is unsustainable. The efforts to force member states and their citizens into the

[100] F.A. von Hayek, 'Nobel Memorial Lecture', December 11, 1974, retrieved from: <http://pavroz.ru/files/hayekpretence.pdf> (last accessed 27 January 2014).
[101] It is worth noting that very similar disappointment are becoming a concern also in the accession states; see for an instructive analysis Bugaric (2013).
[102] Friedrich Hölderlin, Patmos. Dem Landgrafen von Homburg überreichte Handschrift, 1802 (quoted from Hölderlin 1994[1954]: 243).

straitjacket of new economic governance is bound to fail. In this sense at least, the Euro-crisis, somewhat paradoxically and inadvertently, underlines the urgent need for pluralistic variety, the toleration of disagreement and contestation, rather than an ever more and ever more centralised executive Europe. The failures of Europe generate ever more unrest and protest among dis-empowered citizens who are exposed to austerity measures which are experienced as hopeless, and, to a considerable degree, useless suffering; they increasingly seem to provoke the political public, national parliaments and even the EP. It will become ever more apparent that it is simply impossible for the great majority of signatories of the Fiscal Compact to comply with the requirements imposed upon them. It will become ever more apparent that it is simply impossible for the great majority of signatories to comply with the requirements imposed upon them; and '*die neue Umständlichkeit*' (cumbersomeness) of all these procedures[103] will affect their impact.

There is, hence, room for manoeuvre. And yet, to date, any substantial transformation of the regime which has been established is out of sight, and it is hard to believe that the conceptual disorientation and frustration with the implementation of the new European economic governance will somehow generate re-orientation. Is it nevertheless conceivable that, in not too distant future, the new policy co-ordination within the annually repeating European Semester, the reporting and multilateral surveillance obligations, the macro-economic imbalance procedures, the responses to country-specific recommendations will lead to new assessments of the weight of socio-economic diversity, insights into the social embeddedness of markets, acknowledgement of the different regulatory, social and economic cultures in the member states, a search for innovative responses to complex conflict constellations – and, sooner or later, even to the developments of standards and criteria which discipline authoritarian managerialism.

It would be absurdly pretentious to promise a 'solution' to these difficulties. But we must not shy away from the construction of projects which seek to respond to the problems which we have identified. The project which I have pursued for more than a decade

[103] Reconstructed sharply by Braams (2013): 13–44.

is ‘conflicts-law constitutionalism’ (Joerges 2011a; 2013).[104] Its analytical and normative core can be briefly summarised as follows: as long as the shape of a pan-European democracy lacks contours, and the conditions for its realisation remain entirely unclear, we will have to explore alternatives which take the difficulties into account which the European project must not and cannot avoid. How should we respond to the circumstance that the socio-economic disparities in the expanded Union are not melting away? Which conclusions should be drawn from the insight that the neoliberal interventions to which the ‘varieties of capitalism’ in the Union have been exposed have disintegrative effects time and time again? If it is not possible to construct a uniform welfare-state model, is it then advisable to dismantle Europe’s welfare-state traditions altogether? If our goal is not to suppress the painful memories of Europeans, not to iron out the differences between their bitter historical experiences, not to waste the wealth of their cultures, must not then tolerance determine the status of European citizens, tolerance which is established in law and based upon the principle of mutual acceptance? These questions are not merely rhetorical. They have a normative point of reference in the optimistic ‘motto’ of the ill-fated Treaty establishing a Constitution for Europe about being ‘United in Diversity’,[105] which need not remain an empty phrase. My proposal for putting it into practice is as follows: Europe must find its constitutional form in a new type of ‘conflicts law’, which is characterised by two guiding principles: firstly, the supranational European conflict of laws is to require Member States of the Union to take their neighbours’ concerns seriously – in this respect, it aims at compensating the structural democratic deficits of nation-statehood. Secondly, this European conflicts law should structure co-operative solutions to problems in specific areas – thereby reacting to the inter-dependencies of modern societies. Suffice it here to underline three points:

We should shift our attention from the *democratic deficit* of the EU to the *structural democracy deficit* of its member states. Nation states continuously and unavoidably violate the principle that those affected by their laws can ‘in the last instance’ understand themselves as their authors. The Member States of the Union can be requested to

[104] For an evaluation see the contributions in Joerges, Kjaer, and Ralli (2011).
[105] Article 1–8.

take the impact of their own policies on other jurisdictions into account; and *vice versa*: they can expect that their concerns be included in the decision-making processes of the others: in the Union, these commandments correspond to the common commitments to democracy which European law is legitimated to implement. European law has the vocation and some potential to compensate these deficits. It can derive its legitimacy from the potential to correct democracy deficits of its member states.[106]

The second vocation and task stems from the erosion of the potential of the nation state to resolve problems autonomously In the Union, this dependence upon the other transforms itself into duties of – co-operation which European law is legitimated to organise. The 'constitutionalisation of co-operation' must then seek to derive its validity from the normative credentials of the very interactions that it organises.

Conflicts-law constitutionalism was meant to be elaborated further and to proceed as a *re-constructive* project, i.e., a re-conceptualisation of European law which would, to a considerable degree, be compatible with European law as it stood, and be able to orient its further development. The re-constructive status was based upon its sociological premises which reflect the European constellation more adequately than the orthodoxy of European law. It seems, indeed, overdue to re-consider the integration project in the light of Europe's ever growing diversity, to take the conflicts which this diversity generates into account, and to re-orient Europe's agenda from harmonisation and unity to the management of complex conflict constellations.

The last point is the most difficult to defend. The reconstructive status of the conflicts-law approach was based on its sociological premises which reflect the conflict-laden European constellation more adequately than the orthodoxy of European law. All what seemed

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[106] It seems worth noting that Habermas (2007: 176) expresses the same ideas in his recent work on the constitutionalisation of international law: 'Nation-states […] encumber each other with the external effects of decisions that impinge on third parties who had no say in the decision-making process. Hence, states cannot escape the need for regulation and coordination in the expanding horizon of a world society that is increasingly self-programming, even at the cultural level'.

needed, and indeed overdue, was to re-consider the integration project in the light of Europe's ever growing diversity, to take the conflicts which this diversity generated into account and to re-orient Europe's agenda from harmonisation and unity to the management of complex conflict constellations. After the financial crisis such hopes and ambitions are obviously less realistic than ever with substantial backing in actually already existing European law. This bold assertion has suffered numerous setbacks, for example, through the de-legalisation and de-formalisation of European governance.[107] At present, under the pressures European crisis management, it continues to dwindle, and conflicts-laws constitutionalism is, for the time being, a merely critical project (see Joerges and Weimer 2014). What can nevertheless be explored are the conflict constellations which the new modes of economic governance and the imposition of austerity politics on a large part of the Union generate – together with the space for counter-movements which the unfortunate state of the Union may generate. That, however, requires another project.

[107] See Joerges (2009) and note 49 above.

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Chapter 8

The fault of (European) law in (political and social) economic crisis

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Introduction

It is a commonplace that the discipline of economics has contributed to the current crisis, above all, because economic methodologies are charged with fatally inflating debt risk, such that collapse was the inevitable result. But what might be said of the role of law within this constellation? Much ink has been consumed detailing legal shortcomings within regulatory regimes for the financial services. However, a full accounting has yet to be made of the broader fault which may also be attributed to the premises of modern and increasingly post-national law, especially as they coalesce with a broader abdication of political responsibility for crisis. This contribution begins this accounting, investigating the processes by which law has transformed itself into an economic technology within post-national regimes in its contemporary quest for material legitimacy. Above all, in its idolatry of the factual, law has itself become a power locus – especially within the European Union – that

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similarly pre-empts the politics within which social and economic stability might be defined and achieved.

Chronicle of a crisis foretold

Hayek bites back

Social science literature on the causes of economic crisis is polarised. However, schism cannot be equated with simplistic left—right distinctions. Neither can it be captured seamlessly within the couplet of crisis-beating Keynesian interventionism versus deficit-busting Hayekian self-limitation. Instead, the core difference between majority and minority positions is furnished by the degree of optimism or pessimism that each maintains with regard to the effectiveness of the steering 'rationalities' developed during the past three decades of liberalised market operation. A dominant school regards crisis as a primarily economic happening that can be corrected within rational narratives, stressing both the continuing centrality of autonomous market operation and the enduring potency of regulatory oversight. Some analyses start small: the causes of crisis may be reducible to localised 'regulatory failures', whereby individual financial supervisors failed to appreciate the scale of risks posed by evolution of the inappropriate financial products (debt-financing mechanisms) that subsequently gave rise to systemic shocks of macro-economic proportions (Black 2010). Others progress immediately to the big, emphasising the macroeconomic character of crisis from the outset, highlighting the instability that was programmed into the global financial system once sovereign competence to create money passed from nation states, or their central banks, to privately organised, debtcreating credit markets (Teubner 2011). Each position, however, believes that correction is possible within a rational idiom: cognitive failure within the regulatory system can be combated by better co-operative learning strategies within internationally co-ordinated networks of financial regulators (Baldwin and Black 2010); meanwhile, future stability can be better secured with the re-establishment of macro-economic policies of 'sound money', or the granting of monopoly powers to central banks to control capital creation (i.e. debt) through direct supervision of private credit markets (Teubner 2011).

An underlying theme is established and pursued: the self-destructive character of autonomous capital market rationalities has surprised us.

Nevertheless, before credit creation systems 'hit the bottom', corrective steering may be re-established as market rationalities are required (autonomously) to re-adjust themselves to new micro- and macro-economic logics of financial supervision and money creation. Such 'rationality optimism' is comforting, but must immediately be contrasted with a far more pessimistic minority position, highlighting a critical moment of political paradox within economic malaise (Crouch 2011; Scharpf 2011; Streeck 2012). A common feature here is the turning back of the clock: the stagflation of the 1970s sounded a death-knell for command interventionism and government-sponsored policies of full employment. From the 1980s onwards, a consensus established itself across the political spectrum. Direct government interventionism was ended and all political positions subsequently acquiesced in the new liberalising trend as monetary policy was entrusted to central bankers, and centralised steering capacities were divested in line with delegated economic efficiency principles. Vitally, however, the social unrest that negation of the postwar guarantee for public welfare might have engendered was simultaneously militated against by a silent process of 'privatised Keynesianism'. General support was won for liberalisation as the risks and, above all, uncertainties, inherent to market operations that were once borne within the social state were transferred to private markets in line with a 'permissive consensus', in which private money (growth and/or debt) replaced state generated welfare (Crouch 2011).

Recent instances of counterfactual financial operation are thus readily explained as 'welfarist' commonplaces: provision of mortgages to the impecunious and subsequent resale of unsecured debt is not simply an egregious measure of the self-destructive logic of capital market operation. Instead, it is a destructive logic tolerated within the boundless optimism of a permissive consensus that has refashioned the state-financed 'social entitlements' of traditional welfare capitalism as privately-constructed 'economic provisions', or contingent economic opportunities (Dahrendorf 2008; Everson and Joerges 2012). Economic opportunity has been 'universalised', or made available as cheap credit to all, within a liberalised financial market which has miraculously internalised all of the externalities and moral hazard inherent to its operations through ever more refined packaging of unsustainable private debt. At core, a socio-political abdication of responsibility for public welfare, permissive consensus is similarly characterised by a depoliticisation paradox, or an inability to address enduring welfare concerns through anything other than market growth. It is this lack of political capacity that is most apparent at a time of crisis. Although extreme positions decry the re-statalisation of privatised welfare within governmental assumption of bank debt, collapse of financial markets was never a social option for western administrations of any political persuasion. Instead, governments are now trapped in a perverse non-logic, which combines (indirect) re-assumption of private debt and radical deficit reduction, with the preaching to publics of a 'counterfactual credo' (Streeck 2012) in the capacity of autonomous market operation to internalise increasingly brutal social externalities through ever more elusive growth.

The core insight is one that we have not returned to grand ideological divides. The macro-economic problems of the 1970s have not been solved, merely reconfigured; but, in Europe at least, governments of the left and right rise and fall but pursue the self-same debt-assumption/deficit-reduction agendas and may even, where necessary, be seamlessly replaced by technocratic regimes, legitimated only by their increasingly discredited 'structural reform for growth' mandates. In economic crisis, paradoxical permissive consensus has led to political paralysis, and to the distilling down of technocratic models of economic governance to their reductio ad absurdum. And nowhere is this political paralysis and technocratic corruption more apparent than in responses to the historically pre-programmed European sovereign debt crisis that was finally precipitated by financial market collapse (*ibid*.).

Proof for the assertion that academic rupture cannot be captured within interventionist versus non-interventionist divides is given as absurdities in the historical construction of monetary union – undue faith in the corrective macroeconomic powers of labour mobility (Snyder 1996), together with de-contextualised European adoption of the technocratic German model of monetary policy (Scharpf 2011[1]) – as well as fatal ironies in current efforts to stabilise the eurozone, draws the ire both of social democratic and conservative positions. To

[1] The commitment of the *Bundesbank* to price stability occurred within a densely corporatist web of cultural and political history, whereby postwar divestiture of monetary policy was politically coordinated with alternative macro-economic steering capacities such as wage restraint.

the degree that the European Central Bank (ECB) must maintain its commitment to price stability, even where it promises to stabilise the Euro,[2] peripheral economies are now consigned to negative growth, denied reflationary interventionism and subject to the deficit-compounding imperatives of bank rescue within the eurozone core (Streeck 2011). National macro-economic steering capacities are politically and constitutionally emasculated by virtue of abdication of monetary competences and by the enhanced budgetary discipline of fiscal union (Scharpf 2011), or contingencies applying to disbursement under the European Stability Mechanism (ESM). Recession and social collapse is the inevitable result. This unending political-economic trap, however, is one that is wholly of Europe's own making, a predictable consequence of an original sin: the pursuit of a political project of monetary union through a combination of technocratic reductionism, and a misplaced integrationist culture of 'total optimism' that still assumes that economic uncertainties can be brought under control within neo-functionalist models of European integration. As financial crisis has inevitably been followed by sovereign debt crisis, Europe has found it has no plan B and, more importantly, no means of creating one (Majone forthcoming).

And it is here – in the chimera of technocratic control of economic uncertainty that Hayekian truths bite hard: inexorably implicated within the redistributive consequences which structural reform entails (Moe 1990), the ECB is a 'constitutional monstrosity' (Majone forthcoming), operating within an institutional architecture that is devoid of meaningful political co-ordination. As a consequence, the ECB is an affront to the competence limiting origins of the technocratic ideal of value-neutral administration outside the sphere of redistributive policy formation, as technocratic governance is shorn of cultural context, and the ECB is endowed with a governing mandate, not for justified reasons of political self-limitation, but simply because traditional politics would not assume responsibility for the redistributive impacts of European integration. Hayekian paradigms are then wholly inverted as an accompanying culture of

[2] The dedication of the ECB to price stability, demands that any increase in money supply due to Bank purchase of individual national government bonds, must be compensated for by restrictions in money supply elsewhere in the eurozone. How this will work in practice remains one of the great mysteries of efforts to stabilise the Euro.

total optimism contemporaneously posits that structural reform within a context of 'democratic deficit' will achieve the impossible and negate the economic uncertainties that now threaten the whole project of European Union.

Anarcho-liberalism and the end of politics

The routine denial of the Hayekian reality of economic uncertainty, as well as wholesale substitution of universalised market opportunity for politically-defined welfare entitlements, is disturbing, but also provides a point of analytical reference for this analysis in the final writings of Michel Foucault (2008). Delivered on the cusp of the liberalisation surge, and struggling to penetrate the political fog surrounding reformist zeal within France, Foucault's 1978–1979 lectures are also a foray into contemporary politics and must, accordingly, be treated with caution, especially by Foucault novices. Nonetheless, with this caveat in mind, they prove irresistible, foretelling the political paralysis that lies at the heart of current malaise and making specific reference to law as a technological servant of governing economic rationality.

To Foucault, placing responses to 1970s stagflation in their broader historical context, distinctions between political liberalisms mattered. The Scottish Enlightenment, with its efforts to resist the powers of the technology-oriented state through radical reconfiguration of civil society, was revolutionary, but would also find its contemporary global impact in the character of the *homo economicus*, or atomistic member of civil society charged with increasing general welfare, not within domineering state programmes, but rather, within the 'governing rationality' of a free market established in opposition to the state. The roots of modern economic liberalism lie in bourgeois struggle and in defence of civil society against the pastoral impulses of the modern state and its bureaucratic 'non-law' (Foucault 1994). Economically-liberal escape from state technology was nevertheless chimeric, inevitably posing its own conundrum of the establishment of a power of liberal economic thought, or a governing rationality, which, in its turn, 'denatured' man, or forced a conformity of human behaviour within the character of the *homo economicus* to rival, and perhaps even surpass the *dirigisme* of the *loi de police*.

As a consequence, Foucault was concerned to identify the differential treatments of the economic human that arise within political liberalism itself and which, in particular, were impacting upon 1970s liberalising debate. He identifies the two grand designs within which the notion of the 'market without the state' (Joerges 2004) has been transmitted into contemporary (European) debate: the first, the German ordoliberalism, which encompasses but pre-dates and survives the later radicalism of Hayekian positions; the second, the neoliberalism, or 'anarcho-liberalism' that self-evolved within American history and was forcefully reborn in the stark opposition of Chicago's economic science to the legalistic Freiburg School. The difference between the two may stem from a historical-philosophical accident, whereby European liberalism was carved out from strong existing states, whilst American liberalism pre-dated and founded the nation. Yet, the vital distinction in their modern impact is still felt, as ordoliberalism's continuing dedication to Walter Eucken's early dictum that social and economic orders are 'interdependent' (Wegmann 2002), reflects its underlying phobia that economic liberalism is itself 'fragile' (Foucault 2008), subject always to the social counter-movements of the dispossessed. The ordoliberal market is therefore supported by a more expansive notion of the rule of law, which not only protects the economy from the state, but also establishes a stabilising political-constitutional relationship between economic and social orders; or does so, at least as regards the delineation of political responsibility for assumption of negative social externalities and, more importantly, for the economic uncertainty that accompanies market operation. By contrast, the unbounded optimism inherent to anarcho-liberalism might be argued to have facilitated the radically unmediated expansion of neoliberal economic rationalities throughout civil society – most notably, in the guise of governing technologies such as law and economics – to encompass areas as diverse as penal policy or environmental protection.

For Foucault, the radical nature of the dispersal of economic liberalism within civil society is encapsulated in a bio-political technology of governing, which colonises the individual as a *homo economicus* to the degree that the whole sum of human actions may be made reducible to economic operations; a process which Foucault tantalisingly hints could find its climax within the dark side of a then emerging science of behavioural economics that claims to moderate rational choice theory in view of (valued) irrationality, but at perverse core pursues strategies to adapt human behaviour to market imperatives (*ibid.*: 268–270). The denatured *homo economicus*, governed by the logic of rational choice that is enforced in marketising law thus becomes the object of a bio-power of extraordinary strength, and it is this bio-power that might be argued to find its contemporary echo in our current lack of political capacity. To Foucault, 'politics' is to be found in 'agonsim', or the clash between governing rationalities, as well as in constant tension between human subjectivity (irrationality) and the power of rationality (Foucault 1994: 343). But what space is left for irrationality, or Foucault's political agonism, where a single governing thought becomes dominant to the exclusion of all others? What happens where politics is reduced to a boundless liberal optimism, which denies political responsibility for economic uncertainties and places all of its governing faith in the resilience of the de-natured *homo economicus* instead?

The battle for the rule of law

> [International] managerialism turns into absolutism: the absolutism of this or that regime, this or that system of preferences. The lawyer becomes a counsel for the functional power-holder speaking the new natural law: from formal institutions to regimes, learning the idiolect of 'regulation', talking of 'governance' instead of 'government' and 'compliance' instead of 'responsibility'.
>
> (Koskenniemi 2009: 412)

Remaining within the Foucaldian idiom, Martti Koskenniemi has written convincingly about the growth of 'managerialism' within international law (Koskenniemi 2009). In this view, the extension of Foucault's governmentality techniques into newly absolutist 'regimes' of international law is argued to be the result of a paradigm shift away from sovereignty; a shift that has not been mastered by law, but merely accommodated within a falsely naturalistic narrative of rational action, which is itself reminiscent of discourses prevalent at the birth of international law. Koskenniemi draws on Kant's critique of the progenitors of modern concepts of sovereign state action, to found his argument that contemporary shifts from sovereignty to non-sovereignty, are founded in a comparable socially-reductionist vacuum. Grotius and Pufendorf were 'miserable comforters' of the Prince, taking up quasi-natural positions that reserved to him 'the right and convenience of contracting in the interest of his society' (*ibid*.: 411). To Kant, the normative void at the heart of the sovereign accordingly equated with the traducing of his own cosmopolitan order, or the creation of more power for the Prince as his pastoral impulses were extended over his subjects, contemporaneously with their positivised projection into the international treaty sphere in the service of certain peace. To Koskenniemi, the contemporary retreat from sovereignty in international regimes is equally normatively voided, representing a renewed and intensified victory for governmentality. From the viewpoint of a dominant discipline of international relations, just as for Pufendorf, 'treaties are bargains between rational egoists seeking to resolve coordination or cooperation problems so as to minimise transaction costs resulting from unclear communication of their expectations under customary law' (Koskenniemi 2009: 411). The will to international law is governed only by an expansively functional impulse that, in its turn, establishes regimes untroubled by any principles of self-limitation because, in the absence of a constitution of constitutions, they 'will continue to deal with whatever they can lay their hands on' – cloaking their de facto operations with a 'legitimacy' established in a discourse of informal governance, which is 'geared to the production of maximal value' – until they have an 'absolute hegemony of power' (*ibid.*: 408). With the demise of formal government, the last vestiges of a rule of law are swept aside and governmentality claims its final victory in its law-driven diffusion into the web of international social relations, such that none can even recognise its origins.

Koskenniemi's vision is apocalyptic, but is surely irrelevant to European lawyers? From its birth, European integration was an openly functionalist project (Ipsen 1972). Yet, the law of the European Union perforce also has its origins in the self-limiting 'constitutional traditions' of its member states. Certainly, the EU is the post-national cradle of notions of governance and compliance, but has always also explicitly founded itself within a European rule of law, dedicated to self-limitation and the division of economic and social-political competences between the Union and the member states. Where the law of the EU is stylised as an Economic Constitution, it may also be construed – in its post-nationalist aspirations – as a re-invigoration of the eighteenth century project to contain the totalising impulses of the state, which does so within a structure of law that also satisfies insights that an economically-founded civil society is fragile, and must be sustained through the constitutional interdependence of social and economic orders. The liberating civilisation promised by European integration is accordingly reflected, first, in positions which have emphasised the conscious self-limitation of politics within the construction of the EU as a non-redistributive 'regulatory state' (Majone 1996). As well as, secondly, in analyses that have highlighted the 'deliberative sensitivity' of institutions of European economic governance to non-economic issues, where, typically, member states democracies retain their voice (Joerges and Neyer 1997).

Nevertheless, in the meantime, it is striking that such positions – though struggling to assert themselves against a Panglossian majority – now exhibit extreme disquiet about integration processes, demanding in their socially-democratic variant, 'what is left of the European Constitution?' (Joerges 2004), or disavowing in their regulatory form the 'inefficient' expansionist trend within the European project (Majone 2005). Such questioning might be dismissed as simple concern about the correct balance to be drawn between autonomous markets and social interventionism. To ascribe disappointment to such simple roots, however, is also to underestimate the depth and nature of a critique which now equates European non-management of sovereign and debt crises with, respectively, the final victory of Weber's bureaucratic state and establishment of Carl Schmitt's nightmare vision of 'technicity', or with the blindly optimistic inversion of the Hayekian paradigm (Joerges 2012; Majone forthcoming).

Where accusations of technicity and totalising optimism are levelled against a post-national institution that is characterised by its self-consciously civilising mission, the even more striking phenomenon of the colonisation of a 'normativised' integrative sphere by the maximisation of managerial value surely owes to more subtle causes than simple functionality. Here, however, Koskenniemi's analysis may usefully be supplemented in the light of Foucault's final writings on political liberalism and bio-power.

The quest for efficiency or the quest for law?

Read as a simple biography, the story of economic liberalism is also, as noted, a legal narrative, recalling law from the periphery of debate on economic malaise and placing it at the very centre of the problem of depoliticisation. This, in turn, provides a dual object of study: is it possible that adaptation in the application of the rule of law, as well as the development of law as economic technology has also played its role within economic malaise? In modern terms, however, debate on the character of law within economic liberalism is dominated by the methodology of law and economics. The undoubted potency of this school can be measured in extension of a core dedication of law to 'pareto efficiency' far beyond its originating realm of US private legal relations to private and public legal institutions throughout the globe.

Indeterminacy and the 'material basis' for legal legitimacy

In one analysis, wide-scale intrusion of the *homo economicus* of economic liberalism into legal relations, including the assertion that legal subjects are rational actors seeking to maximise their utility, can be ascribed to an economic form of post-colonialism. So, this argument runs, the law and economics movement acts as a vehicle of transmission for the US market, colonising academic journals, endowing chairs and targeting international bodies (the World Bank), in order to promote the Washington consensus (Mattei and Nader 2008). Striking as this analysis is, however, it may be suggested to underestimate the full lure of the movement, even to critical lawyers, and consequently to fail to grasp the true extent of the challenge posed by it. The law and economics movement proves to be so attractive precisely because and to the extent it appears to overcome the enduring problem of transcendentalism within law, furnishing it instead, with a putatively material basis for legitimacy. Law and economics must be placed in a far broader context of the endeavour to identify the basis for the legitimacy of modern, post-natural law. Within the US setting, the rise of law and economics is often associated with the response to American legal realism. Once this movement had implied that law was simply a contingent instrument of political power, it could be emptied of all transcendental concepts and reborn as a mouthpiece for the 'human science' of economics (*ibid*.). One US critic of the movement nonetheless approaches law and economics within the context of the problem of 'legal indeterminacy' and thus also provides this analysis with a vital linkage to early twentieth century European debates on the legitimacy of modern law (Kennedy 1997, 1998).

To Duncan Kennedy, the momentum gained by law and economics from the 1970s onwards can be attributed to its seeming political neutrality. Within the US, the critical legal recognition that formal law was not a monolith, furnishing absolute legal certainty, also had vital practical consequences within the legal system. Above all, the swathe of post-New Deal reformist jurisprudence, both implicated a liberal leaning judiciary in complex processes of policy analysis, and precipitated a conservative backlash, heightening the politicisation of judicial appointment processes. Within this setting, the assertion that private law could align its operation to a 'neutral' efficiency-oriented economic model, maximising the outcomes of individual parties to legal disputes, and delegating all redistributive policies to the legislature, proved attractive both to conservative and liberal positions. From the conservative stance, acceptance of an efficiency criterion within private law was congruent with the view that free markets are best placed to apportion welfare, offered a prospect to end the process of liberal-political judicial intervention into markets, and solved the problem of market distortion more generally posed by imposition of autonomous legal values upon market transactions. To a liberal position, by contrast – one also built on critical recognition of the socially-regressive impact of contractual freedom – the law and economics movement entailed search for a 'method that would legitimate the gigantic liberal law reform project […] carried out in the Courts after World War II' (Kennedy 1998: 468). The vital promise made was one that externalities could be neutrally apportioned between private parties, leaving legislatures free to engage in the redistributive tax policies to which they were best suited, by virtue of their political legitimacy and the fact that the legislature is best placed 'to do redistribution at minimal efficiency cost' (Kennedy 1998).

Today, this distinction made between neutral apportion of market externalities and political management of redistribution, finds vital application far beyond torrid spheres of US judicial politics. Most striking, is the pride of place it has been afforded within EU notions of governance, or the assertion that, its lack of democratic underpinning notwithstanding, EU regulatory policy can be legitimated with reference to the fact that market regulation carried out by technocratic bodies is no more than an expression of the apolitical neutralisation of market externalities (Everson 2012). *Grosso modo*: the limitations in a post-colonial account of the spread of the law and economics movement throughout the globe are revealed as European institutions embrace the human science of an economics that promises a neutrality of governing to which all nominally sovereign positions in Europe might commit themselves without fear of compromising their redistributive positions.

The prominence of 'scientific' notions of efficiency within both private and public European legal constructions is similarly far from surprising in legal theory terms. Early European legal theory – in its 'peripheral' appearances (Rottleuthner 1987) – also recognised the challenges posed by legal indeterminacy, the socially distorting impacts of formal jurisprudence, as well as the need to find an alternative and non-partisan 'material' legitimacy for law. Where Laski's injunction that, '[T]he problem of the juristic philosopher, in short, is the difficult one of validating his purely formal analysis of categories for the actual world about us' (Laski 1935[1993]: 202), translated into his subsequent plea that law reach to political economy, in order to furnish itself with 'an organised and continuous method' that might act as law's window on the material world, the subsequent fascination for European legal thought of the insights of founding law and economics texts cannot be doubted. A scientific model of human behaviour that imputes to Ronald Coase's rancher and farmer alike, a preparedness to maximise personal outcomes, is attractive precisely because it promises to free post-natural law from the ever present spectre of determinism. Legal judgment is voided of its own transcendental morality, its need to find fault for the trampling of crops by cattle. At the same time, law is spared the complexly partisan operation of determining whether wheat or meat is of more value to society. The economics of the rational contractor will determine whether rancher or farmer can best bear the costs of the building of a fence.

What is nonetheless shocking is the by now inexorable erosion of self-limiting 'nuances' that have always attached to the scientification of law within the post-natural environment of European legal theory (see the section 'the self-limiting critical moment' below). As EU law has not only unravelled politically-constituted codes of national labour law (Supiot 2010), but has also – in its tolerance for 'less than legal' ECB operations – dealt a blow to the rule of law within Europe (Everson and Joerges 2012), questions surely arise about the threats posed by the quest for legal efficiency.

'A legal theory without law'

US critique of the law and economics movement focuses upon the chimeric character of 'neutral' efficiency traditions within the law (Kennedy 1998). Nevertheless, in this broader setting of the contribution of law to contemporary malaise, a more immediately relevant critique of law and economics and its distortion of 'the purpose of law' derives from an unexpected quarter: ordoliberalism and, more specifically, the detailed attack made by Ernst-Joachim Mestmäcker – still the most potent (and Hayekian) proponent of ordered liberalism – upon the extreme positions taken up by Richard Posner. This one-sided debate is stylised in its self-projection and object of critique, and cannot be assumed to reflect more nuanced positions within either school of economic liberalism. Nevertheless, comfortably ensconced within Kantian traditions of a rule of law, residing in the 'inalienable rights of citizens against their sovereign to be respected in their dignity and liberty as self-governing individuals' (Mestmäcker 2007: 54), and also untroubled by the fortunate coincidence between Kantian and neo-classical visions of individual justice that complicates the arguments of more critically-minded jurists, Mestmäcker furnishes a striking reiteration of Foucault's concerns about the radicalising impacts of the spread of anarcho-liberalism across the institutions of civil society. Above all, for Mestmäcker, the lure of modern economic science to law and its claim to transform economic fact directly into legal morality, must be resisted to the exact degree that law's legitimacy derives, not from the 'real' world, but from its own autonomous mission to secure justice, and, above all, to do so through the control of power.

Accordingly, Mestmäcker begins his critique by turning Posner's self-identification with Nietzsche's critique of historicism in upon itself. Where Posner turns to Nietzsche to find support for his 'everyday pragmatism' and forceful rejection of the historical normativism that is formed within legal precedent, Mestmäcker reminds his readers that Nietzsche's reliance on 'life as the final arbiter' is also set in the context of his 'understanding of life as ''not the will to live but – hear my word – the will to power''' (Mestmäcker 2007: 60). Historical mysticism is a disruptive factor within legal systems. Yet, as Mestmäcker laconically observes, '[P]ower may certainly be looked upon as one of the great moving factors in history. But in legal theory, the control and limitation of power is certainly more relevant than its praise' (*ibid.*: 61). As a consequence, even the most radical of critical lawyers might concur with ordoliberalism's core concern that, in dismissing historical normativism, law and economics has similarly failed to find its own moment of self-limitation, of (Kantian) moral self-reflection, concomitantly establishing an 'idolatry of the factual' and of 'power' (*ibid.*).

The vital problem here, is one – emphasised by Hayek – of the lack of self-limitation within rational choice analysis: cost-benefit analysis can be applied far beyond limited spheres of rational individual interaction, can itself become 'counterfactual' where it is modelled, or applied to operations where markets and competition are 'arbitrarily mimicked' (Mestmäcker 2007: 48). To this exact extent, where law, in all its eagerness to materialise itself, moves beyond the delineated economic constitution, to create the marketised society instead, the scientification of law project is traduced; the claim to re-found legal morality in universal reality is displaced by a totalising rationality that makes its impossible claim to capture all uncertainty within human relations in its counterfactual models of operation. To Mestmäcker, the problem of neoliberal power within law and economics is dual-sided. On the one hand, in its eagerness to legitimate law within fact, the movement has dispensed with the Enlightenment project to limit power through 'normative' delineation of an (economic) civil society. On the other hand, however, in all its materialising over-ambition, law and economics has simultaneously emerged as a totalising force all of its own. Posner's later adoption of Kelsen and his projection of economic analysis within a positivistic scheme of law, which allows individual judges to dispense with a core rule of legal certainty in line with a *Grundnorm* of modelled economic transactions, represents acceptance of 'ideology in the service of unlimited government and socialism [sic]; the refutation of a concept of justice ignoring viable negative tests of justice that identify unjust norms' (*ibid*.: 55). The postwar re-founding of ordoliberalism within the Federal Republic's political constitution is similarly recalled as 'fascist friendly' jurisprudence is rejected out of hand, and renewed ordoliberal faith placed in Hayek's primary dictum that no form of government can be trusted which promises totalising security in the face of market forces which can never be totally mastered.

As hinted, Metsmäcker's self-depiction cannot be endorsed by critical legal positions, wary of an unconditional return to Weber's 'iron cage' of formalism, and more confident in the ability of the social collective to assert 'mastery over markets'. Nonetheless, his stylised observations uncannily verify Foucault's musings about slippage in European economic liberalism, the potential for radical spread of bio-power throughout the institutions of civil society, and for the prospect for the reproduction of totalising power in a legal movement lying beyond the sovereign technology of our traditional state.

European law as regime of economic technology

From entitlements to provisions

> [I]t would be neither satisfactory nor true to the development of the case law to reduce freedom of movement to a mere standard of promotion of trade between member states. It is important that the freedoms of movement fit into the broader framework of the objectives of the internal market and European citizenship. At present, freedoms of movement must be understood to be one of the essential elements of the 'fundamental status of nationals of the member states'. They represent the cross-border dimension of the economic and social status conferred on European citizens'.[3]

Considering the centrality of the European market within the integration project it is unsurprising that the jurisprudence of the Court of Justice of the European Union (CJEU) has endowed the individual European with an economic character. From the very inception of the EEC, judicial extrapolation of the European treaties has perforce entailed the re-allocation of economic provisions within an emerging European market. Individual economic opportunity is no longer constrained by national borders. Instead, reformulation of primary EU laws guaranteeing cross border movement of labour, services, economic undertakings and capital, as individual rights (the 'four freedoms'), is an indispensable weapon within a judicial armoury dedicated to the dismantling of the barriers to trade that distinctive national regulatory regimes constitute. The European Economic Citizen accordingly emerged as a 'frontier-busting' pioneer of European market formation (Dani 2011).

The persona of the European Economic Citizen may be viewed in a positive light at least to the degree that promotion of her rights by the CJEU has often freed the European from the 'infantilising' excesses of

[3] Opinion of AG Poiares Maduro in Cases C-158 and 159/04 *Alfa Vita Vassilopoulos AE v Greece* [2006] ECR I-8135.

postwar regulation (Dani 2011). Nevertheless, the undoubted virtues of the economic citizen similarly contrast with the destructive challenges that post-national economic citizenship poses to collective values of a non-economic nature established at national level. If primary European law may be understood to constitute an Economic Constitution, the normative measure of the containment of integrationist deregulatory impulses is found in the degree to which the European economic order continues – in the absence of a redistributive function – to co-exist with residual national social competences (Joerges forthcoming). At the pragmatic level of CJEU case law, containment of the 'race to the bottom' accordingly centres upon the jurisprudential limitation of the reach of the four freedoms, as well as of provisions ensuring the free movement of goods. Seen in this light, the rights of the European Economic Citizen, as well as her ability to overturn national market regulation, are not limitless but contingent, delineated by the balance struck by the CJEU between European and national law. And it is here, at this interface between legal orders, that the rationalising impulses of 'science' (economic and natural) have proven most attractive to a European legal order, whose 'supremacy' is a self-declared one: the putatively objective and universal 'truths' of science, provide European law with a vital claim to legitimacy founded in the persuasive power of the 'factual'.

Historically, the happy marriage established by the CJEU between science and principles of European law (proportionality) may be argued to explain the surprising degree of acceptance won by an activist court for its ground-breaking judgments. Where the Court deployed the power of the factual to unmask the paternalistic incoherence of member state regulation, national legal systems were persuaded to lend it their implementing vigour: a ban on wholemeal pasta, could not, after all, be shown to protect the health of Italian diners (Dani 2011). However, in its materialisation efforts, the historic Court also imbued its jurisprudence with a scientific outlook, which has subsequently hardened, with the result that the CJEU has now de-natured the European Economic Citizen, and remodelled the individual European as *homo economicus*. Recently radical CJEU jurisprudence might be attributable to the pressures of eastern enlargement, or the need to bind new member states quickly into the Union (Everson and Joerges 2012). Nonetheless, it is still striking that recent free movement case law has also recalibrated the principle of proportionality, ironed out 'efficiency-jarring' elements within precedent and moved explicitly to a marketised conception of redistribution as redistributive opportunity. The growing power of a new jurisprudential logic that national regulation – regardless of its purpose – must cede to the European principle of the free movement of goods where a product would otherwise be impeded in its access to the market, transforms the principle of proportionality from a revealing rule of reason applied to national regulatory motivations, into an absolute standard of 'trade above all' (Tryfonidou 2010). Similarly, by now infamous judgments on services provision (*Laval* and *Viking*[4]) have also subjected conduct of industrial disputes to marketised proportionality (Bercusson 2007), revealing the exact extent to which economic efficiency postulates have emerged within CJEU thinking as a universal and comprehensive European standard of allocative justice.

For many, the most concerning aspect within *Laval* and *Viking*, is the CJEU's failure to maintain the European legal tradition that labour and economic constitutions are distinct orders which may not be weighed against one another within the adjudicative balance (Supiot 2010): collective bargaining agreements may no longer be imposed upon 'posted' workers, through regulation or strikes, if they are deemed to impact disproportionately on cross-border trade. Seen together with the Court's new market access test for goods, however, *Laval* and *Viking* – as the introductory quotation demonstrates – are also one further example of the manner in which orders governing citizenship, as well as those governing the economic, have now coalesced within CJEU jurisprudence in accordance with a 'justice standard' of allocative efficiency. The emergence of this standard has its own inspirational roots. The posted workers of Laval and Viking were from the new member states, and found themselves denied access by western labour practices to the sole route to prosperity which the old member states had afforded them: their competitive labour advantage. Compensating perhaps for the lack of a European Marshall plan, but establishing a compensatory measure of justice for new member states that is founded in an idolatry of a factual of cheap labour, the Justices of the CJEU have nonetheless similarly undone

[4] Case C-438/05 *International Transport Workers' Federation, Finnish Seamen's Union v. Viking Line ABP, OÜViking Line Eesti* [2007] ECR I-10779; Case C-341/05, *Laval unPartneri Ltd v. SvenskaByggnadsarbetareförbundet, SvenskaByggnadsarbetareförbundet, avd. 1, SvenskaElektrikerförbundet* [2007] ECR I-11767.

the collectively-established universalisms of the social legal entitlements enshrined within national social orders, and replaced them with European 'rights' that are no more than contingent economic opportunities.

The European Economic Citizen has been reborn as *homo economicus* whose life chances are to be pursued and determined within the totalising rationality of law as economic technology. This development is difficult to resist at political level. Primary European law may promote the 'confident' consumer, but, ensconced within its own scientific outlook it cannot recognise the political concerns of the 'ethically-informed' consumer (Everson and Joerges 2007). Equally, in limiting strikes the EU legal order has similarly deprived the European *homo economicus* of a final means of politically asserting her collectively established values above market forces.

From uncertainty to risk

The story of slippage of the European legal order from Economic Constitution to economically-totalising regime is dominated, not simply by a theme of managerialism, but by a struggle to legitimate European legal operations through the putative universalism of science and material fact. This effort may have inspirational roots, but no degree of inspiration can justify the denaturing of the European. Instead, it makes the prevailing rationality even harder to resist, as allocative efficiency is enshrined in the commonplace power of precedent and the socially-regressive realities of contingent economic provisions are masked by reiteration of the glories of European citizenship. To this degree, evolution of primary European law, as colonising economic technology, mirrors gradual metamorphosis within political liberalism within Europe; it shares the wilful blindness of a permissive consensus that disguises the negative social impacts of anarcho-liberalism through rhetorical distractions that obscure the ever present reality of economic contingency through reiteration of the economic benefits of wealth maximisation.

The totalising optimism inherent to the failure to address the consequences of liberalisation is now apparent to some. As a recent editorial in The Guardian, approving of proposals to split UK banking business into retail and casino arms, notes: 'financial economics is heading back towards the world as Keynes and Hayek knew it: where economic uncertainty was recognised as such, rather than mathematised and missold as controllable risks'.[5] Wishful thinking: clarity is the exception rather than the norm. Instead, the backstory of the prevailing collapse of the distinction famously made by Frank Knight (1921) between (unforeseeable) uncertainty and (calculable) risk is one to which law, in its regulatory variant, has also contributed and, vitally, continues to contribute. Within Europe – in common with law throughout the globe – regulatory law has re-enforced unstated and counterfactual assumptions that unquantifiable hazard can be mastered as 'risk', and that economic uncertainty is a normality for which political responsibility need never be assumed.

A rationality of risk

The dominance of techniques of risk assessment, analysis and management within the EU regulatory environment is easily explained. The unexpected demand for supranational administrative capacity to compensate for the deregulatory impact of market-making jurisprudence has not only facilitated proliferation of ad hoc institutions of governance (autonomous agencies) outside the institutional architecture foreseen by European treaties. It has equally posed a legitimation conundrum with regard to the European exercise of a national regulatory competence that was never explicitly transferred to the EU (Dehousse 1994). Within this context, the objectivity imputed to scientific methods of risk quantification and cost-benefit analysis, together with the promise of political neutrality that is conjured by a precautionary approach to risk management, once again offers a prospect of legitimacy for action that is grounded, not within democratic process, but rather within the ability of regulation factually to master the contingencies of market operation.

Early warnings about the limitations inherent to the prominence of a 'rationality of risk' within its technocratic structures have done little to halt an EU belief in its regulatory potency. Responses to the BSE crisis, for example – in part precipitated by scientific inability to transform a hazard of cross-species transmission of spongiform encephalopathy into a quantifiable risk – have been dominated by efforts to improve the quality and independence of European scientific expertise. The reality that scientific method is only scientific method, not an omnipresent God, with the consequence that risk can

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[5] 'Finance and risk: On knowing too much', *The Guardian*, 9 September 2012.

only be modelled where evidence can be gathered to demonstrate its existence, has received concomitantly less attention (Vos 2000). Similarly, the inconsistencies that undermine the claim to political neutrality within a precautionary approach to risk management have largely been obfuscated, as ethical concerns about the hazards posed, say, by the environmental spread of genetically modified organisms (GMOs) have found it difficult to assert themselves against 'non-logics' that demand impossible proof for the uncertain existence of hazard (van Asselt and Vos 2008). The obvious conclusion that risk regulation entails its own measure of redistribution, at least with regard to the question of where the incalculable costs of hazard may fall, that it is not pareto efficient and ill-suited to delegation (Everson 1998), has been disregarded.

Once again, however, wilful blindness often derives from the best of intentions, betimes 'third-way' intentions, whose implication within wealth-maximising permissive consensus is similarly self-justified by a credo of continuing faith in the vitality of steering capacities within contemporary regulatory structures. In this doubly optimistic view, the trend to depoliticised regulation is wholly overstated: although the ideological battle between command interventionism and market autonomy has been comprehensively lost, competing justificatory discourses for regulation do still matter, and do so to the extent that they reflect our varied views of how steering capacities within the modern economy are exercised and to what end (Vibert 2011). Pareto-efficient regulation is revealed as the analytical 'construct' even its supporters concede it to be (Majone forthcoming); instead, a flattening of distinctions between governors and governed is overdue pragmatic recognition that steering capacities cannot be assured through political fiat. Steering is possible only where political capacity acts within a network of public–private relations, wherein mutual knowledge-creation enhances cognitive capacities of regulator and regulated (Baldwin and Black 2010), micro and macro-economic goals are better enunciated and co-ordinated (Vibert 2011), incentive substitutes command, and sanction is replaced by the radical steering-capacity of 'nudge', designed to prompt cognitive re-alignment of private to public interest (Thaler and Sunstein 2008).

The end of (financial) market failure

The persuasive power of scientifically-constructed regulatory optimism may, in its turn, help to explain the surprising acquiescence of the European Parliament within the rapid, post-collapse establishment of a European System for Financial Supervision (ESFS)[6] with its dramatic increase in technocratic European governance structures (Everson 2012). Generally hostile to proliferation in ad hoc EU bureaucracy (Bradley 1997), Parliament nonetheless readily condoned creation of powerfully autonomous agencies to oversee implementation of 'risk-based' Basel III oversight criteria in European banking, insurance, securities and pension sectors,[7] as well as the establishment of a European Systemic Risk Board, headed by the ECB, to combat the spread of systemic risk throughout the services sector. The strange absence of controversy is surprising: after all, the 'pro-cyclical bias' within Basel II risk-based, economic solvency criteria clearly contributed to financial collapse; a collapse subsequently compounded by technocratic 'cognition failure' (Black 2010). However, to the degree that the structures of the ESFS may be argued to run contrary to pareto-efficient presumptions, Parliament may have been persuaded that, in addition to supplying an immediate response to crisis, the ESFS was also constructed to satisfy the optimistic presumption that political steering capacities over financial markets can still be effectively exercised – also at supranational level – within autonomous regulatory structures (Everson 2012). Above all, revocation clauses, allowing Parliament to exercise 'soft political power' over the ESFS by means of the threat of withdrawal of its rule-making powers, might be viewed as a manifestation of ongoing steering capacity which adjusts the system's operation to changing regulatory goals. Equally, apparent tensions between ESFS's market innovation functions – clearly enunciated within the pre-ambles of the founding regulations of its agencies – and a precautionary role with regard to product regulation and systemic shocks (Moloney 2010), might suggest an inefficient lack of clarity within its regulatory mandate. However, it is also simple reflection of the tensions that arise in any modern regulatory enterprise between notions of

[6] The Basel criteria are established by banking regulators throughout the globe.
[7] For banks, see the Directive 2010/76/EU of the European Parliament and of the Council of 24 November 2010 Amending Directives 2006/49/EC as Regards Capital Requirements for the Trading Book and for Re-Securitisations, and the Supervisory Review of Remuneration Policies, OJ L329, 3–35; and the Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the Taking-Up and Pursuit of the Business of Insurance and Reinsurance (Solvency II) (recast), OJ L335, 1–155.

consumer choice, consumer protection and macro-steering: whether the regulator is a representative of social consumer interest, facilitator for 'marketised' consumer opportunity, or vital co-ordinator between micro and macro-economic policy – a choice that is to be made in the instantiated light of prevailing political circumstance.

Nonetheless, doubts remain: can 'flattened' regulation ever establish politically-sensitive macro-economic steering capacity that recognises and takes responsibility for the existence of hazard? In this analysis, the answer is 'no'. Although raising regulatory solvency margins,[8] the Basel III framework for banking remains wedded to the demand for capital growth through financial innovation. Confident that procyclical tendencies can be combatted by better oversight, individual economic solvency is still ensured within the self-same Value at Risk (VaR) formula introduced by Basel II; a methodology that fosters the identically intimate relationship between business, regulators and academics, within which the fatal complacency arose that tolerated unsustainable business models as wealth-maximisation vehicles (Black 2010). Parliamentary failure to question VaR is deplorable; first, as *The Guardian* notes, because of its bewildering detail:

> Modern finance is too complex. As you do not fight fire with fire, you do not fight complexity with complexity [...] If a bank

[8] See the Regulation (EU) No. 1092/2010 of the European Parliament and of the Council of 24 November 2010 on European Union Marco-Prudential Oversight of the Financial System and Establishing a European Systemic Risk Board, OJ L 331, 1–11 (ESRB Regulation); Regulation No. 1096/2010 of 17 November 2010 Conferring Specific Tasks Upon the European Central Bank Concerning the Functioning of the European Systemic Risk Board, OJ L 331, 162–164 (ECB Regulation); Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 Establishing a European Supervisory Authority (European Securities and Markets Authority), Amending Decision No 716/2009/EC and Repealing Commission Decision 2009/77/EC, OJ L 331, 84–118; Regulation (EU) No 1093/2010 of the European Parliament and of the the Council of 24 November 2010 Establishing a European Supervisory Authority (European Banking Authority), Amending Decision No 71672009/EC and Repealing Commission Decision 2009/78/EC, OJ L331, 12–47 (EBA); Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 Establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), Amending Decision No 716/2009/EC and Repealing Commission Decision 2009/79/EC, OJ L331, 48–83. (EIOPA).

> looks like it has borrowed too much, it probably has, no matter what the risk models say.[9]

But, secondly, and more importantly so, because the risk-based approach to regulation adopted within the ESFS continues to perpetuate negation of market failure: '[F]raming regulatory problems as risks allows regulators to argue that certain regulatory failures, are not regulatory failures at all, but normal events, which are to be expected, and for which they are not to blame' (Black 2007: 58).

To radicalise this statement: where permissive consensus at national level has complemented evolution of technocratic risk regulation to fill the legitimation lacunae of the EU, the problem is not simply one of poor regulation. Ideological battle has not been replaced by a new political reality – reproducing the old through establishment of 'government in miniature' (Prosser 2011) – but by a seductive formula of political abdication instead. Conflicting regulatory goals of innovation, consumer protection and macro-steering are no longer opposing political goals, but merely 'neutral' regulatory goods, the quantitative rather than qualitative benefits of which may be 'objectively' balanced against one another in a matrix within which private processes of capital accumulation are a universal good, or 'normality', to which all conflicting political positions might commit without fear of blame for its collapse. Within the folding of uncertainty into risk, the concept of market failure has now been comprehensively expunged, such that the question of political accountability for it need never arise. Rather than being founded upon a differentiation between risk and a situation of uncertainty to which politics would once furnish its pre-emptive response by limiting the sphere of free market operation from the regulatory outset, post-collapse regulation continues to be based upon the false distinction between risk and a normality (of market collapse) for which politics need not answer. Where a rationality of risk normalises potential for failure of financial markets, or where permanent innovation within financial services markets – substitution of ever more refined financing mechanisms for the (politically) defined, if lacklustre, product of traditional markets – forms a part of the permissive consensus which has seen legal entitlements privatised as

[9] 'Finance and risk: On knowing too much', *The Guardian*, 9 September 2012, p. 26.

economic provisions in ever more refined, but ever more illusionary debt securitisation mechanisms, we are all made complicit with a rationality that entails silent abdication of political accountability for public welfare.

The demise of the rule of law, or death by governance

To the degree that the contemporary regulatory environment is preconditioned by wealth-maximisation rationality, sophisticated debate suggesting that steering capacity can be re-established within autonomous market regulation is chimeric. Above all, where it is accepted that regulatory complacency can only be overcome by 'mavericks' (Black 2010), steering strategies that adopt the methodologies of the market in order to command it, are singularly ill-suited to the task of establishing the sceptical parameters for debate within which malcontents might flourish. Most strikingly, 'nudge' methodology draws heavily on the market friendly rationalities of behavioural economics, and is just as surely a product of a preternatural regulatory environment that unthinkingly equates 'governmentality techniques' to 'regulatory tools'(Scott 2004). The irony is painful: at a distance of 30 years, Foucault's musings about the totalising bio-power of the behavioural sciences within human affairs, appear to be nothing if not chillingly accurate. However, blind faith in the effectiveness of steering mechanisms within EU governance, equally forcefully recalls the concerns of Koskenniemi and Mestmäcker about threats now posed to the rule of law.

Reviewing this issue in autumn 2012 in the light of what are still very fast moving events within the European Monetary Union (EMU), it should be noted that the most worrying menace is not always the obvious one. Legal certainty has clearly been undermined within Europe as illegality has followed illegality in response to the current *Außnahmezustande*, albeit with little discernible amelioration of the misery currently being visited upon Europeans. The extension of the 'economic conditionality regime', established within the ESM (Chalmers 2012), to ECB assumption of national bond debt, in a less than convincing effort to satisfy the 'constitutional' duty imposed upon the Bank to maintain price stability (Article 127 in the Treaty on the Functioning of the European Union, TFEU), has done little to break the unendingly destructive cycle of debt austerity established within peripheral eurozone economies. Such ineffective illegalities apart, however, the more potent threat to a European rule of law now resides in the mix of the totalising powers of governance and economic rationality, as the current promise to politicise European policy-making not only proves illusionary, but also obscures the inability of law to exercise any control over counterproductive rationalities established within EMU, as well as within newly-proposed Banking Union.

Democratic (and technocratic) governments throughout southern Europe share a common frustration with European Parliamentarians who have long sought to hold the ECB accountable to its subsidiary goal to 'support the general economic policies in the Union with a view to contributing to the achievement of the objectives of the Union as laid down in Article 3 of the Treaty of European Union' (Article 127(1) TFEU). The ECB may be ready to engage in a co-operative governance environment, choosing freely to take part in parliamentary debates and to be examined before parliamentary committees, even in the absence of a positive legal obligation to do so (Everson and Rodrigues 2010). Nonetheless, the predictable result of such appearances has been reiteration by the Bank of the primacy of its stability mandate: '[T]here is only one criterion on which the ECB […] will be and should be judged, and that is whether it delivers what it is instituted for, namely price stability'.[10] Meanwhile, in relation to growth and employment in the Euro area, it has been noted that:

> [the] falling number of inquiries [parliamentary questions] in this regard either suggests that over time the ECB has worn out MEPs in their efforts to have the ECB place more emphasis on its secondary objective, or that MEPs increasingly trust the ECB to make the right assessments and to take the right decisions.
> (Amtenbrink and Duin 2009: 567–568)

Relocation of 'trust' away from representative bodies to structures of governance, however, now finds its apotheosis in delegation of oversight of the ESM contingency regime to the 'commissarial' European Commission (Joerges and Rödl 2012), and to enhanced powers afforded the ECB within proposed European Banking Union. Others have highlighted the dangers inherent to the transfer of national economic policy competences within the ESM (Chalmers

[10] Monetary dialogue of 9 November 1999, cited in Amtenbrink and Duin (2009).

2012). In the terms of this analysis, however, the Commission proposal for a Council Regulation 'Conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions' (European Commission 2012) confirms all pessimistic interpretations. Where European Banking Union is also about the construction of 'sound money', or the reestablishment of the sovereign ECB competence to create Euros through direct oversight of debt production by private eurozone banks, the Commission's assertion, made under the heading of 'Governance' in its justificatory recitals, are incongruous at best, and fatally obscuring at worst: 'Monetary policy tasks [of the ECB] will be strictly separated from [its] supervisory tasks to eliminate potential conflicts of interest between the objectives of monetary policy and prudential supervision'.

In tandem with the EU's continuing dedication to innovation within the ESFS, Banking Union would therefore appear to be similarly pre-programmed to perpetuate permissive consensus within a paradoxically impossible pursuit of regulated money supply, on the one hand, and wealth maximisation, on the other. At the same time, however, the lie that monetary policy and prudential supervision can be pursued in isolation from one another within a framework of sound money, will surely be revealed as the ECB shatters internal glass walls, in order to reconcile irreconcilable mandates. Within this context, there is little or no hope that law might be used to oversee the Bank's operation, or, more importantly, might re-establish the constitutional context within which the necessarily political choice between wealth maximisation on the one hand, and monetary caution, on the other, might be made.[11]

[11] The independent ECB is (unwillingly) subject to review by European legal provisions, but only insofar as these do not relate to its core function of the pursuit of price stability (Everson and Rodrigues 2010).

The self-limiting critical moment

To critical Europeanists, the current emergency within European governance is horrifying, not least because escape from it appears impossible. Jürgen Habermas' plea for the establishment of a political constitution within Europe cannot but cause discomfort:[12] the call for 'more' Europe to solve problems that are of the EU's own making represents an extraordinary *coup d'etat*, overwhelming myriad states at one stroke, including populations who have so very recently rejected European constitutionalisation in popular referenda. Surely, 'St Jürgen' (Ladeur 1997), in all of his passion for the primacy of deliberative politics, cannot believe in the sustainability of a constitutional patriotism rooted only in the poisonous soil of fear that it could all get much worse? Equally, however, adapting the old Irish joke, if we are setting out on the road to democratic constitutionalism, we would not want to be starting from here: the notion of political union issuing from the mouths of European institutions is predictably chimeric, implicated within the governmentality of the European regime, wherein – under pressure of crisis – the commissarial Commission has become the de facto functional power holder. The measure of Manuel Barroso's political confederation of nation states, after all, is to be found in indirect election by the peoples of Europe of a Commission President from amongst candidates offered by European party blocks in forthcoming elections for the Parliament. Charismatic European parliamentarians (Martin Schulz) might seek to nudge Europe in new directions. But, where democratically-legitimated national governments are constitutionally-emasculated within fiscal and banking union and by emergence of the Commission as overseer for the conditionalities imposed on their economic policy, the indirect election of Commission President is, at best, a democratically-tinted sticking plaster for the ills visited upon individual Europeans (Joerges and Rödl 2012). At worst, it is an enslaving veil for the final victory of an 'ideology [established] in the service of unlimited government' (Mestmäcker 2007: 55).

[12] Jürgen Habermas, Peter Bofinger and Julian Nida-Rümelin, 'Only deeper European integration can save the eurozone', *The Guardian*, 9 August 2012, retrieved from: http://www.theguardian.com/commentisfree/2012/aug/09/deeper-european-unification-save-eurozone (last accessed 23 December 2013).

From the critical legal standpoint, the great European escape will be possible only when the dominant rationality – idolatry of the factual – is challenged by valued irrationality and the competing rationalities of political agonism. Simple return to an originating political liberalism, wherein 'the man of law […] counterpose[s] to power, despotism and arrogance of wealth, the universality of justice and the equity of an ideal law' (Foucault 1994: 128), is not enough. Equally, a recent German Constitutional Court judgment, condoning the Republic's contributions to the ESM, to the degree that 'the Bundestag […] is a participant in decisions on the amount, conditionality and length of stability aids'[13], might serve to protect a German population from the totalising powers of a European regime. Yet, in view of eurozone interdependence, what is good for Germany may still prove to beggar Greece, as the link between economic stability and social austerity is petrified in constitutional law. Disembedded ordoliberalism, applied outside its German context, cannot but perpetuate the torture of peripheral eurozone states.

The undoubted success of the postwar German Constitution must surely also owe – at least within its socially-corporatist variant – to the critical insights of the Weimar Republic, and it is here, within the Continent's long-standing critical tradition that we can at least begin to address the failings of law in its evolution as economic technology. First, in this critical moment, the putative objectivities of science were never considered as being capable of supplying law with a universal legitimacy of its own. Instead, in Laski's formulation, 'continuous' science method would only ever provide law with a 'moral insight' into the limitations of its own operations (Laski 1935[1993]), would act as its window onto the world, revealing the socially-destructive impacts of formalist jurisprudence, especially in its congruence with neo-classical economics (Everson and Eisner 2007). This constitutively limiting critical moment, however, is similarly apparent in the responses of the critical movement to the problems of legal indeterminacy. Adaptation of law to social reality was never to be the function of the 'judge king' (Eugen Ehrlich), but of politics, within, for example, the legislative origin of specialised codes of (labour) law (Hugo Sinsheimer). At the same time, the constitutively-solidaristic

[13] Bundesverfassungsgericht [BVerfG - Federal Constitutional Court], Case No. 2 BvR 1390/12, 12 September 2012, para. 274.

character of politics was to be assured in the evolving cultural and social traditions of an indeterminate – or open – constitution (Hermann Heller). If law has a universal legitimacy at all, it can only be found in this critical schema, within its own forensically-constructed (scientifically-informed) self-limitation of formal method; within its deference to and constitution of a politics, whose totalising impulses are checked precisely because of its indeterminacy, or openness to socially-driven renewal (Everson and Eisner 2007). On all these counts, the European legal order, together with others, has failed: what price evolution of constitutive European solidarity as nation is set against nation within the conditionalities of fiscal union, as worker is set against worker in the persona of the *homo economicus*, and as a socially-divisive, market driven welfare is pursued in an unsustainable fiction of wealth maximisation? Europe's future lies in the hands of Europeans. European law must learn to give them their voice.

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Chapter 9

Who is the guardian for constitutionalism in Europe after the financial crisis?

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Introduction

The issue and problem of 'constitutional guardianship' is one with a long history. It was answered starkly and infamously by Carl Schmitt during and with regard to the final, crisis-ridden, years of the Weimar Republic: The guardian of the Constitution is not the *Reichsgericht*, the judicial branch, but the *Reichspräsident*, a political actor exercising the quasi dictatorial powers defined in Article 48 of the Weimar constitution on behalf of a politically homogeneous *Volk* (Schmitt 1931). This particular understanding of constitutional guardianship has now re-achieved a disquieting degree of topicality within a crisis ridden European Union. This dimension of our topic will be discussed in more details the second part of our contribution. We begin, however, with a series of reflections on the issue of constitutional guardianship within the Union in less troubled times. Even prior to crisis, the problem was a highly troublesome, albeit that very few commentators, and even fewer institutional actors,

[*] A first draft of this essay was presented at the conference on 'Representation in the EU' on 24–25 May 2012 at the University of Exeter, organised by Dario Castiglione and Sandra Kröger. On this background see Kröger (2012). The revised version of our contribution will be published in Kröger (forthcoming).

recognised the true nature of the challenge. Nevertheless, this challenge is now becoming ever more apparent in step with a growing and critical awareness of deeply entrenched – even growing – diversity within Europe and the obviously paradox nature of a voluntaristic response to diversity, which is ever more insistent in its pursuit of a future unity, but which cannot explain how this project might be realised through democratic processes.

When set against this background, the relevance of our topic to a context of debate upon democratic representation should be obvious. To be sure, courts, generally speaking, are the non-majoritarian vanguard and institutions par excellence of constitutional democracies. Non-partisanship defines their very ethos. Nevertheless, constitutional courts, in particular, do not find their prestige and authority exclusively within the legal provisions of the constitutions that establish them. Typically, these provisions do not endow them with powers of enforcement. Instead, constitutional courts rely and build upon a Weberian legitimacy, which they acquire to a significant degree through the modes in which they articulate and thereby 'represent' both the *normed* character, as well as, the normative *dignity* of the order in which they are situated and operate. In other words, constitutional legitimacy is founded within a tense duality of rule-bound, but socially responsive adjudication.

This twofold – formal and social – embeddedness of constitutional courts presents its own very particular problems within a European constellation, and affects – as we shall demonstrate – cumulatively upon the issue of the constitutional guardianship of the EU. The European Union is, as the Preamble of the Treaty of Lisbon and numerous of its Articles assure us,[1] committed to human rights, freedom, equality, democracy and the rule of law. Adherence to these commitments is a condition for membership within the Union; at least in theory. Constitutional adjudication is an American, not a genuine European accomplishment, but one which has nonetheless gained the status of a common European heritage. How, however, might this legacy be understood in the context of a Union which does not comply with the conditions that it imposes on its own members? Which institution is in a position to exercise the function of

[1] Most emphatically in Article 21(1) in the Treaty on the European Union (TEU).

constitutional guardianship within such a constellation? Certainly, the Court of Justice of the European Union (CJEU) springs immediately to mind. But that conclusion would be premature and far too superficial. The European Court has never been formally established as a 'constitutional' body. To be sure, its foundational jurisprudence on direct effect and supremacy, the *Cassis*-jurisprudence and its aftermath, its characterisation of the Treaties as a 'constitutional charter',[2] presupposes and assumes important supervisory function for law 'at all levels of governance,' which are widely recognised by the courts and authorities of many jurisdictions and with great emphasis and near unanimity in European law scholarship. However, this power cannot be considered to be comprehensive, even in theory, as long as 'Union competences are governed by the principle of conferral'.[3] Equally, its validity will be doubted for as long national constitutional courts – most notably Germany's *Bundesverfassungsgericht* [BVerfG, German Federal Constitutional Court] – refuses to make use of the preliminary reference procedure and continue to question the authority of the CJEU by determining unilaterally whether European prerogatives are being lawfully asserted. In other words, constitutional guardianship within the Union cannot yet be regarded as having been entrusted to one single body. It has both national and European masters: masters who may be in disagreement with one another.

This insight is neither new, nor particularly disquieting *per se*. It was discussed particularly thoroughly by Neil MacCormick (1998) a good while ago. There is pluralism in Europe, he acknowledged – adding that wise solutions could and should be found where legal solutions are not conceivable (*ibid*.: 531). MacCormick's suggestions seem to anticipate what various courts, including the notoriously inconvenient *Bundesverfassungsgericht* have learned to do, namely to establish interactive modes of adjudication. These adjudicative modes have by now been doctrinally refined by a host of academic commentators.[4] We will not explore the theoretical premises and

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[2] Opinion 1/91, *Opinion delivered pursuant to the second subparagraph of Article 228(1) of the Treaty – Draft agreement between the Community, on the one hand, and the countries of the European Free Trade Association, on the other, relating to the creation of the European Economic Area* [1991] ECR I-6079.

[3] Article 5(1) TEU.

[4] See, for example, Viellechner (2012) and Kuo (2013).

practical accomplishments of these responses in any further depth,[5] however, returning instead to the earlier conceptualisation of the multiple-guardian problem constellation as a contest for mastery over the *Kompetenz-Kompetenz*. We suggest that the conceptualisation of constitutional guardianship under this heading has, if inadvertently, disclosed a constellation of diversity in the Union which should not and cannot be dealt with through a form of hierarchical ordering, but instead requires horizontal cooperation.

The continuity which we reconstruct is a promising signal as it indicates that a potential exists to cope constructively with Europe's diversity. In the next section, where we consider the various European transformations following financial crisis, we will document responses to Europe's troubles of a different kind. The pragmatically legalised *comitas* among European courts, which proponents for interactive conflict resolution advocate, has now given way to a new primacy of the 'Political' in the Union *sensu* Schmitt. In the last part of this chapter we will investigate the efforts of the judiciary to manage these transformations. We analyse the judicial actions of the usual suspects in relation to two Judgments of exemplary importance. Both the German Federal Constitutional Court (FCC) and the CJEU retain their specific style. But these differences now contrast markedly with their agreement *in re*. Both courts appear to be prepared to accede to the primacy of the Political; they concur in their de-legalisation of constitutional adjudication.

Kompetenz-Kompetenz in a non-unitary union?

Our argument in the following section departs from prevailing modes of European legal scholarship in a twofold manner: failing to trumpet the historical merits of the European Court of Justice (ECJ) now the (CJEU), it likewise appears to question them. Belief in the centrality of law and its judicial enforcement was constitutive for legal scholarship during the formative era of the integration project. Law was prominently presented as both 'the object and the agent' of European integration (Dehousse and Weiler 1990: 243). In that vision, the ECJ necessarily figured as the incarnation of Europe's integrationist vocation. There is, also, more than a kernel of truth in

[5] Although some authors take a more sociological approach to commentary on the historic ECJ, see, Everson and Eisner (2007).

the assertion that the Court's jurisprudence was to prove, at least to the degree that it has withstood political irritations and disagreements. Similarly, the historic Court is noteworthy in that it deepened the normative quality of European law, in particular in relation to its human rights jurisprudence, and mitigated – often successfully – between competing claims and policies, all the while managing to build up an unquestioned authority. Today, however, the court is no longer portrayed so enthusiastically, even by the most faithful of its supporters.[6] How could any judicial institution cope with the ever increasing complexity and growth of its workload and continue to convince national legal systems throughout an ever more diverse Union with its one-size-fits-all philosophy? How might it hope ever to convince with its highly formalistic style of reasoning in cases of fundamental conflict which are characterised by conflicting economic interests and political disagreement? The Court's labour law judgements in *Viking*, *Laval* and *Rüffert*,[7] which assigned supremacy to economic freedoms over national labour law traditions, provide the most spectacular example of this type of failure.[8]

Currently, the factual erosion of the Court's legitimacy is similarly converging with the on-going, if widely unnoticed, transformation of the integration project and the ever more insistent conflict constellations that surround it. An uncompromising defence of the former authority of the Court has become both factually and normatively implausible. The once quite belligerent contest between the German Federal Constitutional Court,[9] on the one hand, and the allies of the ECJ, on the other,[10] has lost its intensity and very provocative nature.[11] It is now largely evident that there can be no one and single guardian of constitutionalism in the Union. The insistence of the Kirchhof Court on a cooperative relationship

[6] Suffice it here to point to the introductory chapter of Dawson, de Witte and Muir in their volume on *Judicial Activism in the European Court of Justice* (Dawson *et al.* 2013).
[7] *Case C-438/05, International Transport Workers' Federation, Finnish Seamen's Union v Viking Line ABP, OÜ Viking Line Eesti* [2007] ECR I-10779; Case C-341/05, Laval un Partneri Ltd v Svenska Byggnadsarbetareförbundet [2007] ECR I-11767; Case C-346/06, Rechtsanwalt Dr. Dirk Rüffert v Land Niedersachsen [2008] ECR I-01989.
[8] See our critique: Joerges and Rödl (2009) and Everson (2011).
[9] See in particular BVerfG, Cases 2 BvR 2134/92 and 2 BvR 2159/92, BVerfGE 89, 155 [Brunner v European Union Treaty, CMLR 57 (1994) 1], 12 October 1993.
[10] Most prominently, Weiler (1995).
[11] See, Pernice (2000: 163 ff); Mayer (2004); *cf.* Mayer (2000: 323 ff).

(*Kooperationsverhältnis*) with the ECJ tells us much about the willingness of national judiciaries to engage with Europe, albeit as equal partners. By the same token, any effort to construe such constitutional dialogue as on-going disobedience can only be substantiated with reference to the untranslatable German dichotomy between *Staatenbund* and *Verfassungsverbund.* There is nonetheless both irony and tragedy in this insight. While pragmatic responses to the *Kompetenz-Kompetenz* issue have become imaginable, the transformation of the European constellation through the financial crisis is eroding the prospects for a *legal* re-conceptualisation of Europe's diversity. The crisis, we will submit, is establishing a new de-legalised primacy of the Political in the Union in which constitutional adjudication is losing its disciplining functions.

Crisis 'law'[12]

Europe's responses to the new challenges are innovative in the sense that European law as we knew it did not provide for them. There legality is questionable, their normative content incompatible with values which were so far in highest regard. The patterns of Europe's transformed constitutional constellation are outlined in chapter 7, text accompanying notes 32 ff.

Dariusz Adamski was among the first to highlight and underline that core concepts used by new economic governance cannot be defined with any precision, either by lawyers or by economists, and are therefore not justiciable (Adamski 2012a; 2012b). This implies that rule-of-law and legal protection requirements are being suspended. This type of de-legalisation is accompanied by a highly discretionary evaluation of member states' performance, which economist Andrew Watt has revealed in his analysis of an in-depth review of thirteen EU countries considered to have macroeconomic imbalances undertaken by the Commission (Watt 2013). It is worth noting that the Fiscal Compact has entrusted the CJEU with task of assessing compliance with 'the budgetary position of the general government of a Contracting Party shall be balanced or in surplus' (Article 3 1.a TSCG). This is an impossible mission which is bound to damage the Court's standing.[13]

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[12] The following passages draw on Joerges (forthcoming 2014).

[13] See the critique by Damian Chalmers 'The European Court of Justice has taken on huge new powers as 'enforcer' of the Treaty on Stability, Coordination and Governance', EUROPP – European Politics and Policy blog of the London School of

What is specific about Europe's new economic governance? Characterisations by commentators oscillate between notions such as 'Executive Federalism' (Habermas 2011), 'Distributive Regulatory State' (Chalmers 2012), 'Consolidating State' (Streeck 2013: ch. 3), 'Authoritarian Managerialism' (Joerges and Weimer 2012), 'New Sovereignty with Unfettered Power of Rule' (Chalmers 2013). They all acknowledge the design failures of the Economic and Monetary Union (EMU) as it was institutionalised by the Maastricht Treaty of 1992 and the Stability Pact of 1997.[14] They all conclude that compliance with that poorly designed framework would have disastrous consequences. Does that mean that the new regime deserves recognition? Both the FCC and the CJEU have wrestled with this problem – but neither appears to have mastered it.

The law or the political as constitutional guardian

The German Constitutional Court has a much contested record with respect to its European commitments and loyalty – even though signals of disobedience have always remained rhetorical. The CJEU has overruled national law in countless cases – but has hardly ever found European legal acts to be at fault. Investigating each of these Court against the background of the new economic governance now evolving within Europe accordingly promises to provide us with nuanced insights into the management of the crisis.

Is the German Court a 'dog that barks and never bites'?[15]

The attention which the complaints before the FCC against the ESM Treaty and the Fiscal Compact have attracted is as unsurprising as the outcome of this controversy which the court delivered in its

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Economics and Political Science, 7 March 2012, retrieved from: <http://blogs.lse.ac.uk/europpblog/2012/03/07/european-court-of-justice-enforcer/> (last accessed 4 March 2014).

[14] Council Regulation (EC) No 1467/97 of 7 July 1997 on speeding up and clarifying the implementation of the excessive deficit procedure, OJ L209 , 6–11.

[15] The metaphor is from Weiler (2009: 505) commenting on Bundesverfassungsgericht, judgment of 30 June 2009, available at: <www.bundesverfassungsgericht.de> (last accessed 4 March 2014); English translation at: <http://www.bundesverfassungsgericht.de/entscheidungen/es20090630_2bve000208en.html> (last accessed 4 March 2014).

judgment of 12 September 2012.[16] What the highest judicial authority of Europe's most potent economy has to say about well-argued complaints matters. And yet, it was easy to 'hazard a pretty good guess at the ending'. Paul Craig's (2013) observation concerns the Pringle Case of the CJEU but is equally valid with respect to the German case. It seemed simply inconceivable that the courts would interfere with high politics in matters of utmost importance. That, however, is not good enough a reason to close the academic files and shrug of the shoulders.

On closer inspection, the Judgment reveals a number of ambivalences. The most important one is the Court's defence of the budgetary power of the German *Bundestag*. This power is a democratic essential, protected by the eternity clause of the Basic Law. Its importance was already underlined in the previous Judgment on the rescue package for Greece[17] and its validity cannot be questioned in principle. Is it a principle with bite? In both judgments, the Court underlined that the *Bundestag* enjoyed wide latitude which the judiciary must respect.[18] Through this move, the rights of the *Bundestag* were re-defined in a proceduralising mode: the Parliament must be adequately informed, enabled to deliberate, and prevented from delegating its evaluation. This reading is in line with a principle of 'integration responsibility'[19] which the Court developed in its Lisbon judgment; a contested notion, but one which can, in our view, be understood as a search for a response to the tensions between integration and democracy. Such a benevolent reading is not evinced by the 12th September Judgment. To be sure, the form of judicial restraint, which the German court exercised when it gave the green light to the extensive indebtedness of the Federal

[16] FCC, Case 2 BvR 1390/12, 12 September 2012; an incomplete English translation is available at: http://www.bundesverfassungsgericht.de/entscheidungen/rs20120912_2bvr139012en.html> (last accessed 4 March 2014).

[17] FCC, Case No. 2 BvR 987/10 - 2 BvR 1485/10 - 2 BvR 1099/10, 7 September 2011, BVerfgE 129, 124. Retrieved from: <http://www.bverfg.de/entscheidungen/rs20110907_2bvr098710en.html> (last accessed 4 March 2014).

[18] See FCC, judgment of 7 September 2011, previous note, paras. 130-132; and judgment of 12 September 2012, note 16 above, para. 180.

[19] FCC, Case No. 2 BvE 2/08 - 2 BvE 5/08 - 2 BvR 1010/08 - 2 BvR 1022/08 - 2 BvR 1259/08 - 2 BvR 182/09, 30 June 2009. I: English translation retrieved from: <http://www.bundesverfassungsgericht.de/entscheidungen/es20090630_2bve000208en.html> (last accessed 4 March 2014).

Republic, is again embedded in procedural and institutional notions. The Court is not careful of 'foreign' concerns. The weight constitutionally placed upon the budgetary powers of the *Bundestag*, so we learn and understand, requires that the German Parliament retains the power to determine the most important conditions for future successful demands for capital disbursements.[20] In this passage, the Court once again strengthened the link between the *Bundestag*'s budgetary responsibility and a distinctly German philosophy of stability (i.e., price stability and the independence of the ECB above all). As a consequence, the nature of the EMU as a stability community (*Stabilitätsgemeinschaft*) is even seen as being protected by the 'eternity clause' of Article 79(3) of the German Basic Law as an unamendable core of Germany's constitutional identity.[21] After this move, the stability principles become the core of a refurbished European economic constitution.[22] All this, the Court hopes, will protect the democratic rights of German citizens. Non-German citizens of the Union, however, should not at all be amused. Why is budgetary autonomy not understood as a *common* European constitutional legacy, respect for which is demanded by Article 4(2) TEU? The one-sidedness of this argument is all the more disappointing as the Court, in an earlier paragraph of its judgment, had opened another and more constructive perspective: The Court explained that 'Article 79(3) seeks to protect those structures and procedures which keep the democratic process open'.[23] The Court did

[20] *Ibid.*, para. 274; this section is not yet translated. In view of the complexity and importance of this pronouncement, we add the German original: '*Da der Bundestag durch seine Zustimmung zu Stabilitätshilfen den verfassungsrechtlich gebotenen Einfluss ausüben und Höhe, Konditionalität und Dauer der Stabilitätshilfen zugunsten hilfesuchender Mitgliedstaaten mitbestimmen kann, legt er selbst die wichtigste Grundlage für später möglicherweise erfolgende Kapitalabrufe nach Art. 9 Abs. 2 ESMV;*' for a critical comment, see Joerges (2012: 560).

[21] *Ibid.*, para. 220, which reads in German: '*Die haushaltspolitische Gesamtverantwortung des Deutschen Bundestags wird in Ansehung der Übertragung der Währungshoheit auf das Europäische System der Zentralbanken namentlich durch die Unterwerfung der Europäischen Zentralbank under die strengen Kriterien des Vertrages über die Arbeitsweise der Europäischen Union und der Satzung des Europäischen Systems der Zentralbanken hinsichtlich der Unabhängigkeit der Zentralbank und die Priorität der Geldwertstabilität gesichert.*' And '*Ein wesentliches Element zur unionsrechtlichen Absicherung der verfassungsrechtlichen Anforderungen aus Art. 20 Abs. 1 und Abs. 2 in Verbindung mit Art. 79 Abs. 3 GG ist insoweit das Verbtot monetärer Haushaltsfinanzierung durch die Europäische Zentralbank.*'

[22] *Ibid.*, see paras. 219–220, 232–233, 239–279, and 300–319.

[23] *Ibid.*, para. 206 in the English extract, para. 222 in the German original.

not indicate that it would be prepared to address the tensions between democratic commitments and the integration process, which would include the concerns of all member states. Instead, the Court's reasoning leads to a strengthening of the links between economic stability and social austerity. This form of judicial self-restraint seems even more questionable in the light of – or, rather, in the shadow of – the Maastricht judgment discussed above. In that judgment, the Bundesverfassungsgericht had made German participation of Germany in the EMU conditional upon the European-wide acceptance of Germany's economic and institutional philosophy. This move is now repeated and significantly modified. While the Maastricht judgment assumed that Europe's economic constitution could be an essentially legal project, the new judgment is moving from law to governmental and executive managerialism, with requirements defined mainly by Germany and its Northern allies. To put it slightly differently, we find it deplorable that the FCC acted as (only) the guardian of the German constitution. The qualification of financial assistance as a matter not of European monetary but of national economic policy,[24] as well as the somewhat euphemistic statements on the respect of the stability commitments,[25] are anything but robust indicators of truly European commitments. They are embedded in the conditionality of existing crisis management. The FCC talks about democratic essentials, Jürgen Habermas (2012) has observed, but has Germany in mind. The one-sidedness of its decision seems indeed obvious – and difficult to overcome. The German Court is not entitled to act as the Guardian of Europe. What we would expect, however, is a readiness to define Germany as a Member of a Union in which the concerns of all the member states and their democratic rights deserve recognition. Only then would the Court document an understanding, or *Integrationsverantwortung*, which might reflect common European commitments.[26]

[24] *Ibid.*, para 169.
[25] *Ibid.*, Paras 201 ff.
[26] For a similar critique see Deters (2013).

'Let's close our eyes' – no alternative for the CJEU in Pringle[27]

What would have happened to the European Union had its Court of Justice found that Thomas Pringle's concerns about Europe's crisis management were well founded, that the support-mechanisms which the EFSF and the ESM have established interfere with the exclusive European competence for monetary policy, that the amendment of Article 136 TFEU were not possible under the simplified revision procedure enshrined in Article 48(6) TEU, that new policies adopted and pursued by the member states jeopardised the primacy of price stability, that the bail-out provision of Article 125 TFEU prohibited the granting of financial assistance to member states whose currency is the euro, that the functions assumed by the Commission, the ECB, and the International Monetary Fund (IMF) were irreconcilable with the principles on the conferral of powers laid down in Article 13 TFEU, or that the mandate allocated to the CJEU in the ESM Treaty exceeded judicial powers? Only a fool would dare to predict the dire consequences. The same kind of uncertainty governs with regard to the success of all of these measures. Under such circumstances, the CJEU could not and should not be expected to interfere, one might conclude. Nonetheless, in so doing, one must similarly concede that this conclusion implies a complete secession of law to discretionary political power. The onus must surely be one – for the lawyer at least – to commence the search for alternatives to this devastating legal default.

The search for such alternatives should allow for escape from the impasses to which Europe's crisis managements must respond, namely the design defects of EMU, its conceptually monetarist background, upon which the dedication of EMU to price stability rests and which has now become the cornerstone and sole possible value of the European economic constitution. It has by now become a *communis opinio* that European monetary policy with its pre-defined objectives and institutional frameworks cannot operate in tandem with the multitude of national actors which are pursuing economic and fiscal policies under a very loosely constructed machinery of European supervision. That insight has triggered the quests for

[27] Case C-370/12 *Pringle v Pringle v Government of Ireland, Ireland and the Attorney Gener*al, Judgment of the Court of 27 November 2012

enhanced controls and generated the new machinery of authoritarian managerialism. There is, however, a twofold flaw in the reasoning of the CJEU in the assumption that the failures of the past justify the unrestrained activism of the present.

The first flaw is the Court's failure to address the implications of its own explanation of the conceptual background to the bail-out clause. 'The prohibition laid down in Article 125 TFEU ensures that the Member States remain subject to the logic of the market when they enter into debt, since that ought to prompt them to maintain budgetary discipline. Compliance with such discipline contributes at Union level to the attainment of a higher objective, namely maintaining the financial stability of the monetary union'.[28] This is indeed a fair restatement of an ordoliberal legacy which we can still identify within EMU. However, the Court is then silent with regard to the philosophy which underlies our current cure to the failures of the past. This is by no means to suggest that the Court should have advocated an ordoliberal renaissance. Nonetheless, what truly disappoints in its presentation of the new modes of economic governance is the lack of any kind of conceptual deliberation about their background and their adequacy. As we have argued in the section on crisis law, the new modes of European economic governance amount to nothing less than a deep transformation of the state of the European Union. The organisers of that transformation should be asked to explain their objectives and the adequacy of the means which they are employing. The lack of any plausible explanation of the means—end relationship within Europe's crisis management reveals a second flaw in the judgment. Wherever the court responds to objections about the legality of the new regime, it merely parrots the orthodoxy that 'conditionality' as a justification.

Conditionality ensures respect for the exclusive European competence in monetary policy and thereby legality of the simplified amendment procedure:

> [T]he reason why the grant of financial assistance by the stability mechanism is subject to strict conditionality under paragraph 3 of Article 136 TFEU, the article affected by the

[28] *Ibid.*, para. 135.

> revision of the FEU Treaty, is in order to ensure that that mechanism will operate in a way that will comply with European Union law, including the measures adopted by the Union in the context of the coordination of the Member States' economic policies.[29]

Conditionality is the glue that keeps transnational actors together:

> [When granting assistance] the EMM 'Board of Governors shall entrust the European Commission – in liaison with the ECB and, wherever possible, together with the IMF – with the task of negotiating, with the ESM Member concerned, a memorandum of understanding (MoU) detailing the conditionality attached to the financial assistance facility. The content of the MoU shall reflect the severity of the weaknesses to be addressed and the financial assistance instrument chosen. In parallel, the Managing Director of the ESM shall prepare a proposal for a financial assistance facility agreement, including the financial terms and conditions and the choice of instruments, to be adopted by the Board of Governors.[30]

Last, but not least, Article 125 TFEU retains its function thanks to conditionality:

> [T]he purpose of the strict conditionality to which all stability support provided by the ESM is subject is to ensure that the ESM and the recipient Member States comply with measures adopted by the Union in particular in the area of the coordination of Member States' economic policies, those measures being designed, inter alia, to ensure that the Member States pursue a sound budgetary policy.
>
> Article 125 TFEU

The deeply undemocratic nature of conditionality goes unnoticed or uncommented upon. The CJEU imposes on the whole of Europe the form of discipline which the FCC has imposed on Germany's neighbours.

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[29] *Ibid.*, para 68.
[30] *Ibid.*, para 18.

De-judicialisation: Europe's Schmittian moment

Germany's constitutional court feels exclusively committed to the country's constitution. The CJEU is certainly motivated by its commitment to the integration project. The discrepancy between these commitments was once perceived of as threat to the European project. That risk did not materialise as anticipated. But we are now concerned with a risk of a new kind. The converging attitudes of both courts in the assessment of the *praxis* of Europe's crisis management is disquieting because it accepts the primacy of discretionary politics in the management of the crisis and fails to develop any criteria against which the legitimacy of these practices might be assessed.[31]

At this point we return to our reference to the 'state of exception' made at the beginning of this essay. Schmittian notions are certainly always engraved in a specific context. [32] History does not repeat itself and situational contexts remain distinct. And yet, recourse to Schmitt is anything but far-fetched.[33] Crisis management practices which are neither foreseen in EU primary law, nor in national constitutions are justified with the argument that compliance with the letter of the law would cause more harm than its breach or daring interpretation. Even Carl Schmitt did not conceive of the state of exception as a permanent condition; his justification of a 'commissarial dictatorship' included an effort to overcome the problems that precipitated departure from the rule of law and to regain normal constitutionality (see Schmitt 1938). In the present state of the Union, pertinent suggestions are urgent – and abound. However, they are mostly merely pragmatic and managerial, albeit that some constitutional

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[31] We should underline that we do not object in principle to the FCC's efforts to insist on parliamentary involvement. One can read this tendency as a step towards a proceduralisation which seeks to engage concerned institutional 'stakeholders' in Europe's crisis management (see Lepisus 2012: 761–762; see also Deters 2013).

[32] See Kennedy (2011) with references to the German original writings and the translations into English.

[33] E.-W. Böckenförde, formerly a judge of the *Bundesverfassungsgericht* and renowned connoisseur of Schmitt's oeuvre, was among the first to characterise the crisis of the Euro and of Monetary Union as an '*Ausnahmezustand*' (state of exception/emergency) which would suspend the rule of law: Böckenförde, E.-W. 'Kennt die europäische Not kein Gebot? Die Webfehler der EU und die Notwendigkeit einer neuen politischen Entscheidung', *Neue Züricher Zeitung*, 21 June 2010, retrieved from: <http://www.nzz.ch/nachrichten/kultur/literatur_und_kunst/kennt_die_europaeische_not_kein_gebot_1.6182412.html> (last accessed 8 February 2014).

lawyers and political philosophers have formulated some new propositions for a new constitutional architecture.

We have little room here to enter in these debates. We have presented our alternative of 'conflicts-law as Europe's constitutional form' elsewhere.[34] This is an approach which takes, 'unity in diversity', the fortunate motto of the ill-fated Draft Constitutional Treaty of 2003 seriously, and rejects the notion that federalist state building is a sustainable project. We argue instead for a radical 'proceduralisation' of the integration project in which the European judiciary engages in continuous juris-generative efforts (a *Rechtfertigungsrecht*), which seek responses to Europe's complex conflict constellations.[35] Democratisation through conflicts-law constitutionalism cannot deliver ready-made responses to the financial crisis, but it can nevertheless claim to provide perspectives for a return to a constitutional European condition. To substantiate this perspective with respect to *Pringle:* monetary policy, fiscal policy and economic policy are assigned to different levels of governance in the Union. They are, however, interdependent. In the terminology of the conflicts-law approach, this generates 'diagonal' conflicts. Their 'resolution' within Europe's crisis management is currently occurring through establishment of the primacy of 'the Political'. Conflicts-law constitutionalism, by contrast, would require legally structured (constitutionalised) cooperative deliberation.

[34] See the introductory chapter to Joerges *et al.* (2011), with contributions by A. J. Menéndez, F. Rödl, M. Amstutz, P. F. Kjaer, M. Herberg and M. Everson.
[35] See Everson and Eisner (2007: 13 ff.; 22 ff on *Rechtsverfassungsrecht*) and Joerges (2010).

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Chapter 10

The European crises and the undoing of the social and democratic Rechtsstaat

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> I reject the intellectual glamour of pessimism that has become pervasive in Europe and that does not lead to any good
>
> Jose Manuel Durao Barroso, 9 December 2012[1]

> The purpose of studying politics is not to acquire a set of ready-made answers to [political] questions, but to avoid being deceived by [politicians].
>
> Joan Robinson, slightly edited[2]

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1 The phrase 'glamour of intellectual pessimism' seems to have become a favourite of Barroso (or of his speechwriter(s)). First time I came across it was in a February 2010 speech before the European Parliament, retrieved from: <http://europa.eu/rapid/press-release_SPEECH-10-21_en.htm> (last accessed 4 April 2014), then it was repeated in October 2010 speech in Brussels, retrieved from: <http://europa.eu/rapid/press-release_SPEECH-10-559_en.htm> (last accessed 4 April 2014), and finally in March 2011, in Ghent, retrieved from: <http://europa.eu/rapid/press-release_SPEECH-11-198_en.htm> (last accessed 4 April 2014). It pops up in the interview to *El País:* 'Barroso: "Los Gobiernos nacionalizan los éxitos y europeízan los fracasos"', *El País*, 9 December 2012, retrieved from: <http://internacional.elpais.com/internacional/2012/12/07/actualidad/1354883340_577802.html>. The quotation is taken from the latter.

> [P]lus des droits pour chacun […] c'est moins de pouvoir pour tous.
>
> Gauchet (2007 : 42)

Introduction

This chapter aims at providing answers regarding the *which* and the *whose* of the crises of the European Union and at offering a constitutional reconstruction and assessment of the decisions taken to govern and overcome the crises.

It is a platitude to say that the European Union is in crisis. But which crisis is it? Is it a crisis or a series of crises? The first section of this chapter aims at providing an answer to these questions. I claim that The European Union is not undergoing one crisis, but is instead suffering several simultaneous, interrelated, and intertwined crises – crises which are global, not exclusively European. My claim is double. Firstly, that we need to clearly distinguish between the 'triggering' factor (the subprime crisis), the underlying structural weaknesses (which predate the crises, which constitute the ground on which the crises have exploded) and the 'crises' as such. Secondly, that we are undergoing five major crises: economic, financial, fiscal, of macroeconomic management and political. The five are closely interrelated and indeed may well be reinforcing each other, heightening the damage that each causes as it unfolds. But there are good reasons to keep distinct each of the five crises. If only because when it comes to take decisions to contain and/or overcome the crises, it is necessary to consider the effects that each measure will have when dealing with each of the five crises.

But after asking 'Which crises?' one should unavoidably ask: 'Whose crises?', or making use of the terminology I propose, how did the European Union came to be plagued by the structural weaknesses that became open crises when the subprime crisis hit European soil? I claim in the second section that the European Union is not only experiencing these crises, but is significantly responsible for the underlying structural weaknesses in the first place. The

[2] The original quote can be found in Robinson (1980: 17): ' The purpose of studying economics is not to acquire a set of ready-made answers to economic questions, but to avoid being deceived by economists'

transformation of the institutional structure of the Union and the substantive policy choices made in the last three decades have fostered the very structural weaknesses that were turned into crises by the subprime crisis. In particular, it seems to me that the self-standing and disembedded understanding of economic freedoms, as expressions of the right to individualistic private autonomy and the creation of an asymmetric economic and monetary union, played a major role in destabilising the Union. In more procedural terms, the specific path followed by the process of European integration is also to blame for the accumulation of weaknesses.

So the Union is in crises which largely result from self-inflicted institutional changes and intentionally endorsed policy choices. But once in crises, what has the European Union done to contain the crises and to overcome them (what in more synthetic terms can be said to be a question about how the Union has governed the crises). In the third section, I reconstruct the government of the crises from a double but combined perspective. I take as my main source the legal texts in which the anti-crises measures have been reflected; but I try to determine what diagnosis of the causes of the crises and of the appropriate remedies underlies them. This leads me to the conclusion that notwithstanding the fact that decisions have been taken on the (constitutional) hoof, clear patterns can be discerned. However, the patterns also reveal that diagnosis and prognosis have shifted at least three times. When the analyses of causes and remedies are shifting, it is unavoidable that the government of the crises is inconsistent.

The crises are very real, and the government of the crises, based on shifting diagnoses and prognoses, have probably made things much worse. But if we stand aside for a moment, and consider not so much where the Union may be going, but how the Union looks like now, how the crises and the government of the crises have transformed the Union, what the answer should be? In the fourth section, I claim that the European government of the crises has unleashed a process of European constitutional mutation. What have been presented as exceptional and temporal measures, have resulted in a major constitutional mutation that has aggravated the already looming tension between this European Union and the European constitutional and political project, as enshrined in the Social and Democratic *Rechtsstaat* at the core of postwar national constitutions, Social and Democratic Rechtsstaat that consequently also underpinned the original European Communities. A key factor in this transformation is that, no matter how shifty the diagnoses and the prognoses, the government of the crises has reinforced the normative and factual standing of the rights of capital holders to see their capital protected, with ample resort to the nationalisation of the losses resulting from financial risk, including the massive risks resulting from the creation of money by financial institutions.

What should then we do, Spinelli? As things stand, neither a reformist strategy (a change in course of policy within the present Treaty and the emerging *para-Treaty* framework) nor a constitutional rupture strategy (via a constituting assembly with a democratic mandate) seem like viable strategies to undertake a democratic rescue of the European Union. If any path holds promise, it is that of national constitutional resistance, based on challenging the policies and decisions of the recent years - especially the last five years – on the basis of the deep constitution of the European Union,[3] and the common constitutional law of the Social and Democratic *Rechtsstaat*. This might allow a reopening of political space and a return to a democratic understanding of constitutional law. Only then would a democratic re-constitutionalisation of the European Union be possible. The future, however, looks very bleak.

Five crises, not one crisis

My first thesis is that we find ourselves in the midst of five closely interrelated crises, not just one. In my argument, I propose to distinguish the following three principles: (1) Five different structural weaknesses of Western socio-economic systems as they stood circa 2007 (economic, financial, fiscal, macroeconomic, and political); (2) the catalytic event of the crises (the US subprime mortgage crisis that started in 2006/2007 that was close to shutting down the global financial system in 2008); and (3) the ensuing five crises, which are the result of the catalytic event turning structural weaknesses into crises. Or to put it differently, five different crises were unleashed by one single catalytic event, which should not be confounded with the

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3 By the deep constitution of the European Union I mean the collective of national constitutions (usually refer in the Community law jargon as 'the constitutional law common to the Member States', the 'common constitutional traditions'). This collective is reflective of the underlying social and economic fundamental norms which underpin the regulatory ideal of the Social and Democratic Rechtsstaat.

crises themselves, no matter how interesting, relevant and revealing the study of the subprime crisis may be.

Five structural weaknesses

Crises do not fall from the sky. They are all the consequence of precedent, institutional designs, procedural arrangements, implemented policies, wrong decisions, and non-decisions.[4] A good start at unpacking the crisis is to distinguish five different structural weaknesses of the Western socio-economic order – including, quite obviously, the socio-economic order of the European Union in – circa 2007: Economic, financial, fiscal, macroeconomic, and political.

First, there was a major underlying *economic structural weakness*, resulting from the fact that while the socio-economic model was based on the assumption that high and sustained increases in the capacity to produce goods and services were possible – resulting in a constant increase in overall wealth – growth patterns had fallen behind expected rates since the 1970s and had indeed been constantly decreasing in the last thirty years (see Eichengreen 2008). The postwar Western social contract assumed the possibility of reconciling the interests of workers, capital holders, and citizens' – roles which overlapped in many cases – through sustained high rates of growth of at least three to four per cent per annum (see tables 10.1 and 10.2). Such high rates of growth made possible the simultaneous achievement of sustained income and wealth increases, high levels of investment, and revenue to fund and expand the key pillars of the welfare state (education, health and pension payments) (See tables 10.3, 10.4 and 10.5). Since the early 1970s, however, no Western country has achieved such high and sustained economic growth (see tables 10.1 and 10.2 for European countries). To the contrary, growth has tended to constantly diminish.[5] Tolerance of inflation and private Keynesianism were two different but equally unsustainable strategies to avoid and/or overcome this structural weakness (Crouch 2011; Streeck 2011). The former strategy was revealed to be a short-lived means of

[4] On non-decisions, see Bachrach and Baratz (1963); Strange (1986: especially ch. 2, 1988).

[5] The only exceptions to this rule have been countries which engaged into the wildest form of financial and fiscal excesses. We know now – and we should have known all the time – that doping growth through an inflow of foreign capital is highly likely to lead to financial bubbles and later misery.

avoiding the problems at the cost of aggravating them, while the latter resulted in a massive redistribution of income and wealth, the devastating effects of which could only be temporarily compensated for by a massive and unsustainable growth of private debt.

Table 10.1: GDP growth in historical perspective (%)

	1913–1950	1950–1973	1973–2000
Western Europe	1.1	4.5	2.1
Peripheral Europe	1.2	6.0	3.4
Eastern Europe	1,7	4.7	-0.2

Source: Eichengreen, B. (2008) *The European Economy since 1945*, Princeton: Princeton University Press, p. 16.

Table 10.2: GDP growth in historical perspective, selected EU countries, decade averages (%)

	1960s	1970s	1980s	1990s
Belgium	4.41	2.21	1.34	1.51
Denmark	3.02	0.70	1.51	2.46
France	4.72	2.16	1.24	1.00
Germany	4.23	2-49	0.79	1.71
Italy	5.59	3.27	1.37	1.08
Netherlands	3.95	1.40	0.66	1.20
Spain	7.04	2.59	2.06	1.80
United Kingdom	2.29	1.35	2.31	1.44

Source: Heitger, B. (2001) ‘ The Scope of Government and Its Impact on Economic Growth in OECD Countries, Kiel Working Paper No. 1034, Kiel: Kiel Institute of World Economics. Retrieved from: <http://www.ifw-members.ifw-kiel.de/publications/the-scope-of-government-and-its-impact-on-economic-growth-in-oecd-countries/kap1034.pdf> (last accessed 8 April 2014)

Table 10.3 Public expenditure on education relative to GDP (%)

	1937	1960	1980	1993/94
Belgium	*n.d.*	4.6	6.1	5.6
France	1.3	2.4	5.0	5.8
Germany	*n.d.*	2.9	4.7	4.8
Italy	1.6	3.6	4.4	5.2
Netherlands	*n.d.*	4.9	7.6	5.5
United Kingdom	1.1	4.0	4.3	5.6

Source: Tanzi, V. and Schuknecht, L. (2000) *Public Expenditure in the XXth Century*, Cambridge: Cambridge University Press, p. 34.

Table 10.4 Public expenditure on health relative to GDP (%)

	About 1930	1960	1980	1994
Belgium	0.1	2.1	5.1	7.2
France	0.3	2.5	6.1	7.6
Germany	0.7	3.2	6.5	7.0
Italy	*n.d.*	3.0	6.0	5.9
Netherlands	*n.d.*	1.3	6.5	6.9
United Kingdom	0.6	3.3	5.2	5.8

Source: Tanzi, V. and Schuknecht, L. (2000) *Public Expenditure in the XXth Century*, Cambridge: Cambridge University Press, p. 38.

Table 10.5 Public expenditure on pensions relative to GDP (%)

	1937	1960	1980	1993
Belgium	3.7	4.3	11.2	10.9
France	*n.d.*	6.0	10.5	12.3
Germany	*n.d.*	9.7	12.8	12.4
Italy	*n.d.*	5.5	11.7	14.5
Netherlands	*n.d.*	4.0	12.6	13.4
United Kingdom	1.0	4.0	5.9	7.3

Source: Tanzi, V. and Schuknecht, L. (2000) *Public Expenditure in the XXth Century*, Cambridge: Cambridge University Press, p. 41.

Second, there was a major underlying *financial structural weakness*, resulting from an unsustainable growth of financial assets and a radical transformation of the actual purpose and role of financial institutions. These financial institutions largely abandoned their role as intermediaries between private savers and non-financial enterprises, becoming key operators of increasingly self-referential financial markets. The financial turbulence unleashed by the end of Bretton Woods created an overnight demand for financial products that *covered* against exchange losses, which subsequently fanned the flame of the transnational financial markets that had been slowly gaining ground in the 1960s, and quite significantly, the Eurodollar market (Block 1977; Brenner 2006; Lesson 2006). The growth of the financial industry, even if partially propelled by the wish to *hedge* against risks, actually multiplied the existing risks, only that for a long period, it was widely believed that such risks were first and foremost opportunities, something that seemed self-evident from the constantly high level of profits of financial investments (Strange 1986; see also Strange

1998). This created the wrong impression that financial investment was a much better investment opportunity than non-financial activities. Financialisation and the transformation of the role of financial institutions were further sped up by technical and conceptual innovations in financial theory that were said to have resulted in the elimination of financial risk through adequate economic modelling and pricing.[6] Risk was no longer to be managed through risk assessment, but was simply assumed to be eliminated when appropriate economic modelling was resorted to.[7] The short-term profitability of the new financial products was facilitated by a permissive approach to regulation and taxation of financial activities by the reopening of old markets, such as those of China and the whole of Eastern Europe, including Russia, which had been largely closed to capitalists by the triumph of communist regimes, and by the shift of the control over the monetary base and the power to create money from governments to central banks, and then from central banks to private banks (Mellor 2010). With financial increases at constant double digit levels and non-financial profits not recuperating in a sustained manner, profits were increasingly reinvested in the financial sector, thus further feeding the growth of the financial sector (Hudson 2012). In such a context, it was only a matter of time before it was assumed that the financial sector had found the means of emancipating itself from its role as an auxiliary of the non-financial sector and had become an alternative growth driver itself. It came to be believed that the declining rates of economic growth (resulting from the first structural weakness) could be compensated for by the growth of the financial sector.[8] When this assumption was adopted, the belief spread that new economic models had wiped out risk, and

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[6] The point was presciently made by Susan Strange (see, for example, Strange 1986 and 1988). More recently, see Admati and Hellwigg (2013); Cassidy (2010); Dunbar (2011).

[7] If one is allowed to use the fashionable Euro-jargon, risk assessment ceased being regarded as a matter of discretion based on knowledge and experience, and began to be regarded as a matter of the mechanic application of the rules written into the economic models. See Derban (2011); Dunbar (2011); Lewis (2010a; 2011); Mellor (2010); Patterson (2010). A journalistic account is Tett (2009).

[8] The financial crisis of 2006 and 2007 has revealed the extent to which these premises were simply false. But because financialisation had become pervasive and enduring in time, it had basically turned the financial sector into a deadweight loss for the economy as a whole. That was true throughout the period, but was covered up by the appearance of buoyance in financial activities and investments.

the fictitious capital started to grow exponentially.[9] The inflation of financial assets was, however, a pattern tolerated, not welcomed, by the central banks of Western countries, including the European Central Bank from its inception. Asset inflation was regarded as innocuous – contrary to what was the case with inflation in non-financial assets – if not beneficial.[10]

Third, there was a variable *structural fiscal weakness* that consisted of a declining capacity of states to implement their tax and regulatory legal frameworks in a fair and sufficient manner. Starting in the early 1970s, all Western states had experienced the decline of the knowledge about the income and the wealth flows subject to their regulatory and tax jurisdiction (Block 1977; Helleiner 1994). This decline in the cognitive basis of tax and regulation activities is a direct consequence of the specific kind of financialisation that we have experienced in the last decades, a mode of financialisation that is closely associated with transnational financial markets growing in a legal and economic space where they place themselves beyond the reach of national regulatory and tax authorities – always, quite obviously, with the support of some of the sovereign states, or a variable coalition of them.[11] Providers of financial services, including banks, operated as key intermediaries between the national and the transnational, and in so doing, eventually eased the way for capital holders to make use of transnational investment opportunities to avoid paying taxes were they were due.[12] The undermining of the

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[9] An analysis based on a historically sophisticated and nuanced understanding of the role of finance in the economy in Amato and Fantacci (2012a; partially followed by 2012b).

[10] Despite the fact that not only its long-term effects, but also its short-term effects, were deleterious. It suffices to consider the implications that asset inflation has had in the geographical configuration of cities – in particular, the radicalisation of the processes of spatial segregation.

[11] The 'recovery' of international financial markets which rendered organisationally possible the financialisation of the economy and the financial crisis created the conditions for undermining the cognitive basis of tax states. A development seen with calculated ambivalence by the Commission since the 1960s, as the Euromarkets were at the same time unregulated, and thus a challenge to the European Communities as a polity in the making, and powerful forces of integration of financial markets in Europe, breakers of the national barriers to the creation of 'deep and liquid' financial markets operating across borders.

[12] Tax havens were never external challenges or threats to the European – and American, and Japanese – financial system, but the creatures of the European – and

cognitive basis of tax states led to the erosion of the state capacities to implement, in a fair and effective manner, their tax and regulatory norms. Three compensatory strategies were developed. First, the erosion of the tax base and of the tax knowledge was expected to be contained by means of reducing the tax burden to mobile sources of income, in the hope of keeping mobile taxpayers in the tax rolls, even if at reduced rates of contribution. The re-dualisation of the income tax, pioneered by the Scandinavian countries in the 1980s, was but the first instance of this pattern (Sørensen 1993).[13] Fiscal amnesties were different means of seeking a rather similar result (Mahlherbe 2011). Second, some states have engaged in the co-optation of financial enterprises, offering as incentive the incorporation in their jurisdiction of a financial regulatory framework in line with the interests of financial capital holders (the so-called light touch financial regulation) – a form of 'financial regulation lie'.[14] By means of attracting the headquarters of companies providing financial services, some states aim at compensating for the general loss of tax capacities and revenue with the revenue resulting from the abnormal concentration of financial companies in their jurisdiction. Alternatively, states have attracted both non-financial and financial companies by creating a regulatory framework and providing a set of bilateral tax treaties that facilitate the minimisation of overall tax burdens. While the United Kingdom is a paradigmatic example of the first strategy, the Benelux and Ireland are good examples of the second

American, and Japanese – financial systems. See Brooks (2013); Deneualt (2010); Murphy (2013); Palan, Murphy and Chavagneux (2010); Shaxson (2011).

[13] On the recent German debate, see German Council of Economic Experts *et al.* (2008).

[14] On light touch financial regulation, see Krippner (2011). The 2009 review of the British Financial Services Authority (the so-called Turner Review) is a scathing criticism of that approach to financial regulation, retrieved from: <http://www.fsa.gov.uk/pubs/other/turner_review.pdf> (last accessed 8 April 2014). The geographical implications of light touch regulation, fundamental from a tax perspective, are considered by Dariusz Wójcik (2013). The very light taxation of the so-called 'non domiciled' persons (the 'non-doms') is a complementary element in the British strategy of maximisation of tax revenue through the attraction of financial activities into London. The tax treatment of non-doms is heavily criticised in the Christian Aid report *Death and Taxes: The True Toll of Tax Dodging* from 2008, retrieved from: <http://www.christianaid.org.uk/images/deathandtaxes.pdf> (last accessed 8 April 2014).

strategy (Van Dijk *et al.* 2007).[15] Third, other states relied on speculative activities and financial bubbles to compensate for the loss of revenue, or even to fund the electoral decision to reduce the tax sacrifice demanded from stable revenue sources. This was the case in Spain and Ireland during the last decade.[16] In all cases, the tax gap (the difference between what should have been collected under the application of the tax law and what actually was collected) has tended to grow as a result of this growing cognitive gap of the tax state. The extent, depth, and evolution of this structural weakness, however, are variable and depend on the specific resilience of the adaptive strategies followed by each state.[17]

Fourth, there was a growing *macroeconomic structural weakness*: A progressive loss of the pulls and levers through which states could steer the economic ship and insure citizens against the uncertainties of the future – to the extent, quite obviously, that this is possible. This resulted from two major developments. First, states lost some of the key means to conduct macroeconomic policy as a direct consequence of the collapse of the postwar monetary order. Both political decisions and non-decisions led to the failure of the Bretton Woods system, through which the Western community, led by the United States as

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[15] See also the reports on the different EU member states in the Financial Secrecy Index, available at: <http://www.financialsecrecyindex.com/> (last accessed 8 April 2014). On the relationship between tax evasion and financial deregulation, see De Maillard, 2011. In the run up to the third phase of monetary union, the European Commission wrote different reports and put forward several initiatives on harmful tax competition (see especially 'Towards Tax Co-ordination in the European Union: a package to handle harmful tax competition', COM (97) 495, 1 October 1997, retrieved from: <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:1997:0495:FIN:EN:PDF>, last accessed 8 April 2014). The reports, which were far from radical, were shelved. On the literature, see Bratton and McCahery (2001); Kiekebeld (2004). On tax competition in the EU see Pinto (2003).

[16] On Ireland, see McCabe (2011), on Spain, see Naredo and Álvarez (2011).

[17] The third strategy is clearly the less resilient, given not only its immediate sensibility to an economic downturn, but also the fact that it is associated with the fostering of a particularly unsustainable economic model. The resilience of the first strategy clearly depends on the residual tax 'ethics' of taxpayers. Of the two 'exploitative' strategies, the one based on fostering a national tax evasion industry is probably the more robust, as it less prone to cyclical downturns and it does not entail massive contingent liabilities from the financial sector when and if it goes into trouble.

monetary hegemon, ensured monetary and financial stability.[18] The very failure of Bretton Woods undermined the very preconditions that rendered operative and effective some of the fundamental macroeconomic pulls and levers (Scharpf 1991). Second, public macroeconomic powers tended to be split and fragmented. While in the early 1970s only Germany and Switzerland favoured the model of an autonomous central bank setting monetary policy without political interference, by the early 1980s the debates on the creation of an autonomous central bank were being won by those favourable to such an arrangement, vindicated by the apparent track record of the Bundesbank, which was regarded as having played a key role in turning Germany into a model of price contention and economic growth (Leaman 2001). Third, the efficiency of macroeconomic pulls and levers was highly undermined by the general trend to lift not only trade barriers, but also most obstacles to any kind of economic activity, including financial activities across borders. Trade liberalisation, without some form of political countervailing institutionalisation could do nothing but undermine the actual capacity of States to make use of macroeconomic levers, no matter the persistence of such formal powers.[19]

Finally, the legitimacy and stability of democratic political systems was severely challenged, resulting in major *political structural weaknesses*. The various processes that have already been described resulted in a schizophrenic political transformation. The two oil crises of the 1970s undermined the postwar Keynesian consensus, radically transforming the shape and structure of public discourse in democratic states, and also undermining the underlying consensus about the very point of transnational and supranational institutional

[18] See Strange (1986, 1988) on the relevance of non-decisions; and Brenner (2006) on the structural economic background of the demise of Bretton Woods;

[19] This was indeed a central argument in favour of moving from European Monetary System (EMS) to European Monetary Union (EMU). See Padoa-Schioppa (1988: 373): 'Unless new items are added to the agenda, the Community will be seeking to achieve the impossible task of reconciling (1) free trade, (2) full capital mobility, (3) fixed (or at any rate managed) exchange rates and (4) national autonomy in the conduct of monetary policy. These four elements form what I call an 'inconsistent quartet': economic theory and historical experience have repeatedly shown that these four elements cannot coexist, and that at least one has to give way'. On the role of political decisions in the unleashing of finance, see Krippner (2011); on the European lead on liberalising capital movements, see Abdelal (2006, 2008).

structures.[20] As a result, a second rescue of the weakening nation-states through transnational arrangements and supranational institutions became problematic, if not impossible. The neoliberal agenda did not only threaten the social and democratic *Rechtsstaat* at home, but it also undermined the capacity of the supranational level of government to become a key instrument in the creation of the structural conditions under which the Social and Democratic *Rechtsstaat* could flourish. As a consequence, the shift from national to supranational democratic politics has not only stalled, but has been reversed, at least in public narratives (a phenomenon usually referred to within Europe as the end of the permissive consensus on European integration). In actual practice, however, the disempowerment of nation-states has been accelerated by the transformation of transnational and supranational institutions from frameworks of public cooperation to structural fosterers of regulatory and tax competition. As a consequence, the structural capacity of states to organise collective action has declined without being replaced by any other institution. Power has consequently shifted from the public to the private realm, to the institutions of power based on the capital medium. The serious, and growing, mismatch of the political aspirations inscribed in the fundamental laws of the nation-states, and of the European Union, and the actual incapacity of nation-states, and the European Union, to act in a way responsive to democratic will formation has resulted in a structural democratic crisis.

The catalytic event

All of these structural weaknesses accumulated over a long period of time: Roughly speaking from the last years of the Bretton Wood system through to the present. The subprime crisis hit the United States economy in the last quarter of 2006 and hit the world economy, at the latest, by August 2007.[21] The original reaction of institutional actors, both politicians and central bankers, was to minimise the breadth and scope of the crisis.[22] That would have been reasonable if

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20 On neoliberalism as a pragmatic political movement, see Harvey (2007, 2010); Dumenil and Levy (2004); Panitch and Gindin (2012).

21 For a general narrative of the catalytic event, see Lybecj (2011).

22 For example, Jean Claude Trichet has claimed: 'The euro has been a remarkable success', see his address at the ceremony to mark the 10th anniversary of the European Central Bank and the European System of Central Banks, 2 June 2008, retrieved from: <http://www.ecb.int/press/key/date/2008/html/sp080602.en.html

a similar crisis had erupted four or five decades earlier. A crisis in the US subprime market should have been a manageable crisis. After all, the subprime market was a small part of the US mortgage market, which in and of itself was a relatively small part of the set of global financial markets. The crisis, however, was very hard to contain because the unsustainable growth of the US subprime market was indeed a symptom of the deep and grave structural weaknesses to which I have just referred. The consequences of the subprime crisis were not proportional to the intrinsic dangerousness of the subprime crisis itself, but to the structural fragility of the socio-economic order. By hitting the weak financial spot of the central national economy of the world system, the subprime crisis transformed the abovementioned five looming weaknesses into five mutually interacting crises.

What do we gain by thinking of the crisis in the plural?

By thinking of the crises within the analytical framework put forward in this section, it seems to me that we derive four main advantages. First, we avoid collapsing the triggering process (the catalytic event) into the underlying crises themselves. More than five years into the crises, it is simply implausible to continue to claim that, 'Were it not for the subprime excesses, were it not for the decision to allow Lehmann to fall', there would have been no crises in the first place, a claim which was occasionally made in the early months of the crises.[23] The subprime crisis was the final drop into a glass that was

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> (last accessed 8 April 2014). Trichet was explicit in rejecting self-complacency, but in the list of the challenges facing the Union one finds none of the main challenges which it has been confronted since. He also stated that: 'In recent months we have seen another benefit of the euro: the financial crisis is demonstrating that in turbulent financial waters it is better to be on a large, solid and steady ship rather than on a small vessel. Would Europe have been able to act as swiftly, decisively and coherently if we did not have the single currency uniting us? Would we have been able to protect many separate national currencies from the fallout of the financial crisis? I believe that we can be proud of the reaction of European authorities, parliaments, governments and central banks. Together we have shown that Europe is capable of taking decisions, even in the most difficult circumstances'. See the summary of his speech 'The euro@10: achievements and responsibilities', 13 January 2009, retrieved from: <http://www.eu-un.europa.eu/articles/en/article_8411_en.htm> (last accessed 8 April 2014).

[23] On the 'No Lehmann, no crisis' frame of mind in late 2008 and early 2009 the op-ed by Neill Ferguson is very revealing and instructing: 'Why a Lehman deal would not have saved us', *Financial Times*, 14 September 2009, retrieved from: <http://www.ft.com/intl/cms/s/0/f96f2134-a15b-11de-a88d-

already full. Had it not been full, the authorities would have actually been able to contain the subprime crisis quite easily.

Second, moving from the singular crisis into the plural crises, we avoid pushing all symptoms and all consequences of the crises into one single and amorphous box called *the crisis*. Collapsing all crises into one crisis is the best strategy to prolong the confusion and avoid the allocation of responsibilities. But it prevents any serious discussion about what went wrong (which entails setting the crises in their historical context and elucidating the process which nurtured the weaknesses and contributed to the gathering of the crises) and what can be done to make things right (which entails mobilising the knowledge of the past to shape the future). This leads me, quite naturally, to emphasise that the main point I am trying to make is not that the crises are five and only five – these five – but that we have to disaggregate the crisis. Perhaps other distinctions should be drawn; perhaps not all crises here described belong to the same level of analysis. But what seems to be of fundamental importance is to avoid the singular and go for the plural – to move from crisis talk to crises talk in a structured way.

Third, the five crises here distinguished allow us to gain perspective, both in geographical and in temporal terms. On the one hand, it allows us to understand why the crisis is not American or European, but rather global in scope, even if the sequence of the crisis, and the virulence of its different symptoms, varies across time and space. On the other hand, it helps us avoid the tendency to focus exclusively on the most recent crisis episode in a fully de-contextualised manner. In particular, it helps avoid the temptation not only of reducing the crisis to the subprime crisis – as already hinted – but also of reducing it to its financial dimension. There is no doubt that there is a serious financial crisis going on, and that such a crisis is especially intense in Europe, with European banks in a more fragile state given their

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00144feabdc0.html#axzz2Rz0InhG6> (last accessed 8 April 2014). While Ferguson plays down the relevance of the no-rescue of Lehmann, he does so *against the current*, describing in detail mainstream opinion on the matter. Let me only add that while it seems to me that Ferguson has a point, the reasons why he finds the failed rescue of Lehmann a non-decisive moment are very different from mine.

world record levels of leveraging.[24] But there is also no doubt that the financial excesses that taxpayers are now being forced to pay for are more the consequence than the cause of the underlying economic and political weaknesses. The radical transformation of the financial sector and the overall financialisation of the economy would not have happened had it not been for the declining rate of profit in the non-financial sector. The attractiveness of financial profits accelerated the decline of investment in non-financial activities, resulting in the aggravation of the economic weakness. The pluralistic analytical framework forces us to consider the way in which the different dimensions of the crises are interrelated.

Finally, the analytical framework put forward in this section is not neutral – none is – but is widely ecumenical. While it is hard to reconcile with neoliberal socio-economic theory, if such things exists, it provides a framework compatible with ordo-liberal, liberist, liberal, social-democrat, or Marxist accounts of the crises. That Western economies have been experiencing a long economic crisis is something that both liberists and Marxists would agree upon.[25] They would disagree, however, on the ultimate causes of the phenomenon: Marxists may be inclined to refer to the secular decline of growth rates, while liberists would emphasise the stifling consequences of regulatory intervention, including the creation of booms and busts by central bankers. Both my analytical framework and indeed the rest of the chapter are compatible with both interpretations.

From five crises to the existential crisis of the European Union: Why the European Union bears major responsibility for the crises

My second thesis is that the European Union *is* the crises, or to put it in less blunt terms, that the European Union has played a significant

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[24] See the 2012 IMF Financial Stability Report 'The Quest for Lasting Stability', April 2012, World Economic and Financial Surveys. Retrieved from: <http://www.imf.org/external/pubs/ft/gfsr/2012/01/pdf/text.pdf> (last accessed 11 April 2014). 26 European banks have deleveraged considerably since 2007, but even after that they have barely reached the leverage levels of US banks in 2007. It goes without saying that such relative levels are not unrelated to the different role banks play in financial intermediation in the USA and in Europe.
[25] For a Hayekian view, see Beckworth (2012). A (heterodox) Marxist view can be found in John Foster Magdoff (2009), and in Foster and McChesney (2012).

role in the adoption of the decisions and policies which have ended up causing the crises. This largely accounts for what is perhaps the one-million-euro-question of the present crisis of the European Union: How come what started as a crisis in a small sector of the US mortgage market (the subprime market) has actually hit the European Union worse than the United States?[26] Part of the answer lies in the way in which the crises have been governed in the United States and in Europe, and to that I return in the next section. But another part lies in the fact that, when the subprime crisis hit, the European Union was in a more structurally fragile position than the United States. This was so because the Union had seen its resilience as a polity widely diminished by the transformation of its constitutional setup from the eighties onwards, and by the belated but substantive triumph of neoliberalism in policy terms at the European level. The present existential crises were, if the reader allows me the expression, a set of disasters waiting to happen.

Does this mean that I assign the European Union a primary or even exclusive responsibility for the crises? Certainly not. That would contradict the analytical framework I have put forward in the first section, as such a framework leads quite naturally to the conclusion that the crises are, if not global, at least as widespread as the dominant socio-economic model of financialised capitalism.[27] My claim is much more circumspect. In general terms, in section I, I affirm that there must be a relationship between the degree of responsibility of a political community for the gathering of the crises and the extent of its powers and competences. I find that either the political science and legal literature were wrong, and that, consequently, the

[26] The IMF estimated the losses resulting from the collapse of the subprime market in the USA at 500 billion dollars, which is a relatively small amount by reference to the size of the global financial market. Admati and Hellwig point that the dot.com bubble collapse caused losses six times that size (for a value of 3 trillion dollars) See Admati and Hellwig (2013: ch. 5).

[27] The 2007 financial crisis ignited a series of crises which were far from limited to the European Union. Clearly the rest of the western world was also hit badly. Areas of the world economy which seem to have been less affected, and even to have recovered from the 2008–2009 relapse by now, however, underwent in the past other financial crises closely related to the present one, and may indeed be hit in the future by new replicas of the underlying crises. Indeed, what was really shocking about the 2007–2008 crisis was not the pattern or sequence of the crisis (to a large extent a replay of previous financial crisis, with recent precedents in Russia, Asia or South America) but that it affected the wealthiest core of the world economy.

European Union was a largely powerless and irrelevant polity, or else it must be conceded that the European Union must have had a share of responsibility for the coming of the crises. In concrete terms, in the following section, I claim that the present understanding of the normative implications and substantive meaning of economic freedoms, next section, and the decision to create an asymmetric monetary and economic union, last section, played a fundamental role in the weakening of the European Union, in making of it a polity less capable of braving the rude sea of the crises.

The general case for the responsibility of the Union

The responsibility to be assigned to the different states and polities on the gathering of the crises cannot be anything but proportional to the clout and influence of each state and polity in the shaping of global and transnational, formal and informal, institutional structures and arrangements.

The Member States of the European Union explicitly agreed or tacitly coalesced to transferring to the Union fundamental competences regarding the moulding of the national and supranational – if these are different – socio-economic orders. Most of these competences are *negative* in character, based on *prohibiting certain courses of action to public institutions (and occasionally private actors*), with supranational institutions being empowered to enforce such prohibitions. The four economic freedoms and the principle of fair competition are paradigmatic examples of these powers.[28] However, the fact that the

[28] The quartet of economic freedoms enshrined in the Treaties of the European Communities are the free movement of goods, the free movement of workers (now redefined as free movement of persons), the freedom of establishment and the free movement of capital. In line with the original design of Bretton Woods, free movement of goods was given a specific and more reinforced status (trade in goods was the key element in the opening up of national economies to other European economic actors), agricultural products were given a rather different status (under the Common Agricultural Policy, under which free movement followed considerable state intervention in the business and conditions of farming), and free movement of capitals was essentially limited to free movement of payment and for all other purposes conditioned in its actual realisation to the taking of further integrative decisions. It was only in the eighties that the Court of Justice worked out a rather similar legal framework for all economic freedoms. Free movement of capital was given full status as an economic freedom by a 1988 Directive. As part of the package deal agreed in Maastricht in 1992 towards the achievement of monetary union, free movement of capital was extended to and from third countries (in the implicit

Union derives largely negative competences from such principles does not mean that enforcing such prohibitions does not result in a very specific moulding of the socio-economic order – indeed, that it thus proves the substantially biased character of the constitutional law of the Union, to which I return *infra* (Strange 1986, 1988). Other competences are positive, from agricultural policy to regional policy. The fact that some of these competences (the harmonisation of tax systems, for example) have not been exercised extensively, due to the structural difficulties to forge a common European will within the present institutional set up and decision-making procedures of the Union, does not mean that the Union did not have any power or competence in the matter, but only that the constitutional setup of the Union made unlikely its exercise, as, quite obviously, non-decisions can be as influential as actual decisions.

So it seems to me that it is quite plausible to claim that, by 2007, the European Union held some of the key powers and competencies through which the socio-economics of Europe were reshaped and remoulded in the last decades. But if the Union had key competences on socio-economic matters, the Union must be proportionally responsible for the present fragility of the socio-economic order and its lack of resilience in the face of the subprime crisis resulting in the unleashing of the five structural crises referred to above.

Allocating the exclusive responsibility for the crises on other polities (for example, to the United States or the Member States of the Union) and consequently depicting the Union as an innocent bystander is indeed only plausible if one shows that the European Union has been either a polity without actual clout or that the Union has opposed the substantive policies and institutional transformations that underpin the five structural weaknesses referred to above.[29]

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understanding that this will enhance the disciplinary potential of international financial markets over national fiscal policies). Undistorted competition completed the original economic constitution underpinning the Treaties with a view to curb the concentration of private power which could distort the allocative and cognitive rules of markets. Classical normative understanding in Robbins (1941[2011]).

[29] On account of its lack of actual influence, as is generally thought to be the case of the Arab League, the Nordic Council or the Council of Europe, or on account of the Union being a *longa manus* of some other polity or powerful actor – a smokescreen behind which the member states hid themselves – or the Trojan Horse of some or another hegemonic design, and many other silly conspiracy theories.

The claim that the European Union has had no clout in the shaping of the socio-economic order may arise from the implicit assumption that negative competences through the affirmation of negative constitutional principles do not render a polity influential at all; or, alternatively, from the assumption that if the consequences of the existent institutional setup and substantive constitutional framework are unintended, they cannot be blamed on any political community.

Regarding the first assumption, it is important to reiterate that the competences of the Union may well be more negative than positive, so that the core of Union powers are competences entitling the Union to prohibit or preclude public regulation, taxation, and, in general, action by national and local public authorities. Thus, the present understanding of the right to free movement of capital may not amount to much as an enabler of legislative, regulatory, and executive action of the Union, but that does not mean that the right of free movement of capital is less of a phenomenal instrument to shape, some would say bias, the socio-economic order. Negative integration is no less integration than positive integration, even if the distributive consequences of each kind of integration may well be very different, as it is the structural capacity of each type of integration to be moulded through democratic decision-making.

Regarding the second assumption, the fact that the structural consequences of certain negative powers, and of the general constellation of Union powers, may have unintended consequences (i.e. the fact that nobody wished the Union to be incapable of acting in a decisive and helpful manner at times of crisis) does not undermine my argument either. It may well be that nobody wished such a thing to be so, but that does not change the fact that this is a necessary consequence of the institutional setup of the European Union and of the substantive content of European Union law.

Furthermore, denying the power and influence of a European Union that has acquired manifold socio-economic competences would go against not only the extensive political science literature depicting the transformation of the European Union into an autonomous political community, system, or regime, but also against the extensive legal literature describing the evolving structural and substantive constitutional principles of Community law. Community law has increasingly stood in tension, if not contradiction, with some national constitutional principles. Indeed, the present institutional discourse that tries to deny that this is a European crisis is hard to reconcile with the past institutional discourse that celebrated the many achievements of integration.[30]

One could argue, alternatively, that the European Union has opposed or confronted the policies and institutional developments at the root of the crises. While a fashion of this line of reasoning seemed to emerge in the days following the collapse of Lehman Brothers (associated to the narrative according to which this was purely an American crisis), blaming the crisis on the specific socio-economic order of capitalism does not absolve the Union of responsibility.[31] As I have already suggested, and will show in more depth later, the European Union has played a key, if far from exclusive, role in shaping contemporary financialised capitalism.[32]

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[30] See, for example, Bendit and Verhofstadt (2012).

[31] European institutions were largely very optimistic in the early days of the crisis, emphasising the 'protection' that EMU extended to the Union. See European Commission (2008) 'EMU at Ten', European Economy 2/2008, retrieved from: <http://ec.europa.eu/economy_finance/publications/publication12682_en.pdf> (last accessed 11 April 2014), p. 5: 'EMU has improved the euro area's resilience against adverse external developments. In its first decade the euro area has been exposed to a series of external shocks associated with the global business cycle, the most significant being the bursting of the dotcom bubble and subsequent downturn in the US in the early 2000s. Nevertheless, the ensuing slowdown in the euro area at the beginning of the decade was considerably more muted than in comparable episodes prior to the adoption of the single currency. Today once again, the euro area appears protected from the worst of the present global financial turbulence. The anchoring of inflation expectations has contributed to this improved resilience, as have the reforms carried out under the Lisbon Strategy for Growth and Jobs and the renewed budgetary discipline since the SGP reform'. In early 2009, the President of the ECB was still depicting the actions of the ECB as a matter of avoiding 'contagion', referring to the USA in a polite fashion as 'advanced economies' (which probably comprised the United Kingdom). See 'Remarks by Jean Claude Trichet', Paris, 9 January 2009, retrieved from: <http://www.ecb.int/press/key/date/2009/html/sp090109.en.html> (last accessed 10 April 2014). The 'American' character of the crisis underlay Sarkozy's call to 're-found capitalism'. See his speech of 25 September 2008 in Toulon, retrieved from: <http://www.lemonde.fr/politique/article/2008/09/25/le-discours-de-nicolas-sarkozy-a-toulon_1099795_823448.html> (last accessed 10 April 2014).

[32] We could certainly move from the role of the European Union in shaping the structural weaknesses of the socio-economic order into the forces shaping the choice of policies within the European Union, but that would imply shifting the analysis from one level to the other, a movement that can be applied to all institutional actors

Specific factors contributing to the acute fragility of the Union in the face of the crises: The role of economic freedoms and asymmetric monetary union

If the Union was not an ineffectual union, it must bear a responsibility for the crises. But if the Union is perhaps not the only, or not the main, party responsible, how could the crises end up affecting the European Union worse than other polities? Answering that question requires focusing on the specific features of the European socio-economic order circa 2008 that rendered it peculiarly fragile when confronted with crises.

The mainstream line of reasoning (reflected in the official discourse that 'more Europe, and not less Europe' is needed to overcome the crises) claims that the existential crisis of the European Union is the direct consequence of the incomplete character of the European Union, and more specifically, of the governance of the eurozone.[33] The present existential crisis would be just another 'infant disease of the Union', a necessary, if disagreeable, episode in the unfolding of the process of creating an ever closer union.[34] Such a line of thought,

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(the Member States of the European Union, the United States or Japan, or for that matter, the IMF or Goldman Sachs) and would not result in any special discharge of responsibility in the case of the European Union.

[33] The analysis of the causes of the crisis, even when considering the structural failures or shortcomings of the constitutional framework of the European Union, especially of EMU, is always made part of an overall argument according to which the shortcomings or incompleteness of the process of integration played a major role in the gathering of the crises. This is a constant in all official documents. Consider one of the first analyses of the crisis (Council of the European Union, *Brussels European Council 15 and 16 October 2008, Presidency Conclusions*, 14368/08, 16 October 2008, retrieved from: <http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/103441.pdf> (last accessed 11 April 2014) with one of the latest (European Commission, *Blueprint for a deep and genuine economic and monetary union, Launching a European Debate*, COM (2012) 777 final/2, 30 November 2012, retrieved from: <http://ec.europa.eu/commission_2010-2014/president/news/archives/2012/11/pdf/blueprint_en.pdf> (last accessed 11 April 2014). One is left wondering how to characterise the existing EMU if we need a deep and genuine one. Perhaps as superficial and fake?

[34] This seems to be, for example, the underlying analysis to Beck (2013). Jürgen Habermas (2012) seems to have abandoned that understanding and favours a more nuanced approach, in which more Europe could be catastrophic if it is not the right kind of Europe. But see his speech in Leuven of 25 April 2013 (Habermas 2013), where not only a more benevolent assessment of the actions and policies of Council

however, besides its mechanist character, fails to consider that this crisis has hit the European Union worse than previous crises, such as the two oil crises of the 1970s.[35] How come this European Union, which was said to have become 'irreversible' thanks to economic and monetary Union and, consequently, 'more complete', reveals itself to be more fragile than the 'less complete' Communities of the 1970s.There are very good reasons to distrust the optimistic reduction of the existential crisis of the Union to a crisis of growth, and the overcoming of the crisis to the addition of allegedly missing blocks to the European constitutional structure, without seriously questioning the effects of the blocks that were previously added or those that are in line to be added.

Indeed, the analysis of the concrete responsibility of the Union in the gathering of the crises, and of the concrete factors that have made the Union especially vulnerable in the face of the crises, seems to me to require the consideration of the key planks of the European socio-economic order. In the following sections, I focus on two of these key planks, perhaps the most fundamental ones: First, I examine the present understanding of economic freedoms as the fundamental standards of the review of the European constitutionality of all European norms. Next, I examine the asymmetric design of economic and monetary union as decided in 1992 (with the signature of the Treaty of Maastricht) and implemented in 1999 (with the 'irreversible' fixing of parities and the start of operations of the European Central Bank). I consider how both planks came to be shaped, and how they nurtured the structural weaknesses described. The historical context of both planks seems to suggest that the fragility of this European Union is not intrinsic to the process of European integration as such,

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and Commission comes to the fore (technocratic bridging) but where the *topos* of incompleteness comes back.

[35] If the solution to the crises is completing and deepening integration, the implicit premise is that had the European Union been more complete and deeply integrated, it would have been more resilient to the crises. But why should there be a direct relationship between integration and resilience? The original Treaties contained numerous safeguards, exit clauses and emergency provisions. Many of which were eliminated in the name of further and deeper integration. This was clearly the case with the provisions regarding balance of payments crisis (see especially Article 108 in the original text of the Treaty Establishing the European Economic Community). In the absence of economic convergence and political union, resilience is not increased, rather decreased, by eliminating flexibility.

but to the concrete constitutional configuration of the present Union – a configuration that has been confirmed, not questioned, by the way the crises have been addressed at the European level, as we will see in the last section.

Economic freedoms: From internal to single market

The famous four economic freedoms (free movement of goods, free movement of workers – later of persons – freedom of establishment, and free movement of capital) were, by 2008, understood to operationalise the supranational right to individual, if not individualistic, autonomy. This supranational right to individual had been elevated by the European Court of Justice to be the yardstick of European constitutionality, defining the substantive validity of all national norms in an autonomous way from national constitutional law. This implied a major break with the original understanding of economic freedoms as operationalisations of non-discrimination, which not only entailed the respect of the socio-economic choices of the member states, but also the primacy of the decisions of representative institutions when it came to the shaping of the emerging supranational socio-economic order.[36] This new understanding was instrumental in the nurturing of the several structural weaknesses referred to in the next section.

The founding Treaties of the Communities made economic freedoms a key means to achieving European integration. The redrawing of the political borders of the old continent (something implicit in the aim of achieving 'an ever closer Union'[37], which effectively boils down to a call for the development of an institutional means of solving conflicts and coordinating actions across borders) was thus to be achieved through the redrawing of economic borders.

There were, however, different understandings of how exactly that should be achieved. During the negotiation process, two different

[36] On the concept of non-discrimination, see Somek (2008, 2011).

[37] As is very well known, the phrase 'ever closer union', mentioned in the Preamble to the Treaty establishing the European Economic Community ('determined to lay the foundations of an ever closer union among the peoples of Europe'), has become established as a catchphrase with which reference is usually made to the need of always progressing in the direction of more Europe. It is quite obvious, however, that from a constitutional perspective quantity has to take the back seat of quality.

visions collided. On the one hand, ordo-liberals and liberists, who had in Ludwig Erhard a key representative, were of the view that economic freedoms should be the key instrument of integration, together with strong European anti-trust rules – what we could label as the *self-standing understanding of economic freedoms* and a forerunner of the present understanding of economic freedoms (see Blyth 2014: ch. 5; Foucault 2004[38]; Nicholls 1994; and the anthology of ordo-liberalism in Peacock and Willgedrot 1989). Individual economic actors, empowered by the economic freedoms, should be the drivers of integration. The actual exercise of their rights to economic freedom through the four economic freedoms would unleash an undirected process of harmonisation of the national regulatory and tax frameworks. According to that understanding, European integration should be a matter of disempowering states and empowering economic actors through the assignment of hierarchical and normative priority to economic freedoms. In such a way, European integration would contribute to the acceleration of economic integration worldwide (Erhard 1954). On the other hand, Christian-democrats and Social-democrats favoured a common market that would lead first and foremost to the opening of national markets to economic actors from other member states without endangering the capacity of each of the member states to decide on the appropriate mix of regulatory and tax policies. Economic freedoms should entail economic actors the right not to be discriminated against, but to be treated in the same way as national economic actors. This was something that, quite obviously, did not predetermine how economic actors should be treated or what kind of regulatory and taxing policies should be pursued as part of the public steering of the socio-economic order. Economic freedoms should be a formal¸ not substantive standard. Further integrationist moves, from the implementation of common national markets to the creation of a single market should be politically mediated, articulated by a harmonised common law, so that the regulatory and tax capacities lost at the national level will be regained at the supranational level.[39]

[38] Especially the lectures of January 31st, February 7th, 14th and 21th, and of March 7th; for the lack of attention in actual policy to the competition plank of ordo-liberalism, see Irene Oswalt-Eucken (1994).

[39] Probably the best theoretical account of this conception is to be found in Milward (1992, 2005).

In such a way, European integration would contribute to a managed process of economic integration at the global scale.

The tension between these two visions was reconciled by the usual constitutional technique of ambivalent drafting. In this case, the drafting of the founding treaties of the European Communities (hereafter, the Treaties), with the choice of an international treaty full of constitutional provisions being in itself a paradigm example of ambivalent drafting. At the end of the day, however, the literal tenor of the Treaties was tilted in favour of the embedded understanding of economic freedoms; the systematic reading of the Treaties supported the construction of economic freedoms as concretisations of the principle of non-discrimination on the basis of nationality for two main reasons. First, there was a separated treatment of, on the one hand, free movement of goods, and on the other hand, the other three economic freedoms. That by itself was reflective of the 'managed capitalism' paradigm of a very Keynesian flavour, according to which free movement of goods could only be liberalised, and the advantages resulting from trade reaped, if the structural conditions were created for a national regulation of the other factors of production, especially capital.[40] Especially revealing was the fact that the norms concerning agricultural policy were placed between the chapter devoted to free movement of goods and the chapter devoted to the other economic freedoms.[41] Even if the Treaties left open the concrete shape of agricultural policy, the general provisions written there assumed that the common agricultural market will be created and thoroughly steered by public institutions.[42] Something that corresponded to not only the actual policy choices of Social-democratic and Christian-democratic governments that were very much influenced by both the New Deal paradigm and by the very pressing needs of a devastated Europe, but also to the conception of

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[40] See Minsky (2008); Newton (2006) and Steill (2013), which is however a trifle too much focused on the pro-Soviet sympathies of White. A general descriptive introduction Meltzer (1983). The *locus classicus* on the characterisation of the postwar order as embedded liberalism is Ruggie (1982).

[41] Treaty Establishing the European Economic Community, Part II, Title II.

[42] See especially articles 38.4 and 39 of the Treaty Establishing the European Economic Community. Free movement in agricultural products will be rendered possible by a common agricultural policy achieving a comprehensive set of objectives, shaping agricultural production according to certain socio-economic values.

managed capitalism itself. Second, free movement of capital was depicted as an aspirational goal,[43] reduced in its operational dimension to the freedom of payments necessary to render effective the other economic freedoms, and very especially, free movement of goods (Art. 67.2).[44]

Moreover, the fundamental decisions taken since the early days of the process of integration strengthened the prevalence of the embedded conception. Perhaps the defining decision was the one on the apparently technical issue of the indirect taxation of exports within the common market.

The moment that coal and steel started to cross the borders, borders that have been rendered more porous by the Treaties, the question was raised of what should be done regarding the practice of reinstituting at the border the indirect taxes that were bearing on the export price of the exported goods. The German government, inspired by the ordo-liberal vision, claimed that no compensation should be made. The French government, advocating the alternative understanding of economic freedoms, claimed that full compensation should be made (Haas 1958: 60–63). The coal and steel community opted for the latter vision.[45]

All parties assumed, however, that this first decision was a mere temporary expedient, as the practice of compensation at the border was easily amenable to the hidden subsidisation of exports. The prevalent mechanics of indirect taxation rendered it almost

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[43] Article 67.1 of the Treaty Establishing the European Economic Community.

[44] Article 67.2 of the Treaty Establishing the European Economic Community.

[45] See 'Report on the problems raised by the different turnover tax systems applied within the common market: report prepared by the committee of experts set up under Order no. 1–53 of the High Authority, dated March 5, 1953, document 1057–53 of the High Authority, usually referred as the Tinbergen report. (*Rapport sur les problems poses par les taxes sur le chiffre d'affaires dans le marché commun établi par la commission d'experts institituée para la Haute Autorité, of the High Authority*), retrieved from: <http://aei.pitt.edu/34921/1/A1064.pdf> (last accessed 12 May 2014). And see Article 5 of Decision 30/1953 of May 2 1953, OJ of 4 May 1953, p. 109, retrieved from: <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=OJ:A:1953:006:TOC> (last accessed 12 May 2014): '[I]t shall be a prohibited practice within the meaning of Article 60 (1) of the Treaty to include in the price charged to the purchaser the amount of any taxes or charges in respect of which the seller is entitled to exemption or drawback'.

impossible to calculate, in an exact manner, how much indirect tax had been imposed on the exported good or service, opening the way to a too generous calculation on the side of the authorities of the state of export. To avoid such distortions was the main objective of the First and Second Value Added Tax (VAT) Directives, and later, the 'definitive' Sixth VAT Directive.[46] By adopting them, member states renounced their autonomy to define the base of indirect taxes, but in exchange were given full autonomy on the setting of VAT rates. That was in itself a way of coordinating state powers with a view to reconcile integration and national political autonomy. More significantly to our present discussion, the power to raise VAT was retained by the state where the good or service was consumed.[47] Such an arrangement was reflective of the drive to open up national markets, while preserving the structural capacity of member states to retain their regulatory and tax powers – the capacity to decide the different ways in which competing socio-economic claims should be reconciled.

Finally, the four-stage drive to a common market consisted in the removal of obstacles at the border to economic goods, actors and services from other member states, and not on a general reconfiguration of national regulatory and taxing norms. The 'single market without internal frontiers'[48] was understood not only as the vision of

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[46] First Council Directive 67/227/EEC of 11 April 1967 on the harmonisation of legislation of Member States concerning turnover taxes, OJ 71, 14 April 1967, 1301–1303; Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment, OJ L 145, 13 June 1977, 1–40.

[47] To be precise, the option for place of consumption (destination) as the connecting tax factor was supposed to be a 'temporary' arrangement, so that in due course VAT would be collected at 'source' (see the 1967 directive, previous note). The 'temporary' arrangement has lasted for decades, and there is no good reason to think that it will be concluded soon. Indeed, the European Commission has now become favourable to taxation at destination for reasons of political expediency. See European Commission, *Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee on the future of VAT: Towards a simpler, more robust and efficient VAT system tailored to the single market*, COM (2011) 851 final, 6 December 2011, retrieved from: <http://ec.europa.eu/taxation_customs/resources/documents/taxation/vat/key_documents/communications/com_2011_851_en.pdf> (last accessed 23 April 2014).

[48] The fashionable expression made popular by the Delors Commission with the 1985 White Paper *Completing the Internal Market,* White Paper to the European Council, COM (85) 310 final, 14 June 1985, retrieved from:

an ultimate and distant goal in need of being politically concretised,[49] but it was also assumed that (a) the timing and the means of achieving it should be decided politically, and that (b) the said objective required a process of positive integration of national socio-economic institutions and legal norms, which would result in the recreation of many of the state capacities at the supranational level.[50]

The prevalence of the embedded conception of economic freedoms would soon be challenged, and ultimately, overcame. Two events were perhaps decisive. First, the Luxembourg compromise resulted in the postponement *sine die* of the move towards qualified majority voting within the Council. This rendered the process of politically mediated integration – of legal harmonisation – prone to be constantly blocked, and consequently, tilted towards the status quo. It was not only that new regulations and directive were difficult to pass – although from the standpoint of the present European Union with a membership of 28 member states, finding an agreement among six member states seems an easy task to discharge – but already existing secondary law was difficult to amend.[51] This fostered the impression that confining integration to politically decided harmonisation was exceedingly slow, resulting in the *sclerosis* of the

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<http://europa.eu/documents/comm/white_papers/pdf/com1985_0310_f_en.pdf> (last accessed 23April 2014).

49 Indeed, the Treaty establishing the European Economic Community was only specific on the four stages leading to the common market, or perhaps to be more precise, to the opening of national markets to economic agents of all member states. On what a fully internal market would require, and how it was to be achieved, the founding Treaties were silent, if one leaves aside general open-ended principles and vague aspirations.

50 Under such circumstances, it was only natural that, for example, personal taxes remained the exclusive competence of member states, even if it was clear from the very first day that they should be Europeanised at some point if the aspiration of creating a single market was to be realised. In line with the general expectations concerning the political road to the internal market, it was assumed that there would be an actual transfer of effective taxing powers to the supranational level, preserving the capacity of public institutions – both European and national – of making use of personal income tax to raise most public revenue, redistribute income within the political community, and macro- and micro-manage the economy. In the meantime, economic integration should be pursued in such a way as to preserve the capacity of each nation-state to regulate, stabilise and correct each national economy. See Lipstein (1974) for the legal articulation of this understanding of the common market project.

51 This is indeed a key part of the joint decision trap, on which see Scharpf (1988).

European Communities. Second, the two oil crises of the 1970s challenged the postwar framework of managed capitalism, of which the embedded conception of economic freedoms was one fundamental part. The apparent failure of Keynesian policies, which seemed to be bound to lead to the odd combination of stagnation and inflation, contrasted with the apparent success of the more liberal approach followed by Germany, thanks to the structural role played by the Bundesbank (Leaman 2001; Scharpf 1991). The *neoliberal paradigm* became part of the mainstream, emerging from the radical wilderness to which it was confined in the 1950's and 1960's.

The re-discovery of the integrationist potential of economic freedoms was only a matter of time once the fight against inflation, and not full employment and growth, became the ultimate goals of economic policy. Slowly but rather firmly, a consensus emerged among European elites concerning the need of inverting the relationship between economic and political integration. In the absence of a thick political agreement on the way, it was hoped that if the complex relationships between economic, insurance, and political communities would be governed by means of accelerating economic integration, the European Communities could solve their mounting problems. In particular, Directorate General III of the Commission, seconded by the European Court of Justice and later by the Council of Ministers, proposed to re-launch European integration by placing market integration at the very centre of the project (Grin 2003). This meant focusing all energy on the completion of the 'internal market without internal frontiers', which was to be regarded as immediately realisable through the mutual recognition of national regulatory standards.[52] Accelerating economic integration to overcome political disagreement could not but lead to dis-embedding economic integration.

Contrary to the embedded understanding of economic freedoms, the project of the single market, as launched by the Directorate General

[52] White Paper on the completion of the internal market, note 48 above; European Commission, *Communication from the Commission concerning the consequences of the judgment given by the Court of Justice on 20 February 1979 in case 120/78 ('Cassis de Dijon')*, OJ C 256, pp. 2–3, retrieved from: <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:31980Y1003(01)&from=EN> (last accessed 9 May 2014).

III of the Commission under Gaston Thorn, and fully fleshed out in the famous White Paper under Delors (*ibid.*), presented economic freedoms as the concretisation of an individual right to private autonomy which, as hypothesised, had always been enshrined in the Treaties, a right autonomous from and transcending national constitutional law. As a result, European integration would not only require rendering porous national economic borders, extending to European economic actors the treatment provided to nationals, but actually reshaping the national socio-economic order in a way compatible with the said European right to private autonomy. The politically driven creation of a single market was substituted by the vision of the single market to be created through the mutual recognition of regulatory structures (Pelkmans 2006: 25ff).

This seemed to offer equal promise to actors upholding rather contrasting conceptions of what the European Union should become. It was welcomed by the growing number of political actors who blamed the economic crisis on the political meddling of the relationships between economic and insurance communities, which effected the Union, and who had been implementing an agenda which basically consisted of narrowing the community of social insurance and increasing the freedoms enjoyed by actors in markets (a double process of privatisation of communities of economic risk and of insurance). For such actors, the European Union held promise as the level of government at which the right constitutional norms could be set up to establish supranational markets. At the same time, and for different reasons, pushing for further economic integration without additional Europeanisation of the insurance and political communities was regarded as a promising alternative route to achieve the ultimate reconstitution of a coherent relationship between economic, insurance, and political communities at the supranational level. In particular, some of the actors upholding a federalising view of the Union came to believe that speeding up economic integration will necessarily result in strong demand for further social and political integration. For those actors, the Single European Act was indeed the kind of measure that was bound to generate the sequence of spill-overs[53] which would lead the Communities to the original

[53] This forms the core of the spillover mechanism, described by Haas (1958). The argument of the spill-over is the background of the key Neumark report of 1962, see 'Rapport du Comité Fiscal et Financier', retrieved from:

destination (political Union in a social-democratic fashion) only through a different route (Delors 1992; Abdelal 2008). In brief, neoliberals saw a major opportunity in the single market to ensure intellectual victory. Christian-Democrats and Social-Democrats warmed to the idea, betting that negative integration would revive the European project, and by itself create a supranational political constituency favourable to reregulation and redistribution at the European level, perhaps in a replay of the original dynamics unleashed by the Treaties of Rome.

The reconstruction of community law in the semblance of this new understanding of economic freedoms was a long process in which the European Court of Justice (ECJ) played a leading role under the instigation of the Commission. This occurred, as time passed, with the support of both the European Council and the Council of Ministers, even though the manifold political implications of the new understanding were largely kept outside public discussion, being presented as largely apolitical.

The first and perhaps fundamental move was contained in *Cassis de Dijon*.[54] The case concerned free movement of goods – in particular, the importation of a French liqueur into Germany. The ECJ would rule that a German law protecting consumers, albeit treating in a perfectly equal manner both German and imported goods, was to be regarded as breaching community law. A German supermarket (Rewe) had had trouble selling French *cassis* on account of the fact that the German authorities insisted on applying a national law that required that any *cassis* had a minimum alcoholic graduation that the French product did not have. It was clear that the rationale of the German law was to avoid the consumers being fooled by the arbitrary labelling of goods by exporters and/or retailers. To avoid confusion, German law reserved the use of the label *cassis* to goods meeting the expectations of the average German consumer (the

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<http://aei.pitt.edu/33686/1/A220.pdf> (last accessed 14 April 2014); English translation available at <http://www.steuerrecht.jku.at/gwk/Dokumentation/Steuerpolitik/Gemeinschaftsdokumente/EN/EEC%20Reports.pdf> (last accessed 14 April 2014)

54 Case 120/78 *Rewe-Zentral AG v Bundesmonopolverwaltung für Branntwein* [1979] ECR-649.

Teutonic person in the Clapham omnibus, if one is allowed to use a rather old fashioned expression).

Formally speaking the ECJ limited itself in its ruling to offer a general and abstract interpretation of the provision on free movement of goods enshrined in the Treaties:

[The concept of] measures having an effect equivalent to quantitative restrictions on imports contained in Article 30 of the EEC treaty is to be understood to mean that the fixing of a minimum alcohol content for alcoholic beverages intended for human consumption by the legislation of a member state also falls within the prohibition laid down in that provision where the importation of alcoholic beverages lawfully produced and marketed in another member state is concerned.[55]

However, the rationale of the *ratio decidendi* of the case goes further: a ban on *any* product that was legally sold in *any* other Member State of the Communities would, *prima facie*, constitute a disproportionate infringement on the constitutional principle of free movement of goods. Consequently, any national norm putting obstacles to the sale of goods legally available in another member state would be considered as a breach of a key European constitutional norm, and thus void unless there were countervailing reasons which could justify this infringement. While the ruling is phrased in general and abstract terms, it is hard to imagine how the German court could avoid the conclusion that the German law prohibiting the sale was to be set aside, as this complete selling prohibition was incompatible with Community law.

There is every reason to concur with mainstream scholarship in stressing the constitutional importance and relevance of the decision. But there are good reasons to contest the normative assessment of the ruling. The apparently innocent affirmation of the interposition of obstacles as an autonomous reason for declaring a national norm in breach of Community law implies a massive constitutional transformation.

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55 Para. 15 of the ruling, previous note.

First, it gives massive concrete legal bite to the structural principles of direct effect and primacy. First, *Cassis de Dijon* turns free movement of goods from a standard which could be used to declare national norms regulating the porosity of the border invalid into a full-fledged standard of European constitutional review, covering all national legal norms.[56] In other words, *Cassis de Dijon* transforms the power of review of the validity of national laws by reference to the constitutional principles of community law from a mouse, restricted to the national norms through which the economic border is established and reproduced, to an elephant, extending to the whole national legal order. Secondly, *Cassis de Dijon* emancipates the review of European constitutionality from the substantive content of national constitutional law. As long as free movement of goods was understood as a concretisation of the principle of non-discrimination, what community law required from national legislation was to merely extend the same treatment to European economic actors as that enjoyed by national economic actors. Free movement of goods as an embedded economic freedom was a formal constitutional yardstick, not a substantive one. The moment in which the breadth and scope of what constitutes a breach is shifted from a discriminatory norm to an obstacle, economic freedoms become autonomous substantive standards of constitutional review. This points to the progressive emancipation of Union law from the deep constitution of the European Union – the constitutional law common to the member states.[57]

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[56] Paras 13 and 14 of the ruling.

[57] Paradoxically not long after the European Court of Justice had come to render explicit the foundational role of the said common constitutional law. The transformation of economic freedoms was given constitutional salience by the fact that the legal services of the Council, Commission and European Parliament (on what regard the law-making process) and the European Court of Justice and national European courts at the adjudication stage, have come to accept that economic freedoms are the fundamental yardstick of European constitutionality, i.e. the substantive values according to which the validity of all European norms (derivative supranational norms and all national norms, including constitutional norms) is to be assessed. It is true that fundamental rights are also said to be a key part of the substantive constitutional law of the European Union, and that should be expected to make them part of the European canon of constitutionality. However, the peculiar synthetic constitutional path followed by the Union accounts for the fact that this is not the case. Fundamental rights were not originally included in the Treaties, an omission that has justified the case law of the Court which limits their salience to the review of the European constitutionality of supranational norms and decisions. That

Second, it shifts control of the process of integration from the political and – directly or indirectly – representative institutions of the Union to the ECJ and the national courts that feed the ECJ with preliminary references. In turn, the private economic actors are empowered by the case law of the ECJ to set aside all national norms in breach of EU law, even in national systems where constitutional courts enjoy a monopoly of constitutional review.

Third, it gives concrete content to the structural empowerment of private actors, especially those with the resources to be repeat litigants before European Courts, to mould the concrete socio-economic implications of Community law.

Fourth, the replacement of political harmonisation by the mutual recognition of regulatory standards operates a drastic revolution in the very understanding of the relationship among member states and national legal orders from one based on political cooperation and mutual self-reinforcement to one based on political competition and consequently mutual self-disempowerment.

Firth, the definition and status of free movement of capital was radically transformed in two steps. The first was the enactment of Directive 88/361, which aimed at overcoming the very secondary status assigned to free movement of capital.[58] Partly an addition to the single market drive consecrated in the Single European Act, partly a preparatory step in the long-winded negotiation that would end up launching an economic and monetary union in Maastricht, the Directive aimed at the complete liberalisation of capital movements within the Union. Very significant was the fact that while it was made clear during the negotiation process that an unqualified liberalisation would risk undermining the cognitive capacities of the tax state,

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implies that they are part of the constitutional yardstick only in these cases. In such a way the ECJ seems to avoid claiming to be the ultimate guardian of constitutional values, as national courts can keep playing that role regarding fundamental rights. Such an outright claim would be hard to sustain given the lesser democratic legitimacy of European constitutional law vis-à-vis national law. But even if less obvious, the claim to guardianship of the economic freedoms – and of the economic freedoms and not of fundamental rights in the same way – is actually even more problematic when juxtaposed to the claim of total primacy of Union law.

[58] Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty, OJ L 178, 08 July 1988, 5–18.

especially on what concerned capital income and cumulated capital wealth, no agreement was reached on parallel measures that would allow the avoidance of the erosion of the actual taxing capacities of the member states. The Directive, as such, was approved and entered into force nonetheless, its approval rendered easier by the fact that states were negotiating under the shadow of qualified majority voting. Any measures required to fight eventual tax evasion would have required unanimous approval at the Council, something highly unlikely in view of the interests at stake. The second major step was the double decision to formalise in the Treaties the new status of free movement of capital as a full-fledged economic freedom, and to extend its breadth to encompass movements of capital from and to third countries.[59] These new *erga omnes* understanding of free movement of capital (an exceptional understanding, as the other three economic freedoms only extend to the territory of the Member States of the European Union, or the European Economic Area) was a fundamental part of the design of the asymmetric economic and monetary union, as I will indicate later.

Sixth, the extension of the new understanding of free movement of goods to all other economic freedoms, a step which also implied blurring the distinction between economic freedoms suggested by the very structure of the Rome Treaty. The timing of this extension (the process started in 1991) with the judgment in *Säger*[60] seems to suggest that the decisions taken by the Council, both with Directive 88/361 and even more with the signature of the Maastricht Treaty, were

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[59] See Article 56.1 of the Treaty establishing the European Economic Community as amended by the Treaty of Maastricht: '[w]ithin the framework of the provisions set out in [that] Chapter, all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited'. Paragraph 2 states that, 'all restrictions on payments between Member States and between Member States and third countries shall be prohibited'.

[60] Case C-76/90 *Manfred Säger v. Dennemeyer and Co. Ltd.* [1991] ECR I-4221; Case C-55/94 *Reinhard Gebhard v. Consiglio dell'Ordine degli Avvocati e Procuratori di Milano* [1995] ECR I-4165; Case C-415/93 *Union royale belge des sociétés de football association ASBL v Jean-Marc Bosman, Royal club liégeois SA v. Jean-Marc Bosman and others and Union des associations européennes de football (UEFA) v. Jean-Marc Bosman*[1995] ECR I-4921; and after the entry into force of Directive 88/361, Case C-163/94 *Criminal proceedings against Lucas Emilio Sanz de Lera, Raimundo Díaz Jiménez and Figen Kapanoglu*[1995] ECR I-4821.

taken by the ECJ as political signals of endorsement of the new understanding of economic freedoms.

The structural implications of the disembedded understanding of economic freedoms seemed to have been suddenly noticed by the academic literature after the rulings in *Viking* and *Laval*, but the transformation had by then been ongoing for decades.[61] *Viking* and *Laval* may have rendered dramatically evident that the ECJ had come to believe that the force of fundamental constitutional principles was to be limited by the constitutional primacy of economic freedoms, but the ruling of the ECJ in these cases was in many senses a mere scribbling in the margins of the lines of case law which had brought under review of European constitutionality national direct taxes and national non-contributory pensions, to refer to only two paradigmatic examples.

This disembedding of economic freedoms contributed to accelerating the neoliberal turn in the whole of the European Union. The new understanding of economic freedoms empowered private actors, especially repeated players before the ECJ, to challenge all elements of national tax and regulatory systems, and, in the process, to deepen the breadth and reach of the rights to which they were now entitled. The ECJ transformed, as indicated, economic freedoms into yardsticks of the constitutionality of all national norms. But the ECJ being a court and not a legislature, the disruptive effect of judicial decisions could not be matched by the capacity of the ECJ to reconstitute in a coherent fashion the said tax and regulatory tax regimes. Moreover, the transformation of economic freedoms took place in the absence of any constitutional decision extending the competences of the Union. The transformation of economic freedoms was purely constitutional, limited to the horizontal effect of such rights as standards of European constitutional review.

[61] Case C-438/05 *International Transport Workers' Federation and Finnish Seamen's Union v. Viking Line ABP and OÜ Viking Line Eesti* [2007] ECR I-10779; Case C-341/05 *Laval un Partneri Ltd. v Svenska Byggnadsarbetareförbundet, Svenska Byggnadsarbetareförbundets avdelning 1, Byggettan and Svenska Elektrikerförbundet* [2007] ECR I- 11767; Case C-346/06 *Dirk Rüffert v Land Niedersachsen* [2008] ECR I-1989. See also case C-319/06 *Commission des Communautés européennes contre Grand-Duché de Luxembourg* [2008] ECR I-4323.

Finally, and perhaps decisively, this transformation came hand in hand with the establishment of a division of labour between the community decision making processes. While the empowering of the European Parliament and the creation of the co-decision procedure, which would blossom in the Maastricht Treaty, were welcomed as essential steps towards closing the democratic deficit of the Union, as a matter of fact, they had more ambivalent consequences. This is so because they resulted in forcing the splitting of issues that were really the same policy problem, depending on which procedure – the standard one that required unanimity in the Council, or co-decision that was based on majorities in the Council and the Parliament – the decision had to follow. Because the chances of getting measures passed were different under each of these processes, the legislative division of labour favoured a structural substantive bias at the core of Union law. In practice, measures which aimed at deepening the breadth and scope of economic freedoms were favoured, while measures aimed at modifying the distributive outcomes of market integration remained very easy to block. Under such circumstances, the joint decision trap was much reduced for measures tending in the direction of furthering a disembedded understanding of economic freedoms, while remained the same – and actually worsened as the membership of the Union grew – for measures aimed at rectifying the case law of the ECJ.

This new understanding of economic freedoms equally reinforced the underlying pattern of both privatisation of public enterprises and of marketisation of the structures of the public administration and of public services, while the liberalisation of economic activities – which failed to heighten the growth potential of European economies – had a major impact on the patterns of income distribution and contributed to the growth of inequalities *within* member states (Nicol 2010).

Moreover, the new understanding of free movement of capital as a full-fledged economic freedom gave a boost to the process of financialisation, opening up heavily regulated financial systems to international financial actors, and consequently, created new opportunities of financial development in less mature financial systems. It led to a dramatic increase of the structural opportunities to engage in a fully legal manner into tax dodging, not only by means of using the conduit of jurisdictions which operated *de facto* as a tax haven (Luxembourg or United Kingdom), but also through corporate tax planning via transfer prices, with the Benelux and Ireland playing a key role as states of incorporation for that purpose. The cognitive capacities of the tax state were given a new blow.

The capacity of European states to undertake investment or industrial policies was also severely undermined. Not only were public investments and public enterprises progressively subject to market rules, but the actual capacity to encourage investment in a specific sector or company was rendered extremely difficult. Ironically, at the very same time that competition law was being transformed by reference to the new standard of consumer welfare maximisation, so was a backdoor to the increasing toleration of private monopolies.

Finally, the new understanding of economic freedoms led to a juridification and judicialisation of citizenship. While embedded economic freedoms were enjoyed by Europeans in the states in which they were not citizens, the disembedded economic freedoms turned the doctrine of reverse discrimination into a mere expedient by means of which the ECJ reduces its workload or avoids entering, for the time being, too controversial of legal waters. Even if this development is coherent with the transformation of economic freedoms into operationalisations not only, and not mainly, of non-discrimination, but of the right to individual private autonomy, the fact of the matter is that this new understanding creates another means of influencing public policy in addition to representative democratic politics. The holders of economic freedoms who have the economic resources to become repeat players before the ECJ or the Commission can influence policy in proportion not to the number of their co-citizens they manage to persuade, but by the depth of their pockets. The structural bias of the supranational legislative process, made worse by the Lisbon Treaty, increases the chances that they enjoy the full benefits of their repeated litigation undisturbed by rectificatory regulations or directives (Fossum and Menéndez 2011).

Asymmetric monetary union: The facilitating of financialisation and undermining of macroeconomic government, leading to a political crisis

The asymmetric economic and monetary union implied the definitive abandonment of the idea of the Union as a means of coordinating public policies in favour of an understanding of the Union as an instrument of enhancing competition between public policies in a narrow set of areas. This radical transformation of the European Union – and of the underlying political project – not only had consequences within the Union, but had deep global effects. The new understanding of the economic freedoms resulted in the Union leading the global juridification of the principle and practice of free movement of capital. The asymmetric economic and monetary union accelerated the global turn towards allegedly autonomous and seemingly technocratic central banks. Taken together, the new conception of economic freedoms and the asymmetric monetary union, created the conditions under which European banks, which play a much more central financing role of non-financial activity than in the US, became more exposed to the process of financialisation and were consequently extremely fragile when the 2007–2008 crises manifested themselves. Similarly, these two developments go a long way to explain the structural incapacity of European institutions to act in a decisive and meaningful way when the crises developed, and the choice of contradictory and damaging policies when the crises continued.

For two decades, the project of European integration was facilitated by the monetary stability provided by the Bretton Woods monetary system, a system that was largely successful in reconciling the liberalisation of free trade in goods with the creation of the structural conditions under which states could enjoy autonomy when defining their fiscal and macroeconomic policies (Bordo 2011). However, the hegemonic role assumed by the United States in the postwar monetary order created the conditions under which it was only a matter of time that the international duties of the United States', as a monetary hegemon, would collide with US democratically decided national fiscal priorities.[62] In the spring of 1971, Nixon had to choose

[62] Simultaneously, the reserve role of the US dollar was bound to be questioned by the very success of the dollar. The more dollars that were kept in non-US hands, the less credible the US gold convertibility pledge would become. That lack of credibility out of success was already nurturing currency instability in the mid-1960s. There was a clear consciousness of the limits of Bretton Woods at the European Commission. See European Commission, *Memorandum of the Commission on the action programme for the Community for the second stage*, COM (62) 300 final, 24 September 162, par. 128 on p. 63: 'But monetary policy is of vital importance to the Common Market from another point of view. From the end of the transition period on, if not even sooner, economic union will involve fixed rates of exchange between Member States with very narrow limits on the variations allowed. Any major modification would so

between, on the one hand, preserving Bretton Woods through deflating the US economy, and on the other hand, neglecting its hegemonic duties and gaining the room to manoeuvre necessary to foster growth, and in the process, obtain a second presidential term. Nixon opted for the latter and *de facto*, if not *de jure*, put an end to international monetary stability (Eichengreen 2011).

The early institutional projects and initiatives towards the establishment of a European common currency and a common European monetary policy resulted from the realisation that the Bretton Woods system was inherently unstable, and that its dismissal would destabilise the achievements of European integration, especially the common agricultural policy (based as it was on a system of public subsidies the value of which would become highly volatile) and the common market (as monetary turbulence would render investment in productive capacities oriented to exportation to other member states an almost impossible task). When Bretton Woods collapsed, not much had been achieved, but there was a clear consciousness of what was at stake for the Communities. A rapid succession of ineffectual plans was made to realise economic and monetary union. All failed until the 1990s. Monetary turbulence was kept within bound by more or less informal, 'grey' central bank cooperation (Saccomanni 2008), and in part, thanks to the painful recreation of bits and pieces of the Bretton Woods system within the European Communities (a recreation which was, however, not deprived of its own problems. While the snake in the tunnel and the snake outside the tunnel arrangements were non-lasting, the European Monetary System ended up providing a decade of

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much upset the trade of countries no longer protected by any customs barrier, and, because of the guaranteed Community intervention price for grain and other basic agricultural products, would cause such sudden changes in prices of farm products and therefore in farm incomes also, that the Common Market itself could be imperilled'. See also Council Decision of 8 May 1964 on cooperation between the central banks of the Member States of the European Economic Community (64/300/EEC), OJ 77, 21 May 1964, p. 1206; Council Decision of 8 May 1964 on cooperation between Member States in the field of international monetary relations (64/301/EEC), OJ 77, 21 May 1964, p. 1207; Declaration of 8 May 1964 of the representatives of the Governments of the Member States of the European Economic Community, meeting within the Council, on the prior consultations between Member States in the event of changes in the exchange rate parities of their currencies (64/306/EEC), OJ 78, 22 May 1964. See Maes (2009).

monetary stability to the Communities Although a stability which came at a price and was far from idyllic) (Collignon 2002; Marsh 2009; Szász 1999). The EMS was inherently unstable. Not only on account of the hegemonic role of Germany – which, thanks to the transformation of the Deutsche Mark in the key European international reserve currency, assumed a role within the ESM akin to that of the United States within Bretton Woods – but also due to the very new understanding of economic freedoms, and especially free the movement of capital, fostered and consecrated by the European Commission and the ECJ in the terms considered in the previous paragraph.[63] Indeed, the capacity of the EMS to stabilise exchange rates came to a sudden end in 1992, just at the time that the new understanding of free movement of capital fully unleashed the destabilising effects of this freedom. The reluctance to realign currencies in response to the different patterns of economic performance built up tensions that exploded under the force of financial speculation (but which had been cumulating before) (Marsh 2009).

The combined effect of the persistent lack of an international replacement of Bretton Woods – and the ensuing potential and reality of monetary instability – the structural instability of the European Monetary System, and the fall of the Berlin Wall – and the resulting political challenges stemming from German reunification – account for the peculiar agreement to both decide on economic and monetary union at Maastricht in 1992, and to implement the said union in 1999 (*ibid.*). All three of these factors, especially the third, created the basis for a political agreement on the need to transcend the European Monetary System and create a common European currency supported by a common monetary policy. There was a wide political agreement on the need of combining German reunification with decisions that would render European integration *irreversible*; a short name for making disintegration prohibitively costly, so as to dissuade

[63] German unification unleashed these two destabilising forces some months after the signature of the Maastricht Treaty and during its convoluted ratification process. When the massive public expenditure resulting from the specific way in which reunification was managed overheated the German economy, the Bundesbank raised its interest rates and forced the rest of the States Members of the ESM to adopt deflationary policies unsuited to their economies. The liberalisation of capital movements implemented in 1992 as part of both the single market completion project and as a preparatory step for monetary union facilitated speculative flows that revealed the structural limits of the ESM.

any member state, especially Germany, from deciding to exit the Union. However, the depth of the political agreement did not extend to the specific configuration of economic and monetary union, and particularly, not to the institutional setup, procedural arrangements and substantive rules governing monetary and fiscal policy in such a way as to ensure a functional equivalent to a well-ordered economic and monetary union.

The result of this peculiar set of circumstances was a very idiosyncratic mix of muddling through and constitutional experimentation in the form of an asymmetric monetary and economic union. Monetary policy was federalised and de-politicised. Not only the federal ECB, but also its federal components – the national central banks making up the European System of Central Banks – were to be configured as autonomous institutions, freed from political pressures and political cycles, in the template of the until-then-odd-bank-out, the Bundesbank (Sparve 2005). Monetary policy was trusted to technicians, who were given the mandate to maintain monetary stability first and foremost, paying attention to the realisation of the other goals of the European Union, such as fostering economic growth and ensuring full employment, only when that was compatible with monetary stability. In their turn, fiscal policies remained national and, formally speaking, at least the outcome of political decision-making processes. National autonomy was framed, however, by caps on yearly deficits and overall public debt – although, in practice, attention will focus exclusively on yearly deficits – as well as by substantive principles forcing member states to adopt strict fiscal policies. Key in that regard was the prohibition of central banking financing of national debts, the prohibition of the imposition of forced loans on financial institutions, and the intentional elimination of the provision of financial assistance between member states, including a ban on the mutualisation of debts. This framework was still said to be neutral given that states remained free to decide by what concrete means they will comply with the requirements of *rigeur* in fiscal policy, and reach their deficit targets.[64] Moreover, the sanctions foreseen in and further detailed by

[64] A very interesting rationalisation of *rigeur* in fiscal policy can be found at Smaghi (2010), now superseded by the last book of the same author, *Morire d'Austerità*, (Smaghi 2013). Bini Smaghi was a key player within the ECB in the aftermath of the crisis.

the Stability and Growth Pact of 1997 remained essentially symbolic. This was so because not only was the decision to sanction ultimately a political decision (as the Franco-German episode of the early 2000s will reveal), but also there were some member states too large to be sanctioned, as sanctioning them would throw the whole eurozone into recession.[65]

The coherence of this unique and unprecedented mix was trusted to *governance arrangements* and to the disciplinary force of financial markets. The former, the governance arrangements, were characterised by the substitution of the certainty of the form of law by the flexibility of the form of *soft law* (the broad economic policy guidelines produced by the Council every year, the macroeconomic benchmarks, and arguably the debt thresholds once monetary union was launched), and the replacement of the institutional coercion of law by a form of group pressure (peer pressure) rather akin to that characteristic of positive morality. The latter, leading actors in financial markets, had been already empowered them to play a key disciplinary role by the transformation of free movement of capital into a full-fledged economic freedom by Directive 88/361 (the role of hedge funds in the European Monetary System crisis of 1992 was indeed largely courtesy of the said Directive) (Mohamed 1999: 240ff). The structural power of key financial actors was further strengthened by the transformation of free movement of capital into an *erga omnes* freedom. Contrary to the 'internal market' logic, capital movements were made free not only within the Union, but also outside the Union (Hindelang 2009: 22; Ståhl 2004: 52).[66] That increased the ease with which financial markets could 'vote' for the fiscal policies of the different member states.[67] Whether that would turn financial markets into good judges of fiscal policy was a totally different question, rather taken for granted than substantiated during the Maastricht negotiations.

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[65] Indeed, what the French-German episode of the 2000s revealed was not the lack of willingness of the big countries to play by the rulers, but rather the very nature of the said rules.

[66] On the nitty-gritty of the negotiations, see Dyson and Featherstone (1999); Mazzucelli (1997): Chapter 4.

[67] Germany had also been the odd state out, having liberalised outgoing capital movements since the foundation of the Federal Republic. Incoming capital movements were, however, subject to regulation, and indeed flows of hot money were periodically discouraged in order to avoid their having an inflationary impact.

This asymmetric economic and monetary union heightened the financial and macroeconomic weaknesses of the European Union. First, the key role assigned to financial markets in disciplining the autonomous fiscal policies of the states participating in monetary union gave a major impulse to the process of financialisation. The revamping of free movement of capital as a fundamental economic freedom gave a new impulse to the process of financialisation within the European Union, at the same time turning the Union into the leading force in the process of juridifying the new orthodoxy on the blessings of financial liberalisation. While the driving economic forces in the process of financialisation had been US financial institutions, the driving legal force was the European Union. Second, the projection of the *Bundesbank* model to the European scale implied the renunciation of one key pull and lever in the discharge of state responsibilities: monetary policy. Moreover, fiscal *rigeur* necessarily implied abandoning the key pulls that made public debt an extremely safe asset. By simultaneously renouncing to finance its deficit through the central bank, or through its monetisation, and to impose forced loans, in a context marked by the prohibition of the mutualisation of debts or the provision of financial assistance to countries in fiscal difficulties, the states participating in the monetary union made themselves more prone to bankruptcy and payment defaults. Indeed, it was this mix of original decisions at Maastricht, and not the Deauville agreement of 2010 between France and Germany that created the conditions under which a Member State of the European Union could default.

For ten years, EMU was regarded as working very efficiently and very smoothly. Massive outflows of capital from the core eurozone states (Germany, Austria, Netherlands, Finland, and to a much lesser extent, France) to peripheral member states (Spain, Portugal, Greece, Ireland, and, to a lesser extent, Italy) seemed to be leading to income and wealth convergence within the eurozone. In reality, however, EMU masked growing divergence, papering income and wealth differences with the flows of credit. From a political standpoint, it is important to notice that the formal national political autonomy was highly conditioned by the different structural position of the different States, which created powerful incentives to follow peculiar strategies of adaptation: exporting competitiveness in the Euro-core, real estate and consumption bubbles in the South, and specialisation on tax avoidance in the Benelux.

The asymmetric economic and monetary union provided answers to two rather urgent challenges to the process of European integration, namely, how to avoid the strong disintegrative forces of international monetary turbulences – of which the September 1992 monetary crisis was an *ex post facto* example, revealing the structural limits of the ESM – and how to avoid German reunification unleashing another kind of disintegrative force. But while providing short-term solutions to these two problems, we should also consider what effects asymmetric and monetary union had on the five underlying weaknesses referred to above. At the end of the day, it seems to me that asymmetric and monetary union made the European Union much more fragile on each of the five dimensions.

First, EMU explicitly led to the intentional weakening of the macroeconomic steering capacities of eurozone states, and necessarily to the overall weakening of macroeconomic steering capacities within the eurozone, as the powers that were renounced by member states were not recreated at the supranational level. In the first instance, the specific kind of monetary union decided implied renouncing monetary policy as a politically controlled macroeconomic lever. Indeed, the philosophy underlying the German socio-economic constitution – although not so much the actual practice beyond the myth – now transferred to the European level, affirming that it was preferable to depoliticise monetary policy. Secondly, fiscal policy was subject to a set of general and allegedly politically neutral principles, essentially budgetary stability (defined in general terms in the Treaties, and then further concretised in the Stability and Growth Pact) and budgetary *rigeur*. While the former were constructed in widely flexible terms, too flexible according to the mainstream view, the latter implied from the moment in which they were in force the undermining of the structural solvency of public debt, and consequently, of the role of public debt as the safest asset, the investment asset of last resort. It was the Maastricht framework, and not decisions in 2010, that turned eurozone states into potential defaulters. When states renounce the monetisation of debt and the imposition of forced loans on financial institutions and citizens, they turn public debt into just an ordinary investment, in terms of the guarantees that support its solvency. But if public debt is an ordinary investment, then it follows that *like any ordinary investment*, it may be fruitful or it may turn out to leave the investor with a net loss. Finally, the combination of free movement of capital *erga omnes* with the design of a eurozone financial market without a supranational insurer of last resort rendered uncertain the capacity of member states to act as insurers of last resort of their national financial institutions, in the sense of financial institutions established in their jurisdiction. A banking union based on mutual recognition and not on the creation of common institutional structures led not only to a transfer union by stealth (from Northern European financial institutions to Southern citizens, and to a lesser extent, states), but occasionally led to elephantiastic financial sectors, with liabilities that were multiples of the gross national product of the host state of the financial institution. This was the case of Iceland in the European Economic Area (EEA) and, closer to home, of Ireland.

Table 10.6 Size of the banks relative to GDP (as a multiple of GDP) in 2009

Country	**Size of the banks (% of GDP)**
Austria	3.8
Germany	3.1
Finland	2.3
Netherlands	3.9
France	3.8
Italy	2.4
Spain	3.3
Portugal	3.1
Ireland	8.1
Greece	2.1
United Kingdom	6.0
Slovenia	1.5
Cyprus	8.2
Luxembourg	21.2

Source: The Organisation for Economic Co-operation and Development via Helgi Library, indicator for Bank Assets (as % of GDP). Available at: <http://www.helgilibrary.com/indicators/index/bank-assets-as-of-gdp> (last accessed 12 May 2014).

Second, EMU accelerated the process of financialisation in the member states of the eurozone and, in general, of the European Union. First, free movement of capital was turned, as indicated, into erga omnes freedom as part of the Maastricht deal. Second, the launch of the monetary union in 1999 not only eliminated the currency risk in financial operations within the Union, but also created the wrong impression that when the financial chips came down, the eurozone as a whole would band together and act as insurer of last resort. The latter assumption explains why the cost of issuing debt to member states of the eurozone became essentially the same. The massive spreads of the ESM era were followed by almost identical borrowing costs. Given that the underlying solidity of the national tax systems remained different, the homogenisation could only be explained by the wide assumption by financial and political actors that it was a matter of time that some form of pooled risk was established.

Table 10.7 Capital to assets ratio of banks in selected EU countries in 2012

Country	**Capital to asset ratio (%)**
Austria	7.4
Germany	4.4
Finland	4.4
Netherlands	8.9
France	4.8 (2011)
Italy	9.4 (2011)
Spain	6.1 (2011)
Portugal	6.0
Ireland	7.1
Greece	5.8
United Kingdom	5.1 (2011)

Source: World Bank, indicator 'bank capital to assets ratio'. Available at: <http://data.worldbank.org/indicator/FB.BNK.CAPA.ZS/countries> (last accessed 6 May 2014)

The acceleration of the financialisation of the economy further weakened the long-term growth perspectives of the whole eurozone, and, especially, those of the peripheral countries. On the one hand, capital holders in core eurozone countries (especially in Germany and Finland) increased their income share thanks to structural reforms that depressed wages and increased the competitiveness of the external sector. Increased competitiveness was translated into higher profits thanks to the gain of growing market shares – critically in the eurozone itself, or by becoming more competitive than producers in peripheral eurozone countries. The growing piles of capital in the form of profits were then recycled through financial capital investments, a good deal of which ended up fuelling the unsustainable growth of private debt in peripheral eurozone states. Heavy reliance on foreign trade, in the German case, exports represent close to 50 per cent, and imports a bit less,[68] has made core eurozone countries heavily exposed to the evolution of international trade, as the first months of the 2008/2009 recession rendered abundantly clear. On the other hand, peripheral states were flooded with cheap capital from core eurozone states. While that was found a salutary development for almost a decade, as capital will naturally move towards better investment opportunities, a good deal of the incoming capital ended up in investments that offered short-term profitability but which were clearly unsustainable. The real estate booms in Spain and Ireland, and the growth of private consumption despite stagnating economic capacity in Portugal and Greece were rendered possible by a dramatic growth of private debt, which was essentially external debt.[69] Private Keynesianism generated the mirage of income and wealth recovery in the South, but only at the price of increasing the structural weaknesses of the national economic models (Bagnai 2012; see also Giachhé 2011 and Passarella and Brancaccio 2012).

Moreover, the mirage of economic catching-up created a flow of unsustainable, but massive, tax revenue (clearly in the cases of Spain and Ireland, resulting from frenzy real estate speculation) and an abnormally low cost of issue of debt, drastically reducing the costs of

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[68] According to the World Bank, the value of German exports was 50 per cent of the GPD in 2010. According to the IMF these were 48 per cent in 2007, 42 per cent in 2008, and 47 per cent in 2009. Imports were at 45 per cent in 2010 (and 42 per cent in 2007, 37 per cent in 2008 and 41 per cent in 2009).

[69] Bagnai (2012), makes the point abundantly clear, and places it in the historical context of centre/periphery relations in financial terms (see especially pp. 134–164) Bagnai, who is a developmental economist (as Albert O. Hirschmann and Ha-Joo Chang, by the way) applies Frenkel and Rapetti's theoretical framework on financial crisis in developing countries to the core-periphery relationship within EMU. See Frenkel and Rapetti (2009). Indeed, it is interesting to note that the Maastricht Treaty made explicit reference to the obligation of European institutions of monitoring the evolution of the current account imbalances (See Article 3.A.3 of the Treaty of Maastricht: 'These activities of the Member States and the Community shall entail compliance with the following guiding principles: stable prices, sound public finances and monetary conditions and *a sustainable balance of payments*' (my italics). However, such an obligation was honoured in the breach, in view of the enormous current account deficits accumulated by the PIIGS (all of them, and not only the 'chronic' deficitarians such as Greece or Spain, but also Italy: See Table 10.8).

very high levels of debt in the cases of Italy and Greece. What were once regarded as once-in-a-lifetime revenues were now largely regarded as ordinary, and this created the almost irresistible political temptation to reshape the revenue side of the public budget so as to maximise the political short-term gains in the form of ensuring re-election. This created very large structural deficits, which were suddenly revealed when the subprime crisis of 2007 hit European economies, resulting in an evident slowdown of economic activity in Ireland and Spain, whose real-estate-fed growth was bound to be especially sensitive to the tremors of the international financial system.

Table 10.8 Current account balance in selected countries (% of GDP, 3-year average)

Country	2001	2003	2005	2007	2009	2010
Austria	-1.1	1.2	2.0	2.8	3.7	3.7
Germany	-1.0	1.3	3.9	6.3	6.5	6.1
Finland	7.2	7.2	4.8	3.9	2.9	2.0
Netherlands	2.8	3.6	6.9	7.8	5.4	5.7
France	1.8	1.1	0.2	-0.7	-1.4	-1.5
Italy	0.4	-0.3	-0.7	-1.2	-2.0	-2.8
Spain	-3.6	-3.6	-5.4	-8.8	-8.1	-6.3
Portugal	-9.8	-8.3	-8.4	-10.4	-11.2	-11.2
Ireland	-0-3	-0.5	-1.4	-4.1	-4.5	-2.3
Greece	-6.2	-6.8	-6.7	-11.2	-13.6	-12.1
United Kingdom	-2.4	-1.8	-2.1	-2.8	-1.8	-2.1

Source: European Commission, Macroeconomic Scoreboard, available at: <http://ec.europa.eu/economy_finance/economic_governance/macroeconomic_imbalance_procedure/mip_scoreboard/index_en.htm> (last accessed 12 May 2014).

Finally, asymmetric economic and monetary union accelerated the weakening of the link between state responsibilities and state capacities. As indicated, states renounced key levers to ensure the macroeconomic steering of the economy, while the responsibility for ensuring economic growth and stability was retained by the states. This created not only a major democratic deficit, but also a latent and massive political deficit.

The inconsistency of the European government of the crises

A whole set of supranational policy decisions and structural reforms have been put forward in the last five years with the aim of containing the crises and overcoming them. Leaving aside the final judgment on their effects, it can be said at this point in time that (1) the measures have been based on shifting and rather incompatible diagnoses of the nature of the crises, and (2) have led to openly contradictory policies.

Inconsistent diagnoses

The punctual policy decisions and the structural reforms taken by the European Union as a means to steer the crises have relied on shifting diagnoses of what kind of crisis the European Union is going through. The abrupt character of the shifts, and the very different implications that different diagnoses imply in terms of the adequate measures to be adopted, are strong indicators that the management of the crises has been inconsistent over time. We can distinguish at least three different diagnoses of the crises and three different set of policies and reforms aimed at addressing them.[70]

A financial liquidity crisis?

From mid-2007 to late 2009, it was assumed that the crisis was mostly a financial liquidity crisis. Excesses in the US subprime mortgage market had spilled over the whole American financial system. Because of the close intertwining of the American and the European financial systems, the crisis of confidence in American financial institutions soon infected European financial institutions.[71] However, financial investors were deemed to be over-reacting. After too many

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[70] Developing this argument fully would require a previously detailed analysis of the measures taken by the Union since 2007. For that I refer to Menéndez (2012, 2013).

[71] 'BNP Paribas investment funds hit by volatility', *Financial Times*, 8 August 2007, retrieved from: <http://www.ft.com/cms/s/0/9a4cabc4-464d-11dc-a3be-0000779fd2ac.html#axzz1XePLtVVH> (last accessed 28 April 2014); 'UK to guarantee Northern Rock deposits', *Financial Times*, 16 September 2007, retrieved from: <http://www.ft.com/intl/cms/s/2/39199b78-6489-11dc-90ea-0000779fd2ac.html#axzz1XePLtVVH> (last accessed 28 April 2014); 'Northern Rock in state hands', *Financial Times*, 18 February 2008, retrieved from: <http://www.ft.com/intl/cms/s/3/3f406b76-de05-11dc-9de3-0000779fd2ac.html#axzz1XePLtVVH>; 'The Big Freeze', *Financial Times*, 3, 4, 5 and 6 August 2008, available at www.ft.com. See also Tett (2009) (First Failures).

years *under-pricing* risk, a euphemism to refer to the already mentioned belief in the *overcoming* of risk thanks to economic modelling, investors were now *overpricing* risk. The fundamentals of the economy– both the financial and the non-financial sectors – were good, and, once the breakdown of trust in the viability of financial institutions was overcome, the European economy would return to normal.[72] Countercyclical measures were needed only to avoid a financial panic creating lasting damage to the economy.[73]

This diagnosis accounts for the fact that the government of the crisis was largely confined to concrete policy measures that were largely presented as temporary and exceptional. Most of these policy decisions boiled down to the granting of state aid to financial institutions. From August 2007 to October 2008, the ECB engaged in

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[72] Pisany-Ferry and Sapir (2009: 69): 'On the whole the euro is bound to live with this governance structure in the years to come. This does not mean that it is doomed to fail. In fact it has thrived in its first ten years of existence. The euro has provided price stability to previously inflation-prone countries. It has offered a shelter against currency crises. It has by and large been conducive to budgetary discipline. It has attracted five new members in addition to the eleven initial ones. And many countries in Europe wish to adopt it'. The gathering storm leads the authors to conclude in a more cautious key, however: 'Although we regard recent remarks on the possible exit or expulsion of those members from the euro area as pure fantasy, we acknowledge that the lack of clarity on how to resolve their debt problems is a source of worry' (*ibid*: 83). One of the many paradoxes of the crises is that the US institutions ended up bailing out many big European banks. See 'German and French banks got $36 billion from AIG bailout', *Business Week*, 15 March 2009, retrieved from: <http://www.businessweek.com/the_thread/economicsunbound/archives/2009/03/german_and_fren.html> (last accessed 28 April 2014); 'Deutsche Bank, Credit Suisse Lead Traders of Fed's Mortgage-Backed Bonds', *Bloomberg*, 1 December 2010, retrieved from: <http://www.bloomberg.com/news/2010-12-01/deutsche-bank-credit-suisse-lead-traders-of-fed-s-mortgage-backed-bonds.html> (last accessed 24 April 2014); 'Foreign Banks tapped Fed's secret lifeline most at crisis peak', *Bloomberg*, 4 January 2011, retrieved from: < http://www.bloomberg.com/news/2011-04-01/foreign-banks-tapped-fed-s-lifeline-most-as-bernanke-kept-borrowers-secret.html> (last accessed 28 April 2014); 'Fed opens books revealing foreign megabanks were biggest beneficiaries', *Huffington Post*, 31 January 2011, retrieved from: <http://www.huffingtonpost.com/2010/12/01/fed-opens-books-revealing_n_790529.html> (last accessed 28 April 2014). A narrative account in Irwin (2013), slightly updated in 'How Ben Bernanke saved Europe's Banks' *The Globalist*, 12 May 2013, retrieved from: < http://theglobalist.com/StoryId.aspx?StoryId=9994> (last accessed 28 April 2014).

[73] European Commission, *From financial crisis to recovery: A European framework for action*, COM (2008) 706 final, 29 October 2008.

abnormal amounts of refinancing operations, easing, and drastically cheapening, the costs of obtaining credit for banks. The ECB experimented (although only once, in actual limited amounts and with a very short maturity) with a fixed rate full allotment tender, the non-orthodox monetary tool that would become normalised as time passed.[74] After October 2008, the non-orthodox monetary measures of the ECB became much larger, with longer maturity rates, and in the case of refinancing operations, based on the acceptance of collateral of more dubious solvency status. As a result, the ECB became not only a key market player in the interbank money market, but increasingly a full alternative, if not a substitute, to it (Lenza *et al.* 2010: 20). But, by October 2008 the action of the ECB was insufficient to contain the crisis of financial institutions. In the absence of supranational decision-making processes and institutional structures, including tools for sharing the costs of supporting banks or undertaking the resolution of a failed bank, the attempts at spontaneous supranational coordination among national government to prop up several transnational financial institutions – Dexia and Fortis come as paradigmatic examples[75] – failed, and member states engaged in

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[74] 'Central banks' aggressive moves stun markets', *Financial Times*, 9 August 2007, retrieved from: <http://www.ft.com/cms/s/0/569c9418-46a0-11dc-a3be-0000779fd2ac.html#axzz1XePLtVVH> (last accessed 28 April 2014); and Lenza *et al.* (2010): 13–14. See also some of the speeches by Jean-Claude Trichet at the time, for example, Trichet to the Economic and Monetary Affairs Committee of the European Parliament, 11 September 2007, retrieved from: <http://www.ecb.int/press/key/date/2007/html/sp070911_1.en.html> (last accessed 30 April 2014); Trichet, 'The US economy, the euro area economy, and their central banks', Hamburg, 7 December 2007, retrieved from: <http://www.ecb.int/press/key/date/2007/html/sp071207.en.html> (last accessed 30 April 2014); also the speech by then ECB board member Bini Smaghi, 'Financial globalisation and excess liquidity: monetary policies and new uncertainties', 21 October 2007, retrieved from: <http://www.ecb.int/press/key/date/2007/html/sp071021.en.html> (last accessed 30 April 2014). It is perhaps not fully irrelevant – and it is at any rate very revealing – that the non-standard monetary measures came one week after the decisive lost battle on the exclusion of the ECB from the Treaty list of EU institutions. See 'Central bank chief urges change to EU treaty', *Financial Times*, 11 August 2011, retrieved from: <http://www.ft.com/intl/cms/s/0/2129d4a0-4775-11dc-9096-0000779fd2ac.html#axzz309nK5245> (last accessed 28 April 2014).

[75] The Benelux states came to the rescue of Fortis after BNP withdrew from the negotiations to acquire Fortis en bloc (BNP will end up buying the Belgian share of the fractioning of Fortis, a decision that will have major political consequences in Belgium). While the Benelux governments were all smiles before the cameras, the ink of the deal was barely dry before there were serious accusations being exchanged on the bad faith and the unfairness of the costs borne by each state. On the convoluted

different unilateral strategies to support the banks, either by extending loans, guarantees or recapitalising the banks by means of the state becoming a shareholder.[76] The appearance of a coordinated European response was kept by means of the Commission giving a European wrapping to national decisions, and some degree of supranational control was ensured by means of reaffirming the subjection of all state measures to state aid control by the European Commission, although duly adapted and relaxed in order to take into account the specific circumstances.[77]

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history of Fortis, it is very much worth reading Smit (2009). On 3 October, the governments of France, Belgium and Luxembourg came to the rescue of Dexia, a bank dragged down by its investments in the United States. The bank was to be recapitalised and the states were to underwrite its deposits. Intergovernmental bargaining was far from smooth. See 'Comment Sarkozy a mangé tout crus les "p'tits Belges"', *Courrier International*, 11 December 2008, retrieved from: <http://www.courrierinternational.com/article/2008/12/04/comment-sarkozy-a-mange-tout-crus-les-p-tits-belges> (last accessed 28 April 2014) .

[76] That decision was taken the night of the 29 September 2008 in a closed doors meeting between Taoiseach Cowan, Chancellor of the Irish Exchequer Lenihan and the CEOs of the six big Irish banks. The decision was rushed through the Irish Parliament and approved without any significant debate on 2 October 2008. The bill of 30 September, Credit Institutions (Financial Support) Bill 2008, can be found at <http://www.oireachtas.ie/viewdoc.asp?fn=/documents/bills28/bills/2008/4508/b4508d.pdf> (last accessed 28 April 2014); and the statute, Credit Institutions (Financial Support) Act 2008, at: <http://www.oireachtas.ie/viewdoc.asp?fn=/documents/bills28/acts/2008/a1808.pdf> (last accessed 28 April 2014). Article 6 of the statute gives the Chancellor of the Exchequer the power to decide on the transfer of all assets she sees fit from the Banks to the Exchequer. This implied authorising the assumption of contingent liabilities twice the Irish GDP at 2008 value (which was perhaps 'inflated' by the bubble), or what is the same, an amount equal to that of six years of public spending, taking 2009 as the reference year (public expenditure was in that year 34.1 per cent GDP). On the political background of that wild fiscal night, see 'The big gamble: The inside story of the bank guarantee', *Irish Times*, 25 September 2010, retrieved from: <http://www.irishtimes.com/newspaper/weekend/2010/0925/1224279646952_pf.html> (last accessed 9 may 2014).

[77] Council of the European Union, *Immediate responses to financial turmoil*, Council Conclusions – Ecofin Council of 7 October 2008, 13930/08, retrieved from: <http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/en/misc/103202.pdf> (last accessed 9 May 2014); Directive 2009/14/CE of the European Parliament and the Council of 11 March 2009 amending Directive 94/19/EC on deposit-guarantee schemes as regards the coverage level and the payout delay, OJ L 68, 13 March 2009, 3–7; Council of the European union, Presidency Conclusions, 16 October 2008, retrieved from: <http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/103441.pdf> (last accessed 28 April 2014), especially par. 5: 'In the current exceptional circumstances, European rules must continue to be

A much lower priority was given to the stimulus of the non-financial economy. Lack of supranational institutional structures and decision-making procedures led to a failure of effective coordination, so that the Commission, perhaps even more so than was the case with support for financial institutions, limited itself to adding up the many and very different national stimulus plans.[78] Some central states of the Union, led by Germany, were very reluctant to engage in direct stimulus policies, and preferred to allow the pre-existing automatic stabilisers to work, stabilisers which, in the case of Germany, included the massive public funding of schemes to reduce working hours but preserve employment in the mid run.[79]

Finally, the European Union engaged in three small-scale schemes of financial assistance to Hungary, Latvia, and Romania.[80] Aid was

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implemented in a way that meets the need for speedy and flexible action. The European Council supports the Commission's implementation, in this spirit, of the rules on competition policy, particularly State aids, while continuing to apply the principles of the single market and the system of State aids'. See also European Commission, *Commission Staff Working Paper: The effects of temporary State aid rules adopted in the context of the financial and economic crisis*, SEC (2011) 1126 final, 5 October 2011; European Commission, 'Communication from the Commission on the application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis', OJ C 270, 25 October 2008, pp. 8–14; European Commission, 'Communication from the Commission on the recapitalisation of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortions of competition', OJ C 10, 15 January 2009, pp. 2–10; European Commission, 'Communication from the Commission on the treatment of impaired assets in the Community banking sector', OJ C 72, 26 March 2009, pp. 1–22; European Commission, 'Communication from the Commission on the return to viability and the assessment of restructuring measures in the financial sector in the current crisis under the State aid rules', OJ C 195, 19 August 2005, pp. 9–20.

[78] European Commission, 'Communication from the Commission to the European Council: A European Economic Recovery Plan', COM (2008) 800 final, 26 November 2008.

[79] See the International Labour Organisation on the German response to the crisis, which emphasises the German recipe for reducing the destruction of employment by means of subsidisation of working time reductions: International Labour Organization (2011) 'Germany: A job-centred approach', retrieved from: <http://www.ilo.org/wcmsp5/groups/public/@dgreports/@dcomm/@publ/documents/publication/wcms_153779.pdf> (last accessed 28 April 2014). See also the report of the European Trade Union Institute: Schömann and Clauwert (2012).

[80] EUI Country Report (Hungary), October 2008, available on subscription at www.eui.com, p. 14; 'Crisis comes to Hungary in Loans of Francs and Euros', *The*

granted on the basis of the old financial assistance fund (preserved for non-Euro states and based now on Article 143 Treaty on the Functioning of the European Union), but contrary to what could be expected, and despite the small amounts involved, the Union decided not to act on its own, but instead involved the International Monetary Fund (IMF) and a variable coalition of willing partners in each of the programs.[81] Although not much attention was paid, it should be kept in mind that the basic design of the bailouts of eurozone states was already at work in these schemes of financial aid. The paradigm of 'growth through austerity and without deflation' was put to work then (See Alesina and Ardagna 1998, 2009).[82]

Structural reform in this period was confined to the supervision of financial markets. Although it was largely assumed, as has been said, that the crisis was one of liquidity, reflecting an excessive distrust on the solidity of financial institutions by market actors, the fall of Lehman Brothers rendered almost unavoidable a wider reflection on the shortcomings of the supervision of financial institutions.[83]

New York Times, 19 October 2008, retrieved from: <http://www.nytimes.com/2008/10/19/world/europe/19hungary.html> (last accessed 9 May 2014); 'Hungary rescue a bid to contain crisis', *Financial Times*, 29 October 2008, retrieved from: <http://www.ft.com/cms/s/0/513de4ca-a5b0-11dd-9d26-000077b07658.html#ixzz1XDBAcFHD> (last accessed 28 April 2014); 'Latvia to receive 7.5bn € in financial aid', Financial Times, 19 December 2008, retrieved from: <http://www.ft.com/cms/s/0/1dae8b84-ce1c-11dd-8b30-000077b07658.html#axzz1W1jBHhfS> (last accessed 28 April 2014); 'Romania to receive €20bn of IMF-led aid', *Financial Times*, 25 March 2009, retrieved from: <http://www.ft.com/cms/s/0/c1119564-1953-11de-9d34-0000779fd2ac.html#axzz1W1jBHhfS> (last accessed 28 April 2014).

81 For details of the composition of the variable coalitions of the financial willing, see Menéndez (2013).

82 See Alesina and Ardagna (1998, 2009). The key document is however the policy paper presented at the Madrid ECOFIN meeting of April 15 (Alesina 2010)., 'Fiscal Adjustments: Lessons from Recent History', available at <http://scholar.harvard.edu/files/alesina/files/fiscaladjustments_lessons-1.pdf> (last accessed 9 May 2014). For a devastating criticism, see Guajardo *et al*. (2011) And now, see, of course the act of self-accusation penned by Blanchard and Leigh (2013).

83 See the report by the independent Group of Experts (the so called De Larosière report) of 25 February 2009, available at <http://ec.europa.eu/internal_market/finances/docs/de_larosiere_report_es.pdf> (last accessed 30 April 2014). This was followed by a paper of the European Commission, *Communication from the Commission European Financial Supervision*, COM (2009) 252 final, 27 May 2009.

A modest, even though wide-ranging, reform of financial supervision was launched immediately. Although the five regulations that will result from it would not be approved until November 2010, the key debates on the contents of the reform would take place in late 2008 and early 2009. The very weak supranational framework of micro-prudential supervision was enhanced by means of turning the three existing authorities into actual supervisors, and increasing their mandates by rendering them competent to supervise transnational financial actors and giving them some powers of supervision over national regulators.[84] Moreover, a new Systemic Risk Board was established, made up of the ECB and the upgraded supervisors.[85] The Board should monitor, prevent, and minimise systemic risks to the financial system, something that entails determining when the normal and microprudentially sound of individual financial institutions does, however, create massive systemic risks for the whole financial system.[86]

[84] Regulation (EU) 1093/2010 of the European Parliament and the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC, OJ L331, 12–47; Regulation (EU) 1094/2010 of the European Parliament and the Council of 24 November 2010, establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC, OJ L331, 15 December 2010, 48–83; Regulation (EU) 1095/2010 of the European Parliament and the Council of 24 November 2010, establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC, OJ L331, 15 December 2010, 84–119; Directive 2010/78/EU of the European Parliament and the Council of 24 November 2010 amending Directives 98/26/EC, 2002/87/EC, 2003/6/EC, 2003/41/EC, 2003/71/EC, 2004/39/EC, 2004/109/EC, 2005/60/EC, 2006/48/EC, 2006/49/EC and 2009/65/EC in respect of the powers of the European Supervisory Authority (European Banking Authority), the European Supervisory Authority (European Insurance and Occupational Pensions Authority) and the European Supervisory Authority (European Securities and Markets Authority), OJ L 331, 15 December 2010, 120–161.

[85] Regulation (EU) 1092/2010 of the European Parliament and the Council of 24 November 2010, on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board, OJ L331, 15 December 2010, 1–11; Regulation (EU) 1096/2010 of the Council of 17 November 2010 conferring specific tasks upon the European Central Bank concerning the functioning of the European Systemic Risk Board, OJ L331, 15 December, 162–164.

[86] See especially Articles 1, 3 and 16 of Regulation 1092/2010, see previous note.

Financial and fiscal liquidity crises?

From late 2009 to mid-2010, both the policy prescriptions *and* the diagnosis of the causes of the crises shifted radically. From the generalised agreement on the crisis being a financial crisis, resulting from the neoliberal belief in the self-regulating capacities of financial markets, and leading to 'contagion' of the whole financial sector, and the emphasis of public stimulus, international institutions (such as the IMF and the OECD) as well as national and supranational governments moved towards a preference for 'growth through austerity' and the affirmation that the structural roots of the crisis were to be found in the too liberal and spendthrift steering of public finances.

While the new diagnosis and prognosis were gaining momentum on the wings since mid-2009 (turning the minority views of the German government into mainstream), they gained ascendancy thanks to the timely collapse of the Greek finances. The inadequate management of fiscal policy in Greece, combined with the sheer falsification of statistical data, was said to have created a major hole in the accounts of the Greek exchequer. Still, it was assumed that a combination of austerity policies and temporary external financing would be sufficient to turn around the situation. Soon, serious doubts emerged regarding the solvency of other peripheral eurozone states (the PIIGS Portugal, Italy, Ireland, Greece and Spain, also referred – more benevolently – as GIPSI states) were said to be a new overreaction of some of the key operators in financial markets. Indeed, the allegedly coordinated bilateral credits granted to Greece in late April 2010,[87]

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[87] Council of the European Union, 'Statement by the Heads of State or Government of the European Union', 11 February 2010, retrieved from: <http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/112856.pdf> (last accessed 28 April 2014): 'Euro area Member states will take determined and coordinated action, if needed, to safeguard financial stability in the euro area as a whole. The Greek government has not requested any financial support'; 'Statement by the Heads of State or Government of the Euro Area ', 25 March 2010, retrieved from: <http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/113563.pdf> (last accessed 9 May 2014): 'Euro area member states reaffirm their willingness to take determined and coordinated action, if needed, to safeguard financial stability in the euro area as a whole, as decided the 11th of February'. As part of a package involving substantial International Monetary Fund financing and a majority of European financing, Euro area member states, are ready to contribute to coordinated bilateral loans. This mechanism, complementing International Monetary Fund financing, has to be considered *ultima ratio*, meaning in particular that market

and the allegedly temporal multilateral and open-ended framework for financial assistance were premised on the assumption that eurozone states may be suffering from liquidity crises,[88] but that their solvency was rock solid.

This double focus explains why the European government's handling of the crisis consisted of a new set of temporary and exceptional measures. On the one hand, the propping up of the banks continued, despite persistent discussion of the need to define an exit strategy, especially on what concerned the ECB. On the other hand, the fiscal problems of Greece and the other peripheral states were first

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financing is insufficient. Any disbursement on the bilateral loans would be decided by the euro area member states by unanimity subject to strong conditionality and based on an assessment by the European Commission and the European Central Bank. We expect euro-member states to participate on the basis of their respective ECB capital key. The objective of this mechanism will not be to provide financing at average euro area interest rates, but to set incentives to return to market financing as soon as possible by risk adequate pricing. Interest rates will be non-concessional, i.e. not contain any subsidy element. Decisions under this mechanism will be taken in full consistency with the Treaty framework and national laws. See also 'Smoke and Mirrors', *The Economist*, 31 March 2010, retrieved from: <http://www.economist.com/node/15829886/print> (last accessed 28 April 2014); Council of the European Union, 'Statement on the support to Greece by Euro area Members States', 11 April 2010, retrieved from: <http://europa.eu/rapid/press-release_MEMO-10-123_en.htm> (last accessed 9 May 2014): 'Following the statement by the Heads of State and Government of the Euro area on 25 March, Euro area Members States have agreed upon the terms of the financial support that will be given to Greece, when needed, to safeguard financial stability in the Euro area as a whole. Euro area Members States are ready to provide financing via bilateral loans centrally pooled by the European Commission as part of a package including International Monetary Fund financing'. And finally, the Memorandum of Understanding and related documents, at 'The Economic Adjustment Programme for Greece', European Economy, Occasional Papers 61, Luxembourg: Office of Publications, retrieved from: <http://ec.europa.eu/economy_finance/publications/occasional_paper/2010/pdf/ocp61_en.pdf> (last accessed 9 May 2014).

88 Council of the European Union, 'Press release: Extraordinary Council meeting, Economic and Financial Affairs', 9596/10 (Presse 108), 9 and 10 May 2010, retrieved from: <http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/114324.pdf> (last accessed 28 April 2014). Council Regulation (EU) 407/2010 of 11 May 2010 establishing a European financial stabilisation mechanism, OJ L118, 1–4; the framework agreement of the European Financial Stability Facility of 7 June 2010 can be found at <http://www.boe.es/boe/dias/2011/07/11/pdfs/BOE-A-2011-11824.pdf> (last accessed 30 April 2014). The incorporation of the special purpose vehicle at <http://www.efsf.europa.eu/attachments/efsf_articles_of_incorporation_en.pdf> (last accessed 30 April 2014).

minimised and when they were tackled, the main thrust of the answer was to put forward purely ad hoc and rather exceptional measures. For example, the coordinated bilateral credits granted to Greece, that resulted from a convoluted exercise of constitutional funambulism and even the European Financial Stability Facility which implied more dense institutional machinery and defined decision-making processes was programmed to be unwrapped within three years. Rather similarly, the ECB improvised a securities market program through which it took the rather unorthodox decision to acquire public debt of troubled member states in secondary markets.[89] It was also in this period that the Strategy 2020 was approved as a replacement of the failed Lisbon Strategy.[90]

Opening the Pandora box of solvency: Moving towards a complex understanding of the crisis?

A third diagnosis became prevalent in autumn 2010. There was an open recognition of the fact that the crises of peripheral eurozone states went beyond a temporary and irrational disbelief in the solidity of the exchequer of some states. Not only did Ireland, in November

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[89] Decision of the European Central Bank of 14 May 2010 establishing a securities market programme (ECB/2010/5) (2010/281/EU), OJ L124, 8–9. See press release of 10 May 2010: 'ECB decides on measures to address severe tensions in financial markets', retrieved from: <http://www.ecb.int/press/pr/date/2010/html/pr100510.en.html> (last accessed 28 April 2014): 'To conduct interventions in the euro area public and private debt securities markets (Securities Markets Programme) to ensure depth and liquidity in those market segments which are dysfunctional. The objective of this programme is to address the malfunctioning of securities markets and restore an appropriate monetary policy transmission mechanism. The scope of the interventions will be determined by the Governing Council. In making this decision we have taken note of the statement of the euro area governments that they 'will take all measures needed to meet [their] fiscal targets this year and the years ahead in line with excessive deficit procedures' and of the precise additional commitments taken by some euro area governments to accelerate fiscal consolidation and ensure the sustainability of their public finances. In order to sterilise the impact of the above interventions, specific operations will be conducted to re-absorb the liquidity injected through the Securities Markets Programme. This will ensure that the monetary policy stance will not be affected'.

[90] European Commission, 'Communication from the Commission, Europe 2020: A strategy for smart, sustainable and inclusive growth', COM (2010) 2020 final, 3 March 2010. The Strategy will largely be overcome by the move towards a revamped coordination of macroeconomic policies as a part of the European Semester (in the form of the monitoring and resolution of macroeconomic imbalances).

2010,[91] and Portugal, on Easter of 2011,[92] join the ranks of the rescued member states, undermining the narrative according to which Greece was a fully exceptional case, but the eurozone states decided in the Autumn of 2010 that all issues of eurozone national debt should include collective action clauses and that a discussion should be started on how to articulate a eurozone resolution framework for insolvent eurozone states.[93] In brief, eurozone states, under forceful Franco-German leadership, came to acknowledge that they may fail – something which, as was already indicated, was a necessary consequence of some of the basic supranational principles framing the fiscal national policy decided at Maastricht. Furthermore, there was a recognition, somehow *à rebours*, of the fact that the crises were also macroeconomic management crises. Leaving aside the assessment that we should pass on the process and outcomes of the on-going reform of economic governance in the eurozone, the very fact that this was launched – instead of limiting reform efforts to

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[91] Council Implementing Decision of 7 December 2010, on granting Union financial assistance to Ireland, OJ L30, 04 February 2011, 34–39. http://ec.europa.eu/economy_finance/articles/eu_economic_situation/pdf/2010-12-07-council_imp_decision_en.pdf; Council Implementing Decision of 30 May 2011, amending Implementing Decision 2011/77/EU on granting Union financial assistance to Ireland, OJ L147, of 02 June 2011, 17–19. Memorandum of Economic and Financial Policies, retrieved from: <http://ec.europa.eu/economy_finance/articles/eu_economic_situation/pdf/2010-12-07-mefp_en.pdf> (last accessed 6 May 2014); Technical Memorandum of Understanding, retrieved from: <http://ec.europa.eu/economy_finance/articles/eu_economic_situation/pdf/2010-12-07-technical_memorandum_en.pdf> (last accessed 6 May 2014); Memorandum of Understanding on Specific Economic Conditionality, retrieved from: <http://ec.europa.eu/economy_finance/articles/eu_economic_situation/pdf/2010-12-07-mou_en.pdf> (last accessed 6 may 2014).

[92] Council Implementing Decision of 30 May 2011 on granting Union financial assistance to Portugal, OJ L159, 17 June 2011, 88–92. Memorandum of Understanding, retrieved from: <http://ec.europa.eu/economy_finance/eu_borrower/mou/2011-05-18-mou-portugal_en.pdf> (last accessed 6 May 2014).

[93] This was agreed by Germany and France in October 2010 (see 'Germany confident of "crisis resolution" deal', *Financial Times*, 20 October 2010, retrieved from: < http://www.ft.com/intl/cms/s/0/6816b234-db6f-11df-ae99-00144feabdc0.html#axzz2IbK2vGs5> [last accessed 28 April 2014]) and then agreed by the European Council (European Council, Presidency Conclusions, 24/25 March 2011, EUCO 10/1/11 REV 1, retrieved from: <http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/120296.pdf> [last accessed 28 April 2014]).

financial supervision, as in the first and second phases – is indicative of a radical turn.[94]

The nature of the third shift goes a long way to explain why structural reforms were mainly undertaken in this third period of the government of the crises. First, this was the period in which financial assistance programs mushroomed: Ireland, Portugal, Spain (in the form of a credit line aimed at recapitalising a part of its financial sector),[95] Greece (for the second time and after several extremely convoluted renegotiations),[96] Cyprus[97] and (almost) Slovenia.[98] But it

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[94] European Council, Presidency Conclusions, 24 and 25 March 2011, retrieved from: <http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/120310.pdf, see previous note; Regulation (EU) No 1173/2011 of the European Parliament and of the Council of 16 November 2011 on the effective enforcement of budgetary surveillance in the euro area, OJ L306, 23 November 2011, 1–7; Regulation (EU) No 1174/2011 of the European Parliament and of the Council of 16 November 2011 on enforcement measures to correct excessive macroeconomic imbalances in the euro area, OJ L306, 23 November 2011, 8–11; Regulation (EU) No 1175/2011 of the European Parliament and of the Council of 16 November 2011 amending Council Regulation (EC) No 1466/97 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies, OJ L306, 23 November 2011, 12–24; Regulation (EU) No 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances, OJ L306, 23 November 2011, 25–32; Council Directive 2011/85/EU of 8 November 2011 on requirements for budgetary frameworks of the Member States, OJ L306, 23 November 2011, 41–47; Council Regulation (EU) No 1177/2011 of 8 November 2011 amending Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure, OJ L306, 23 November 2011, 33–40; European Commission, Proposal for a Regulation of the European Parliament and of the Council on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area, COM (2011) 821 final, 23 November 2011; Proposal for a Regulation on the strengthening of economic and budgetary surveillance of Member States experiencing or threatened with serious difficulties with respect to their financial stability in the euro area, COM (2011) 819 final, 23 November 2011.

[95] See European Commission (2012) 'European Economy: The Financial Sector Adjustment Programme for Spain', Occasional Papers 118, Brussels, retrieved from: <http://ec.europa.eu/economy_finance/publications/occasional_paper/2012/pdf/ocp118_en.pdf> (last accessed 9 May 2014).

[96] European Commission (2012) 'European Economy: The Second Economic Adjustment Programme for Greece', Occasional Papers 94, Brussels, retrieved from: <http://ec.europa.eu/economy_finance/publications/occasional_paper/2012/pdf/ocp94_en.pdf> (last accessed 28 April 2014).

[97] The draft Memorandum of Understanding on Specific Economic Policy Conditionality, as it stood on 9 April 2013, can be found here:

was also the period in which financial assistance was given a permanent institutional form, again through a convoluted constitutional formula (a mini-reform of the Treaties which created the legal basis on which to hang the international Treaty which creates the European Stability Mechanism).[99] In a parallel move, the ECB first expanded its securities markets program by starting to acquire Italian and Spanish debt in August 2011)[100] and then replaced it by outright monetary transactions, premised on the previous existence of a program of financial assistance agreed with the *troika* by the member state whose debt would be purchased by the ECB.[101]

<http://blogs.r.ftdata.co.uk/brusselsblog/files/2013/04/Cyprus-MoU-9-April-20132013.pdf> (last accessed 29 April 2014). The 'new' debt sustainability analysis by the European Commission, of 12 April 2013, can be found here <https://zoek.officielebekendmakingen.nl/blg-220224.pdf> (last accessed 12 May 2014). Two splendid analyses of the rather convoluted Cypriot affair are Willem Buiter, Ebrahim Arhabari, Giada Giani and Jürgen Michels, 'Cyprus is systematically important: it changed the rules of the game', 10 April 2013, retrieved from: <http://willembuiter.com/citi65.pdf> (last accessed 29 April 2013); James Meek, 'The Depositor Haircut: James Meek reports from Cyprus', *London Review of Books*, 35(9): 11–15, 9 May 2013, retrieved from: <http://www.lrb.co.uk/v35/n09/james-meek/the-depositor-haircut> (last accessed 12 may 2014).

[98] A synthetic background note on the state of the play in Slovenia by Cardiff García, *Ftalphaville*, 24 April 2013, retrieved from: <http://ftalphaville.ft.com/2013/04/24/1469552/a-slovenia-qa/> (last accessed 29 April 2014).

[99] European Council, Presidency Conclusions of 24 and 25 March 2011, retrieved from: <http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/es/ec/120310.pdf> (last accessed 29 April 2014), p. 21, annex II; For the Treaty creating the Stability Mechanism, see <http://www.european-council.europa.eu/media/582311/05-tesm2.en12.pdf> (last accessed 29 April 2014).

[100] 'ECB resumes bond-buying scheme', *Financial Times*, 4 August 2011, retrieved from: <http://www.ft.com/cms/s/0/d1a530a6-be7f-11e0-ab21-00144feabdc0.html#axzz1d0YvZMyD> (last accessed 29 April 2014); 'Intervention fails to quell nerves', *Financial Times*, 4 August 2011, retrieved from: <http://www.ft.com/cms/s/0/a42f1508-bebe-11e0-a36b-00144feabdc0.html#axzz1d0YvZMyD>; 'Bond move deepens ECB divide', *Financial Times*, 7 August 2011, retrieved from: <http://www.ft.com/cms/s/0/70dbb426-c103-11e0-b8c2-00144feabdc0.html> (last accessed 29 April 2014).

[101] European Central Bank, Press release on 'Technical features of outright monetary transactions', 6 September 2012, retrieved from: <http://www.ecb.int/press/pr/date/2012/html/pr120906_1.en.html> (last accessed 29 April 2014). The same day the ECB announced laxer criteria on collateral, see European Central Bank, Press release on 'Measures to preserve collateral availability', 6 September 2012, retrieved from:

Second, the institutional, procedural, and substantive structure of the economic governance of the eurozone was radically altered. First, the coordination of fiscal policies was drastically tightened by means of creating what seemed to be more dense fiscal targets, and by means of turning sanctions quasi-automatic through the move to qualified majority voting. Second, macroeconomic coordination was made a competence of the Union by reference to a set of macroeconomic indicators. Third, a new overarching procedure (the European Semester) was introduced. And fourth, states were forced to patriate the principle of budgetary stability and to amend their national budgetary procedures to be compatible with the requirements of the Euro Semester (including a shift from annual budgetary laws to quinquennial budgetary frameworks).

Third, there was a principled decision to strengthen the competences and the means of the European Union on what it concerned banking supervision and financial crisis resolution, although the concrete terms of the agreement, and very especially the common resources at the disposal of the structures, are still to be worked out.[102]

From shift to shift into temporal inconsistency

If the reconstruction that I have sketched out is correct, it is hard to avoid the conclusion that the understanding of the crises has shifted over time. The government of the crises, the conjunctural policy decisions, and the structural reforms supported by the Union, have also shifted. But because the shifts were of fundamental importance, and because it is hard to imagine how a coherent policy could have developed based on such contradictory diagnoses, there seem to be very good reasons to suspect the efficiency of the European government of the crises. If some form of banking union is now regarded as essential to overcome the crises, it is hard to escape the conclusion that the confinement of structural reform to the upgrading of supervisory authorities and the creation of the Systemic Risk Board was inadequate, and reflected an inadequate understanding of the crisis. If there is a need of some form of permanent European

<http://www.ecb.int/press/pr/date/2012/html/pr120906_2.en.html> (last accessed 29 April 2014).

[102] See especially European Council, Conclusions on Completing EMU, 18 October 2012, retrieved from: <http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/132986.pdf> (last accessed 29 April 2014).

Monetary Fund, the indecisiveness with which the Greek fiscal crisis was tackled is hard to justify, and so on.

One could add, and I am willing to add, that the shift is destined to continue as the diagnosis of the crises continues to be incomplete and flawed. In particular, there is mounting evidence that the design of austerity programs was based on wrong macroeconomic assumptions. But if that is so, the whole reform of the economic governance of the Union should be revisited, because it has consolidated into Union law what amounts to a flawed policy. But even if one doubts my latter statement, one should agree that shifting diagnoses are powerful indicators that the government of the crises has been inconsistent over time.

Substantive inconsistency

The inconsistency of the European government of the crises is not merely a matter of shifting diagnoses of the crises. It is also a matter of making contradictory decisions, sometimes simultaneously and occasionally in one and the same legislative act or package. For reasons of brevity, I focus in this subsection on only two instances of fundamental importance: (1) the move to deepen and curtail the free market at the same time, and (2) the decision to structure the new economic governance of the eurozone on the simultaneous quasi-automaticity of sanctions for breaches of the Stability and Growth Pact, and the provision of financial assistance to the breaching and sanctioned states.

Fostering and undoing the market at the same time

The official narrative of European institutions since the beginning of the crises has stressed the fundamental importance of preserving and deepening the single market. On the one hand, the single market has to be preserved against any protectionist temptation stemming out of the crises. On the other hand, the deepening of the single market (the final completion of the market) has been said once and again to be one of the best strategies to overcome the crises. In that regard, it suffices to keep the Commission White Paper of 2010[103] in mind – on

[103] European Commission, *Communication from the Commission to the European Parliament, the Council the Economic and Social Committee, and the Committee of the Regions: Towards a Single Market Act For a highly competitive social market economy: 50 proposals for improving our work, business and exchanges with one another*, COM (2010)

whose drafting, it might be said *en passant*, the late Mario Monti played a key role[104] – and the two sets of specific actions contained in the so-called Single Market Act I[105] and Single Market Act II.[106]

At the same time, however, that the Union is said to be intent on sheltering and further developing the single market, concrete policy decisions and concrete policy reforms point in exactly the opposite direction. Consider the following three examples: First, the ECB has come to play a key role in the allocation of financial resources within the eurozone, and very especially on what concerns financial institutions. Trapped between the hard rock of allowing the disintegration of the single financial market following the financial crisis of 2007-2008 and the retrenchment of transnational financial activities as a side effect of massive state interventions in financial institutions, the European Central Bank has become not only the underwriter of the interbank money market, but a full-fledged alternative to the said money market. What were presented as exceptional and unorthodox refinancing operations in 2007, have now become established as features of the way in which financial resources are allocated in the Union seven years later. Indeed, the extent of the intervention of the ECB has grown over time, as not only the amounts involved in this refinancing operations at a fixed allotment rate have grown over time, but the length of the refinancing

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608 final, 27 October 2010, retrieved from: <http://eur-lex.europa.eu/resource.html?uri=cellar:d5edde23-2d09-4a52-8604-2f215e0bac62.0001.03/DOC_2&format=PDF> (last accessed 29 April 2014).

104 Monti, M., *A new strategy for the single market: At the service of Europe's economy and* society, Report to the President of the European Commission, José Manuel Barroso, 9 May 2010, retrieved from: <http://ec.europa.eu/internal_market/strategy/docs/monti_report_final_10_05_2010_en.pdf> (last accessed 29 April 2014).

105 European Commission, *Communication from the Commission to the European Parliament, the Council, the Economic and Social Committee and the Committee of the Regions: Single market act: Twelve levers to boost growth and strengthen confidence "Working together to create new growth"*, COM (2011) 206 final, 13 April 2011, retrieved from: <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2011:0206:FIN:EN:PDF> (last accessed 29 April 2014).

106 European Commission, *Communication from the Commission to the European Parliament, the Council, the Economic and Social Committee and the Committee of the Regions: Single market act II: Together for new growth*, COM (2012) 573 final, 3 October 2012, retrieved from: <http://ec.europa.eu/internal_market/smact/docs/single-market-act2_en.pdf> (last accessed 29 April 2014).

operations has also grown, with two massive long term refinancing operations (LTROs) or more than a trillion euro being allotted in late 2011 and spring 2012, while the requirements of the collateral have been relaxed.[107] Leaving aside the question of whether such operations were fully sound from a constitutional perspective, or desirable from a normative perspective, what is hard to contest is that they necessarily involve a suspension of the principle according to which the allocation of financial capital should be governed by market criteria. Given the central role of capital allocation in the present form of financialised capitalism, this specific pillar of the single market has been set aside. To temporarily add five years after the policy started, and with no end in sight, would perhaps be exceedingly optimistic as discourses on exit strategies from unorthodox monetary policy, abundant in 2009, have become unsurprisingly scarce ever since.

Second, a central plank of the otherwise relatively modest reform of financial supervision implemented in 2010 was the decision to create the institutional means with which to undertake macroprudential supervision of the European financial system and, in particular, to prevent systemic risk – thus the very tellingly Systemic Risk Board, in which the European Central Bank plays a fundamental role. What seems to me of essence for our present purposes is that the concept of systemic risk cannot but assume that the normal functioning of financial institutions, of individual financial institutions, which are in full compliance with individual micro-prudential standards, may however pose existential threats to the whole financial system. The quantum leap in the understanding of how markets work, and what role there is for public institutions – even if not yet political in the terms of European macroprudential norms – in creating and stabilising markets is hard to overstate. The very concept of systemic risk entails a plain rejection of the assumption that financial markets necessarily tend towards equilibrium, that financial forces would by themselves generate a socially desirable outcome. The contrary assumption pervades the acceptance of the monitoring of systemic risk, and the further assumption that when such risk emerges, it is public institutions that should act to conjure such risk.

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107 See European Central Bank, Monthly Bulletin, September 2011, retrieved from: <http://www.ecb.europa.eu/pub/pdf/other/box5_mb201109en.pdf> (last accessed 29 April 2014): Box 5.

Third, the so-called reform of the European economic governance has resulted in the considerable reinforcement of what was until now the very weak powers of the Union on what concerned macroeconomic coordination. From our present purposes, what matters is indeed that the key concept in that regard is that of *macroeconomic imbalance*, a concept that assumes, in parallel fashion to that of systemic risk, that the individual market actors acting in full compliance with the constitutional and legal norms which define the single market could lead to very negative, if not disastrous, aggregate outcomes. This calls for not only the collective monitoring of the aggregate macroeconomic balance of the economy as a whole, but for specific intervention of public institutions to correct the way in which the economy performs. That the relevant unit which should be balanced is national economies, and not the eurozone or the Union economy as a whole, that surplus and deficit imbalances are treated in asymmetric ways, and that the set of corrective measures are *de facto* – and largely *de jure* – restricted to wage repression and the reduction of the tax burden of capital holders, are very telling of the preferences which have shaped the concrete text of the Regulation and have guided its implementation, but do not contradict the structural departure from the single market project.

Sanctioning and rescuing the states who undergo a fiscal crisis

The convoluted process leading to the new governance architecture of the eurozone has led to the simultaneous facilitation and strengthening of the sanctions applicable when member states breach the deficit and debt thresholds of the Stability and Growth Pact *and* the creation of a permanent mechanism to provide financial assistance to states who undergo a fiscal crisis.

On the one hand, the reform of the two regulations that make up the Stability and Growth Pact, together with key provisions from the Stability Treaty, have drastically transformed the role of sanctions in the governance of the eurozone. From symbolic measures, aimed at deterring certain patterns of conduct, but destined to be applied only in rare and extreme occasions, sanctions have come to be quasi-automatic once a breach of the fiscal thresholds occurs. On the other hand, the tightening of the fiscal thresholds is perhaps more apparent than real; what is hard to challenge is that the process leading to the application of sanctions has been radically overhauled. The introduction of reverse qualified majority voting on what concerns the final decision to sanction in the six-pack legislation, and its transformation into a general voting rule in the Stability Treaty, makes the Commission, and not the Council, the decisive actor in the process

The European constitutional mutation

My fourth thesis is that the European government of the crises has unleashed a process of mutation of European constitutional law.

Firstly, although temporarily inconsistent and substantively ineffective as means of overcoming the crises, the manifold policy decisions and structural reforms taken since 2007 have had a major effect in the structure and substance of European constitutional law. The changes, although initially presented as mere temporary measures, have come to operate a massive change, which may well be of superior transcendence to formal Treaty reform processes, including the ill-fatted Lisbon process. Consider, in particular, the following: (1) very significant new powers have been transferred to the supranational level of government; (3) most of the new powers are to be exercised within the Union through decision-making powers in which non-representative institutions have either the last word or massive influence. This is something that is not only problematic from a general democratic perspective, but also from the perspective of the preservation of institutional balance within the Union – a fundamental channel of transmission of democratic legitimacy from member states to the Union; (3) the principle of equality between member states has been simply set aside, as not only different constitutional regimes for eurozone and non-eurozone states have consolidated, but also, an more worryingly, the legal status of surplus/deficit countries has come to be different; the immediate consequence is a relapse into 'international law' that threatens the integrity of the national and the supranational constitutions; (4) The reform of the economic governance of the European Union, far from resulting in a move from governance to law as the means of social integration on the coordination of fiscal policies, has actually led to the hardening of governance, and to the combination of under-formalised common action norms with highly institutionalised forms of coercion, which, however, are difficult to characterise as legal sanctions given the insufficient attentiveness to responsibility and overlap between the responsible actor and the passive subjects of the sanctions; (5) the reform of the economic governance of the eurozone implies a serious challenge to the structural room for democratic decision-making on what concerns fiscal policy, and, more generally, economic policy.

A drive towards the centralisation of the competences to shape the socio-economic order

It is far from surprising that the interrelated and inter-twinned crises we are examining have led to significant shifts in the allocation of powers. As is generally the case in major socio-economic crises, the shift has largely resulted in the centralisation of power, pushing competences upwards, both from local and regional to national governments, and from national governments to the supranational structure.

Firstly, six major powers have been shifted from the member states and its regions to the European Union:[108]

(1) The European Commission and the eurozone Council have been decisively empowered to shape national economic policy. These two institutions (a) have been granted new powers concerning the monitoring and control of national macroeconomic policy (member states are now mandated to prevent and correct *national* macroeconomic imbalances);[109] (b) have seen their powers strengthened (very especially the Commission) when it comes to the coordination and supervision of national fiscal policy, as a result of firstly, the tightening of pre-existing fiscal 'rules' (viz. the medium-term budgetary objective)[110] and the introduction of new ones,

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[108] In some cases the granting of competencies to the Union implies a formal and material shift of power from member states and eventually their regions to the European Union (this is clearly the case with the much strengthened power to monitor and control national fiscal policy). In others, it may well be argued that the formal shift of the competence does not imply a shift of real power, but the recreation at the European level of a power which nation-states had lost a long time ago.

[109] Regulation (EU) 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances, OJ L 306, 23 November 2011, 25–32; Regulation (EU) 1174/2011 of the European Parliament and of the Council of 16 November 2011 on enforcement measures to correct excessive macroeconomic imbalances in the euro area, OJ L 306, 23 November 2011, 8–11.

[110] Vid. See Article 2a, second paragraph of the consolidated text of Council Regulation (EC) No. 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies,

including 'rules' on the trajectory of reduction of excessive deficits[111] and public debt.[112] New procedural rules according to which not only automatic correction mechanisms will be triggered when deficits go astray,[113] but also the sanctioning proposals of the Commission will be approved when a qualified minority, and not a qualified majority, of eurozone states supports the Commission (in the rather odd jargon that is widely used, we have moved from qualified majority to 'reversed qualified majority').[114] This centralisation of fiscal policy is reflected on the structure of the (relatively) new budgetary procedure, the 'European Semester', through which it is ensured that the key economic, budgetary and fiscal choices of all eurozone states are monitored by the Commission and the eurozone Council *before* each national budget bill is sent to the corresponding national parliament.[115] All these changes imply a clear break from the Maastricht 'model' of asymmetric monetary union, as is hard to keep

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OJ L209, 2 August 1997, 1–5. Further tightened by Fiscal Articles 3.1a) and b) of the Stability Treaty to 0.5 per cent GDP, except for countries with debt levels significantly below 60 per cent and clearly 'sustainable' public finances, as specified in Article 3.1 d of the same Treaty.

[111] Article 5.1 second paragraph of the consolidated text of Regulation 1466/97. Article 6.3 establishes a specific limit to the 'deviation' that may occur in the implementation of the budget.

[112] , Article 2.1.a of the consolidated text of Council Regulation (EC) No. 1467/97 of 7 July 1997 on speeding up and clarifying the implementation of the excessive deficit procedure, OJ L209, 2 August 1997, 6–11. For a country such as Italy, with a debt of roughly 120 per cent of its GDP, this implies reducing the debt by 3 GDP points per year. It does not take much imagination to foresee that this will lead to (mis-)sale of public assets. And indeed contributed significantly to the quick rise in the interest that the Italian state had to pay for issuing debt in the early summer of 2011, leading to the eleventh chapter in the eurocrisis.

[113] Fiscal Compact. Article 3.1.e. For the common principles laid down by the Commission, see European Commission, *Communication from the Commission: Common principles on national fiscal correction mechanisms*, COM (2012) 342 final, 20 June 2012.

[114] These new powers can be seen as codifying to a large extent the practice that has evolved in the several 'programmes' of 'financial assistance' to eurozone and non-eurozone member states, in the framework of which the Commission, assisted by the ECB and the IMF (the famous troika) has shaped (if not micro-managed) the fiscal, labour and social policy of the bailed out states through the *Memoranda of Understanding* and the periodical revisions of the national compliance of the Memoranda.

[115] Unsurprisingly, the breadth, scope and schedule of national budgetary processes has been radically altered, with the detailed framing norms enshrined in the one directive that is part of the Six-Pack Council Directive 2011/85, note 94 above.

on affirming that member states retain the power to conduct their fiscal policy autonomously.

(2) The leeway with which the European Central Bank conducts the monetary policy of the eurozone has been substantially increased. 'Saving the euro' (or being more precise, avoiding a reduction in the number of eurozone states) has emerged as a meta-goal which trumps the spirit if not the letter of some Treaty provisions; in particular, keeping open and unclogged the transmission channels of monetary policy has been invoked repeatedly by the ECB to justify what the Bank itself has characterised as 'non-standard' monetary policy measures, and very especially those through which the ECB has undertook two new roles: (a) that of lender of last (increasingly in some cases, first) resort of eurozone banks, by means of moving from providing refinancing for fixed amounts at variable rates to offering refinancing for unlimited amounts at fixed rates (at the same time that the collateral eligible to guarantee the loans was progressively expanded, i.e. the quality standards of collateral have been reduced); as a result, it is perhaps not far-fetched to conclude that ECB has been either a market-maker or full alternative to interbank financing for the last six years (and counting); this implies, at the very least, a different understanding of what articles 127.1 and 119 TFEU (which mandate that the allocation of capital be the result of the operation of markets) imply for the conduct of monetary policy; (b) an indirect lender of last resort to eurozone states, by means of reducing the costs of borrowing by means of acquiring sovereign debt in secondary debt markets (through the securities markets programme launched in May 2010, radically expanded in August 2011 when the ECB started buying Italian and Spanish debt, and replaced by the outright monetary transactions in September 2012)[116] or by means of

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[116] The programme remains a legal '*nasciturus*'. We basically have the words spoken by President Draghi and Vice-President Constancio at the press conference of 6 September 2012 (http://www.ecb.europa.eu/press/pressconf/2012/html/is120906.en.html) and the press release of the ECB with the 'technical details' of OMT (http://www.ecb.europa.eu/press/pr/date/2012/html/pr120906_1.en.html). The lack of a full legal text may well be due to the high probability of the constitutional validity of the mechanism being challenged before the German Constitutional Court, as indeed was the case. In the absence of a legal text, perhaps the chances of the programme being declared unconstitutional by the judges sitting at Karlsruhe are fewer.

lending states money via massive refinancing opportunities to financial institutions (this was perhaps the case of the two massive refinancing operations – the three-year LTROs, in jargon – of late 2011 and early 2012[117], oversubscribed by financial institutions from the periphery of the eurozone, and which led to massive purchases of debt of the ailing eurozone states); both moves seem to require a rather innovative understanding of Article 123 TFEU, different from that which seemed unanimous before the crises erupted in 2007, even if the specific way and extent to which the ECB has conducted this latter role is rather restrained, not going beyond what is needed to avoid fiscal asphyxia.

(3) The newly created European Stability Mechanism has been given the power and (apparently) the means to grant financial assistance to eurozone states undergoing a (liquidity) crisis,[118] a power which seemed to have been cancelled after the entry into force of the Maastricht Treaty (even if, paradoxically, the European Union as whole preserved the capacity to assist non-eurozone states).

(4) The supranational Systemic Risk Board (an institution where the European Central Bank is bound to play a leading if not decisive role) is now the institution responsible for the macroprudential supervision of European financial markets, a task which before the crises was largely seen as an unnecessary interference in financial markets, capable of self-stabilising themselves, or at least, not prone to suicide.[119]

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117 See the ECB's press release of 8 December 2011 'ECB announces measures to support bank lending and money market activity, retrieved from: <http://www.ecb.europa.eu/press/pr/date/2011/html/pr111208_1.en.html> (last accessed 6 May 2014) that announced two massive refinancing operations at fixed rate. In December 2011 529 billion euros were lent, while in March 2014 credit was refinanced for an amount of 488 billion euros. A total sum exceeding thus the trillion euro figure, equivalent to the GDP of Spain, or around 10 per cent of the eurozone GDP.

118 European Council Decision of 25 March 2011 amending Article 136 of the Treaty on the Functioning of the European Union with regard to a stability mechanism for Member States whose currency is the euro, OJ L91, 6 April 2011, 1–2; Treaty Establishing the European Stability Mechanism, 2 February 2012, retrieved from: <http://www.european-council.europa.eu/media/582311/05-tesm2.en12.pdf> (last accessed 29 April 2014).

119 Regulation (EU) 1092/2010, note 85 above; Regulation (EU) 1096/2010, note 85 above.

(5) There is a clear commitment to transfer the power of micro-prudential supervision of financial institutions to the European Central Bank, a commitment that has been translated into secondary legislation,[120] even if the sinews of that power (the financial means to render possible effective decisions on the liquidation of banks) are still being negotiated, with chances of a rather muddled and ambivalent, if not ineffective, outcome.[121] These decisions follow the beefing up of the powers of supranational agencies supervising financial activities in 2010 and [122, 123] these changes have put an end to the assumption that a monetary union could be stabilised without a centralisation of the power of granting banking licences and of supervising the operations of financial institutions; if banks are European in life, they cannot be national at birth and in death, to paraphrase Goodhart's famous dictum.

(6) Article 8 of the Stability Treaty assigns to the European Court of Justice the power to review of the (now mandatory) national constitutional clauses patriating the principle of budgetary balance (the so-called 'golden' rule) into national constitutional law (previously Article 8 of the Stability Treaty). If the ECJ finds the national clauses defective, and the State does not amend its fundamental law in line with the requirements of the ECJ, the Luxembourg judges are given the power to fine that reluctant state.

[120] Council Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions, OJ L287 of 29 October 2013, 63–89; Regulation (EU) No 1022/2013 of the European Parliament and of the Council of 22 October 2013 amending Regulation (EU) No 1093/2010 establishing a European Supervisory Authority (European Banking Authority) as regards the conferral of specific tasks on the European Central Bank pursuant to Council Regulation (EU) No 1024/2013, OJ L287 of 29 October 2013, 5–14.

[121] See the Commission's proposal, which at the time of going to print was still the relevant drafting to consult. 'Proposal for a Regulation of the European Parliament and of the Council establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Bank Resolution Fund and amending Regulation (EU) No 1093/2010 of the European Parliament and of the Council', COM (2013) 520 final, 10 July 2013.

[122] Regulation (EU) 1093/2010; Regulation (EU) 1094/2010; Regulation (EU) 1095/2010, see note 84 above.

[123] Something that accounts for the need of a specific regulation dealing with the relationship between the ECB and the European Banking Authority, see Regulation (EU) No 1022/2013, note 120 above.

Against this general trend of centralisation, some national institutions are regarded as having managed to retain, if not increase, their authority. Unsurprisingly, this is perceived to be the case with the institutions of the 'core' eurozone countries, less touched (at least for the time being, and at least in aggregate terms) by the crises.[124] German institutions, in particular, are perceived as having retained power, if not gained authority. So much so that they may turn to be a potential check on a (reluctantly) hegemonic German government.[125] However, it may well be that all that glitters is not real power. The German Constitutional Court has found itself in a fix, caught between the will to modulate but not revert the process of integration and the deadweight of its own past jurisprudence and the constrains resulting from its being a national institution. The bottom line of the judgments rendered by the German Constitutional Court on the crises may well be summarised into 'fine as long as you keep the German parliament on the loop'.

Similarly, the German Parliament has indeed been seen its role sheltered once and again by the constitutional judges, but only (as I reiterate below) to be empowered to do things it may well not be actually capable of doing. The Bundesbank retains a major latent veto power over ECB heterodox policies; a power which largely derives from the fact that it is national central banks that actually operate in markets, and not the ECB; and the Bundesbank is the *key* national central bank, by sheer size (and not only). However, as is also the case with the other institutions, the Bundesbank is confronted with the fact that were it to use its power, this act will at the same time confirm its utmost authoritative position, and end that authority, as

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124 Many observers point that the effective authority of national institutions is closely tied to the creditworthiness of each state, or in operational terms, the rates that state has to pay when issuing sovereign debt. However, that indicator has not been thoroughly consistent, as Italy enjoyed rather affordable rates until mid-2011. Indeed, Italy had modest surpluses in Target 2 in the early months of the crises. But were Italian institutions really holding up even then?

125 That trend may also have to do with the strong institutional identity of the Court or the Bundesbank (which is related to German history and to the evolution of the German economy, but that it would very odd to explain by reference to the export successes of Germany), and by the way in which German politicians have played their cards (the two *großekoalitionen* led by Merkel perhaps reflecting the awareness of the increasingly hegemonic role played by Germany, as well as reflecting the wide consensus on socio-economic policy among Christian-Democrats and Social-Democrats).

the exercise of its ultimate veto power is likely to unleash an unstoppable process of disintegration. The authority of national institutions may well be an optical illusion: what may be sound from a unilateral national perspective may undermine the Union if generalised. Additionally, black-letter legal scholarship tends to ignore what is a key question, namely, whether the granting of powers to national institutions makes much of a real difference. German parliamentarians have been saying off the record what should be evident after what may be labelled the 'Finnish' affair. Namely, that the German Parliament does not know what to do of the powers Karlsruhe insists in granting it. The Finnish story is revealing. The Finnish Parliament conditioned support to the first Greek bailout to adequate collateral being provided to the Finnish government (as part of a special deal). This agreement was essentially kept out of the public sight (secrecy grows exponentially during crises, sometimes for good reasons, others for the obvious temptation to reduce the chances of public criticism). Later on, a Finnish newspaper not only got hold of the details of the agreement, but revealed that the guarantees could well be described as hot air in a rush. Had it been necessary to make use of them, the Finnish citizens would have found there was a hole in the pocket where the guarantees were kept.

The accrual of new powers to the supranational level of government, or the reinforcement of pre-existent powers, is an ambivalent phenomenon. On the one hand, it should be kept in mind that some of these powers were only nominally in the hands of states or regions. States have long lost the effective power to engage in a macroprudential supervision of the national financial system, given that its national character has faded out as a result of the progressive unleashing of capital movements.[126] Similarly, the effective margin of

[126] The moment in which banks made use of the free movement of capital to engage into cross-border activities, macroprudential supervision cannot be effective at the national level. National regulators lack the cognitive basis (leaving aside the banks not disclosing fully their activities, for examples those activities channelled through tax havens – Northern Rock being a very fitting example in that regard – national regulators lack the local knowledge essential in assessing the risks banks are engaging into by operating outside of the national jurisdiction). They may also lack the resources to combine macroprudential supervision with their role as being the lenders of last resort of the banks. The Irish government thought it had the means to

discretion of states when setting their budgetary and fiscal policy, though variable, has tended to be far less than what derived from a pure abstract reading of the Treaty provisions. In that sense, it could be thought that the assignment of new powers to the Union is not necessarily a loss for the member states, but a way of recovering room at the supranational level for the political decision making that had been lost at the national level. On the other hand, the very decisions to shift powers to the supranational level have been adopted through procedures with a very limited democratic legitimising capacity, while the new powers are not actually exercised in a way that is far from compliant with the democratic principle.

Radical changes in the institutional structure

The government of the crises has led to the relativisation of the principle of institutional balance, and consequently, the undermining of the main belt for transmitting democratic legitimacy from the state to the supranational level.

Power has not only shifted across levels of government, but also (and crucially) along the supranational level of government. The new competencies attributed to the European Union have all resulted in gains by institutions whose legitimacy is indirectly democratic (to be pedantic, whose 'chain' of democratic legitimacy is long, with many links) while the competencies and authority of both the European Parliament and of national parliaments (with the rather more formal than substantive exception of some national parliaments, as just indicated) have largely stalled.

To summarise in a systematic fashion what results from the shifts just described:

(1) The *European Central Bank* has (a) become the decisive actor within the Systemic Risk Board, and thus the institution that is called to shape macro-prudential policy; (b) made into the prudential supervisor of European financial institutions (and eventually, although doubtfully, into the key institution in the process of

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prop up the Irish banking system, but sooner rather than later it discovered the catastrophic consequences of having done so.

resolution of failed or failing financial institutions); (c) unleashed from some of the constrains which seemed to be placed on the conduct of its monetary policy, as it seems that other institutional and national governments have accepted, when not welcomed, its role as lender of last (in some cases first) resort of eurozone banks, and indirect lender of last resort of eurozone states (at least to the extent that this is required to avoid fiscal asphyxia).

(2) The *Eurozone Council* (non-existent at the outset of the crises) has gained considerable power. The Eurozone Council is the institution that decides financial assistance, while it plays a decisive role in the monitoring and supervising national fiscal policy. The creation and empowerment of the Eurozone Council has also transformed the way in which the European Council at large acts and decides, among other reasons because the principle of equality between member states has been relativised (something to which I come back *infra*). Not only do creditor states seem to have and exert more power than debtor states within the Eurozone Council, but the Eurozone Council as a whole is in the process of becoming the real centre of gravity of power within the Union, something which has sparked the protests of some non-eurozone member states, and which has led to a rather convoluted practice through which the circle of allowing some influence to those who are not inside while affirming the identity of the eurozone as a whole is expected will be squared. Furthermore, the empowerment of the Eurozone Council has been at the cost of weakening the traditional role of the Commission on what concerns political and legislative initiative. The procedure followed in the drafting of the several legal instruments through which the reform of the European economic governance has been substantiated is revealing that shift, with the President of the European Council leading the debate and brokering the final deals to a much larger extent that the President of the Commission.

(3) While the Commission may have seen some of its traditional powers weakened, the monitoring and disciplinary power of the Commission (or perhaps one should say of the *Commissioner of Economic and Financial Affairs*) has been much reinforced on what concerns macroeconomic and fiscal policy (and not so indirectly also labour and tax policy, as I argue below). The shift from majority to minority voting makes the Commissioner of Economic and Financial

Affairs a key actor when it comes to monitoring and sanctioning eurozone states in breach of deficit and debt thresholds and targets.[127]

(4) The European Court of Justice has also been given new powers, in particular as custodian of the primacy of Union law vis-à-vis the national *pouvoir(s) constituant(s)*. A power which perhaps can only exist as long as is not made use of.[128]

(5) Finally, the constitutional practice followed since May 2010, now codified in the legislative six-pack reform and the Stability Treaty, has made the International Monetary Fund an institutional actor which is formally assigned powers and competences by European Union law as part of the *troika*. It seems more likely that it will be the IMF itself, and not the EU, the institution that will put an end to the IMF involvement.[129]

By contrast, the European Parliament has been assigned no substantive powers in the reform European 'economic governance'. Besides having ensured some (arguably more symbolic than effective) changes in the drafting of the Six-Pack and the Two-Pack, the European Parliament has been confined to being the 'lieu' where 'economic dialogue' regarding the monitoring and disciplining of economic policy will take place. Certainly the public discussion of the reasons underpinning fundamental decisions on the economic governance of the eurozone may in the long run contribute to a different institutional structure and substantive consistency, but it remains unclear how the democratic legitimacy of the new procedures and decisions could be ensured in the short and mid runs.

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127 These two contradictory developments may further the trend towards multiplying the power poles within the Commission along its President (the double-headed Representative for Foreign Affairs, and the President of the Eurogroup).

128 A ruling of the ECJ that would impose a fine, say, on the French state for a wrong transposition of the golden rule after the transposition was enshrined into the French Constitution and approved in a referendum would perhaps be the last judgment ever rendered by the ECJ.

129 See, for example, Ousmène Mandeng, 'The IMF must quit the troika to survive', *Financial Times*, 17 April 2013, retrieved from: <http://www.ft.com/intl/cms/s/0/a9e49a86-a6bb-11e2-885b-00144feabdc0.html#axzz30GPC0zb7> (last accessed 29 April 2014). Mandeng was once deputy director of the IMF.

A double challenge to the integrity of union law

The stability of an asymmetric monetary union was pledged to a federal but apolitical European Central Bank (and the transformation of national central banks in the semblance of the ECB), a (thin) set of constitutional principles, two (short) Regulations making up the Stability and Growth Pact, the soft law that will emerge in the process of peer learning and reviewing, and the capacity of market actors to contribute both to the stabilisation of financial markets, and to the disciplining of 'autonomous' national budgetary decisions. This entailed that to a rather large extent, EMU was pledged to the ideal of self-stabilising and public-disciplining financial markets (or perhaps we should say actors). The fact that there were Member States of the European Union which were not members of the eurozone was regarded as not only 'temporary', but also as something essentially manageable.

Still, the practical functional needs of coordinating fiscal policy led to the slow emergence of eurozone institutional structures (the eurozone equivalent of the ECOFIN, now referred as the Eurogroup). The negative outcomes of the euro referenda in Denmark (2000) and Sweden (2003),[130] amplified by the scepticism towards monetary integration in some of the new member states (such as the Czech Republic) rendered naïve the assumption of a quick and orderly fusion of the EU at large and the eurozone. It is thus not surprising that the Treaty of Lisbon codified the Eurogroup, and foresaw the designation of a stable President.[131]

More to the point, we know now that, once monetary integration was achieved: cross-border capital flows grew very rapidly. Once the 'structural reforms' implemented by the Schröeder government were fully effective, German financial institutions started to recycle the huge German trade surpluses into loans to the periphery of the eurozone, which was then duly flooded with cheap credit. Cross-

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130 Danes and Swedes were asked whether they favoured their country joining Monetary Union. Denmark had negotiated a permanent opt-out at Maastricht, but had been de facto anchored its monetary policy to that of the ECB (resulting in a de facto fixed parity with the Euro). Sweden does not have an opt-out. In both cases, the incumbent governments favoured joining, but in both cases the outcome was clearly negative. See Marcussen and Zølner (2003); Miles (2004).

131 See Protocol 14 attached to the Lisbon Treaty.

border capital flows created a community of economic risks in a regulatory, redistributive and insurance vacuum; in brief, no community of insurance was built alongside the community of economic risks.

And then the crises hit. The various (and not all fruitful) initiatives aimed at establishing a supranational regulatory framework of financial activities, the beefing up of European regulatory agencies, the creation of the Systemic Risk Board, and last but not least, the assignment of powers of micro-prudential regulation to the ECB result from learning the hard way the sheer limits of trusting too much on the action of financial markets as a means to ensure 'good governance'. The Eurozone European Council, in which the heads of state and government of the eurozone states meet, was brought into existence in 2008, immediately after the collapse of Lehman Brothers and the reaching of critical stage of the financial crisis has become consolidated as a key institutional structure, the question being whether fundamental decisions are actually taken in the largest EU-27 Council or in the eurozone more restricted one.[132] The different transformations of the governance of the eurozone have resulted in a constitutional convention which requires that the key positions in European institutions be held by nationals of the eurozone countries, and the eurozone countries alone. Given the heightened powers of the Commissioner for Economic and Financial Affairs vis-à-vis eurozone states, it is simply inconceivable that she will be a national of a non-eurozone state. The creation of the position of President of the Eurozone European Council, together with the strong functional need that the President of the Eurozone European Council and the President of the European Council at large are the same person,

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[132] First Eurozone European Council (Euro Summit) took place on 12 October 12. See 'Summit of the euro area countries: Declaration on a concerted European action plan of the euro area countries', retrieved from: <http://ec.europa.eu/economy_finance/publications/publication13260_en.pdf> (last accessed 30 April 2014). Somehow paradoxically, Gordon Brown, then Prime Minister of a non-eurozone country – Great Britain – is widely believed to have played a key role in the creation of the Eurozone European Council, and did participate in its first session. The Eurozone European Council has been 'codified' by Article 12 of the Stability Treaty. Its rules of procedure were adopted in March 2013, see European Council, 'Rules for the organisation of the proceedings of the euro summits', available at <http://www.eurozone.europa.eu/media/401510/20130314-eurosummits-rules-of-procedures.pdf> (last accessed 30 April 2014).

renders almost unconditional that she be a national of a eurozone state. That convention is likely to be extended to the President of the Commission. And the idea has already been floated that an eventual increase in the participation of the European Parliament on the decision-making process concerning the eurozone would require creating a separate eurozone parliament, as the democratic legitimacy of MEPs elected in non-eurozone member states having a say on eurozone policies is of dubious democratic lineage.

In brief, a wide consensus has emerged in the last six years on the need of reintroducing a modicum of regulation and of government. But the moment in which it is established that the stability of monetary union requires more than soft law and the discipline of financial markets, the moment in which being inside or outside the eurozone starts to matter, and to matter much. After rather abstract talk about differentiated integration in the last two decades, we woke up and inequality among member states started to be legally codified:

(1) Of the eight pieces of secondary legislation that made up the Six-Pack and the Two-Pack, four of them are explicitly addressed *only* to eurozone member states.

(2) The Fiscal Compact is an intergovernmental Treaty signed by 25 of the (then) 27 Member States; all non-eurozone states bar the United Kingdom and the Czech Republic have signed it, and Denmark and Romania have declared their being fully bound by the Treaty as a whole.[133]

[133] As is well-known, the Fiscal Compact was enshrined in an intergovernmental Treaty because not all member states would have agreed to its being incorporated to a standard reform Treaty. The fact that the signatories to the Fiscal Compact are twenty five reflects that the cleavage between insiders and outsiders of the Eurozone does not only depend on the formal status of eurozone state. Much will depend on the concrete way in which the complex mechanism foreseen in the micro-prudential regulation unfolds. Non-eurozone member states may subject themselves to the authority of the ECB. Probably out of the hard lessons of the last years, specific provisions are included in the Regulation to govern the 'exit' of a non-eurozone state for such voluntary submission. But which would be the circumstances in which a non-eurozone state could discontinue such arrangement without endangering the stability of 'its' financial institutions?

(3) The European Stability Mechanism has been created outside of the formal Treaty framework, in application of amended Article 136.

(4) And while formal differentiation is very relevant, perhaps the cleavage is being made wider by the daily conduct of European business. The very dynamics of the steering of the crises plus that stemming from the new institutional structures and decision-making procedures have unleashed a process of 'duplication' of supranational institutions. We do now have the European Council *and* the Eurozone Council. And there is clear structural pressure to find ways of ensuring the coherence between the constituency of the eurozone and the representatives sitting in the European Parliament.

A second major cleavage results from the different legal position of creditor/surplus and debtor/deficit states. The move from majority to minority voting on what regards the monitoring, and especially, the disciplining, of national fiscal policy results, *de facto*, in empowering creditor/surplus states (a minority within the eurozone) against debtor/deficit states. Given the interplay of the rules assigning votes in the Council and the national interests at stake, it is not too far-fetched to see that a Commission seeking to sanction a debtor/deficit state (say Greece) will look for the votes of the creditor/surplus states, namely, Germany, Austria, Finland and the Netherlands, which happen to make up a qualified minority. While it could be argued that the credit/debit position of a state may change in the long run, this has largely not been the case in the last two decades. It perhaps suffices to read the Preamble to the 88/361 Directive, especially the list of countries to which special provisions apply, and the reasons why this is the case, to observe that the condition of creditor/debtor is indeed very sticky. Similarly, while the European Stability Mechanism can only act by unanimous consent when taking important decisions (including the decision to provide financial assistance to one eurozone state), there is one exception, which allows decisions by 85 per cent of the votes when there is urgency. Votes have been attributed in a rather peculiar fashion (according to democratic standards), as the voting weight of each state depends on the capital of the Mechanism it has subscribed. This means that some, but not all, states have formal *solo* veto power: Germany, France and Italy. Of which perhaps only Germany can effectively make use of it without setting a precedent that may apply in the long run to itself.

It is important to stress, that, moreover, the formally bilateral financial assistance to Greece in May 2010 and the institutionalised and collective financial assistance to Ireland, Portugal, Spain, Cyprus, and Greece, the second bailout, have been articulated at the margins of European Union law. In the case of the Greek bilateral rescue, the operation was said to be disciplined by public international law.[134] In the case of the other institutionalised bailouts, the key institutional structure (the EFSF) is a *societe anonyme luxembourgeois*, constituted in Luxembourg, and which signed an agreement with its shareholders, the eurozone member states that the financial assistance is rendered legally possible by an odd mix of private law and public international law.

The new EFSM has a formal, although thin, legal basis in the Treaties, thanks to the new Article 136.3 TFEU.[135] This new article is constructed as a license to establish the institutional structure that renders possible the provision of financial assistance to eurozone member states on the basis of an intergovernmental agreement, literally at the margin of European Union law, in what has been labelled the *Union Method*, and which constitutes a serious challenge to the integrity of Community law and to the consistency of the actions of the European Union itself.[136] While the ECJ seems to have given its unconditional approval to this choice, it remains to be seen whether this opt out from community law is so easy to reconcile with national constitutional standards.

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[134] Technically speaking, the aid was granted by means of bilateral, even if coordinated, loans from each member state to Greece. This purely bilateral character of the agreement has resulted in some member states (such as Spain and Italy) incurring in actual costs to lend to Greece, resulting from the lower rates applied to Greece than those at which they can lend at international markets. See European Commission, 'The Economic Adjustment Programme for Greece', Occasional papers 61, May 2010, available at: <http://ec.europa.eu/economy_finance/publications/occasional_paper/2010/pdf/ocp61_en.pdf> (last accessed 30 April 2014).

[135] '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'.

[136] See the Brugge speech of Merkel where she enumerated the main contours of the Union Method, of 2 November 2010, available at <http://www.bruessel.diplo.de/contentblob/2959854/Daten/> (last accessed 30 April 2014).

From soft to hard governance

The reform of the economic governance of the Union entails an abandonment of soft government as the means of social integration of fiscal and macroeconomic coordination. A good deal of the institutional actors, and even of the scholarly literature, has spoken of a shift towards rules, which suggests the completion of the process of juridification of the law governing the now enlarged Stability and Growth Pact. This may be so because not only have the key fiscal thresholds (the deficit and the debt thresholds, complemented by much more detailed adjustment trajectories) been regulated in such detail as to be properly called rules, but the key fiscal thresholds are now are backed up by sanctions in a strict legal sense, very different from the peer pressure and symbolic sanctions of the first years of the original Stability and Growth Pact days, thanks to the shift towards qualified majority voting, ensuring the quasi-automaticity of sanctions. In brief, the shift from soft governance to hard law (i.e. to law proper) would be the result of common action norms with the normative density of rules and of characteristically legal means of fostering compliance.

There are reasons to doubt that we have in fact transcended soft governance in favour of law. On the contrary, it seems to me that the said reforms have led to the transcendence of soft governance in favour of hard governance. First, the new rules are less normatively dense than they seem. The precision of the rules is limited by the reliance on the highly undetermined concept of *structural deficit*. There is no consensus among economists on how we should calculate the structural deficit. Moreover, there have been manifold political controversies on the exact meaning of the term in specific cases, for example, whether the credit line offered to Spain in order to prop up a good chunk of its financial sector in 2012 should be counted as part of the deficit, as part of the debt, or neither; The decision on Spanish debt was, quite obviously, far from deprived of major consequences. Second, it is far from obvious that the quasi-automaticity of the new sanctioning procedure can overcome the purely symbolic nature of the sanctions (as sanctions that are not intended to be actually applied) without questioning the very structural basis of the rule of law For one, legal sanctions are always premised on the actual legal or moral person being sanctioned being responsible for the action or omission triggering the sanction. But it must be kept in mind that the key criterion to impose sanctions in the new Pact remains not what a government does or does not do, but the state of public finances and/or the evolution of the national economy.[137] The lack of responsiveness of the national government speeds up the sanctioning process and may aggravate the sanctions, but indeed the quasi-automaticity of the sanctions implies that sanctions may be applied even if governments act, and indeed especially if governments decide, with the support of their electorate, to try policy measures different from those recommended by the Commission. But the actual capacity of a national government to steer the national economy is to be seriously doubted, especially in view of the serious constrains that community law imposes on the policy instruments that governments resort to in order to manage national economies out of structural crises. Secondly, legal sanctions are premised on a quite precise overlap of the formal sanction and the material consequences of the

[137] As it results from the amended version of Regulations 1496, 1497, and the new one on the correction of macroeconomic imbalances, the imposition of sanctions is not conditioned to the inaction of the member state, not even to the member state not following the recommendations of the Commission as endorsed by the Eurogroup. Indeed, the new Stability Treaty foresees the introduction of automatic mechanisms of fiscal correction, which would have to be implemented in a purely mechanical way. See Article 3.1 e: 'in the event of significant observed deviations from the medium-term objective or the adjustment path towards it, a correction mechanism shall be triggered automatically. The mechanism shall include the obligation of the Contracting Party concerned to implement measures to correct the deviations over a defined period of time' and Article 3.2: 'The Contracting Parties shall put in place at national level the correction mechanism referred to in paragraph 1(e) on the basis of common principles to be proposed by the European Commission, concerning in particular the nature, size and time-frame of the corrective action to be undertaken, also in the case of exceptional circumstances, and the role and independence of the institutions responsible at national level for monitoring compliance with the rules set out in paragraph 1. Such correction mechanism shall fully respect the prerogatives of national Parliaments'. The common principles were outlined on June 2012: European Commission, 'Communication from the Commission: Common principles on national fiscal correction mechanisms', COM (2012) 342 final, 20 June 2012. There is a clear relation between the very idea of automatic correction of deficits and the two new regulations further transforming the constitutional framework of fiscal policy within the eurozone: Regulation (EU) No. 473/2013 of the European Parliament and of the Council of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area', OJ L140, 27 May 2013, 11–23, and Regulation No. 472/2013 of the European Parliament and of the Council of 21 May 2013 on the strengthening of economic and budgetary surveillance of Member States in the euro area experiencing or threatened with serious difficulties with respect to their financial stability, OJ L140, 27 May 2013, 1–10.

sanction, or what is the same, that the sanction affects first and foremost the natural or legal person being sanctioned. That is again to be seriously doubted. A sanction of any one single member state of the eurozone exerts a deflationary pressure over the eurozone as a whole. The strength and scope of the externalisation of the effects of the sanction will depend on the size and centrality of the economy of the state being sanctioned. What would be the consequences of sanctioning Germany, not to say Germany and France at the same time? The whole eurozone would suffer. On such grounds, one may conclude that, indeed, we have more of an appearance of legal sanctions than actual legal sanctions. We have what looks like sanctions, but these are not genuine legal sanctions but fake sanctions. Together with the lesser actual normative density of the rules, we have good reasons to conclude that there is no shift from soft governance to law, but from soft governance to hard governance.

The end of democratic fiscal policy?

The reform of the economic governance of the Union has drastically increased the thickness of the supranational framework of all national fiscal laws, policies and decisions. There are perhaps three key changes. First, the Stability Treaty requires Member States to patriate into their national constitutions, or norms with an equivalent dignity and force, the key components of budgetary stability, including the principle of balancing the budget, the so-called *golden rule*.[138] It may be argued that the claim to primacy of Community law already comprised the normative contents of the Stability and Growth Pact.

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[138] Article 3.2 of the Stability Treaty: 'The rules set out in paragraph 1 shall take effect in the national law of the Contracting Parties at the latest one year after the entry into force of this Treaty through provisions of binding force and permanent character, preferably constitutional, or otherwise guaranteed to be fully respected and adhered to through national budgetary processes. The Contracting Parties shall put in place at national level the correction mechanism referred to in paragraph 1(e) on the basis of common principles to be proposed by the European Commission, concerning in particular the nature, size and time-frame of the corrective action to be undertaken, also in the case of exceptional circumstances, and the role and independence of the institutions responsible at the national level for monitoring compliance with the rules set out in paragraph 1. Such correction mechanism shall fully respect the prerogatives of national Parliaments'. See also the Euro Plus Pact which established this very same obligation, see European Council, Presidency Conclusions, 24/25 March 2011, EUCO 10/1/11 REV 1, retrieved from: <http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/120296.pdf> (last accessed 28 April 2014).

But, quite obviously, it is highly contested that the said claim to primacy extends to primacy over national norms. If the Spanish constitutional reform of 2011 is a good teller of the new constitutional times, it is very likely that the ensuing constitutional reforms will imply major changes in the normative code of the Social and Democratic *Rechtsstaat*. The unqualified preference given to the repayment of debt may or may not be wise, but it clearly implies weakening the constitutional force and dignity of socio-economic rights. Second, the European Semester, together with the Directive on National Budgetary Procedures, is bound to result in a massive transformation of national fiscal procedures. Not only are national yearly budget laws bound to become secondary to quinquennial national fiscal frameworks, but all national budgetary procedures are going to take place after fundamental decisions on their general design have been taken at the European level. Third, the new Stability and Growth Pact, and in particular, the quasi-automatic character of sanctions, implies a major effective constrain on national fiscal autonomy, due to the new pillar on macroeconomic stability, on national autonomy on the design of economic policy , which, as has been said, is increasingly more formal than real.

In this new framework, member states are not only left with a very limited set of effective macroeconomic pulls and levers (essentially tax and labour laws), but they are now almost forced into making use of them in only one direction. Namely, reducing taxes burdening capital holders and reducing the legal protection of workers, to aim at what formally is characterised as the *increased competitiveness of the external sector*,[139] but that given the actual set of open options, it will

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139 See the different Memoranda of Understanding of the country programmes, and the stability programmes of all eurozone states. For the latter, see <http://ec.europa.eu/economy_finance/economic_governance/sgp/convergence/index_en.htm> (last accessed 12 May 2014). The ideology of competitiveness is well illustrated by the annual competitiveness report (For 2012, see European Commission, 'Reaping the benefits of globalization', European Competitiveness Report 2012, available at <http://ec.europa.eu/enterprise/policies/industrial-competitiveness/competitiveness-analysis/european-competitiveness-report/files/ecr2012_full_en.pdf> [last accessed 30 April 2014]). The implications in terms of labour and social policies were clearly revealed by Draghi in March 2013. See 'Exclusive: Draghi lectures euro zone leaders about labor costs', *Reuters*, 15 March 2013, retrieved from: <http://www.reuters.com/article/2013/03/15/us-eurozone-summit-draghi-idUSBRE92E0I220130315> (last accessed 30 April 2014). See

be less euphemistic to describe it as regressive redistribution of income, which may or may not result in higher investment rates in the external sector of the national economy. The substantive bias, it goes without saying, is not so much the result of an explicit decision, but of a complex set of decisions. Given the present institutional structure, the division of competences among levels of government, the structure and division of labour between decision-making processes, and the substantive content of positive norms, the policy options left to states in fiscal troubles are indeed those just mentioned.

What to do, Spinelli?

I have claimed in the previous sections that (a) the European Union *is* in economic, financial, fiscal, macroeconomic, and political crises; that (b) these crises, while global in nature, have revealed the special and intense weaknesses of the European Union, weaknesses that can be traced back to the very transformation of the European Union and its constitutional law in the last three decades, especially to the assignment of a founding value to economic freedoms and to the asymmetric economic and monetary union started in 1999; (c) that the attempts at governing the crises, based on shifting diagnoses in contradictory measures, have aggravated the crises, instead of solving them; and (d) that they have unleashed a process of constitutional mutation that has consecrated the subordination of the normative values of the Social and Democratic *Rechtsstaat* to the protection of the value of capital assets. As a result, it is not only the European Union that is undergoing an existential crisis, it is the European political project and its key component, the Social and Democratic *Rechtstaat*, that are going through an existential crisis.

It would be pretentious and silly to claim that one has the magical solution to such a complex problem, or more precisely, set of problems. Moreover, if a central part of the present diagnosis is that democracy is at stake and is being undermined, it would be contradictory to offer a ready-made solution to the problems, instead of referring back to democratic discussion and decision-making. But it might be odd to simply conclude that the way in which the crises

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the PowerPoint presentation, very revealing, at: <http://www.ecb.europa.eu/press/key/date/2013/html/sp130315.en.pdf> (last accessed 30 April 2014).

should be overcome is something on which nothing can be said. So it seems almost unavoidable to answer the question of what can be done, even if very tentatively.

In the following I consider three alternative strategies: (1) A reformist strategy within the framework of the present European Union; (2) democratic re-foundation of the Union by means of a democratic constitutional convention; and (3) national constitutional resistance, if possible, grounded on the deep constitution of the European Union, the collective of national democratic constitutions. The first two strategies seem to me unpromising; the third is plagued with difficulties, but also seems to me to be the only viable choice.

The impossible status quo

The first strategy consists of the implementation of structural and policy changes intended to overcome the crises within the framework of the present European Union and the present Treaties. This strategy seems to me highly unpromising for what may be said to be structural reasons. The fundamental reason lies with the key assumption that underlies it. The reformist strategy assumes that the passing of new regulations and directives, perhaps in tandem with the development of some constitutional conventions, would allow us to implement the institutional, procedural, and substantive changes necessary to stabilise the European Union and slowly regain the path of growth and socio-economic improvement. For that to be true, either the importance and complexity of the crises has been overestimated, or the neutrality and plasticity of the European Union as a set of institutional structures and of European supranational constitutional law remains very high, or some combination of the two accrues. However, both assumptions seem to be wrong.

On the depth and intensity of the crises, there seems to be a decreasing margin to contest that the European Union is undergoing an existential crisis, a crisis that finds part of its cause in the very structure of the Union and the substantive content of European Union law. More than five years into the crises, the government of the crisis has been largely based on wrong and shifting diagnoses, and moreover has led to the further entrenchment of the very elements of the structure of the Union and the substantive content of Union law at the root of the crises. The Union is undergoing an existential crisis that challenges its present configuration, as any existential crisis does.

Moreover, European leaders have been taking measures for five years assuming that the crisis they were dealing with was rather different from what it actually was (and is), aggravating the crisis and further entrenching the very institutional structures and principles more heavily challenged by the crises. On such a basis, can we really conclude that we can overcome the crisis without a radical break within the present supranational constitutional law? That break might have been possible at the beginning of the crises, although there may be reasons to conclude differently, but can it be possible after five years of further entrenching into the constitutional law of the Union the very provisions that must now be modified?

This conclusion leads us to consider the plasticity of the Treaties. The Treaties are not neutral and malleable; they have become increasingly rigid and biased in favour of specific substantive outcomes. The crowning of economic freedoms as the fundamental substantive content of Union law, together with the structural biases latent in the asymmetric economic and monetary union, already loaded the European constitutional dice. And the new two Para-Treaties and the secondary norms that have reformed the Stability and Growth Pact and created a supranational framework for national budgetary processes have increased the bias. As was already indicated, the trouble lies not so much with specific substantive provisions, as with the implications of the overlap of (1) the division of competences between the Union and the Member States – the rapid centralisation of competences as part of the government of the crises – (2) the procedures of decision-making – the European Semester and reverse qualified majority-voting – and (3) substantive constitutional norms – already biased, as indicated, in favour of the rights of capital holders.

Constitution-making

If what I have argued in the previous section is correct, then we have to conclude that constitutional law has broken down for good. The obvious implication of such a conclusion is that we need to rewrite constitutional law through a democratic constitution-making process. Either that is possible and will actually be done, or the breakdown of constitutional law will result in the mid- or long-run in the breakdown of the Social and Democratic *Rechtsstaat* as a social, economic, and political form. Thus, we need a *constituent assembly*, and we need it soon, if not now.

In abstract terms it is hard to contest the appeal of a constituent assembly. However, democratic politics, of which constitutional politics is but one part, is not only about normative ideals, but also about the right strategy to realise such ideals. It seems to me that there are four major problems with the constitutional solution which render it inadequate, all things considered.

Firstly, the European constitutional card has recently been raised in vain. The Laeken process failed. That was in itself more than fine in constitutional terms (a democratic process should fail if the people say no). The problem was that the popular rejection expressed in the French and Dutch referenda (probably reflecting a wider and pan-European discontent) was not taken seriously, but was actually circumvented through the Lisbon process (Fossum and Menéndez 2010: ch. 4). Raising the constitutional card again should be taken very seriously, given the risk that a new constitutional failure may backfire, questioning not only the viability of a democratic reconstitution of the Union, but even the feasibility of democratic constitutionalism in Europe itself.

Second, doubts can be raised about the accrual of the necessary political preconditions for starting a Euro-wide democratic constitution-making process. How should we forge the European democratic constitutional will? Who should participate? And who should not? And which concrete process should be followed? All constitution-making processes that have borne constitutional fruit have relied on the existence of a background constitutional theory, a public philosophy that provides ready-made answers to these and related questions, a public philosophy that reflects a latent normative consensus, and a common perception of the past and a latent willingness to share the future. The lack of a background constitutional theory ten years ago may come a long way to explain the peculiar procedure then followed and the odd way in which the French and Dutch constitutional rejection was simply left aside by the Council (*ibid.*, conclusions). There are good reasons to think we are far from having forged a background constitutional theory now.[140]

[140] During the Laeken process, as might be remembered, it was unclear whether the citizens of member states, and member states only, should be represented. What about applicant states such as the 12 states that were set to become Members by then? What about the associated half, if not more, member states, such as the EEA

First, we cannot take for granted who should be called on to participate in the constitution-writing process. Should the constitution writing process comprise the European Union at large, or perhaps only the eurozone countries, or more simply, the countries willing to engage in such a process? Could the process go on even if against the will of the majority of the electorate of some or the other state of the Union that does not wish a European constitution to be written? What should the relationship be between the EU states in the new constitutional compact and those outside of it? Second, how should the process of constitution-making proceed? Given that we have to add the failure of the peculiar assembly model that characterised the Laeken process to the repeated failures of the IGC model, what would the constitutional assembly look like? What would be, if any, the role of the European Council in relation to the Assembly?[141] The *no demos* thesis is a flawed theoretical construct that corresponds, however, to genuine problems, problems that have been aggravated, not solved, in the last years.

Third, the mis-government of the crises has shaped and transformed public discourse, essentially leading to the weakening of political trust, not only across borders, as the underlying socio-economic conflicts have been quite cunningly reduced to national differences, opposing creditor, and debtor nations, instead of creditors and debtors as individuals, but also within borders, with secessionist tendencies in richer regions bound to rise over time, following the template of Catalonia.[142] Can a democratic constitution-making

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states? What about Turkey? Even worse, there was no clear answer to the question of how the representatives should be elected. Having no answer to this question that could be used as the basis for electing the Convention, the issue was avoided by a complex combination of titles of indirect representation. The price to be paid was that the Convention could not vote – and no constitutional convention can be a serious decision-making without voting.

141 The procedure followed by Altiero Spinelli in 1984, the election of a new European Parliament and the writing of a draft constitution there, later ratified by all national parliaments, seems the less controversial option, but would only work if the whole European Union, the whole constituency of the European Parliament, were to be reconstituted.

142 That is, of secession being requested by one of the richest region within the country, in the name of the 'fiscal exploitation' of that region by the 'central state', usually under the combined claim that the state wastes too much money, and that there is a trifle too much redistribution to poorer regions. A similar socio-economic

process take place in such a context? Is there any chance that the *reductio ad nationem* which obfuscates the distributive implications of the crises may not result in irreducible conflicts that would prevent any constitutional reform capable of overcoming the present crises?

Finally, there are reasons to doubt that any process of constitutional reform of the European scale could be undertaken within a short period of time. The longer the process, the easier that it would be for powerful actors to gain undue influence over it by making use of their structural power, which has only been heightened over time. A constitution-making process lasting two and a half years could easily be pushed off track by financial and fiscal crises, and largely influenced by bouts of speculative activity in financial markets. At the end of the day, it seems to me that there is a serious risk that the *laudable-in-abstract* call for a democratic constitution-making process is a strategically unadvisable option.

The national rescue of the European Union

If support for a radical democratic strategy is not likely to be found in this European Union, while it is neither very probable that we can reconstitute this European Union into a different European Union through democratic constitution-making, then what can be done to rescue the European political project? It seems to me that third alternative lies in attempting a national rescue of the European Union, or what is the same, in realising the democratic potential of national constitutions as the deep constitutional law of the European Union.

The key move in this strategy is to contest the constitutional soundness of the present governance of the eurozone. Supranational constitutional law has mutated and tilted in favour of capital holders in ways that are incompatible with the Social and Democratic *Rechtsstaat*. But why should this change be the last European constitutional word? In other words, why should we take *Pringle*[143] as

template prevails in the Flemish and the 'Padanian' cases (Padania standing for a variable chunk of Northern Italy which always includes Lombardia and Veneto).

[143] Case C-370/12, *Thomas Pringle v Government of Ireland, Ireland and The Attorney General,* Judgment of 27 November 2012, *nyr*. The case resulted from an Irish preliminary reference resulting from Mr Pringle challenging the European

the last word on the constitutionality of the Stability Treaty? Why should we accept that this transformation is a sound transformation from a constitutional perspective?

Quite simply, we do not have to. The deep constitution of the European Union, the ultimate normative foundation of the whole edifice of the Union, is not the Treaties, but the collective of national democratic constitutions. It was the democratic, open, and integrationist postwar constitutions, together with the constitutions of the member states that joined the European Union afterwards, that enabled and mandated integration. When integration starts going against the key normative content of the national constitutions, it is time to start using such constitutions not as national limits to this or that secondary supranational norm, but as the ultimate source of the yardstick of European constitutionality. According to such yardstick, neither the centralisation of power without corresponding democratic control, nor the structural bias in the socio-economic constitution of the Union can be constitutional. They have to be actively contested as unconstitutional.

It seems to me that this strategy holds some promise for two reasons. First, the national constitutional rescue is the opposite of a mere regression into constitutional autarchy. This form of national constitutional resistance takes seriously the open and integrative character of national democratic constitutions. It justifies national constitutional resistance, not on idiosyncratic and parochial grounds, but to the contrary, on the basis of appealing to a common normative ideal, an ideal that should be reflected in all national constitutions. It is also very different from the artificial federalism into which some national constitutional courts have relapsed in the past, defining procedural and substantive requirements for integration to proceed which are simply not generalisable, which can only be reconciled with integration if only some states, but not others, impose such conditions. It structurally fosters that constitutional resistance grows across borders, as the more the member states in which it is resorted to, the more effective it will be, not only economically, but also normatively.

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constitutionality (the validity according to Union constitutional law) of the Treaty establishing the European Stability Mechanism.

Second, this strategy could lead to immediate changes, as there is no time lag between opting for it and changing things in the Union. It suffices that a majority in a democratically elected Parliament embraces it and challenges the status quo in a way that is compatible with the central claim of the strategy. All decisions in apparent breach of the present Treaties and para-Treaties, but which can be said to be necessary to avoid the collapse of the social fabric of a member state, are covered by this strategy. It offers argumentative cover for the restoration of the primacy of socio-economic goals over the imperative of preserving the value of financial assets. At the same time, the articulation of an alternative European constitutional discourse, one grounded on the Social and Democratic *Rechtsstaat*, may be conducive to the forging of a background European constitutional theory.

And still, the permanent state of fiscal emergency in which the peripheral member states seem to be submerged undermines both the democratic and the social pillars of the Social Democratic *Rechtsstaat*, and also renders highly problematic this third strategy. The lack of time to debate, the series of decree-laws decided on the hoof, create the structural conditions under which the general, wide-ranging social policies characteristic of the postwar welfare state are bound to take a back seat to the promotion of special interests capable of adjusting to the economics of turbulence and cloaking, in the name of collective goods – the stability of the financial system and employment promotion – their narrow concerns. It feels very much the Euro has become a mousetrap.[144]

So how better to conclude than with a riddle: A European constitution should be written, will be written, and simply cannot be written.

[144] The metaphor is used extensively. See Offe (2013); Seco (2013).

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Chapter 11

From expert to politician and stakeholder? Constitutional drift in the role of the ECB

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Introduction

The economic and financial crisis has put many of the European actors in situations where they have been able or even forced to take new roles. Most of the actions that have created or shaped these new roles have been based on more or less ad hoc decisions, in which the constitutional issues involved have been tackled at a relatively superficial level if at all. It is perhaps less than surprising that while many of these decisions have failed to reach their intended consequences they have had a broad list of unintended and unforeseen consequences.

The European Central Bank (ECB or more broadly the ESCB) is naturally only part of the complex financial and institutional set-up involved in the financial crisis. However, it is also one of the clearest examples of the constitutional drift in roles and also a potentially unfortunate example of the unintended constitutional and also other consequences of the ad hoc decisions. In the same vein, it should also be included in the solution for the legitimacy problem of the EU economic governance after the crisis.

In this chapter, I will first discuss the original constitutional position of the ECB as defined by the relevant constitutional principles of the Economic and Monetary Union (EMU). Second, I will elaborate on the potential theoretical roles that could be used to describe the economic-administrative organs generally and the ECB especially. I will start with the ideal model roles of independent expert and politician. However, I suggest complementing them with a third role, namely stakeholder. I devote some special attention to the demarcation lines between the roles before turning to the new actual roles of the ECB in the third section. Fourth, I will analyse these new roles from the constitutional law and control perspectives. It should not come as a surprise that constitutional control mechanisms envisaged for a limited expert role are hardly appropriate for the role of politician or stakeholder. This has also implications for the democratic legitimacy of the institutions involved. I will present some suggestions for the way forward taking into account also the resurfaced need for democratic legitimacy in the EU economic governance. Finally, I conclude.

European economic constitution and constitutional principles for common monetary policy

As is well known the European economic constitutionalism has its origins in the German ordoliberal thinking. However, at the constitutionalisation of the economic framework has broadly followed its own logic at European level, also reflecting the idea that elements that had the least frequent demand for democratic input could most easily be supra-nationalised. This could partly explain the notion by Fritz Scharpf that the EU has relied almost exclusively on liberal legitimation discourses (Scharpf 2009: 176) in contrast to more balanced legitimation drawing also from the republican discourses.

The economic constitutional elements of the Rome Treaty are the core of the European economic constitution. It consists of the four freedoms as well as the competition and state aid rules. It is therefore typical rule-based economic regulation with relatively clear addressees and objects. All the rules and regulations had someone that was given a right or that was forbidden to do something. The application of the rules and regulations was formally straightforward legal (and economic) techniques. It is well reported[1] that the European Court of Justice (ECJ) took the primary role of constitutionalisation on the basis of its mandate to create and maintain an effective rule of law for the community economic law. The ECJ was responsible for the necessary experimentalism with regard to the unforeseen situations, hence the slogan 'integration through law'.[2] However, in practice it was hardly a straightforward application of law in new situations, but rather a more nuanced development in which the Court had to keep an eye on majoritarian acceptability of its more far-stretching interpretations.[3] In addition, already in the Treaty of Rome and even more so in the Single European Act, there were elements that could not be considered as part of the economic constitution at least in the ordoliberal sense. Common Agricultural Policy and later Common Industrial Policies were typical economic political programmes that were concentrated in and decided upon interest battles. They could probably be defined as administrative programmes and policies that were designed to allocate public resources to specific fields in order to (hopefully) gain some desired societal outcomes. The role of judiciary was mostly small and focused on administrative law. In addition, despite the fact that they ate up most of the Common resources, they actually had relatively small impact at the level of the whole economy and even less to the future shape of national economies of the Community.[4]

The second main layer of European economic constitution was introduced with the Maastricht Treaty that was signed in 1992. Most important provisions included the common monetary policy and the related rules for the conduct of national fiscal policies. The envisaged role of the ECB was also designed in the Maastricht Treaty, but the legal provisions of the Treaty need to be complemented by other material in order to become understandable as a functional whole, a consistent set of constitutional principles. This material include the general economic constitution and economic constitutionalism,

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[1] For example, in de Búrca and Weiler (2001)

[2] Probably first times used by Cappelletti, Seccombe and Weiler (1985)

[3] Miguel Poiares Maduro (1998) has explained the process more thoroughly with regard to previous article 30 on free movement of goods

[4] One could claim that they represented some sort of terminal treatment for some sectors that were financed as a down-payment for agreement on other parts of the economic constitution.

influence of the German Bundesbank as a model for the common central bank and the consensus of the monetary economics that started to emerge from the late 1970s onwards until the finalisation of the Maastricht Treaty in the early 1990s. A thorough constitutional analysis of common monetary policy framework is not the purpose of this chapter. The key constitutional principles I have derived elsewhere[5] could be summarised in six elements.

Price stability (I) has a fundamental role not only for the ECB and euro-system but for the EU economic policy framework as a whole. Stable prices are a fundamental part of the economic and social systemic choice rather than only a question of economic optimisation based on narrow theoretical and empirical research. There are hence no situations where the ECB could compromise the primary objective or balance it with other objectives.

Prohibition of public financing (II) is a protection principle that safeguards the primary objective. In the EU context, the prohibition also protects member states from the accumulation of liabilities by the ECB, which could indirectly lead to a loss of national budgetary control. In that respect it also mirrors the non-bail out clause of the Treaty, which contains budgetary responsibility within national borders. Against this background, it is clear that the necessary leeway given to the ECB in using government bonds in its monetary policy operations should be interpreted with extreme caution. In addition, a resulting creditor role for the ECB towards member states governments would also be against the institutional balance and hence a further argument against public sector financing of the ECB.

Independence of the central bank (III) is a key institutional element that is safeguarded in a number of ways and it is supported by all the three additional legal materials mentioned earlier. Indeed, the broader acceptance of the argumentation for central bank independence was one of the reasons facilitating the creation of EMU. Only if central bank independence was an elementary and useful part of monetary policy set-up, was it plausible to transfer it to the EU level, where there were no effective means for democratic controls nor were such controls designed as part of the transfer.

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[5] For example in Klaus Tuori (2012).

Advancing and respecting principles of an open market economy with free competition (IV) link the common monetary policy directly to the objectives of the European economic constitution. The ECB has to obey market economy based economic rationale in its own actions and should assess the impact of its decision and objectives with a reference to the principles of free competition based market economy.

The role of central bank is limited to achieving pre-defined objectives and excluding areas needing political value judgements (V). The ECB is given very limited discretion to expand its role even with the consent of the EU Council. Designed as an independent organisation with limited or no democratic control, the ECB is a typical European economic constitution institution. Hence, its role should be limited to pre-defined tasks that can be controlled also by judicial means. A corollary of the limited role and lack of democratic control is that it excludes any redistributive elements in the ECB policy as it is not given power to make political value-based decisions.

Defined strategy and operational targets (VI) are less obvious parts of the constitutional principles. The pre-defined strategy is needed to facilitate the accountability of the ECB in particular towards the people of the euro area. In addition, pre-announced strategy and intermediate targets were important part in the institutional set-up of the Bundesbank facilitating the de facto independent role and public respect.

These six constitutional principles shape the boundaries of common monetary policy and central bank. Within these limits, the central bank seems to have been given a relatively wide discretion to define and conduct its monetary policy. The constitutional principles and the European economic constitution more generally should not be seen to contain or follow some political ideology as such. In the same vain, no political ideology could claim priority in the interpretation of the constitutional principles. That being said, it is obvious that the market-liberal undertone in the constitutional principles can hardly be neglected as that comes through the Treaty articles rather than interpretation.

Before turning to discussion on theoretical models to describe the ECB and its role in the economy, an additional clarification on the somewhat complex EU central banking model is warranted. Namely, should see the European System of Central Banks (ESCB) comprising national central banks as well as the ECB as a uniform entity that can be analysed as one unity or should it rather be perceived as a network of national central banks in which internal relations deserve a major role. I would also argue that in the conduct of core common monetary policy, there is one uniform central bank whose actions are conducted by national central banks as its agents. They have the same objectives and task and the same decision-making. Hence, for the present analyses the ESCB (or eurosystem) could be seen as a uniform body and can be analysed under its decision-making body, namely the ECB. In the areas that are less easily qualified as monetary policy, there could be considerable cross-country variation in the roles of the national central banks and also in their reactions to the events of the economy. However, asymmetric reactions of the eurosystem or the discussion of potential influence of the national needs in common decision-making remains outside the scope of this chapter.

The main roles of the administrative organs

In order to analyse the role and actions of the ECB, we need some theoretical ideal models that help to clarify what kind of coherent and consistent roles economic-political institutions can have within a society and what kind of requirements should be assigned to such roles. The two main ideal model roles are expert and politician. At the institutional level they could be labelled as independent expert body and political agent, at least to the extent that the institutions are defined solely by one type of a role. However, I would claim that the two ideal models are not exclusive and sufficient to define the actions and roles of contemporary administrative organs such as the ECB, and they need to be complemented with something that I would call a stakeholder role. The theoretical ideal models are hardly exclusive to central banking or to economic governance more generally. They have a direct link to general governance theories at the national and transnational level and the present legal study can draw on the legitimacy theories developed on those broader and more advanced areas of scientific inquiry.[6]

Some terminological clarifications could be needed as the terms used do not have exact scientific definitions. The term ideal model refers to

[6] See for example, Fernando Losada (2012), or Jürgen Habermas (1971).

a pure example of a role that can include a relatively wide set of elements, for example, the type of processes and information that is used, formal position as well as control and accountability techniques. At the institutional level the ideal models of expert and politician have their equivalences in expert body and political agent. In practical world institutions can take more than one type of role at the same time, and the two ideal models are not sufficient to describe the relevant content of those roles. Hence, there is the need for a complementary stakeholder role that does not have an institutional equivalent, because no institution could be exhaustively defined by a stakeholder role. The actual roles that institutions can have need to be revealed by analysing processes, shifting the focus from static institutional analysis towards more dynamic process analysis.

Expert

In the economic constitutional approach the ideal model of independent expert is very important. The role of independent expert is pivotal in a number of key areas of actual conduct of economic constitution with a crucial difference compared to the role of politician. At the general level, the role of independent expert has two pre-conditions. First of all, there needs to be a strong belief that an expert role is best suited to perform a given task in a society. Normally that type of role requires a specific knowledge that is cumulative in organisations. The elementary main substance of the role also needs to involve applying scientific or quasi-scientific tools and information on specific cases. As is clear, modern societies are full of expert functions that are performed by the publicly funded or administered organisations. As a rule, these roles are played by ministries or separate bodies with at minimum some top-level political control. The political control comes for example in the form of funding to the independent expert body or by legislation facilitating that funding.

The second, and more specific is the requirement to perform tasks independently from outside influences, particularly political influences. In practice, an expert can often be and is expected to be independent. It does not need to or is not assumed to take into account issues outside its given field of responsibility. The input information is solely defined by the 'scientific' needs of the process. However, the practical independence of an expert should not be mixed with the intentional or even formal independence of an expert body. In the latter case, there is a perceived possibility or risk of a political intervention, which is seen harmful. Hence, an explicitly independent expert body should not take orders or even advice from and should not be allowed to be given them by, for example, politicians. In this regard, a formally and intentionally independent expert body is always an exception and hence needs strong specific reasoning to argue for such a position.

Jürgen Habermas has labelled this type of decision-making as a technocratic model. There is no longer any room or need for political decision-making when scientific rationalisation reduces available options to one. Decisions are based on the most efficient way of applying available techniques to solve problems. However, the model crucially assumes that there is a continuum of objective rationality that can and must be applied (Habermas 1971: 63–64).

The purest examples of the independent expert bodies include judicial courts and also competition authorities. In the case of courts, it is a surprisingly recent development that they were given a constitutionally protected independent position (see for example Hayek 2006[1960]: 168–173). Nowadays it is obviously one of the elementary principles of the *Rechtstaat* that legislative, executive and judicial powers are separated. And even the much debated blurring between the roles of the executive and the legislative in the EU context has kept the independent expert role of the courts intact with the reservation that court faces criticism when it is reaching too far with its interpretations, which could be seen as taking a political role.

To assign competition authorities an independent expert role started to gain theoretical and also practical support during the first half of the twentieth century. It is particularly European or more precisely German ordoliberal notion that the role of competition authority is of elementary importance in maintaining the proper functioning of the economic system and eventually a liberal society.[7] In order for the competition authority to play this important role it needs both strong expert knowledge and full independence. Without expert knowledge it is not able to apply very specific rules to varying type of situations

[7] Of course, one should not underestimate the importance of the US tradition that facilitated the implementation of German competition authority after the war.

in a coherent manner. Independence must be guaranteed as the economic interest involved could be such that they would risk taking over the political system with harmful consequences for the economic system but more fundamentally also for the political system.[8]

The independent expert role of the central banks is an even more recent phenomenon, and actually the first clear example of macro-economic management being assigned to independent expert bodies. The idea of independent central bank has been based on both empirical and theoretical consideration in economics. On the theoretical side, the main new innovations took place in the 1970s with the introduction of rational expectations and game-theoretical considerations to the conduct of economic policy. At the same time, there was more empirical evidence that Western economies had become inflation-prone with seemingly negative implications to growth and economic stability. There the solution offered was to basically follow the practice of the German Bundesbank that had gained at least practical independence in conducting monetary policy that aimed at price stability. In practice, countries started to give independence to monetary authorities from the 1980s onwards,[9] and it continues to be the preferred form of organising the monetary institutional set-up that is suggested by the International Monetary Fund (IMF) to countries up to this day:[10] 'Legal structure and autonomy: Government interference can undermine a central bank's autonomy and increase the risks in its operations'.[11]

The means to safeguard the independent position of an expert body are mostly legal and even constitutional. The most straightforward means to create a protected field of operation is to stipulate it in a written constitution. However, it is by no means the only one. Societies with longer tradition can have unwritten constitutional norms (England is the prime example). In addition, a protected

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[8] This refers to the ordoliberal nightmare of interest group society that is well described for example in Eucken (1950/52).

[9] One of the most influential examples is the practical non-inflationary independence given to the US Federal Reserve during the period of Paul Volcker in 1979–1987.

[10] See for example, Arnone *et al.* (2006).

[11] IMF (2013) *Protecting IMF Resources: Safeguards Assessments of Central Banks*, International Monetary Fund Factsheet, retrieved from: <http://www.imf.org/external/np/exr/facts/safe.htm>(last accessed 10 February 2014).

independent expert position can also be achieved through popular support of the people as was the case with the German Bundesbank, the notoriously independent German central bank. In the same vein, if an organ does not gain public support for its role and actions, its independent position will become in the longer term increasingly more difficult to maintain, even if it is formally protected in the constitution. In that respect even the independent and non-democratically controlled institutions still continue operate 'in the shadow of democratic majorities' (Scharpf 2009: 176).

Hand in hand with the independent expert role is the constitutional control of a body acting in that role, accountability of the independent institution. The control mechanisms for the independent expert bodies need to be designed in a specific way. On one hand, control mechanisms should be such that they do not effectively remove the independence of the expert. On the other hand, they should make sure that the expert body does not misuse the discretion it has been given. There needs to be an effective juridical control of the actions, which is considerably more complex to organise than would appear at first sight. Actions must be such that they can be exposed to judicial scrutiny, which also demands that the underlying issues are such that there is a possibility to make straightforward and rule-based judgements on them. In addition, there needs to be an effective possibility and even responsibility to start legal proceedings against the independent organisation in case there is any serious doubt of failures or exceeding of the mandate.

In addition to judicial control, the second and possibly the most important means for control is public accountability through transparency and publicity of actions. This again has more to it than would first appear. Actions need to be taken in forms that allow for effective transparency, not full publicity as such (Issing 2005). Indeed, many of the functions that are assigned to independent experts are such that it is deemed that full publicity does not serve the best interest of the society, but that should not be misused to prevent accountability of the institutions actions. It simply puts additional pressure on the institution to find effective ways to remain transparent and accountable. Public discourse needs to have sufficient amount of information to facilitate formation of views, which often demands that the independent expert goes to great lengths in explaining its actions and itself facilitates external scientific analyses of its activities.

What supports transparency is that it is often deemed necessary for the institution to achieve its aims. It both facilitates public support for the actions and also helps to guide activities of the institutions addressees to the aimed direction without recourse to more coercive means. Be it court, competition authority or central bank, getting potential addressees of its action to understand and internalise the rationality of its action greatly reduced the need to use more drastic measures. In contrast, if the main rationality is based on undisclosed private information, the possibility for an independent position is far more difficult to argue.

Politician

If the independent expert role is the exception, the role of politician is the rule. The political decision-making is the basis for all the public decision-making and its results are the acts of self-representation of a given population or a state. In the public decision-making, all the deviations from the political decision-making should be seen as exceptions and in need of specific rationalisations. The ideal model for a role of politician refers to an actor that makes political decisions. Its institutional equivalence is political agent, a body that derives its powers directly from the political decision-making, which for the purpose of this analysis have a few crucial features. First of all, political decisions can contain value judgements. They are decisions that shape societies and give expressions of their views on broad range issues that by definition do not have 'scientifically' derived correct single alternatives. In a democratic society, delegating value judgements to administrative bodies, let alone independent bodies is highly problematic. Administrative bodies obviously give physical appearance to those value decisions on individual cases, but should have only limited discretion in the actual formulation of the values-decisions.

Second, at core of the political decision-making is determining how the tax burden is shared and how the proceedings are spent. For example, the German constitutional court has emphasised that parliaments budgetary power is a core element of the Germanys self-representation. The contrary argument should make it clear. If we would assume that any group of people could be subjected to unlimited amount of financial liabilities without any say on the issue, we would use words like slavery or dictatorship rather than democracy. Indeed, in a modern liberal society, the majority of the self-representation of a nation takes the form of deciding about public expenditure and the allocation of the financing burden of the aggregate expenditure. That includes also the allocation of financing burdens between generations. The link between democracy and taxation is also reflected in the classical 'no taxation without representation'–slogan initially used by the Thirteen Colonies spokesmen.

Thirdly, ideal model for a role of political decision-making includes an assumption that there is some kind of process to decide between conflicting views in an organised and hopefully open manner. The conflicting views should represent those of the people and the decision-making process should have some direct or indirect input from the people at best on equalitarian terms. Here one elementary feature is that the process does not necessarily anticipate or have preconditions for the type of issues that could be tackled.

The constitutional requirements for the political process are manifold and depend on the specifics of a given system. However, the ideal model of politician or political agent has the backing of the long history of the republican traditions and the development of the republican legitimacy discourses. Without being exhaustive, I could site Scharpf:

> [t]he orientation of representatives to the common good is to be ensured by the twin mechanisms of public deliberation and electoral accountability, while the egalitarianism of democratic republicanism is reflected in the fundamental commitment to universal and equal suffrage.
>
> (Scharpf 2009: 174–175)

Indeed, the constitutional demand for the political role is that it needs to have continuous input from the people, and if that takes place via representative democracy, the mandates need to be renewed at relatively constant intervals. Obviously, for the EU these legitimacy mechanisms are struggling even though there is the vast number of theories assuming various democratic input mechanisms, either through the EU parliament or through member states own democratic processes.

Stakeholder

There are a number of examples of actual roles of public institutions that cannot be described by the ideal model roles discussed before or some combination of the two. I suggest that the ideal models are complemented by a role of stakeholder that is not an ideal model role nor does it have an institutional equivalent. The role of stakeholder is conceptually more difficult than roles of expert and politician, because it elaborates an institutions role with regard to some processes or some other institutions. As a static or stand-alone role it has a very limited content. However, in a dynamic observation, it is helpful and important in order to show how other influences than 'science'-based information force their way into the decision-making processes of institutions, particularly independent expert bodies. In order to understand how the role of stakeholder could be seen as complementary role for an institution or particularly the ECB, it is necessary to discuss stakeholder role more generally.

A stakeholder is commonly defined as a party that is affected by the outcome of the process or the decision of an institution. A stakeholder has something at stake in the process. Generally speaking this is not perceived good or bad as such. An elementary part is that the driving forces of stakeholders are such that it has a vested interest in a given outcome. Actually, a stakeholder influence can be seen as complementary to democratic legitimacy particularly in some areas of economic governance (Losada 2012: 4–5).

Stakeholder is different from the owner of the process. A broadly defined owner is the core beneficiary or the main responsible body of the process. Some examples could help clarify the difference between owners and stakeholders. Private companies have owners in the form of shareholders that have ultimate say in the company and also are entitled to economic profit generated by the company. Company has also a large number of stakeholders that have something at stake in the success of the company: employees in the form of decent work environment and salary, clients in the form of being able fulfil their needs and also public sector not least in the form of tax revenues. Similarly, an independent central bank is often core owner of the price stability, when it is defined as the main responsible body for achieving it. Price stability can have other owners as well if it is assigned as an objective for general economic policy as is the case in the EU. In addition, the owner of process aiming at price stability tries to incorporate a large number of parties as stakeholders in the process, including social partners, financial markets but also normal citizens.

Stakeholder analysis is commonly looked from the owners or initiators perspective. As a first step, the aim of the analyses is to reveal what are the important parties that would need to be engaged in the process to achieve the targets. Second step is then to define strategies or shorter-term tactics on how to increase the likelihood of getting key actors behind desired actions or outcomes. The matrix below is a simplified example of how to classify potential parties by using two variables: the power of the stakeholder and the level of interest of the stakeholder. Key players are the one that have both substantial power over the outcome of the process and also have a high level of interest in the positive outcome.

Table 11.1 Stakeholder matrix

Level of power	Keep Satisfied	Key Players
	Minimum effort	Keep informed

Level of interest

An independent expert that is assigned a task to apply scientific information and tools to a specific set of issues is the owner of its own process. In practice independent experts need to engage stakeholders in their processes in order to yield desired outcomes. However, that should not be a problem for either independence or accountability of the expert. It remains the main responsible body for the process and it can be judged on the basis of its actions and outcomes. Judicial courts have a large number of stakeholders in producing legal certainty and generally respectable legal order. They keep public informed about their actions; they need press to transmit information, legal professionals to run the cases and so on. However, these stakeholders hardly risk independence or accountability of the courts. Similarly, using the table above for competition authorities, they need to keep high level political power satisfied and broad public involved with the provision of information of its actions and their positive impacts. They also need to engage company sector in the process so that companies understand what actions are not accepted.

In the case of central banks, their key stakeholders are social partners and also financial markets that need to play their part in the process in order to achieve stable prices with the least social cost. They also need the support of the other economic agents and to keep the man on the street informed about their aims and also successes in achieving these aims. Bundesbank has been considered particularly skilful in this respect, as it managed to convince the German public that monetary stability and the postwar *wirtschaftswunder* were linked to and facilitated by a strong and independent central bank. In addition, Bundesbank was claimed to have made social partners as stakeholders in its price stability process, which reduced the social cost of achieving it.[12]

Having hopefully described what is meant by stakeholder role generally, it is time turn to the crucial distinction for the purpose of this analysis. What happens to the independent experts of politicians when they become stakeholders in someone else's process? I would argue that particularly for independent expert that can be problematic. If it has something at stake in someone else's process, it is no longer in full charge of its own destiny. Its role as stakeholder can easily cause a conflict of interest with its main area of responsibility. It would seem that with regard to ideal model role of politician, the situation is less problematic. In that case, the stakeholder role could be seen in the light of the pragmatistic model by Habermas, in which 'the strict separation of between the function of the expert and the politician is replaced by a critical interaction' (Habermas 1971: 66). In that form, political (democratic) inputs penetrate the process of the expert to fill the gaps in the scientific rationality and also to facilitate the self-understanding of the polity. In that case, the political role could continue to claim ownership of the process or part of it.

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[12] Slightly simplified, if a central bank manages to steer the wage expectations and negotiations closer to the level of productivity increases, it can keep the level of wage-inflation at a desired level without causing negative effects on employment.

The stakeholder role can complicate the accountability and legitimacy considerations of the ideal models, as increases vagueness of the actual roles. This would again be the most complicated in the case where independent expert becomes a stakeholder in someone else's process outside its stipulated mandate. If the is not the case, there could be accountability vacuum particularly if the independent expert is not excessively open and transparent in its stakeholder role and potential conflicts of interest. In order to facilitate control or corrective measures, it should also be as open as possible.

Theoretical roles in the context of analysing ECB

It is clear that the role of independent expert was envisaged for the ECB by the constitutional principles mentioned previously. Actually, the institutional guarantees for its independence are quite exceptional even among central banks or other independent expert bodies. The position of the ECB is stipulated at the level of EU treaties meaning that any change in its formal status needs to be approved by all the member states. Being the outmost example of the independent expert body, does the ECB fulfil the criteria set for such a position? Firstly, was it perceived that the central bank independence from political was needed? The answer is clearly affirmative. Although the member states might have had varying views on the organising monetary affairs nationally, it is quite clear from the preparatory work and most importantly from the actual Treaty stipulations that the common central banking system was not to become a battleground for political the discussions. The political interference in the monetary policy decision-making was excluded as harmful.

The other criterion for the independent expert position raises more questions with regard to the ECB, namely that the tasks assigned to expert body are such that purely scientific rationalisation can be applied in order to yield optimal societal outcomes. If the scientific rationalisation would not apply in all circumstances, it raises the question of whether political inputs are needed to fill the gaps and how these political inputs could be incorporated. While I see a lot of value in the original thinking whereby the narrow central banking role could be defined in a manner that would fulfil the expert role, it obviously remains an open question. If the tasks given to the ECB or even more so tasks the ECB has assumed during the crisis are such that they cannot successfully carried out without recourse to actions that are only compatible with a political role, it shakes the foundations of the original thinking. However, I would claim that it is ultimately a scientific question formulation of which the current chapter also tries to contribute to.

For the purpose of present analysis, the relevant issue is whether the ECB has remained within borders of independent expert role. Two potential risks need to be analysed. First, has the ECB assumed a political role? Second, whether the owners of some other processes have been able to engage the ECB as a stakeholder in their processes. There are at least two main suspects that I will discuss in the next section: (a) has the ECB become a stakeholder in the financial stability of the euro area banking system or even in the profitability of individual institutions and (b) has the ECB's deep involvement and also financial exposure to single member states deprived it its ability to act as an independent expert vis-à-vis a member states fiscal situation. In other words, has the independent expert role of the ECB become questioned by the potential roles of stakeholder in either euro area banking sector solvency or in member states' public finances or in both.

The new roles of the ECB

In order to focus on the major substantive constitutional issues, I will only describe the stylised facts of the most interesting new type of actions by the ECB. I have discussed the actual measures taken by the ECB elsewhere more thoroughly (Tuori 2012). They could be put in two groups according to the main concern of the action, financial market crises actions and fiscal crises actions. It is somewhat arbitrary to draw a line between the two types of actions, as many of the measures by the ECB since early 2010 could be explained by either of the crises, which furthermore have become increasingly more interlinked not least through the actions of the ECB.

The link between banking sector and the central bank is generally not very simple and straightforward. Modern central banks have always had close ties with the banking sector.[13] Banking sector is the main channel through which central banks try to influence the supply of money and liquidity condition of the financial system more generally.

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[13] The US Federal Reserve was even initially founded to support banking sector liquidity.

In the case of the ECB, the banking sector was intentionally made to be a debtor towards the ECB by imposing minimum reserve requirements on banks, which forced banks to make minimum reserve deposits at their local central banks.[14]

Notwithstanding or even because of these close and substantial ties between banks and central banks of the ESCB, there was supposed to be a very clear borderline between the banking sector and the ECB. In concrete term, the ECB was not supposing at any case to be involved in the provision of solvency support to the banks (i.e. capital support). Hence all the lending was to take place only against sufficient collateral and have short term maturity as a rule. The demarcation line between allowed liquidity support and prohibited solvency support is somewhat unclear en ante. And even ex post, it is possible that fully justified liquidity support results in credit losses, and that measures aiming at restoring capital position of banks do not cause any visible losses. This notwithstanding, the principle is very clear. No such situation should arise, where the ECB needs to concern itself with the fact that its monetary policy action might result in its own capital being eroded through losses incurred by banks. In that case, the ECB would have become a stakeholder in banking sector profitability, which would be directly against the constitutional principles mentioned earlier.

The broad list of action during the peak of the financial market crises circled around means to resist the falling liquidity of the banking sector. Firstly, with the extensive expansion of the list of eligible collateral and resulting variability and average decline in the collateral asset quality, the ECB has potentially become more exposed to the profitability variation of the banking sector. Obviously, this is also demonstrated by the fact that ECB's total exposure towards the banking sector has increased from approximately 200 billion euros in the middle of 2000, and from 480 billion in the middle of 2007 to more than 1400 billion as of the end of September 2012. At the end of

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[14] See for example European Central Bank, *Monetary Policy Transmission in the Euro Area, a Decade after the Introduction of the Euro*, Monthly Bulletin, May 2010, retrieved from: <http://www.ecb.europa.eu/pub/pdf/other/mb201005en_pp85-98en.pdf> (last accessed 6 March 2014); and also Guideline of the ECB of 20 September 2011 on Monetary Policy Instruments and Procedures of the Eurosystem (recast) (ECB/2011/14) OJ L 331, 14 December 2011, 1–95.

January 2013, the claims on banks stood at 1140 billion euros. While all this expansion with the exception of the so-called Emergency Liquidity Assistance (ELA) by some national central banks has nominally been simply liquidity provision and has as of now resulted in very marginal actual credit losses, it cannot be denied that the ECB has become a major stakeholder in the euro area banking system. This was further expanded with the creation of European Systemic Risk Board under the organisation of the ECB,[15] which made the explicit division between monetary policy and supervisory policy responsibilities less clear and opened the door for further involvement of the ECB in the support operations of the financial sector, which is currently discussed under the heading of banking union.

The main actions of the ECB with regard to the fiscal crisis could be summarised in three groups. First group consists of verbal interventions and other involvement in drafting rescue plans of the member states facing fiscal challenges and also controlling the implementation of those plans. The involvement has exceeded the more traditional commenting on the fiscal policy stance and even more often on the fiscal sustainability, which was part of the ECB expert role from the start. However, before the Greek situation, the ECB refrained from commenting on individual member states and made sure that it did not get involved in the actual fiscal policy discussions of individual countries in order not to disturb the institutional balance and responsibilities. However, as the Greek fiscal situation became worse and the country was becoming excluded from credit market, the ECB became heavily involved in the rescue operations of Greece and also some other euro area member states. The ECB was also insisting with the voice of its governor (Mr. Trichet) that Greece was not allowed to default on its debts.

Second, the ECB changed its collateral policy for Greece and most likely engaged in large scale liquidity creation at abnormally long

[15] Regulation (EU) No 1092/2010 of the European Parliament and of the Council of 24 November 2010 on European Union Macro-Prudential Oversight of the Financial System and Establishing a European Systemic Risk Board, OJ L331, 15 December 2010, 1–11 (the 'ESRB Regulation'); and Council Regulation (EU) No 1096/2010 of 17 November 2010 Conferring Specific Tasks Upon the European Central Bank Concerning the Functioning of the European Systemic Risk Board, OJ L331, 15 December 2010, 162–164.

maturities to encourage market participants to invest in higher-yielding government bonds. Third, and most controversially, the ECB started its Securities Market Programme (SMP), i.e. outright purchased of government bonds of the countries facing fiscal hardships. The programme has been justified by monetary transmission arguments, which however, have raised more questions than provided convincing explanations.[16] The claim is that there has been some sort of renationalisation of money and capital markets in the euro area with the result that monetary transmission differs between areas of the euro area. Most crucially, this differentiation could be fought by purchasing government bonds of the troubled member states. The programme was activated in May 2010 and closed by the end of autumn 2012 with the total exposure of somewhat more than 200 billion euros.[17] It has been replaced by Outright Monetary Transactions programme that was announced in August 2012, which is similar to a large extent but makes the conditionality and a link to adjustment programmes conducted by the euro area member states by the EFSF/ESM a more explicit part of the programme.

How should these new ECB roles be assessed? It could be claimed that the safeguards that were designed for the ECB in the Treaty and also carefully respected in its initial operational framework have been eroded by its own decisions during the crisis. In the short history of central banking, there is an ample amount of examples of failures when central banks become stakeholders in areas that are in potential contradiction with their primary tasks. In the Treaty context two threats of this kind were tackled. First of all, new central banking system was not to become stakeholder in government finances and secondly, it was designed to distant itself from the banking sector potential problems. In both of these regards, the ECB (ESCB) is unlike other central banks working in the nation state setting, but relatively close to the actual conduct of the Deutsche Bundesbank.

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[16] See for example ECB press conference of May 2010 and press release on 10 May 2010 – 'ECB decides on measures to address severe tensions in financial markets', retrieved from: <http://www.ecb.europa.eu/press/pr/date/2010/html/pr100510.en.html> (last accessed 4 April 2014).

[17] The composition of the SMP debt held by the ECB by the end of 2012 was published on 21 February 2013 - Details on securities holdings acquired under the Securities Markets Programme, according to which the total amount was 209 billion euros in book value. The largest holdings were Italian, Spanish and Greek government debt, respectively.

It is in the heart of the monetary policy part of the European economic constitution that the EU central bank was not supposed to have any responsibility of government finances at any level (municipal, member state or EU). This was safeguarded by the prohibition of central bank financing of governments and by the requirement that all lending of the central bank should be based on adequate collateral. In addition, the central bank was assigned an extensive independence also to be able to resist political pressure to finance member states: long fixed-term assignments for the management, own primary objective that was supposed to be respected also by others, and also prohibition to seek or to take advice from external sources.

The above mentioned central banking stipulations of the public finances part of the European economic constitution were one side of the coin where the other side was the member state's responsibility of its own and only of its own public finances. The latter obviously consisted, inter alia, of no-bail out clause of Art 125 in the Treaty of the Functioning of the European Union (TFEU) and excessive deficit procedure of the SGP based on Art 126 TFEU. The central banking part was distancing central bank from a public finances at the member state level and the other part was protecting the common monetary from negative spillover effects of reckless public finances. The ECB was not involved in the operational part of the SGP or any other disciplinary mechanism, because it would have made it a stakeholder in the public finances.

I already made the point that there is a major risk that the ECB has been made a stakeholder in the euro area banking sector. With the massive increase in the lending exposure and simultaneous decline in collateral quality, the ECB would face potentially unbearable losses, if a large number of banks would default on their debts. As the ECB possesses two main elements of banking sector profitability, provision of liquidity and level of short-term interest rates, it is not irrelevant whether it can consider financial difficulties of individual banks primarily private sector problems and secondarily a member states problems or whether it is in the front line being hit by those difficulties. My assessment would be that there is no longer a certainty that the ECB could function purely as an independent monetary expert, because its stakeholder position vis-à-vis banking sector.

The same analysis would seem to apply in Greek and also some other member states fiscal problems. The ECB has clearly been made a stakeholder in those situations, as it has been involved in the actual rescue operations. Obviously, there is an increasing link between the banking sector problems and fiscal problems as the local banks have been encouraged and also given incentives to buy local government bonds with helpful funding from the ECB. However, it could also be claimed that the ECB has actually taken a political role in the fiscal crisis. The massive increase in indirect and even direct lending to member states is effectively government financing which is fully analogous to spending tax payers' money. For example, the SMP programme and even more the Outright Monetary Transactions (OMT) programme could from the debtor's perspective been exactly the same as having the ECB as their creditor.[18] This is further emphasised by the fact that the ECB has started to act like a creditor towards the countries in question. The letters sent to both Italian and Spanish governments were a case in point.[19]

Against this background, it should not come as a major surprise that particularly the ECB's outright purchases of government bonds have faced fierce criticism from multiple fronts. Most dramatically, current and respected retired German monetary officials have been outspokenly against the programmes, insisting that they have expanded the role of the central bank beyond its constitutional boundaries. In the next section I will discuss how these new roles could be assessed from the constitutional control and legitimacy points of view.

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[18] Decision of the European Central Bank of 14 May 2010 establishing a securities markets programme (ECB/2010/5), OJ L 124 , 20 May 2010, pp. 8-9; ECB Press Release, 6 September 2012 'Technical features of Outright Monetary Transactions', retrieved from: <http://www.ecb.europa.eu/press/pr/date/2012/html/pr120906_1.en.html> (last accessed 18 April 2014).

[19] For the Italian Letter, Federico Fubini, Ecco la lettera di Trichet e Draghi, *Corriere della Sera*, 6th August 2010, retrieved from: <http://www.corriere.it/economia/11_agosto_08/lettera-trichet_238bf868-c17e-11e0-9d6c-129de315fa51.shtml> (last accessed 4 April 2014); For the Spanish letter, see Rodríguez Zapatero (2014).

ECB constitutional controls and democratic legitimacy with new roles?

The constitutional structure for central banking in the euro area relied heavily on the model of apolitical expert function that could in the European economic constitution be assigned to an independent central bank. There are at least three crucial elements in that delegation of powers. First, the tasks assigned are deemed to be such that their operation can be controlled with dual means of juridical control and accountability, mainly through transparency of actions. Second, functions and decisions containing value judgements could be excluded or at least be defined in a rule-based form that can then be assigned to the expert.[20] Thirdly, and related to the previous ones, the functions that are delegated to an independent expert body must be such that they can be defined ex ante relatively precisely. This means that the delegated process is well known and outcomes of given actions are known with relatively high level of certainty, which would be in line with the technocratic model by Habermas. Obviously, there must be some ability to confirm *ex-ante* democratically that the process description and objectives are preferred by the polity, preferably with a large majority. In particular, if the legitimacy discourse is primarily based on the liberal tradition, the role of the broad consent of the people would be highly supportive for the legitimacy of the independent guardian of the monetary stability.

The demand for the above mentioned conditions are stricter if the delegation is made at the higher level, i.e. if the position of the independent expert is constitutionally protected rather than a result of administrative action or normal laws. In the same vain, the more independent the expert function is, the more closely the delegation should follow the preconditions. Against this background, the demands for the delegation in a nation state setting are looser than they are in a Treaty based constitutional set-up such as the EU (or the euro area).

In the case of the ECB, I would argue that the delegated function largely fulfilled the criteria although with some arguably very demanding assumption. The most crucial assumption was that the role of money and monetary policy was seen in a monetarist or in

[20] Obviously this has been a contested perception of central banking.

German ordoliberal perspective. There is also an interesting issue linked to the Scharpf's division of the legitimacy discourses to liberal and republican, respectively. Namely, in the German ordoliberal discourse narrow central banking model with sole objective of monetary stability, central bank could be seen as one main guarantor of the systemic choice for free market economy and ultimately free society.[21] As a result, the euro area monetary environment was closer to an enhanced gold standard than a field of activist monetary policy. However, it would seem questionable, whether all member states realised this or subscribed to it, even if this is the way it was very clearly written in the Treaty of Maastricht.

For the narrow role of the central bank, one could argue that constitutional control mechanisms met at least some minimum criteria. However, a lot was left to the new institution to meet the requirements of transparency and accountability and also to exercise considerable self-restrain with regard to its actions in the borderline cases of its mandate. I have argued that this was well understood by the ECB when designing its monetary policy strategy and also during its first decade of operation.

These constitutional control mechanisms seem to be struggling with the new roles that have elements from stakeholder or politician roles. Transparency and accountability only work if the institution reveals all its influences and aims, and does not try to mislead the public. The main risk in this respect is that the institution continues to describe its actions according to the independent expert function although the substance of the actions is that of a stakeholder or a politician. That would effectively prevent those actions of becoming exposed to public scrutiny they would require even more than the pure expert functions due to their inherent value judgements.

In the unfortunate situation in which accountability through transparency of actions has become void, we are left with judicial control mechanisms. In the case of the ECB this is still mostly untested territory. However, I would give a relatively miniscule probability that in the middle of the crisis, the Court of Justice of the

[21] This is particularly well described in Eucken (1952) in which monetary stability is even the first of the constituent principles of the economic order.

European Union (CJEU) would, for example, order the ECB to narrow down its collateral list and to sell all the government bonds in its possession that it cannot justify on the ground of controlling short-term liquidity. In a recent Pringle case, the Court even failed to find any means in the Treaty to define monetary policy and showed quite limited willingness or ability to engage in argumentation concerning monetary policy related issues.[22] More generally, the juridical control and contested macro-economic policy choices make a poor match as the famous decision on the Stability and Growth Pact also has shown.

Hence, if we assume that the envisaged constitutional control mechanisms are not sufficient to correct the situation, we have to come back to the old question of democratic legitimacy and a given model of administration or governance. The complexity starts with the varying perceptions of the legitimacy itself. Following Christopher Lord (2012) on the subject, there is, first of all, the empirical notion that relies on the acceptability of the use of political power. Without qualifying the concept of acceptability with some moral criteria, it is an ultimately nihilistic (or even Schmittian) description.[23] Indeed, often some notion of moral justification is added to the definition[24] with a potentially detrimental impact on the preciseness and also testability of the concept. The relatively easy and not necessarily uncomfortable way out would be to hold as a starting point that private persons are autonomous subjects that can judge on their own behalf what is acceptable and justified, and this becomes manifested in processes where these people can participate on equal footing. This also justifies some form of coercive actions towards people as long as these actions and their rationales have been deemed justified by the same people acting as a polity (Habermas 1996: 67). Obviously this is not more than to say that democratic processes are the least controversial ways to find out acceptable and justified, i.e. legitimate forms of governance.

If we define criteria of legitimacy as something whereby people consider justified even decisions or administrative actions that they are opposed to, it is easy to see that some link to democratic decision-

[22] Case C-370/12, *Thomas Pringle v Government of Ireland, Ireland and The Attorney General*, [2012] ECR-00000.
[23] Lord (2012: 11) with a reference to both Beetham (1991) and Grafstein (1981).
[24] For example Buchanan (2002)

making is close to elementary. This would seem to hold even in the cases where direct democratic mechanisms are not preferred due to time-inconsistency and prisoners dilemma type of situations, which are obviously also in the heart of delegation of public power to independent experts. The same argumentation has been used to legitimise the whole approach of constitutionalising the main framework for economic action, namely the economic constitution.[25]

With regard to EU there are two additional issues involved in the legitimacy discussion. The first is question of legitimacy to whom, governments or people of EU. It seems clear that at least legitimacy towards or consent of the governments of the member states is necessary. Without consent of the governments (and national courts of justice), the decisions of the EU could not be implemented (Scharpf 2007: 7). More difficult question is, whether the EU needs to be perceived legitimate also towards the people of the EU. There are less convincing arguments to make that hold continuously, but clearly if nothing else the lack of legitimacy should feed into the perceived legitimacy towards the governments. Another issue concerning EU and legitimacy comes from the fact that it is still founded by and based on international treaties. Hence the original commitments of the member states, their consent to the powers of the EU, have a far bigger role than in national political processes. Hence the 'the notion of "no legitimacy without consent" does seem to have a special significance for the European Union' (Lord 2012: 21).

Much has been written about the democratic legitimacy of the ECB or the lack of it. It is clear that in the conduct of ECB monetary policy, there is no mechanism for democratic inputs to influence its action. Quite the contrary, as explained before, the ECB has been carefully protected from democratic inputs to the same manner as from other undue influences. To conclude that the ECB has never been democratic legitimised, is not correct in my view. Here the reference to courts or competition authorities should be useful if not conclusive. Hardly anyone would considerer courts undemocratic because their decisions are not based on democratic process rather than expert knowledge and protected independence in their reasoning.

[25] Among the earliest proponents of the economic constitution, ordoliberals, there was considerable variation in the emphasis of the democratic basis of the systemic choice.

The ECB's relationship with legitimacy is based on a few elements. First of all, the most important democratic legitimatisation takes place at the time system is decided upon. In the case of the ECB, its' position is defined by the European economic constitution that was decided upon in the Maastricht Treaty concerning the supra-nationalisation of monetary policy. In the democratic processes of the member states, monetary order was constitutionalised to contain a certain type of objectives and institutional set-up. The second, and slightly more problematic form of legitimacy, comes from the so called output legitimacy. The system is considered legitimate as long as it provides people of euro area with prosperity and economic stability it has promised.

Both the systemic choice and output legitimacy deserve a fresh look after the series of events we have witnessed in the course of last five years. In particular, the pre-conditions for an independent expert organisation need to be continuously met. If that was not the case, the constitutional control mechanisms would hardly be sufficient. Using constitutional controls of independent expert on political decision-making simply would not make any sense. There are simply no mechanisms to make value-based political decisions in a legitimate manner. In conclusion, if my fears are substantiated, the lack of democratic legitimacy of the ECB has become a problem also from the European economic constitution point of view due to the new roles of the ECB. This goes to the heart of the whole monetary order by questioning the underlying fundamental principles.

The way forward

If my analysis is correct, the current situation, in which the ECB is constitutionally protected as an independent expert and at the same time potentially acting as a stakeholder and a politician, is very problematic on a number of grounds. First, constitutional control mechanisms based on accountability through transparency and deliberations demand sincere openness about all the relevant factors affecting its decisions and actions. That cannot be the case, if the ECB decides or is forced to frame its actions according to the narrow mandate of the independent expert. Second, its decisions in the new areas hardly meet the requirements of the technocratic decision-making model that there should not be any gaps that contain value-judgements in rationalistic application of the scientific information and tools.

Is the Maastricht model of central banking still a viable option?

It could be claimed that the central banking model designed in the Maastricht Treaty and summarised by its constitutional principles in the first section is still a viable option. Looking strictly at the monetary policy part in the narrow sense, it is not obvious that monetary policy could or should have reacted to the economic development fundamentally differently since the start of the euro. In this regard, I would like to discuss three arguably harmful economic developments that have facilitated the crisis and the role strictly and narrowly defined monetary policy should have played in them.

First and most important is the loss of external competitiveness of individual countries of the euro area that has been the root cause of private sector and also public sector problems at least in Greece, Portugal and Spain. With considerable simplifications, the main reasons for the changes in external competitiveness result from internal combination of productivity improvements and wage increases as well as from real effective exchange rate. In addition, there could have been external shocks to individual countries, of which one good example is the Chinese competition to Portuguese textile industry. In a nation-state setting, monetary policy could play a major role in maintaining of the external competiveness. For example, as explained earlier German Bundesbank was an active participant in the labour markets by providing objective and non-partisan information of productivity development to social partners and also credible threat of adverse monetary policy impulses in the cases of wage-inflation. In the cases of small open economies, exchange-rate was extensively used to regain competitiveness, but eventually with quite high social costs and potentially negative medium-term growth effects and adverse structural implications for the economy.

How did the ECB react to the loss of competiveness of individual countries and how should it have reacted? Exchange rate was not considered a tool for the ECB, and indeed an active exchange-rate policy to combat weakened competiveness of individual countries was never an option. While the fluctuations in, for example, euro/USD exchange rate were probably somewhat extensive, they were hardly the main cause of problems. Another issue is whether the ECB or even more so national central banks managed to communicate with (still) national labour markets and national fiscal authorities. My claim would be that there was a clear discontinuation of communication in a number of countries. The central banking expert inputs to labour markets and also fiscal authorities were discontinued or lost relevance, when the local central bank lost its monetary policy power. It is of course also possible that the quality of communication and the level of trust needed were never achieved in many countries.

Second and related problem was the increased level of private indebtedness and vulnerability of the banking sector. In the narrow central banking model, the ECB had only a very limited role vis-à-vis the banking sector. Only the safety of the payment systems was a assigned responsibility, while all the other areas were left at the national responsibility. In this regard, the ECB could not be blamed for the unsustainable development in the banking sector. However, the ECB could have reacted to the continuous increase in the bank lending that clearly showed signs of becoming unsustainable. In the ECB monetary policy strategy, bank lending was given a major although indirect role as a counterparty to monetary aggregates that had a prominent role.[26] However, it is notoriously difficult to analyse whether the credit expansion is unsustainable or not, and in the case of the ECB that was further complicated by the fact that credit expansion varied considerably between countries and were extended to different sectors in different countries.

Third, real and also cyclically-adjusted fiscal deficits in some member states could be seen as a failure also on the part of the ECB. However, in the narrow central banking model in which the ECB only has monetary policy tools in its disposal, it is somewhat difficult to see, how monetary policy should have reacted to fiscal imbalances in individual countries. In the policy-mix discussion, it is sometimes claimed that too restrictive monetary policy on the part of the ECB forced national fiscal policy to take too large a burden of the economic stabilisation. I find this quite unrealistic, as the countries with larger cyclically adjusted fiscal deficits also suffered from wage-

[26] In the ECB monetary policy strategy, money (monetary aggregates) had a prominent role as the second pillar of the strategy.

inflation and losses of competitiveness, the combination that would rather point to structural than cyclical problems, and would have, ceteris paribus, demanded rather higher than lower interest rates.

In conclusion, I find it unresolved whether the Maastricht narrow central banking model was and is a viable solution. In the short analyses, it is not been demonstrated that the conduct of monetary policy could have made a substantial difference on the economic development of the euro area. At the same time, it is easier to point to areas where national responsibility failed. The main democratic and legitimacy problems related to the Maastricht narrow central banking model seem to relate to the national democratic processes that seemed to neglect or disregard demands arising from the new economic and banking policy set-up.

Obviously, with regard to the ECB all the problems mentioned with regard to the stakeholder and political roles raise immediate democratic legitimacy issues that cannot be solved in the narrow central banking model. However, if it was deemed that they resulted from the combination of failures at the national level that are corrected and the very exceptional circumstances in the financial markets that are unlike to re-occur in the foreseeable future, the failure of the ECB to stick to its limited mandate could be resolved by its own actions to reduce its role to fit the narrow central banking model of Maastricht Treaty. In this approach, the areas demanding continuous democratic inputs should be clearly separated from the central banking system.

The extended role requires democratic input-mechanisms

Currently, the narrow central banking model does not seem to be the favoured solution in the EU. In addition to the expansion of the roles of the ECB to include stakeholder and political roles, the ECB is to be given a substantial role in the banking supervision in the so-called banking union that has been decided but still lacks final agreement on the main operational elements.

The extremist independence of the ECB does not bode well with the political role or the role of banking supervisor.[27] The constitutional

[27] In the economics discussions there have been some support for the independent

control mechanisms that could be considered for monetary policy, in particular accountability through transparency added with judicial control as the last frontier, do not work for the stakeholder roles and even less so for a supervisory role. In banking supervision, action is based on confidential information that cannot be disclosed or used to rationalise actions in public.

Supervisory failures lead in practice to implicit responsibilities to guarantee banking sectors even in the cases where no explicit guarantees were given. In particular, protecting deposits is nearly impossible without also guaranteeing whole banking sector, because it is very difficult to keep deposits and other banking liabilities separated. Indeed, the protection of deposits is ultimately a responsibility of the fiscal authority, be it national or supra-national. Bailing-out banks can cause extensive burden on public finances that limit the core democratic decision on taxation and public expenditure. In the actual national cases of banking sector failures with central bank responsible for supervision, it has been ultimately fiscal authority that has buried the cost. Hence, in the cases of supervisory responsibilities and banking failures, the central bank independence has taken a backseat. For example, central bank governors have taken part of the political responsibility of the supervisory failures as a sign of the majoritarian electoral responsibility.

At the EU level, this more flexible model, which is ultimately based on the fact that legislator can change the position of the central bank, cannot be guaranteed to work. If there is deemed to be a need for the stakeholder and political roles including supervisory roles, it would need to be acknowledged and taken into account in building sufficient mechanisms to both incorporate a possibility of accountability and also some form of democratic legitimacy.

The forms of accountability needed for the ECB would seem to depend on the type of argumentation and information that the ECB needs to use for rationalising its actions. If the argumentation is based on sensitive (private) information, it reduces the possibility to gain

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supervisor role, but the case is far more contested than the one on the independence of the monetary authority. These analyses have also neglected the constitutional issues involved, at least to my knowledge.

accountability through explicated transparency towards the general public. In this regard, I would draw the line in banking supervision. If the extended roles of the ECB will also in practice involve a responsibility for actual banking supervision, it needs to be accountable towards the general executive (the euro group?), directly or through a body that is set by that executive. For this accountability to be effective, the level of independence currently assigned to the monetary authority would be totally inappropriate. For example, the people responsible for the banking supervision would need to be replaced on the grounds of lack of trust by the executive.

With regard to the extended responsibilities related to ECB's role as monetary authority, I basically see two options. If we assume that the new functions are approaching the area of political decision-making, they basically would need to be approved by the same bodies that are legitimated to make those decisions in the other areas of the EU. For example, the direct or indirect financing of the member states would need to be approved by the euro area member states. One relatively simple solution would be that the monetary policy strategy is approved by the euro group and potentially also a special committee of the European Parliament. This strategy would include also instruments considered for the conduct of monetary policy.

With regard to the issues related to the ECB's role as a stakeholder in banking sector profitability or member states fiscal position, the above mentioned mechanism would probably need to be accompanied with enhanced transparency. If there are serious doubts on the true motives of the central bank decisions, the speedy publication of the minutes would be of essence if not sufficient. Here, earlier considerations of the national biases dominating discussions would seem quite minor if the credibility of the institution is put in jeopardy by serious perceptions of undue influences.

Re-nationalised monetary policy

Large monetary areas have benefits and problems, and both seem to be dependent on the ability of the national democratic process to solve the (economic) problems that arise internally or through external shocks. In the EU, monetary area was created on the basis of narrowly defined central banking function and on the assumption that although it was not considered an optimal currency area, it would approach one over time. In addition, it was assumed that currency adjustments were not elementary policy tools and that they could be replaced by other types of adjustment mechanisms and policies. The benefits were expected from the increased stability, further economic integration and potentially a bigger say in the global economic discussions. It could be claimed that many of these pre-conditions and assumption were not properly discussed let alone subscribed to in a number of euro area countries, even though they were to a large extent constitutionalised. That has proven to become a major source of instability, both economically and politically.

Against this background, it seems appropriate to ask whether in some euro countries it is only democratically viable option to at least openly discuss the requirements for the euro area membership also in the light of the current experiences. It could well be that the benefits of the membership would have hard time matching the costs particularly in the case of Greece. In either case, the fact that there would be true democratic discussion and decision would help to end the erosion of democracy and trust in public institutions. Current no-alternatives approach could seriously undermine democracy at the member state level and legitimacy of the EU.

The problem of democratic legitimacy could become worse if the current trend of imposing mutual responsibility continues without some democratic inputs. I would argue that even the previously mentioned model, which includes fundamental changes to the constitutional position of the ECB and common economic and supervisory policies, is too large a step without some form of consent. In particular, the actual implications for the national social policy, labour markets and economic policy more generally are such that they could fundamentally alter the costs and benefits balance of the EMU for some member states.

It has been claimed that the any serious option for countries to reconsider their membership in the euro area would lead to a chaos and likely to be the end of EU. However, I would argue that it is possible or even likely that some countries will continuously feel that the costs of the euro membership are far higher than its benefits. If they are not given a possibility to democratically decide on an orderly exit that would turn out to be very destabilising for the euro area and destructive for the democratic legitimacy of the EU (and national governments in those countries). Exclusion of the most pressing questions from the public discussion is hardly the most fruitful way forward.

Conclusions

When the institutional set-up for the common currency and monetary policy was designed, the newly established central banking system and its core, the ECB, was based on model of independent expert body. Monetary policy was to be conducted in a manner that did not need democratic inputs, because the objective of stable prices was to be achieved best through 'scientific' process based solely on expert knowledge. The role of politician was excluded from the central bank. The central bank was also to distance itself from other influences like banking sector problems or reckless public finances of the member states. It was not to become a stakeholder in either banking sector or public finances.

The financial and fiscal crises have questioned this model. It is no longer clear that the ECB does not play a political role. In the same vain, it is far from obvious that the ECB can consider banking sector problems outside its concerns. Similar stakeholder role could have developed vis-à-vis member state public finances. With these potential roles of a political agent and a stakeholder, the constitutional control mechanisms envisaged for the ECB are struggling questioning the core legitimacy of the institution. The choice is quite obvious. Either the ECB needs to go back to its independent expert role or constitutional control mechanisms need to take this change into account. In the latter case, at least, the legitimacy basis from the Treaties is hardly sufficient.

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Chapter 12

Europeanising prudential banking supervision
Legal foundations and implications for European integration

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Introduction

The establishment of the Single Supervisory Mechanism (SSM) is a milestone in European integration. The Council decided to transfer to a European institution – the European Central Bank (ECB) – the direct exercise of a wide range of supervisory competences in the single market. The last comparable precedent is the introduction of the euro, which transferred monetary policy to the European System of Central Banks (ESCB), and, before that, the completion of the single market more than twenty years ago in 1992.[1]

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[*] The views expressed are those of the author and do not represent necessarily those of his institution. Comments are welcome to pedro.teixeira@eui.eu

[1] The SSM was established on […] 2013, on the basis of Council Regulation (EU) No. 1024/2013 of 15 October 2013 Conferring Specific Tasks on the European Central Bank Concerning Policies Relating to the Prudential Supervision of Credit Institutions (henceforth, 'the SSM Regulation'), OJ L287, 63–89. The Council Regulation was adopted on the basis of Article 127(6) of the Treaty of the Functioning of the European Union (TFEU), which enables the Council to unanimously, and after consulting the European Parliament and the European Central Bank, confer specific tasks upon the European Central Bank concerning policies relating to the prudential supervision of credit institutions and other financial institutions with the exception of insurance undertakings. See also European Parliament, Banking Union, Banking Union and a Single Supervisory

The creation of the SSM is a response to the 'eurocrisis', the combination of the financial and public debt crises affecting Europe and the euro area. It follows a now long line of successive institutional and legal responses since 2007, which included the establishment of the European Financial Stability Facility and later the European Stability Mechanism (ESM); the amendment of Article 136 of the Treaty to legitimise the setting-up of ESM outside the Treaty; the adoption of the 'Euro Plus Pact'; the creation of three European Supervisory Authorities as agencies with broad competences and powers of intervention, as well as of the European Systemic Risk Board to safeguard financial stability; the reform of economic governance on the basis of the 'Six-Pack' proposals to strengthen the Stability and Growth Pact; and the Treaty on Stability, Coordination and Governance in the EMU (TSCG).[2]

There are several political, legal and institutional undercurrents to this sequence of European responses. They become visible through recurring constitutional trends, which, while deepening integration stitch by stitch, also end up questioning fundamental principles of the existing European constitutional order, including its democratic

Mechanism, retrieved from: <http://bookshop.europa.eu/en/banking-union-and-single-banking-supervisory-mechanism-pbBA3112149/downloads/BA-31-12-149-EN-C/BA3112149ENC_002.pdf?FileName=BA3112149ENC_002.pdf&SKU=BA3112149ENC_PDF&CatalogueNumber=BA-31-12-149-EN-C> (last accessed 2 April 2014); and Opinion of the ECB of 27 November 2012 on a Proposal for a Council Regulation Conferring Specific Tasks on the ECB Concerning Policies Relating to the Prudential Supervision of Credit Institutions and a Proposal for a Regulation of the European Parliament and of the Council Amending Regulation (EU) No 1093/2010 establishing a European Supervisory Authority (European Banking Authority) (CON/2012/96), OJ C 30, 1 February 2013, 6–11, p. 6. The functioning of the European Banking Authority was adjusted to the establishment of the SSM by Regulation (EU) No. 1022/2013 of the European Parliament of the Council of 22 October 2013 Amending Regulation (EU) No 1093/2010 Establishing a European Supervisory Authority (European Banking Authority) as Regards the Conferral of Specific Tasks on the European Central Bank Pursuant to Council Regulation (EU) No 1024/2013, OJ L287, 29 October 2013, 5-14.

[2] The most relevant decisions are conveyed in the Statements of the Heads of State or Government of the Euro Area from 25 March 2010 till 29 June 2012, available at http://www.european-council.europa.eu/council-meetings/conclusions (last accessed 4 April 2014).

legitimacy, as argued extensively in academic literature and public commentary.[3]

The constitutional trends in the responses outlined above are many, but are encapsulated in the following three main processes. The first is the emergence of a new EU method of action characterised by a minimisation of the role of the Community channels and a reinforcement of intergovernmental decision-making. The main example is the role of Euro Summits in addressing the crisis. The second process corresponds to the legal evolution of EU action, which is progressively replacing 'soft governance' by 'hard enforcement' structures to ensure compliance by member states. This is also marked by the preference for technocratic solutions, which are insulated from the political interests of individual member states. The legal and institutional instruments operating such shift are both within and outside the Treaty, combining EU law, public international law, and national laws. This, in turn, is also leading to a composite architecture of integration combining European and national competences. Examples include the ESM Treaty, the 'Euro Plus Pact' and the TSCG. The third process regards the gradual but quick forging ahead of integration around EMU. There is an increasing differentiation of EMU within the EU, which manifests itself in specific decision-making bodies, institutional arrangements and legal instruments of integration, such as the Euro Summits, the Eurogroup, the ESM, the TSCG and others. Furthermore, the differentiation is not limited to the core EMU policies but extends itself to policy fields relevant for the EU as a whole, including the single market. This challenges the unity of the Union, as demonstrated by the political dynamics of opting-in and opting-out by the member states leading to variable geometries and variable configurations.[4] More deeply, such differentiation underpins the gradual transformation of EMU from a 'community of benefits' to a 'community of risk-sharing', where all member states not only share the benefits from integration but also the risks and potential costs it brings. This is a profound transformation that presupposes, not only the strengthening of

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[3] For a critical analysis of the key responses to the crisis, see Joerges 2012, Offe 2013. See the arguments expanded in Chiti *et al.* (2012).

[4] For example, 18 of the 28 member states participate in the euro area, in the European Financial Stability Facility (EFSF) and in the ESM Treaty, but 23 member states have agreed the Euro Plus Pact, and 25 member states have signed the TSCG.

solidarity and loyalty between member states, but also new sources of democratic legitimacy at the European and national levels.[5]

This contribution, while describing and analysing its unique features, takes the SSM as a 'case-study' to assess the extent to which the underlying constitutional trends of previous European responses to the crisis are also present in its legal and institutional construction. It starts with a brief history of the single financial market (Section 1). Each phase of its legal and institutional evolution, while reflecting the spirit of the time in the approach to integration, also represented a delicate equilibrium between the expansion of European competences and the safeguarding of national sovereignty. One equilibrium gave way to another when new legal and institutional innovations were introduced to deepen integration at the boundaries of what could be achieved under the Treaty. Likewise, the responses to the 'eurocrisis' have touched the limits of the Treaty and triggered a number of constitutionally relevant processes that are reshaping European integration as a whole.

From this analytical perspective, Section 2 addresses the rationale of the decision of the Euro Area Summit of June 2012 to establish the SSM, which related to the need to enable the direct assistance of banks by the ESM to contain the public debt crisis. The debated choice to use Article 127.6 TFEU as the legal basis of the SSM is the subject of Section 3. This provision is key for understanding the SSM's 'genetic code': the unique legal and institutional features of the SSM reflect the tensions of belonging to the framework of both the EMU and the single financial market. Such unique features are analysed in the successive sections and include: the complex matrix of competences of the SSM (Section 4); the mechanisms for the participation of the member states from outside the euro area in the SSM (Section 5); the principle of separation from monetary policy as encapsulated in the design of the decision-making process of the SSM, involving both a Supervisory Board and the Governing Council of the ECB (Section 6); and the supervisory independence and democratic accountability of the SSM, which involves specific channels, including relations not only with the European Parliament but also with national parliaments (Section 7). The contribution

[5] This represents a summary of the analysis in Chiti and Teixeira (2013).

concludes by identifying the legal and institutional trends marking a new phase in the evolution of the single financial market – the Banking Union – with wider constitutional implications for the process of European integration. Avenues for further research are also suggested at the end.

A brief legal history of the single financial market

A single financial market was not one of original objectives of European integration. The Treaty of Rome of 1957 did not envisage a financial market as one of the components of the common market; and the movement of capital was not a basic freedom in the framework of the Community until the Single European Act entered into force some thirty years later.[6] The underlying reason was the same that has been at the heart of the evolution of the single financial market until the present day: the fact that finance and its regulation stands at the core of national sovereignty in areas that include economic and industrial policy, monetary policy, budgetary policy, including the financing of the state through public debt, and taxation, which includes the capacity of the state to bail-out financial institutions with public funds. Relinquishing sovereignty in these areas constrains the core of political sovereignty.[7]

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[6] The original version of Article 67 of the Treaty of Rome of 1957 provided that the liberalisation of capital movements was to take place in the transitional period of twelve years only '*to the extent necessary to ensure the proper functioning of the common market*'.

[7] This tension was already debated as early as in the 1956 *Spaak Report*, which provided the basis for the discussions at the The Intergovernmental Conference on the Common Market and Euratom that prepared the Treaty of Rome, argued for the economic benefits stemming from the freedom of movement of capital. It pointed to the nationalism and protectionism underpinning capital controls among the founding member states and to the progressive irrelevance of such controls in an integrated economic area. At the same time, it acknowledged the need to avoid that unrestrained capital flows would lead to imbalances among member states, affect their ability to implement monetary policy or to tax capital income, and lead to insufficient or more costly financing of less-developed regions. The way forward would be to follow a flexible process, without a precise calendar or milestones, for the progressive liberalisation of capital movements, which would adapt itself to development of the common market. The Spaak Report concludes its chapter on capital movements by stating that full economic integration will not be achieved until member states renounce to autonomous budgetary, financial and social policies, and also until they create a single currency. In the meantime, the dynamics of economic integration would have to be based on a sufficient degree of convergence of such policies. See *Rapport des Chefs de Délégation aux Ministres des Affaires*

Since the Treaty of Rome, the evolution of the single financial market has mirrored to a large extent the key legal and institutional steps in European integration as a whole. Four phases can be distinguished, with each representing the equilibrium achieved between the expansion of European competences for deepening integration and the preservation of national sovereignty. Along the way, new legal and institutional innovations were introduced to deepen integration at the boundaries of what could be achieved in each period under the Treaty.[8]

Integration through harmonisation (1973–1984)

The first phase corresponds to the period between the mid-1970s, when the first generation of Community law instruments in the field of finance were adopted, and the mid-1980s, before the Single European Act. This period was marked economically by high inflation, unemployment, and economic recession. The Bretton Woods system of pegged exchange rates was abolished in 1971, which raised the need in Europe for the convergence of exchange rates to support trade and economic integration, culminating with the European Monetary System (EMS) in 1979.[9] In institutional and legal terms, it was a period where the Community started to expand its competences. At the historic Paris Summit of October 1972, the Heads of State or Government declared their intention to expand the range of Community policies into areas not explicitly covered by the Treaty, including economic and monetary issues, if required also through the use of the exceptional clause of Article 235 of the Treaty of Rome (now Article 352 TFEU).[10] The Court also contributed to this expansion of competences with the judgements in *Dassonville* in 1974 and *Cassis de Dijon* in 1979, which provided the basis for removing

Étrangères, Comité Intergouvernmental crée par la Conference de Messine, presented in Brussels, 21 April 1956, especially at pp. 92–96.

[8] For a more detailed overview, see Teixeira (2010); and also the follow-up analysis in Teixeira (2011)

[9] See Eichengreen (2007: 246–251); and more recently James (2012: 96–ff).

[10] Statement from the Paris Summit (19 to 21 October 1972), Bulletin of the European Communities, October 1972, Luxembourg, Office for Official Publications of the European Communities, pp. 14-26. On the historical and political background of the summit, see the recent work by van Middelaar (2013: 113–114).

restrictive national measures even in the lack of harmonisation of national laws in a particular area.[11]

This was the context in which the first measures to build a single financial market were introduced in the 1970s. The legal approach was to start a process of full harmonisation of national laws as the means to address the distortions created by regulatory differences across member states, and also to prevent discrimination in the freedom of establishment on the grounds of nationality.[12] One of the legal innovations was the introduction of the concept of the principle of home-country control, according to which a national authority is responsible for the regulation and supervision of a bank licensed in its respective member state and operating across the common market, including its foreign branches. This principle stemmed from the Basel Concordat of 1975.[13]

In reality, however, there was very little progress in financial integration in this period, if any at all. Legally, the challenge of ever achieving sufficient uniformity of national laws for realising a single financial market was unsurmountable at the time. Member states safeguarded fully the application of national laws as a matter of public interest, which prevented any expression of home-country control. Moreover, in the spirit of the Luxembourg compromise of 1966, the member states maintained unanimity voting on matters of

[11] Case C-8/74 *Procureur du Roi v. Dassonville*, [1974] ECR-00837. Case C-120/78 *Rewe Zentrale v Bundesmonopolverwaltung für Branntwein* [1979] ECR-00649.

[12] This corresponded to the approach advocated early on by the *Spaak Report*, pp. 60–66, and also by the report of the first of many 'Comité des Sages': 'The Development of a European Capital Market: Report of a Group of Experts Appointed by the EEC Commission' (the *Sergé Report), Brussels, November*1966. For an analysis of the meaning of harmonisation of national laws in this period, see Stein (1964: 7). The most significant Community measures in this period were the First Banking Directive and Council Directive of 28 June 1973 on the Abolition of Restrictions on Freedom of Establishment and Freedom to Provide Services in Respect of Self-Employed Activities of Banks and Other Financial Institutions 73/183/EEC), OJ L194, 16 July 1973, 1-10; and the First Banking Directive, The First Council Directive of 12 December 1977 on the Co-ordination of Laws, Regulations and Administrative Provisions Relating to the Taking Up and Pursuit of the Business of Credit Institutions (77/780/EEC), OJ L322, 17 December 1977, 30–37, p. 30.

[13] Committee on Banking regulations and supervisory practices, *Report to the Governors on the Supervision of Banks' Foreign Establishments*, 26 September 1975, retrieved from: <http://www.bis.org/publ/bcbs00a.pdf> (last accessed 7 February 2014).

national interest such as finance. The political and economic context – including the general scepticism of European integration, which became known as 'eurosclerosis' – was also more conducive to protectionism of the national financial industry, including through capital controls, than to market liberalisation.[14]

Integration through competition (1985–1998)

The second phase corresponds largely to the pursuance of the single market programme, as triggered by the 1985 White Paper of the Commission.[15] By the mid-1980s, while still recovering from the economic recession, the member states were increasingly interdependent as a result of the growing trade linkages, capital flows, and their obligations in the EMS. This provided the background for the convergence of political and economic preferences among member states towards market liberalisation and deregulation. The Community was seen as the platform to deregulate protected sectors of the economy, in some cases to circumvent domestic resistance, and in others, notably the UK, to expand the scope of domestic reform, particularly in financial services. This led to the support of the single market programme, which equated economic growth to further market integration, and to the adoption of the Single European Act.[16]

The vision of the 1985 White Paper was that market integration would develop out of the dynamics of competitive forces in free and efficient markets. The priority was dismantling the barriers to trade and services across the Community. This would operate through the removal of national regulatory requirements, which were deemed both excessive and largely designed to protect domestic business. The approach to financial integration turned from attempting the harmonisation of national laws to unleashing, not only economic

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[14] This was also the official diagnosis, as the Commission stated in 1983 that 'financial markets are probably even less integrated now than in the 1960s, since capital movements within the Community are less free and the differences between the Member are more marked'; European Commission, *Financial Integration, Communication from the Commission to the Council*, COM (83) 207 final, 20 April 1983.

[15] European Commission, *Completing the Internal Market*, White Paper to the European Council of 28/29 June 1985 in Milan, COM (85) 310 final, 14 June 1985.

[16] For an account of the national economic preferences underpinning the SEA, see Moravcsik (1998: 314–ff). See similar interpretations by van Middelaar (2013: ch 3) and also Eichengreen (2007: 339–340).

competition, but also the 'competition among rules' between member states.[17]

In the context of the single financial market, this was translated into three legal principles: the mutual recognition of national laws, the minimum harmonisation of national laws, and freedom of movement of capital.[18] The application of these principles – which represented essentially an extension of the *Cassis de Dijon* doctrine – provided a 'single passport' to financial institutions for the provision of services throughout the Community.[19] As these institutions would be free to select the member state of origin, member states would be required to adapt their laws and regulations in order to both attract and retain them in their jurisdiction. The minimum harmonisation of national laws would prevent a 'race to the bottom' by member states on regulatory standards.

This legal method did not deliver the level of market integration that was expected. The national financial industry remained highly regulated and protected. The minimum harmonisation of national laws did not prove sufficient for the functioning of the mutual recognition. The 'general good exception' that could be invoked by member states represented a powerful obstacle, both explicitly through the application of the laws of the host-country and implicitly

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17 The expression 'competition among rules' was used in the 1987 Padoa-Schioppa Report: Report of a study group appointed by the Commission of the European Communities, and presided by T. Padoa-Schioppa, *Efficiency, Stability and Equity, A Strategy for the Evolution of the Economic System of the European Community*, April 1987, retrieved from: <http://ec.europa.eu/economy_finance/emu_history/documentation/chapter12/19870410en149efficiencstabil_a.pdf> (last accessed 4 April 2014). For an explanation of the concept of regulatory competition applied in the field of finance, see also Padoa-Schioppa (2004: 40–ff).

18 The freedom of movement of capital was turned into a full blown economic freedom, on a par with other fundamental economic freedoms, by Directive 88/361/EEC of 24 June 1988 for the Implementation of Article 67 of the Treaty, OJ L 178, 8 July 1988, 5–18. It was expanded into an *erga omnes* freedom, also covering third countries, as part of the changes introduced by the Maastricht Treaty in view of Monetary Union.

19 The single passport concept took its main expression in the banking field, where a complete liberalisation of the sector was envisaged. The Second Banking Directive was the main instrument in this context: Second Council Directive 89/646/EEC of 15 December 1989 on the Coordination of Laws, Regulations and Administrative Provisions Relating to the Taking Up and Pursuit of the Business of Credit Institutions and Amending Directive 77/780/EEC, OJ L 386, 30 December 1989, 1–13.

through the enforcement practices of national authorities. As a result, the cross-border provision of financial services did not expand out of the single passport. Instead, the preferred mode of market entry for financial services remained the acquisitions of local firms, also due to factors such as proximity to customers, taxation, labour laws, and protectionist practices.[20]

The period of 'integration through competition' had, however, deep implications. Its legal and institutional approach was particularly successful in placing market integration as the core objective, regardless of political and regulatory integration among member states. From then on, the ever deepening of market integration as the basis for economic growth would become a political, economic and legal value in itself. In the field of financial services, this was achieved through the concept of the single passport, which introduced the premise that finance could expand unlimitedly through the single market, independently of the member state of origin. Ultimately, this framework contributed later to the financial and public debt crisis stemming from the excessive growth of the financial industry.

Integration through governance (1999–2007)

A third phase in the legal evolution of the single financial market starts with the transfer of the conduct of monetary policy to the ECB and the introduction of the euro in January 1999. It is characterised by two main developments to overcome the limitations of the previous phase of integration: the expansion of the law of the single financial market beyond minimum harmonisation on the basis of the 1999 Financial Services Action Plan (FSAP); and the introduction in 2001 of the Lamfalussy framework of governance.

[20] The completion of the single financial market was not achieved in practice by 1992 due to a number of shortcomings, as diagnosed by the Sutherland Report. These included failures by member states in transposing Community legislation into national law, as well as failures in the implementation by national authorities, for instance due to different regulatory practices or different interpretations. In addition, the market participants and the consumers affected by such failures did not have access to rapid and effective means of redress. See *The Internal Market After 1992: Meeting the challenge* (Sutherland Report), Report to the EEC Commission by the High-Level Group on the Operation of the Internal Market presided by Peter Sutherland, of 28 October 1992, SEC (92) 2044.

The FSAP was justified by the need to reap the benefits of the single currency for the European financial market, which required the elimination of legal and capital fragmentation. It comprised more than forty initiatives for harmonising by 2005 a wide spectrum of the legal framework for the provision of financial services.[21] It marked, therefore, a shift from the 'negative integration' of the previous period, focused on dismantling barriers to market entry, to 'positive integration', based on the European re-regulation of financial services.[22]

At the same time, the expansion of European financial services law was challenged by the uneven patchwork of national laws, regulations, and supervisory practices. The question was how to ensure that legislative proposals would be adopted on time, implemented into national laws consistently, and enforced effectively by national supervisors across the single financial market. The Lamfalussy Report – the result of one of the many 'Comité des Sages' on a European financial market[23] – introduced a multi-level framework of governance. It comprised essentially two elements. First, the expansion of the use of comitology procedures, which would enable more flexible, swift and detailed enactment of Community legislation. Second, the establishment of several technical committees of national supervisors, which were mandated to provide technical advice to the Commission and to promote the convergence of supervisory practices.[24]

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[21] European Commission, Commission Communication, *Financial Services: Implementing the Framework for Financial Markets: Action Plan,* COM (1999) 232, 11 May 1999, 1–32.
[22] *Ibid.*
[23] The European Commission commissioned policy reports on the European financial market, on average, every ten years. On the basis of their respective chairperson, the reports included the Segré Report: Report of a Group of experts appointed by the EEC Commission *The Development of a European Capital Market*, Brussels, November 1966; the Schmidt Report: Commission of the European Communities: *The Advantages and Disadvantages of an Integrated Market Compared with a Fragmented Market*, Brussels, March 1977; the Cecchini Report: *Europe 1992, The Overall Challenge*, SEC (88) 524 final, Brussels, 13 April 1988; the Lamfalussy Report: The Committee of Wise Men, *Final Report of the Committee of Wise Men on the Regulation of European Securities Markets*, Brussels, 15 February 2001; and the De Larosière Report: *The High-Level Group on Financial Supervision in EU*, Brussels, 25 February 2009.
[24] The Committee of European Banking Supervisors (CEBS), Committee of European Insurance and Occupational Pensions Supervisors (*CEIOPS)*, and Committee of European Securities Regulators (CESR).

The innovation was setting-up a multi-level framework of governance, which combined the Community method with intergovernmental comitology procedures, and also with networks of national authorities in the adoption and enforcement of Community law. Its appeal was to enable the development of a regulatory system, without requiring any Treaty change, and without imposing mandatory obligations on either the Community institutions or national authorities. This was very much in line with the strategy of the time to promote 'new forms of governance' for pursuing European policies.[25]

Financial integration did increase in the decade following the introduction of the euro, including financial markets, pan-European banking groups and conglomerates, and market infrastructures. At the same time, integration led to deeper systemic interlinkages which increased the likelihood that a financial crisis could affect several member states or the single market as a whole. The governance framework was however based on the principle that each of member state and respective authorities would be exclusively responsible for the prevention and management of financial crises. This was due to the principle that, while the benefits of financial integration would be shared by all, the public costs of a crisis would not be shared. The reliance on soft, non-binding, governance arrangements also implied that compliance with European rules could only be loosely enforced.

This period ended thus with a more developed single financial market, but subject to a peculiar regime: a single financial market, a single monetary jurisdiction, but combined with multiple national supervisory jurisdictions and without meaningful European arrangements for preventing or managing a financial crisis.[26]

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[25] 'New governance' was one of key strategic objectives in the programme of the Prodi Commission, which started its mandate in 1999. The approach was set out in European Commission, *European Governance: a White Paper*, COM (2001) 428 final, Brussels, 25 July 2001; and on the follow-up *Report from the Commission on European Governance*, Luxembourg: Office for Official Publications of the European Communities, 2003. It was extensively dealt with in academic doctrine. For an overview, see Joerges *et al.* (2001); and also Snyder (2002)

[26] Tommaso Padoa-Schioppa was one of the first alerting to the inconsistency between a single monetary jurisdiction and multiple national supervisory jurisdictions. See Padoa-Schioppa (1999: 303–ff).

(Dis-)integration through crisis (2008–2012)

The financial crisis, which unfolded in Europe in the summer of 2007 and reached its peak after the fall of Lehman Brothers in October 2008, challenged fundamental assumptions of the single financial market and led to a significant retrenchment in financial integration. The responses to the crisis consisted largely of unilateral actions by member states, which in a domino effect sought to protect their respective financial systems and institutions from spillover effects. This led to the effective renationalisation of the single financial market. A major consequence of unilateral actions, such as bank rescues and guarantees, was that the soundness of financial institutions became then dependent on the budgetary capacity of the member state backing them, which in turn incurred in large liabilities that affected the soundness of its respective public finances. This laid the seed for the ensuing public debt crisis. The implication was that the paradigm of market integration based on the provision of financial services independently of the state of origin was no longer tenable.

The lack of European crisis prevention and management revealed by the events provided a justification for reforming the architecture for financial regulation and supervision. The impetus came from the recommendations of yet another 'Comité des Sages': The 2009 De Larosière Report.[27] The reform consisted of three legal and institutional changes.

First, the supervisory committees were replaced by European agencies with wide-ranging powers, from rule-making in the form of standards, to the enforcement of European law and crisis management.[28] The main innovation was to enable these agencies –

[27] The full text of the report is available at <http://ec.europa.eu/internal_market/finances/docs/de_larosiere_report_en.pdf> (last accessed 4 April 2014).

[28] See, respectively, Regulation (EU) 1093/2010 of the European Parliament and of the Council of 24 November 2010 Establishing a European Supervisory Authority (European Banking Authority), Amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC, OJ L331, 15 December 2010, 12–47; Regulation (EU) 1094/2010 of the European Parliament and of the Council of 24 November 2010 Establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), Amending Decision No 716/2009/EC and Repealing Commission Decision 2009/79/EC, OJ L331, 15 December 2010, 48–83; and Regulation (EU) 1095/2010 of the European Parliament and of the Council of 24 November 2010 Establishing a European Supervisory Authority (European Securities

the European Supervisory Authorities (ESAs) – to take legally binding decisions in certain cases with regard to national supervisors and financial institutions. This stood at the borderline of the *Meroni* doctrine on the delegation of powers to European agencies.[29] Most importantly, however, was the restraint imposed by member states: a 'fiscal safeguard clause' according to which the ESAs cannot take such directly applicable decisions when they may give rise to a fiscal burden, for instance, by imposing a certain action in a financial crisis that may lead to the use of taxpayers' funds. This safeguard clause signalled the limits set to the exercise of European competences that may have a bearing on fiscal sovereignty.[30]

The second institutional change was the establishment of the European Systemic Risk Board (ESRB) with the objective to safeguard the stability of the financial system through macro-prudential oversight.[31] The crisis made evident that the development of the single financial market had been solely focused on market integration, without taking account of the arrangements required to prevent and manage the resulting systemic risks. The ESRB marked a shift from this focus, which led to introduction of new European competences to manage and possibly restrain market integration in order to achieve financial stability. This also tested the boundaries of the single market framework. It gave rise to the question of whether the legal basis for building-up the single financial market – the 'harmonisation clause' of Article 114 TFEU (ex Article 95 EC) – could enable the creation of a body responsible for a public policy not directly conducive to integration. Such legal basis could not, in any

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and Markets Authority), Amending Decision No 716/2009/EC and Repealing Commission Decision 2009/77/EC, OJ L331, 15 December 2010, 84–119 (henceforth, the ESA Regulations).

[29] On the *Meroni* doctrine, see Chiti (2010).

[30] This applies in particular to decisions in emergency situations and for settling disagreements among national supervisors. Where a member state considers that a decision by an ESA impinges on its fiscal responsibility, it may notify that the national supervisor does not intend to implement the decision, together with a justification. In case of continuing disagreement, the Council may be involved. For a detailed analysis of the powers of the new European Supervisory Authorities, see and Teixeira, (2011).

[31] Regulation (EU) No. 1092/2010 of the European Parliament and of the Council of 24 November 2010 on European Union Macro-Prudential Oversight of the Financial System and Establishing a European Systemic Risk Board, OJ L 331, 15 December 2010, 1–11.

case, provide the ESRB with powers beyond the adoption of non-binding warnings and recommendations.[32]

The third change operated since the crisis corresponded to the replacement of the single passport framework by the concept of a 'single rulebook'. It was a concept first advocated also by Tommaso Padoa-Schioppa in the early 2000s and later by the De Larosière Report. It aimed at realising integration by subjecting the single financial market to a single set of rules defined by European law, thus replacing the multi-layered regime comprising EU directives and related implementing acts, national laws and supervisory regulations.[33] This approach also implies replacing the single passport framework since minimum harmonisation and mutual recognition of national laws are no longer applied or relevant. Instead, the single rulebook is realised through the increased use of directly applicable European regulations aiming at the 'maximum harmonisation' of the single market rules. To some extent, it is a remarkable return to the approach of the first period of 'integration through harmonisation' of the single financial market, as analysed above.[34]

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[32] The establishment of the ESRB represented another confirmation of the very wide scope of Article 114 TFEU, which follows the line defined in the *Tobacco Advertising* case-law of the Court where the question also related to the legal basis for a new European public policy related to health in the context of harmonisation measures. Accordingly, the ESRB Regulation quotes in its Recital (31) Case C-217/04 *United Kingdom of Great Britain and Northern Ireland v. European Parliament and Council of the European Union*, [2006] ECR I-03771, para 44, where the Court ruled on the permissibility of 'the establishment of a Community body responsible for contributing to the implementation of a process of harmonisation in situations where, in order to facilitate the uniform implementation and application of acts based on that provision, the adoption of non-binding supporting and framework measures seems appropriate'. For a critique of the gradual expansion of the scope of Article 114 TFEU and its implications in terms of the constitutional division of powers in the EU and also for the EU's legitimacy, see Weatherill (2011: 863).

[33] On the original concept of the single rulebook, see Tommaso Padoa-Schioppa (2004), 'How to Deal with Emerging pan-European Financial Institutions?', speech at the Conference on Supervisory Convergence, The Hague, 3 November 2004, retrieved from: <http://www.ecb.europa.eu/press/key/date/2004/html/sp041103.en.html> (last accessed 8 April 2014].

[34] The single rulebook approach was implemented especially in the banking sector with the so-called 'CRD IV', the fourth generation of capital requirement rules, which corresponds to the implementation of the global capital standards following the crisis (also known as Basel III agreement). See in particular the Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on

By 2012, the evolution of the legal and institutional framework of the single financial market had probably touched the limits of what could be achieved under the single market provisions of the Treaty and the jurisprudence of the Court as regards the powers of European agencies in the form of the ESAs, the creation of European bodies such as as the ESRB under Article 114 TFEU, and the scope for maximum harmonisation also under Article 114 TFEU. This, however, remained far from providing a sufficient framework to address the public debt crisis in the euro area, which was being aggravated by the increasing interdependence between the banks and the respective member states of origin.

Origins: the Euro Area Summit of June 2012

The Euro Area Summit of 28 and 29 June 2012 represented a watershed in the management of the public debt crisis. The relatively short and convoluted statement of the summit in the early hours of 29 June did not do justice to the institutional change that had been agreed among the euro area member states: the mutualisation of risks of the euro area banking sector by opening up the possibility of direct recapitalisation of banks by the ESM, and the transfer of competences on banking supervision to the European level.

In June 2012, the public debt crisis in the euro area had probably reached its peak. The ability of Italy and Spain to manage its public finances without external financial assistance was openly questioned by the markets, as reflected in the consistent rise to unsustainable levels of the interest rates on the public debt of these countries. This, in turn, raised existential doubts on the euro itself, giving rise the so-called 'redenomination risk'. If it were ever to happen, the provision of financial assistance to Italy and Spain would involve significant amounts and would be politically challenging. The sustainability of the EMU framework was at stake.[35]

Prudential Requirements for Credit Institutions and Investment Firms and Amending Regulation (EU) No 648/2012, OJ L 176, 27 June 2013, p. 1–337.

[35] For an account of the Euro Area Summit, see, for example, 'Monti's Uprising: How Italy and Spain Defeated Merkel at EU Summit', *Spiegel Online*, 29 June 2012, retrieved from: <www.spiegel.de/international/europe/merkel-makes-concessions-at-eu-summit-a-841663.html> (last accessed 7 April 2014).

The breakthrough in the summit was the agreement to make the functioning of the ESM more flexible in order to facilitate the granting of financial assistance, if ever required. First, it enabled the ESM to provide assistance without additional conditionality other than that already agreed under the normal economic governance procedures (European Semester, Stability and Growth Pact, and Macroeconomic Imbalances Procedures). Second, and much more significant in institutional terms, it allowed the ESM to recapitalise directly euro area banks. This implied that the financial burden of rescuing an undercapitalised bank would no longer fall on national public accounts, thus increasing the debt of a single member state. Instead, the cost of a euro area bank rescue would be mutualised among all the euro area member states which underwrite the ESM. At the same time, it would provide relief to the member states which had to seek assistance to recapitalise their banks.[36]

The ability of the ESM to directly recapitalise banks in the euro area was made dependent by the summit statement on the establishment of a single supervisory mechanism 'involving the ECB'. Although this wording was somewhat vague, the statement invoked at the same time Article 127.6 TFEU as the legal basis for the mechanism, which clearly implied that the ECB would become the single banking supervisor in the euro area. The reticence of the summit to clearly spell out the decision to entrust the ECB with banking supervision reflects the fact that this was, to some extent in the circumstances surrounding the summit, a second order decision, made to validate and manage the implications of the main decision to enable the direct recapitalisation of banks by the ESM. At the same time, it reflects the

[36] European Council, Euro Area Summit Statement, Brussels, 29 June 2012, retrieved from: <http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/131359.pdf> (last accessed 8 April 2014). The first paragraph of the statement reads as following: 'We affirm that it is imperative to break the vicious circle between banks and sovereigns. The Commission will present Proposals on the basis of Article 127(6) for a single supervisory mechanism shortly. We ask the Council to consider these Proposals as a matter of urgency by the end of 2012. When an effective single supervisory mechanism is established, involving the ECB, for banks in the euro area the ESM could, following a regular decision, have the possibility to recapitalise banks directly. This would rely on appropriate conditionality, including compliance with state aid rules, which should be institution specific, sector-specific or economy-wide and would be formalised in a Memorandum of Understanding'.

political will to avoid any change of the Treaty to transfer competences to the European level.

The member states decided at the Summit that the mutualisation of liability for the euro area banks could only come about once it was matched by supervision at the euro area level.[37] The rationale was that euro area liability was not compatible with national supervision, whose political and regulatory capture may have played a factor in the excesses in bank lending that fuelled the financial crisis and exacerbated the macroeconomic imbalances in Europe. In addition, both banks and national supervisors would lack incentives to minimise the potential costs of banking for a euro area fiscal backstop, thus giving rise to issues of free-riding or moral hazard. Therefore, a euro area banking supervisor, free from national capture, would have instead its incentives aligned with those of the ESM, namely of minimising the banking risks and potential costs for the whole of the euro area member states and their respective taxpayers.[38]

The establishment of the SSM had therefore at its heart a quid pro quo between the mutualisation of banking risks in the euro area and the loss of national sovereignty over banking supervision. This also corresponded to the long-term vision for the EMU put forward in the interim report of the President of the European Council, which was presented at the June 2012 Summit. This vision included 'four building blocks for EMU': integrated financial, budgetary and economic policy frameworks, together with democratic legitimacy and accountability. The concept of an integrated financial framework corresponded largely to what became known as a 'Banking Union': a system comprising single European banking supervision, a single bank resolution mechanism, and a common deposit insurance. The

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[37] See, for example, the speech by Chancellor Merkel to the Bundestag on 27 June 2012 stressing that a joint liability can only occur once a joint control had been established, retrieved from: <http://www.bundeskanzlerin.de/ContentArchiv/DE/Archiv17/Artikel/2012/06/2012-06-27-regierungserklaerung.html> (last accessed 8 April 2014).

[38] See Wolff, G.B. and Pisani-Ferry, J. (2012) 'The Fiscal Implications of a Banking Union', *Bruegel Policy Brief* 2012/02, Bruegel, retrieved from: <http://www.bruegel.org/publications/publication-detail/publication/748-the-fiscal-implications-of-a-banking-union/> (last accessed 8 April 2014).

aim was to provide the institutional basis for an integrated and stable banking system for EMU.[39]

The immediate need to stem the crisis through the direct recapitalisation of euro area banks precipitated, therefore, a lasting institutional decision which was being considered only for the long-term. At the same time, the credibility of the decisions depended on whether they could be implemented quickly enough. This implied the recourse to Article 127.6 TFEU, which allowed entrusting banking supervision to the ECB on the basis of a fast-track procedure. Otherwise, the only alternative was establishing a new European authority, most likely through a Treaty change, which was hardly conceivable at the time given the political challenges. Moreover, the credibility of the decision was also enhanced by the fact that the ECB resources and reputation would underpin the new European competences.

Accordingly, the Euro Area Summit requested a legislative proposal on the basis of Article 127.6 TFEU and asked the Council to consider it as a matter of urgency by the end of 2012. The Commission put forward its proposal on 12 September 2012, which provided the basis for the general agreement of the ECOFIN exactly three months later at the dawn of 13 December of the same year. The process was finalised with the consultation of the European Parliament, which then led to the entry into force of the Council Regulation on [...].

Treaty limits: the challenge to the legal basis of the SSM

The explicit reference by the Euro Area Summit to Article 127.6 TFEU for the establishment of the future SSM was remarkable for many

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[39] European Council, the President, Report by President of the European Council, *Towards a Genuine Economic and Monetary Union*, EUCO 120/12, 26 June 2012, retrieved from: <http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/131201.pdf > (last accessed 8 April 2014), especially pp. 3–5. On the concept of a Banking Union, see Vitor Constâncio (2013), 'Towards the Banking Union', speech at the second FIN-FSA Conference on EU Regulation and Supervision 'Banking and Supervision under Transformation' organised by the Financial Supervisory Authority, Helsinki, 12 February 2013; Wolff, G.B., Pisani-Ferry, J., Sapir, A. and Véron, N. (2012) 'What kind of European Banking Union?' *Bruegel Policy* Contribution2012/*12*, Bruege, retrieved from: <http://www.bruegel.org/publications/publication-detail/publication/731-what-kind-of-european-banking-union/>(last accessed 8 April 2014); Elliott (2012); and Goyal *et al*. (2013).

reasons. It reflected once more the tension, which is present throughout Europe's responses to the financial and public debt crises, between the political constraints of member states and the limits set by the framework of the Treaty. This section explores the political and legal rationale for using such provision of the Treaty and contributes to the debate of whether it is the appropriate constitutional basis for the transfer of competences for banking supervision to the European level.

Reasons and concerns in entrusting supervision to the ECB

The legal basis of Article 127.6 TFEU invoked by the Euro Area Summit resulted from a combination of several factors, both political and legal. First of all, it expressed a credible political will of the Council to take an operational decision to transfer banking supervision competences to the European level, thus also enabling the direct recapitalisation of banks in the very short-term. The Council could decide expeditiously, also outside the normal co-decision procedure with the Parliament, to entrust banking supervision to a European authority without the need to amend the Treaty. To a certain extent, this should be understood in the context of the other institutional and legal decisions to address the crisis which did not require a Treaty amendment, namely the establishment of the ESM and the TSCG on the basis of public international law instruments outside the Treaty. In this sense, the reference to Article 127.6 TFEU could be interpreted as dispelling possible doubts as to whether financial integration could be further deepened within the Treaty framework. The credibility of the decision was also underpinned by the reputation, resources and capacity of the ECB to start carrying out a supervisory function without much delay. If a whole new authority had to be created, a short transition period would likely not be conceivable and the direct recapitalisation of banks by the ESM, as a means to address the crisis, would take longer to materialise. For example, the European Monetary Institute was created in 1994, five years before the introduction of the euro and the start of the single monetary policy.

Entrusting supervisory tasks to the ECB was further justified by the institutional trend to combine central banking and banking supervision as a lesson from the financial crisis. The model for the conduct of supervision on the basis of a single authority separate from the central bank, which had started with the UK's Financial

Services Authority in 1997 and had spread for 10 years in Europe and globally, was deemed largely inadequate to prevent and contain the crisis. This marked the return or the reinforcement of supervisory competences to central banks, including in the UK but also in the US where the supervisory responsibilities of the Federal Reserve were reinforced by the Dodd-Frank Act. Moreover, the involvement of central banks in supervision is the predominant model among member states, particularly in the euro area.[40]

At the same time, there were at play concerns as to the desirability of fully entrusting the ECB with supervisory tasks, which would explain the vague wording of the Euro Area Summit statement as to 'involving the ECB'. This, as it would be later reflected in the core provisions of the SSM Regulation, was due to three main political and institutional concerns.

The first relates to whether the ECB could also conduct banking supervision tasks without prejudice to its central banking tasks and in particular to the primacy of price stability in the conduct of monetary policy. The argument is that the combination of the two set of tasks could lead to a conflict of interests, for instance, in the provision of liquidity to the banking system which could take into account supervisory interests and not exclusively monetary policy. Furthermore, it may be also argued that it could affect the central banking independence of the ECB since the conduct of banking supervision may be connected to the use of fiscal funds, notably in a financial crisis, thus involving an additional dimension of political accountability.[41]

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[40] The deeper involvement of central banks in financial stability and both in micro- and macro-prudential supervision also led to a debate on the extent to which multiple objectives may be pursued simultaneously by a single institution. It calls into question the well-known 'Tinbergen rule' according to which the effective pursuance of economic policies depends on the existence of independent policy instruments for each policy target. For an overview of the arguments in this debate, see Masciandaro and Quintyn (2011: 467–ff). See also European Central Bank (2010) *Recent Developments in Supervisory Structures in the EU Member States (2007–2010),* Frankfurt am Main, retrieved from: <http://www.ecb.europa.eu/pub/pdf/other/report_on_supervisory_structures2010en.pdf> (last accessed 8 April 2014).

[41] In this sense, see S. Eijffinger and R. Nijskens, 'Monetary Policy and Banking Supervision', VOX, 19 December 2012, retrieved from: <http://www.voxeu.org/article/monetary-policy-and-banking-supervision> (last accessed 8 April 2014).

The second was that entrusting supervision to the ECB would imply confining the jurisdiction of the single supervisory mechanism to the euro area member states. This would create a mismatch with the single market and exclude the member states which have not adopted the euro from deeper integration regarding the provision of banking services across the Union, thus undermining the single market principles.[42]

The third regarded the democratic accountability of the ECB as a banking supervisor. Entrusting supervision to the ECB would imply that its statutory independence as a central bank would spill over to its supervisory tasks. This was deemed incompatible with the nature of these tasks, which require closer and deeper accountability due to the potential impact on taxpayers' funds, as demonstrated by the financial crisis.

Article 127.6 TFEU as the constitutional foundation of the SSM

The activation of Article 127.6 TFEU could have been questioned as the appropriate legal basis to transfer banking supervision competences to a European authority. It reads as follows:

> The Council, acting by means of regulations in accordance with a special legislative procedure, may unanimously, and after

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[42] The argument of the conflict of interests was advocated explicitly by the Bundesbank, which questioned whether Article 127 (6) could provide the legal basis for a major transfer of supervisory tasks to the ECB: '[…] the ECB's assumption of supervisory functions requires special measures in order to avoid conflicts of interest between monetary policy and banking supervision and to prevent any encroachment on central bank independence, which per se also includes tasks pursuant to Article 127 (6) of the TFEU'. In addition, the eurosystem's primary objective of safeguarding price stability must not be jeopardised. The draft regulation stipulates for this purpose, inter alia, the creation of a separate supervisory body; this should prepare and implement decisions for the ECB Governing Council, which is ultimately responsible, and perform certain tasks independently. However, it is doubtful whether the granting of decision-making powers to a new body alongside the ECB Governing Council is consistent with European primary law. Moreover, on account of the fiscal effects of regulatory decisions, it is appropriate to weight the votes of the members in accordance with the ECB's capital key and not with the simple majority of one vote per council member, which otherwise prevails in the eurosystem'. Deutsche Bundesbank (2012) *Financial Stability Review 2012*, pp. 82–83, retrieved from: <www.bundesbank.de> (last accessed 8 April 2014).

> consulting the European Parliament and the ECB, confer specific tasks upon the ECB concerning policies relating to the prudential supervision of credit institutions and other financial institutions with the exception of insurance undertakings.
>
> (Article 127.6 TFEU)

This represents an enabling clause and a fast-track procedure to the Council to entrust tasks to the ECB. Until the establishment of the SSM, Article 127.6 TFEU had only been used once to entrust the ECB with the task to support the functioning of the European Systemic Risk Board.[43]

The first issue as to the use of Article 127.6 TFEU is whether its somewhat convoluted wording could enable the transfer of a wide range of direct supervisory tasks. More specifically, whether the reference to 'specific tasks concerning policies relating to prudential supervision' could imply that the ECB would replace national authorities as the competent authority for the conduct of banking supervision in accordance with Union law.

The extent of the potential involvement of the ECB in banking supervision was very much disputed in the preparatory work of the Treaty of Maastricht and the Statute of the ESCB and the ECB. There were two largely opposite concepts. Most Governors of national central banks were inclined to provide that the ECB, in line with the predominant model in Europe, would also exercise banking supervision tasks. The draft text prepared by the Committee of Governors in 1990 indicated very clearly that the ECB could be designated as competent supervisory authority. It reads as follows:

> The ECB may formulate, interpret and implement policies relating to the prudential supervision of credit and other financial institutions for which it is designated as competent authority.[44]

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[43] Council Regulation (EU) No 1096/2010 of 17 November 2010 Conferring Specific Tasks Upon the European Central Bank Concerning the Functioning of the European Systemic Risk Board, OJ L 331, 15 December 2010, 162–164.

[44] Draft text proposed by the Committee of Governors for Article 25 of the Statute (which would replicate Article 127 TFEU (ex 105 TEC), transmitted to the President

This text was contested by governments, some banking supervisors and also the Bundesbank, very much on the basis of the concerns mentioned above as to the combination of central banking and supervision tasks. As a compromise, the Delors Report proposed that the ECB would exercise coordination tasks of banking supervision (see James 2012: 313–ff.).

The outcome of these conflicting positions was that they were all largely incorporated in the final texts of the Treaty and the Statute. The ECB was entrusted with three tasks of different nature relating to supervision. First, Article 127.5 TFEU (ex 105.5 TEC) provides the ESCB with the task to contribute to the smooth conduct of policies pursued by the competent authorities relating to the prudential supervision of credit institutions and the stability of the financial system. This task falls short of coordination of supervision and may be interpreted as a contribution of the central banking perspective to the conduct of national supervision, thus reflecting those arguments against the ECB's involvement. Second, Article 25.1 of the Statute provides that the ECB may offer advice to and be consulted by the Council, the Commission and national supervisors on the scope and implementation of Union legislation relating to the prudential supervision of credit institutions. This is a task which is closer to a coordinating function, since the ECB could play the role of supporting a uniform formulation and implementation of Union law relating to supervision, as proposed by the Committee of Governors. The third task is that of Article 127.6 TFEU, which should be interpreted as reflecting the views of the Committee of Governors that the ECB could be designated as a supervisory authority, with the exception of insurance undertakings (Louis 1989).

The wording of Article 127.6 TFEU draws from the proposal of the Committee of Governors, with two main differences. The first is that it refers to entrusting the ECB with 'specific tasks', instead of formulating, interpreting and implementing supervisory policies. This does not necessarily imply a narrowing down of the potential role of the ECB as supervisor. It represents instead a procedural condition for the Council to explicitly specify the supervisory tasks to

of the Ecofin Council on 27 November 1990. Europe, Document No. 1669/1679, p.9, quoted from Smits (1997: 335).

be conferred upon the ECB. The second difference is that there is no explicit reference to the ECB as a 'competent authority'. This omission broadens, in reality, the scope of the legal basis for the tasks that may be carried out by the ECB, since they may be tasks not limited to those of supervisory authorities. One example is the support to the ESRB, which is provided on the basis of Article 127.6 TFEU. The fact that the ECB is not mentioned as a competent authority could, however, also have been read as limiting this possibility. This interpretation is not supported though by the origins and by any of the wording of the provision, which does not limit the type of tasks which can be conferred upon the ECB. At most, it could be argued that the ECB cannot be entrusted with all supervisory tasks but only specific ones. However, the wording only seems to imply that the tasks need to be explicitly specified in the enabling Council Regulation – which was the approach followed in the SSM Regulation – and cannot be general such as formulating or implementing supervisory policies.[45] The legal basis of Article 127.6 TFEU was, therefore, appropriate to entrust the ECB with a range of supervisory tasks at the European level.[46]

Alternatives to Article 127.6 TFEU

A final issue regarding the use of Article 127.6 TFEU was whether this was the only available legal basis in the Treaty to transfer supervisory competences to the European level, i.e. to the ECB or to a newly established European authority. This question was crucial in view of the concerns mentioned above as to the appropriateness of combining central banking and supervisory tasks as well as of limiting European banking supervision to the euro area. In the lack of any other alternative, only Article 352 TFEU (ex 308 TEC), which enables the Council to take action to attain the objectives of the Union

[45] A third difference is that Article 127.6 TFEU excludes specific tasks regarding insurance undertakings from its scope. The restriction to insurance was introduced by the Dutch Presidency, late in the process of negotiations.

[46] In the interpretation of Jean-Victor Louis, 'this enabling clause makes it possible, albeit with substantial procedures impediments to be overcome, to provide for a form of direct Europe-wide supervision of financial institutions'. Also against a limited reading that might seem to stop short of attributing a competence to execute supervision. Instead, it should be read to authorise the conferring of specific elements of broad, Europe-wide supervisory policies upon the ECB to be implemented by the ECB itself. For an analysis, see Louis (1995: 44–ff). This is also the conclusion of Wymeersch (2012: 6-7).

when the Treaty has not provided the necessary powers, could have presented a competing legal basis to Article 127.6 TFEU.[47]

This raises the question of the nature of Article 127.6 TFEU. Being included in the EMU chapter of the Treaty and in the Statute of the ESCB and the ECB implies that it is a component of the framework of the single currency. At the same time, the conduct of banking supervision refers to competences relating to the provision of financial services, which is an area of the single market. This implies that, in fact, Article 127.6 TFEU is also a single market clause in the line of Article 114 TFEU (ex 95 TEC) which provides the legal basis for harmonisation in the field of financial services. Another indication in this direction is that, in contrast with most of the other EMU provisions, Article 127.6 TFEU applies to all member states, including those with a derogation, namely Denmark and the UK. All member states have a vote in the unanimous decision to adopt a Council Regulation to entrust supervisory tasks to the ECB. Therefore, Article 127.6 TFEU reflects the unitary and inclusive framework of EMU with regard to the Union, which assumes a perfect coincidence of the two perimeters over time. The institutional tension resulting from the mismatch of the euro area and the single market is reflected in the core provisions of the SSM Regulation, as analysed below.

In conclusion, following the well-established jurisprudence of the Court, Article 352 TFEU could not have been invoked either to confer tasks to the ECB or to actually create a new authority: Article 127.6 TFEU already provides the Union with the powers to transfer supervision to the European level both for the purposes of the EMU and the single market. Furthermore, using Article 352 TFEU to transfer national competences to a new European Authority would raise issues of institutional balance and constitutional legitimacy within the Union. A Treaty change was therefore the only alternative to Article 127.6 TFEU to transfer supervision either to the ECB in different terms or to a new European body. Such Treaty change was however hardly conceivable given the context of addressing the crisis

[47] In this context, Article 114 and the case law regarding Meroni do not provide for the possibility to delegate to a European agency, such as the European Banking Authority, autonomous and supranational powers of decision-making and regulation such as in prudential supervision. See Chiti 2010.

through the direct recapitalisation of banks by the ESM, which also required the direct banking supervision by the ECB.[48]

The political commitment to treaty change

While Article 127.6 TFEU provided the basis for the SSM Regulation, the political and institutional concerns about its use remained. This regarded, specifically, the separation between the conduct of monetary policy and banking supervision within the ECB, the ability of member states outside the euro area to join the SSM in equal terms as the others, and the democratic accountability of the ECB as a banking supervisor. These concerns became a key-defining feature of the provisions of the regulation, as analysed in the following sections.

Eventually, in the context of the final negotiations for the adoption of the SSM Regulation by the Council, member states took the political commitment in April 2013 to 'work constructively' on a proposal for a Treaty change with regard to Article 127.6 TFEU or other provisions of the Treaty. The possibility for such a Treaty change is also stated in Recital 85 of the SSM Regulation. This was aimed at assuaging the above concerns, which could conceivably imply either modifying the institutional framework of the ECB with regard to the conduct of supervisory tasks or establishing under the Treaty a new European institution fully devoted to banking supervision. The question would be to which extent such amendment of the Treaty would represent an increase of the Union competences under Article 48 TFEU, which would require either an ordinary or a simplified revision procedure.[49]

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[48] Case C-45/86 *Commission of the European Communities v. Council of the European Communities* [1987] ECR-01493.

[49] See Declaration by Member States at the Informal Meeting of Ministers and Governors, 12 April 2013: 'The member states reaffirm their commitment to the urgent completion of all the agreed elements of banking union, as set out by the European Council, in particular in its Conclusions of 13/14 December 2012. Whilst respecting the integrity of the single market and with reference to Recital 45(a) of the Regulation and the Commission's Communication of 28 November 2012 on a Blueprint for a deep and genuine economic and monetary union, member states declare that they are also ready to work constructively on a proposal for Treaty change made in accordance with provisions of Article 48 TEU. Should Article 127 paragraph 6 TFEU or other relevant Treaty provisions be amended the current Regulation should, if necessary, be appropriately adjusted', retrieved from: <http://www.euo.dk/upload/application/pdf/01ba46b2/Uformelt.pdf%3Fdownload%3D1> (last accessed 8 April 2014).

Later in the same year, the need for Treaty change was also raised with regard to the Commission's proposal for a Single Resolution Mechanism, which was based on Article 114 TFEU. Once again, it was questioned whether the boundaries of the Treaty framework for the development of the single financial market had been reached.[50]

The matrix of competences of the SSM

The SSM consists of a unique and unprecedented juxtaposition of European and national competences, which defies any clear definition or categorisation. It includes, at least, the following layers of competences: exclusive competences of the ECB regarding the direct supervision of euro area banks; national competences of supervision regarding the tasks not transferred to the ECB and also the banks not within the scope of the supervision of the ECB; oversight competences of the ECB over national supervisors, including the powers to give instructions; shared and parallel competences among the ECB and national authorities regarding some supervisory tasks; and the combination of both European and national competences to give effect to certain tasks.[51]

The rationale for such matrix of competences relates to several factors, including: the legal mechanics of Article 127.6 TFEU; the constitutional foundations of the ECB, notably its institutional independence; the appropriateness of having recourse to national authorities for the operational conduct of supervision; the multitude of powers and layers of the legal framework for banking supervision, which includes both European and national laws; as well as the inclusion of competences such as macro-prudential supervision that may have a bearing on fiscal sovereignty. This legal and institutional complexity begs the question of the extent to which the SSM can still be considered a single system.

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[50] Commission Proposal for a Regulation of the European Parliament and of the Council Establishing Uniform Rules and a Uniform Procedure for the Resolution of Credit Institutions and Certain Investment Firms in the Framework of a Single Resolution Mechanism and a Single Bank Resolution Fund and Amending Regulation (EU) No 1093/2010 of the European Parliament and of the Council, COM (2013) 520 final, 10 July 2013.

[51] This is why the SSM Regulation defines the SSM as 'the system of financial supervision composed by the ECB and national competent authorities of participating member states'. For a first overview of the SSM, see Ferran and Babis (2013).

The mechanics of Article 127.6 TFEU

The provision of Article 127.6 TFEU was constructed as a fast-track procedure to attribute to the ECB additional tasks. In principle, the Council Regulation under Article 127.6 TFEU would only be required to list the specific supervisory tasks transferred to the ECB. The ECB would then perform such tasks on the basis of the same framework and instruments provided by the Treaty and the Statute for its other central banking tasks. For example, Article 132.1 TFEU and Article 34.1 of the ESCB and ECB Statute already enabled the ECB to adopt regulations to the extent necessary to implement the tasks relating to prudential supervision (by reference to Article 127.6 TFEU and Article 25.2 of the Statute, respectively).

There was, however, one important difference between the tasks entrusted under Article 127.6 TFEU and the central banking tasks referred to in Article 127.2 TFEU, notably to define and implement the monetary policy of the Union. The central banking tasks are to be 'carried out through the ESCB', which in turn is governed by the ECB decision-making bodies. The supervisory tasks are instead 'conferred upon the ECB'. The main implication of this difference is that the central banking tasks are performed by the ESCB as a whole, which provides a degree of own autonomy and responsibility to the national central banks. In fact, Article 12.1 of the Statute imposes upon the ECB to have recourse to the national central banks to carry out operations which form part of the tasks entrusted to the ESCB. This principle of executive decentralisation of central banking tasks Zilioli and Selmayr (2001), which was applied extensively for central banking tasks, does not apply to supervisory tasks, which are both decided and implemented exclusively by the ECB in the meaning of Article 127.6 TFEU.

Accordingly, using Article 127.6 TFEU also implied entrusting tasks to the ECB with a much higher degree of centralisation than previously was the case for central banking, which was entrusted to a system of central banks. As a result, national supervisors would be much less involved compared to national central banks. One other implication of using Article 127.6 TFEU was that the jurisdiction of the ECB for supervisory tasks could not extend beyond the central banking jurisdiction, which is limited to the euro area member states. Although the Council Regulation activating Article 127.6 TFEU requires unanimity of all member states, the supervisory tasks are exercised by the ECB. The provisions regarding the powers of the ECB decision-making bodies do not apply to the member states with a derogation.[52]

The mechanics of Article 127.6 TFEU implied therefore that the supervisory tasks would be conducted within the institutional framework of the ECB, including its decision-making bodies, instruments and jurisdiction, and, on top of that, in a much more centralised manner than the central banking tasks. This did not leave much space for discretion to the Council in shaping the overall framework for the exercise of European competences of supervision. It put into question how to cater for the specific needs to safeguard the single market, insulate central banking tasks from supervision, and also to allow for some degree of decentralisation to national supervisors in the conduct of European supervisory tasks, which seemed wise in view of the around 6,000 banks in the euro area subject to supervision. This had a significant bearing in the design of a multi-layered system of European competences, as analysed in the following sections.

A System of Exclusive Competences

The exclusive competences of the ECB in banking supervision have the most significant and immediate relevance. The ECB is entrusted with the large part of the supervisory competences provided by Union law to national supervisors as competent authorities. This includes, among others, the authorisation of banks and the withdrawal of their license, ensuring compliance of credit institutions with prudential requirements, supervisory review, supervision on a consolidated basis, supervision of branches from credit institutions authorised in the EU, supplementary supervision of a financial conglomerate, early intervention measures, limits to compensation of managers, administrative sanctions, and imposing structural changes in banks. For the purposes of the application of the Union's banking law, the ECB becomes the competent authority for banking supervision in each euro area member state, with the corresponding powers, thus fully replacing national supervisors.[53]

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[52] Article 139 of TFEU and Article 42.1 of the Statute of the ESCB and the ECB.

[53] Article 4.1 in SSM Regulation, Regulation No. 1024/2013, OJ L287, see note 1 above. National supervisors are only left with [Recital 22], and anti-money laundering and the supervision of branches from third-countries (US, Japan).

The main implication for the single market of the attribution of these exclusive competences to the ECB is the end of the single passport framework within the euro area. This essentially implies that the principles of home-country control and mutual recognition no longer apply. The credit institutions subject to the supervision of the ECB have a single supervisor in the euro area, independently of the extent of their cross-border business through subsidiaries, branches or direct provision of services. This also implies that the credit institutions are subject to a single law and body of rules, although still including national layers.[54]

The exclusive supervisory competences of the ECB lead, therefore, to the unification of a considerable part of the single market in banking services. As intended by the June Summit, the euro area banks are basically removed of their 'nationality' in order to break the vicious loop between sovereigns and their respective banks. The banks are 'Europeanised' in the sense that the competences for their licensing, for ensuring compliance with Union law in their activities, and for closing them down, is exclusive to a European authority. The judicial review by the ECJ is substantially expanded as a result, which will bring its own set of challenges. In regulatory terms, the member state of origin becomes, in principle, unconnected to a banking institution. The involvement of the ESM in direct recapitalisation and the establishment of a European banking resolution mechanism would complete the detachment from individual member states.

A decentralised system

It is clear that the legal basis of Article 127.6 TFEU can only be used to confer supervisory tasks upon the ECB itself. It could not provide the basis for also attributing supervisory competences to national supervisors, for instance as with central banking tasks, which are to be carried out collectively through the whole ESCB. This implied that national supervisors would have been divested of large part of their

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[54] The SSM will apply the existing multilayered European banking law. Following the principle of primacy of European law, the layers of law and regulation may be ordered as follows: (i) legislative acts by the Council and Parliament, both regulations and directives; (ii) delegated and implementing acts by the Commission; (iii) non-legally binding EBA guidelines and recommendations to supervisors, including the SSM; (iv) ECB regulations and other legal acts; and (v) any national legal acts within the competences of national governments and authorities.

existing responsibilities. It also implied that the ECB alone would be exclusively responsible for the supervision of the whole euro area banking system, which comprises around 6,000 banks. Such a sudden centralisation of competences previously entrusted in the euro area to possibly more than twenty national authorities would have been, in the least, very challenging. It would also have been not proportional to dismiss the expertise of national supervisors and their local involvement in the economic and legal context of each member state.
It was therefore imperative to devise a system of decentralisation that would involve national supervisors in the conduct of supervisory tasks by the ECB. Conceivably, there were three options. The first was to follow to some extent the model of the ESCB, where decision-making is centralised in the decision-making bodies of the ECB with a large executive decentralisation for the implementation of decisions. This option would still require the ECB to take all supervisory decisions regarding the universe of the euro area banks. In turn, these decisions could only be subject to the judicial control of the Court.

A second possibility would be to enable the ECB to delegate extensively the implementation of its supervisory tasks to national authorities. This would represent a significant break from the 'Meroni doctrine' if the delegation would go beyond measures to apply technical and objective criteria, without discretion for policy judgement. However, policy judgement is central in the area of supervision and it would likely be difficult to avoid it in any meaningful delegation of supervisory tasks. It would also appear somewhat incongruous for the Union to transfer competences to the ECB to only be delegated back to national authorities.

The third option was then to adopt a dual banking model, similar to the U.S. system of banking supervision. In this model, there is a coexistence of two regulatory structures: the banks are chartered and regulated either at the national or state level, to which it corresponds different regulatory authorities, laws and standards. In Europe, this would be translated by a two-tier system where banks could either choose a license, or be allocated to supervision, at the European or national level. Although institutionally feasible, this option could raise questions regarding its compatibility with the framework of the single financial market, as it has been developed over several decades. For example, the banks in the top tier could benefit from enhanced freedom to provide services since they would report to a single supervisor. The banking law of the Union provides the single passport to all authorised credit institutions in the same conditions, in line with the freedoms of establishment and to provide services, which are inclusive of all economic operators. The top tier banks could also be perceived as safer than national banks if they would have privileged access to direct recapitalisation by the ESM. Accordingly, a dual banking system would likely create an enhanced single market for the banking institutions regulated at the European level which would be inconsistent with fair competition and non-discrimination.

The SSM Regulation combines elements of the above three options to create a sui generis system of banking supervision, namely decentralisation of operational tasks, possibilities to achieve delegation of tasks, and aspects resembling a dual banking model.

The main decentralising mechanism was introducing a distinction between 'significant' and 'less significant' banks within the SSM. The purpose is to enable the ECB and the national supervisors to have supervisory competences of a different nature with regard to each category of banks. The exclusive supervisory tasks of the ECB with regard the banks, banking groups and respective component banks which are considered 'significant'. This includes at least the banks with total assets above 30 billion euro, or with a ratio of total assets over the GDP of the domestic economy of above 20 per cent GDP, and also the banks receiving direct or indirect assistance from the EFSF/ESM. The ECB can add more banks on the basis of their cross-border relevance or domestic significance, in this latter case at the request of a national supervisor. The scope of 'significant bank' is quite broad. It goes much beyond that of 'systemic bank', which is associated with the potential of a bank to cause significant disruption to the financial system as a whole. Instead, the criteria set in the SSM Regulation appear to aim at encompassing in the exclusive supervision of the ECB the largest part of the banking sector as long as of a relevant size and importance to the economy, as well as those banks providing financial services on a cross-border basis in the member states of the SSM.

The national supervisors, on the other hand, are competent for specific supervisory tasks regarding the banks considered 'less significant'. Since Article 127.6 TFEU cannot confer supervisory competences upon national authorities, the SSM Regulation carves out from the exclusive competences of the ECB a list of tasks regarding the day-to-day supervision of less significant banks. These tasks are not transferred to the ECB but remain with the national supervisors. However, the national supervisors will exercise such tasks within the framework defined by the ECB and under its oversight. They take the decisions regarding less significant banks on the basis of the regulations, guidelines or general instructions of the ECB in order to ensure the consistency of supervisory outcomes within the SSM. The ECB will also define the instances where national supervisors are obliged to notify any material supervisory procedure and draft decisions. Most importantly, the ECB may, at any time, decide to exercise directly itself all the relevant supervisory powers for one or more banks, when it deems it necessary to 'ensure consistent application of high supervisory standards'. In addition to its exclusive supervisory tasks, the ECB is therefore entrusted with another layer of competences regarding the effective and consistent functioning of the SSM as a whole, including the oversight and control of national authorities regarding their own exclusive supervisory tasks regarding less significant banks.

Furthermore, the ECB can request the assistance of national supervisors for the supervision of 'significant' banks, including that they prepare draft decisions for the Supervisory Board. This enables some degree of executive decentralisation of supervisory tasks and even the delegation of specific executive tasks, such as implementing a decision of the Supervisory Board or other specific tasks within the confines of the Meroni doctrine, that is, without involving discretionary judgement. In specific cases, the ECB may also give instructions to national supervisors to make use of their powers under national law, when such powers are not available to the ECB as a competent authority under European law, for example in the case of the imposition of certain type of sanctions.

A system of parallel competences

The SSM also comprises the exercise of parallel competences by the ECB and national authorities. The most significant case relates to macro-prudential supervisory tasks, which is a concept of supervision that has been significantly developed in the aftermath of the financial crisis. It relates to the activation of tools aiming at adapting the behaviour of banks to developments in the real economy and the financial system as a whole, in order to prevent systemic risk.

The SSM Regulation provides a framework of parallel competences whereby both the ECB and the national authorities may exercise macro-prudential tasks and activate the respective tools provided by European law. This is due to the fact that there is both a European and national dimension in the developments of the financial system and the economy. For example, a bubble in the prices of certain assets may occur either as European-wide trend or a specific national event. The national authorities should thus have the competence to also influence their respective economic cycle. At the same time, the concrete macro-prudential instruments are seen as a complement to the classic supervisory tools to safeguard the soundness of individual banks. Accordingly, the ECB should also be able to use them to ensure the effectiveness of its supervisory tasks.[55]

According to the SSM Regulation, the ECB is entrusted with macro-prudential tasks and tools, which basically should be exercised at two levels. First, there is an obligation of national authorities to consult the ECB on macro-prudential decisions based on European law, to which the ECB can object. The national authorities need to consider the objection, but are not pre-empted from proceeding with the decision. Second, the ECB may also apply macro-prudential requirements – for all SSM member states or a specific one – but in an asymmetric manner: it can only set higher requirements than those applied by national authorities. This may be interpreted as including the possibility of setting macro-prudential requirements when the national authorities have not acted. The ECB can decide on its own initiative or at the request of a national authority for its own member state. When acting on its initiative, the ECB has to notify the national authorities before the decision and take into account any objection. When acting on request of a national authority, the ECB may consider extending the macro-prudential measure which is proposed for one member state also for others.

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[55] The main difference between micro- and macro-prudential instruments is that the former are calibrated to ensure the safety and soundness of each bank, while the latter are mainly set from a systemic perspective, taking into account the findings from developments in the economy and financial system.

This system of parallel competences operates therefore within a framework based on the mutual consultation of ECB and national authorities. It bears some resemblances to the parallel competences in competition law, with the main difference that the ECB cannot preempt, as the Commission can, the actions of national authorities. By contrast, it is a more a constraining framework to the extent that the ECB may go beyond national authorities, thus preventing any 'race to the bottom' or passivity in macro-prudential supervision.

A single system?

The SSM is a multi-layered system of European and national competences, but where national competences are integrated and conducted within a common institutional framework. It may be interpreted, at first sight, as a federal system, with a division of tasks and powers between the centre and the national level. In reality, it is a rather compressed system of competences where the ECB has overall responsibility and control over all its parts. In this sense, it presents marked differences to a two-tier system such as the dual banking system of the U.S. referred to above.

First, all banks in the jurisdiction of the SSM are subject to the exclusive competence of the ECB regarding the authorisation and withdrawal of their license. There is no distinction for this purpose between 'significant' and 'less significant' banks, which implies that there are no different banking charters at European or national levels. This brings unity to the banking supervision system, since all banks are Europeanised. Another important difference in this context is that the banks cannot choose between being considered 'significant' or 'less significant' since this depends on the criteria set in the SSM Regulation and to some extent also on the supervisory discretion of the ECB. [56]

Second, the ECB may decide to exercise itself the supervision of 'less significant' banks when necessary to ensure high supervisory standards, thus removing the competence of national authorities regarding specific banks. This sort of 'call-back clause' could appear as an exercise of preemption powers, but it is rather a power of European intervention to preserve the unity and integrity of the

[56] Article in SSM Regulation No. 1024/2013, OJ L287, see note 1 above.

supervisory system: every bank should be subject to the same quality of supervision across the SSM.

Third, all banks are subject to the same law, the European banking law, which is applied by both the ECB and national authorities. This is also one of the areas of innovation stemming from this fusion model of competences. The banking law of the Union comprises both directly applicable Union regulations and Union directives, which require national transposition measures to have direct legal effect. This implies that the SSM, including the ECB and national authorities, will apply a body of law with mixed nature including both directly applicable Union law and national law transposing Union directives. However, the SSM will be subject to two different judicial jurisdictions: the Court of Justice for decisions taken by the ECB regarding 'significant' banks and national courts for decisions taken by national supervisors regarding 'less significant' banks.

Lastly, another element of the singleness of the system is that, as a principle, every euro area bank, 'significant' or 'less significant' is subject to a single supervisor and the same type of supervision. One of the criteria for a bank to be supervised exclusively by the ECB is that it has more than one subsidiary in another SSM member state. This implies that the banks either using or not using the single passport are subject in practice to a single supervisor, the ECB or a national supervisor, respectively. The framework of home- and host-country supervision disappears in the SSM.

The differentiation of the SSM within the single market

While being a major evolutionary step, the SSM represents a challenge to the unity and inclusiveness of the single market in financial services. It is another instance where the response to the crisis leads to the legal and institutional differentiation of EMU within the EU. This stems essentially from the legal basis of the SSM and to the nature of the ECB as an institution of EMU, whose jurisdiction does not encompass the member states from outside the euro area. The mismatch between the jurisdictions of the SSM and the single market's has not only legal and institutional consequences, but potentially also economic implications. A unified banking supervision will, at the very least, reduce the compliance costs in the provision of banking services within the SSM. In addition, the aim is also to enhance the resilience and confidence in the banking system by disentangling it from pernicious links with sovereigns. There is the risk that such mismatch may also represent a stigma for the EU banking institutions from outside the euro area, e.g. leading to increasing costs in capital, thus undermining the basic tenets of the single market. Or it could be detrimental for the member states outside the euro area if their financial institutions migrate towards the euro area.[57]

In this context, the SSM framework introduces additional innovations in European law in order to address the implications of the differentiation between member states of the euro area and those outside. This includes an intergovernmental contractual system for member states to join the SSM jurisdiction and a double-voting system in the EBA among SSM and non-SSM national authorities.

The concept of 'close cooperation'

The solution found to mitigate the mismatch between the SSM and the single market was largely of a voluntary and contractual nature. The member states from outside the euro area may request to join the SSM and have their banks subject to the supervision of the ECB. The SSM Regulation defines it as 'close cooperation' between the ECB and the national supervisors from those member states. The SSM's jurisdiction is extended by the commitment of the member states that their respective national supervisors will follow the instructions of the ECB.

The framework of ECB competences based on the distinction between 'significant' and 'less significant' banks continues to apply with regard to the member states in 'close cooperation'. The ECB continues

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[57] Article 1 of the SSM Regulation includes in this context the principle that the ECB cannot directly or indirectly discriminate against any member state or group of member states as a venue for the provision of banking or financial services in any currency. Likewise, Recital 44 of the SSM Regulation states that the regulation should not lead to incentives for banking institutions to change, essentially, subsidiaries in member states outside the euro area into branches, which would prevent the host-country authorities from exercise effective regulation and supervision (since branches are fully regulated and supervised by the home-country authorities, which in the euro area is the SSM).

to exercise exclusive supervisory tasks over 'significant' banks, with the difference that the national supervisors have to exercise a jurisdictional intermediation to give effect to ECB decisions in their respective territory.[58]

The commitment of member states is however purely contractual and not a legal obligation under the SSM Regulation. If a member State does not comply with the conditions for 'close cooperation', the ECB may suspend or terminate it. Moreover, the 'close cooperation' is not a permanent arrangement. A member State may request the ECB to terminate it at any time after three years of its establishment. Most importantly, a member state in 'close cooperation' also has special rights with regard to the involvement of the Governing Council of the ECB in the SSM decision-making process, as it is analysed in the next section.[59]

This solution expands de facto the supervisory jurisdiction of the ECB to member states outside the euro area, but in an incomplete and imperfect fashion. It does not change the nature of the ECB as an institution of the euro area with its own decision-making bodies. It also represents a looser supervisory jurisdiction over the member states outside the euro area vis-à-vis the others. This has implications for the decision-making process of the SSM and in particular for the possibility of the member states to opt-out of the SSM if it opposes certain decisions.

The concept of 'close cooperation' leads, therefore, to a combination in the SSM of two distinct legal frameworks: European law on the basis of the Treaty for the member states of the euro area, which is combined with an intergovernmental and contractual framework for the relations of the SSM with the member states outside the euro area. In the euro area, the competences and powers of the SSM are exercised in accordance with the Treaty, including, for example, in compliance with the primacy of European law and on a permanent and irrevocable basis. Outside the euro area, the SSM acts on the basis of a 'contract' with member states. The primacy of the SSM's legal

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[58] 'Close cooperation' is regulated in Article 7 in SSM Regulation No. 1024/2013, see note 1 above. Distinction from delegation of tasks and responsibilities under the EBA and banking directives.
[59] *Ibid.,* Article 7.5, 7.6, 7.7. and 7.8.

instruments is conditional on the willingness of the member states outside the euro area to make them binding in their jurisdictions through national legal acts. The 'close cooperation' may also be terminated by either the SSM or the member state, which leads to the exceptional case where a member state may opt-in and opt-out, even repeatedly, from a European system of competences. The differentiation of the SSM within the single market has, therefore, unique legal and institutional implications in the context of European law.

The relationship with the European Banking Authority

Another area of intersection between the SSM and the single market is the role of the EBA as the European agency responsible for supporting the regulation and supervision of banking services. This role has been enhanced by the recent move towards the development of a single rulebook for all banks, which relies on the combination of wider harmonisation of national laws, the increased use of directly applicable regulations, and the EBA tasks in the formulation of technical standards and in the convergence of supervisory practices.

Given the mismatch between the single market and the euro area, the SSM had the potential to destabilise the role of the EBA, including its main tasks and its internal processes of decision-making. In principle, the roles of the EBA, as essentially the single market regulator, and the ECB, as the supervisor in the euro area, do not overlap or conflict. They have however different institutional positions, with the EBA as an agency and the ECB as a Union institution. Furthermore, the ECB has regulatory powers of its own, including the possibility to adopt guidelines, recommendations, and directly applicable regulations, which may potentially conflict with the EBA's instruments. For this reason, the SSM Regulation provides that the ECB should comply with the EBA's guidelines and recommendations as any other national supervisor. In the same way, the ECB is subject to the mediation procedures of the EBA and may also need to comply with EBA decisions in emergency situations.

At the same time, the establishment of the SSM implied a change in the balance of the representatives of national supervisors in the EBA's decision-making body, its Board of Supervisors. With at least seventeen national supervisors being part of the SSM, there was the concern that they would exercise their vote in a coordinated way, effectively subjugating the interests of the single market to those of the SSM. One answer to this concern was avoiding to provide a voting right to the ECB in the EBA's Board of Supervisors (remaining a member without voting rights). The other answer was changing the voting modalities of the Board of Supervisors for certain decisions into a double-voting system, grouping the supervisors of the SSM and those from outside the SSM into separate voting constituencies.

The double-voting system applies to the most relevant decisions of the EBA. It includes the decisions regarding the adoption of draft standards and guidelines and recommendations, actions in emergency situations, and those proposed by an independent panel to the Board of Supervisors concerning breaches of Union law and the settlement of disagreements between supervisors. In these cases, the decisions should be adopted either by qualified majority or simple majority by the Board of Supervisors, but including both a simple majority of its members from competent authorities of participating member states and a simple majority of its members from competent authorities of non-participating member states.[60]

The banking law of the SSM

The differentiation of the SSM within the single market has also implication as regards the application of banking law for the purposes of the conduct of banking supervision: the banking law of the SSM.

As mentioned above, one of the latest legal innovations in the single financial market was the introduction of the concept of the 'single rulebook'. Its implementation relies essentially on the 'maximum harmonisation' of national laws, the use of directly applicable European regulations, delegated and implementing acts by the Commission, and the elaboration of technical standards and the convergence of supervisory practices by the EBA. The main implication of the 'single rulebook' is that the European source of the law of the single financial market does not require transposition through national laws and regulations. It applies directly to market participants. Currently, until the 'single rulebook' is fully realised, the law of the single financial market remains, however, fragmented and

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[60] Article 1.7 of the Council Regulation amending the EBA Regulation, OJ L287, 29 October 2013, 5-14.

multi-layered, comprising European regulations and directives, national laws transposing the provisions of directives, delegated and implementing acts of the Commission both on the basis of regulations and directives, the guidelines and recommendations of the ESAs, and the administrative acts and supervisory practices of national authorities.

The SSM will lead, in this context, to a substantial unification of banking law within its jurisdiction. This will happen mainly through a unified interpretation, application, and enforcement of banking law in the conduct of supervision. Moreover, besides supervisory decisions, the ECB will have the powers to issue guidelines and recommendations, as well as regulations in the jurisdiction of the SSM. These powers may be exercised over both banks and national supervisors.

When taking decisions or exercising regulatory powers, the ECB will remain subject to the full body of the banking law of the single market. This means that it will be the first time that a European institution – the ECB as the SSM – will apply such a multilayered body of law, including European laws, national laws, as well as the non-legally binding acts of a European agency such as the EBA.[61] This may seemingly challenge the principle of the primacy of European law since the ECB's legal acts, notably decisions, will apply not only European law, but also national law transposing directives, which in principle cannot prevail over acts of a European institution. For this purpose, the ECB takes over the role of the national authorities in accordance with the SSM Regulation.[62] However, this application of national law transposing directives reflects the composite nature of the law of the single market as developed over decades. From this perspective, it does not affect the primacy of European law since it simply reflects its current state of evolution.[63] It will lead, in any case,

[61] Article 4.3 of the SSM Regulation explicitly provides that the ECB should apply Union law, including the national law transposing directives and the national legislation exercising options provided in European regulations. It also recalls that the ECB should comply with the Commission's delegated and implementing acts under Articles 290 and 291 TFEU; and it subjects the ECB to the EBA's single supervisory handbook.

[62] Article 9.1 of the SSM Regulation.

[63] *Ibid.,* Article 34 states that the application of national law by the ECB is without prejudice to the principle of the primacy of Union law.

to the situation where the ECB will need to consider potentially different national laws in its decisions and exercise of regulatory powers. This will also represent a challenge to the Court in reviewing the ECB's legal acts of banking supervision. There might be also situations, notably in areas regulated also by other fields of law, where the application of banking law will not be sufficient for the ECB to conduct effective banking supervision. In such situations, the SSM Regulation provides that the ECB may give instructions to national authorities to make use of their powers in order to support the SSM's supervisory tasks, and specifically also to impose sanctions.[64]

The legal acts of the SSM will lead to a differentiated banking law in the single market, which will be much more unified vis-à-vis the member states not part of the SSM's jurisdiction. It will also be subject to the direct judicial review of the Court, which will also contribute to its unified interpretation and enforcement. At the same time, the SSM will provide an additional factor for the expansion of the 'single rulebook', for example by justifying a more extensive use of European regulations in the field of banking services.

The implications for the single market

The establishment of the SSM leads to a deepening of integration with regard to only part of the member states, thus impacting on the unity and inclusiveness of the single market framework. In principle, this would have been also the case if member states would have made use of an enhanced coordination process, with the difference that all member states could participate without constraints, which is not the case with the activation of Article 127.6 TFEU.

The solutions found to address the differentiation of the SSM within the single market are far from ideal. Both the concept of 'close cooperation' and the double-voting of the EBA attempt to mitigate the implications of such differentiation. However, they may end up by achieving the opposite effect of actually reinforcing the differentiation within the single market. The framework for 'close cooperation' enables member states from outside the euro area to participate in the SSM but with additional rights compared to the other member states. The member states in 'close cooperation' may decide not to comply

[64] *Ibid.,* Articles 9.1 and 18.5.

with the ECB's instructions and may request the ECB to terminate the 'close cooperation' at any time after three years. This confirms yet another of the processes triggered by the European responses to the crisis: the variable geometry and configurations of member states. Furthermore, the double-voting system in the EBA gives rise to a disproportional voting weight in favour of the member states not participating in the SSM. It leads to the over-empowerment of these member states in voting rights.

Despite the detrimental implications of the differentiation of the SSM within the single market, the SSM presents clear benefits for the single market as a whole. The scope for protectionism and ring-fencing of national markets is reduced considerably both within and outside the SSM jurisdiction. The same happens with the possibility of coordination failures among national supervisors. This is particularly relevant for the banking law of the Union, including the EBA's instruments, whose implementation and enforcement becomes unified in large part of the single market, thus supporting the development not only of the 'single rulebook' but also of the 'single supervisory handbook', a novel instrument of the EBA introduced by the amendment of the EBA Regulation.[65]

The principle of separation from monetary policy

The dual-nature of Article 127.6 TFEU as a provision of the Treaty relating both to EMU and to the single market in financial services is the key for understanding the 'genetic code' of the SSM. This regards, in particular, one of the foundational legal principles of the SSM: the principle of separation within the ECB between the conduct of monetary policy and of banking supervision.[66] This was dictated by the concerns regarding the appropriateness of combining monetary policy and banking supervision in the same institution, as well as, the differentiation of the SSM within the single market stemming from the euro area jurisdiction of the ECB. Accordingly, the ECB is obliged to only pursue the objectives of the regulation in the performance of

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[65] Article 1 of Regulation 1022/2013 amending the EBA regulation, OJ L287, 29 October 2013, 5-14.

[66] Article 25 of the SSM Regulation, Regulation No. 1024/2013, note 1 above.

supervisory tasks, and to carry out such tasks without prejudice to and separately from monetary policy.[67]

The main expression of the separation principle is the unique decision-making process of the SSM. The separation is first implemented through the establishment of a 'Supervisory Board' as an internal body of the ECB. It comprises a Chair and a Vice-Chair, four ECB representatives, as well as representatives from each of the national supervisors of the euro area member states and from those in 'close cooperation'. The SSM Regulation provides that the key competence of the Supervisory Board is to 'fully undertake' the planning and execution of the ECB's 'supervisory tasks', which includes the preparation of 'complete' draft supervisory decisions for final decision by the Governing Council.[68]

The separation principle in the decision-making process of the SSM is also implemented by the introduction of reverse voting procedures, which have now become widely used in European economic governance as a means to insulate enforcement procedures initiated by the Commission from the preferences of individual member states.[69] The 'complete' draft supervisory decisions prepared by the Supervisory Board are considered adopted by the Governing Council unless it objects within a period of time not exceeding ten working days (or 48 hours in emergencies). If the Governing Council objects, it

[67] The separation principle was publicly argued by the Finance Minister of Germany before the Commission proposal for the SSM Regulation, see Wolfgang Schäuble (2012) 'How to Protect EU Taxpayers against Bank Failures', Financial Times, 30 August 2012. The separation principle is explicitly stated in Article 25.2 of the SSM Regulation, which, besides the separation in decision-making, also requires the ECB to introduce organisational separation of the staff involved in supervisory tasks.

[68] *Ibid.,* Article 26.1 and 26.8. The Supervisory Board acts on the basis of simple majority voting, except when taking decisions on the adoption of regulations, which is subject to qualified majority in the terms of the Treaty, as provided by Article 26.7 SSM Regulation. In the case of qualified majority voting, the four ECB representatives have a vote equal to the median vote of the other members, which vote in accordance with the voting weight of their respective member states.

[69] While the move to reversed qualified majority voting was introduced in the Six Pack, its breadth and scope has been widened by the Stability Treaty. See Article 7 of the Stability Treaty.

has to state the reasons in writing, in particular stating monetary policy concerns.[70]

The competence of the Supervisory Board may be interpreted as akin to the exclusive right of initiative of the Commission to make proposals to the Council and the Parliament as co-legislators in the Treaty. The expression 'fully undertake', interpreted together with the reverse voting procedure and other relevant provisions of the SSM Regulation, means that the Supervisory Board has the exclusive competence to prepare and put forward proposals for decision to the Governing Council. This also implies that the Governing Council cannot take supervisory decisions without the procedural step of involving the Supervisory Board in the preparation and submission of draft decisions. This is why Article 26.8 of the SSM Regulation provides that the Supervisory Board should propose to the Governing Council 'complete' draft decisions, which do not require additions or revisions. In this sense, the Supervisory Board represents an internal body without decision-making powers, but with the exclusive competence to propose decisions and execute them once they are adopted by the Governing Council.

This framework for the decision-making process of the SSM allows achieving a large degree of separation from decision-making on monetary policy since the Governing Council is not responsible for the preparation of supervisory decisions, thus limiting the potential for conflict of interests. At the same time, such separation safeguards the institutional framework of the ECB set out in the Treaty and the Statute, which could not be modified by the activation of Article 127.6 TFEU. The involvement of the Supervisory Board required by the SSM Regulation represents a procedural condition for the exercise of the supervisory tasks within the ECB, and without prejudice to the final supervisory decision-making by the Governing Council.[71]

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[70] Article 26.8 of the SSM Regulation, Regulation No. 1024/2013, note 1 above. In accordance with Article 25.5 of the SSM Regulation, 'the ECB shall ensure that the operation of the Governing Council is completely differentiated as regards monetary and supervisory functions. Such differentiation shall include strictly separated meetings and agendas'.

[71] The setting of procedural conditions for the exercise of competences by European institutions has been accepted by the Court in previous occasions. See Case C-147/96 *Kingdom of Netherlands v. Commission of the European Communities* [2000] ECR I-04723;

From this perspective, the establishment of the Supervisory Board as an internal body of the ECB pursues the three objectives underpinning the principle of separation. First, the supervisory tasks of the ECB are prepared and executed by a specialised internal body comprising representatives of national supervisors and with the appropriate expertise. It mitigates the scope for potential conflicts of interest between monetary policy and banking supervision. Second, the Supervisory Board enables the participation in the governance of the SSM of national authorities in 'close cooperation' in equal terms as those of the euro area, thus addressing the jurisdictional mismatch with the single market.[72] Third, the Supervisory Board provides the basis for distinct and specific accountability arrangements. As analysed below, the Chair and the members of the Supervisory Board are those required under the SSM Regulation to fulfil the accountability obligations of the SSM. It, therefore, also enables the ECB to separate its accountability for monetary tasks from supervisory tasks.[73]

The separation principle in the decision-making process of the SSM is also safeguarded by a 'mediation panel' that the ECB should create under the SSM Regulation. In the words of the SSM Regulation: *'the panel shall resolve differences of views expressed by the competent authorities of participating Member states concerned regarding an objection of the Governing Council to a draft decision by the Supervisory Board'.* The panel comprises one representative per participating member state among the members of the Governing Council and the Supervisory Board, and decides by simple majority.[74] Accordingly, the 'mediation panel' of the SSM represents an additional line of defence for the separation principle, enabling the national supervisors, including those from the member states in 'close cooperation', to address an

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Case C-76/01P *Comité des industries du coton et des fibres connexes de l'Union européenne (Eurocoton) and Others v Council of the European Union* [2003] ECR I-10091.

[72] The representatives of national authorities in 'close cooperation' with the SSM have full membership and voting rights in the Supervisory Board without any distinction from the euro area members. This requirement is reinforced by an explicit obligation of the Governing Council to adopt rules of procedure for the Supervisory Board ensuring equal treatment of all participating member states, in accordance with Article 26.12 of the SSM Regulation, note 1 above.

[73] *Ibid.,* Articles 20 and 21 of the SSM Regulation.

[74] Article 25.5 of the SSM Regulation, note 1 above.

objection of the Governing Council to a draft decision of the Supervisory Board.

Lastly, the separation principle also justifies the possibility that a member state in 'close cooperation' expresses its disagreement with an objection by the Governing Council to a draft decision prepared by the Supervisory Board and notify the ECB that it will not be bound by the potential amended supervisory decision resulting from that objection. This special 'opt-out right' of member states in 'close cooperation' aims at preventing the full jurisdiction of the Governing Council, as a decision-making body of the ECB, over member states outside the euro area.[75] The ECB may then suspend or terminate the 'close cooperation', but it needs to take into account a large array of considerations, including the integrity of the SSM, adverse consequences for the fiscal responsibilities of member states, and whether the supervisor of that member state has taken measures not treating its banks more favourably or equally effective as the objection of the Governing Council.[76]

Independence and democratic accountability

The SSM Regulation also introduces a number of legal innovations regarding the independence and accountability of the SSM.

The first innovation regards the concept itself of independence of the SSM, which is defined by the SSM Regulation in terms similar to the central banking independence of the ECB under the Treaty and the Statute. The obligation of independence falls upon both the ECB and national authorities acting within the SSM, as well as the members of the Supervisory Board.[77] This implies providing the supervisory function with the broadest legal and institutional independence. It represents an innovation to the extent that supervisory independence

[75] According to Recital 72 of the SSM Regulation, the Governing Council of the ECB should invite the representatives from non-euro area participating member states to take part in the discussion, whenever it is contemplated by the Governing Council to object to a draft decision prepared by the Supervisory Board, when such decision is addressed to the national authorities in respect of credit institutions from non-euro area participating member states.
[76] Article 19 of the SSM Regulation, and, with regard to the ECB's central banking independence, Article 130 TFEU and Article 7 of the Statute of the ESCB and the ECB.
[77] Article 7.7 of the SSM Regulation, note 1 above.

has, traditionally, been granted less extensively in comparison with central bank independence. The conduct of supervision has been considered, for several reasons, as a policy function which should be close to political institutions. The reasons for that include the need to avoid the risk of capture by the financial industry, the relevance of this industry for the economy and the citizens, or political reluctance in the delegation of regulatory authority to an independent institution.[78]

The other innovation regards the framework for the democratic accountability of the ECB in the performance of supervisory tasks. The rationale of the framework is threefold.

First of all, it introduces clearly defined requirements of accountability for the conduct of banking supervision, particularly with regard to the relations with the Council and the Parliament. This is justified by the nature of supervisory tasks, which require close scrutiny from political institutions due to the potential risks and costs of banking activities for the financial system, economy, and individual citizens.

Second, it fulfils the principle of separation from monetary policy by establishing distinct accountability channels for supervisory tasks and designating the Chair of the Supervisory Board as the representative of the ECB for such purpose.

Third, the accountability framework also reflects the unique matrix of competences of the SSM, which combines the exercise of European, euro area and national competences at various levels and with variable configurations. At the European level, the ECB is primarily accountable for the conduct of its supervisory tasks to the European Parliament and the Council, in line with the basic principle that accountability for the exercise of European competences is at the level of the Union institutions. However, it also reports to the Eurogroup, which should include, for this purpose, representatives from the member states outside the euro area with are in 'close cooperation' with the SSM.[79] The specific configuration of the member states participating in the SSM thus gives rise to a new form of political

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[78] As explained in Quintyn *et al.* (2007: 34–ff).
[79] Article 20.3, 20.4 and 20.6, all SSM Regulation.

accountability in the Union in the shape of the Eurogroup, as an informal body, and in extended composition.

Furthermore, there is a layer of reporting at the national level. The ECB should also forward its reports to the national parliaments of the participating member states. In turn, the national parliaments may put forward questions to the ECB or invite the Chair of the Supervisory Board for hearings.[80] This does not represent a formal relationship of accountability with national parliaments but more the provision of information along the lines of Protocol (No 1) of the Treaty on the role of national parliaments in the Union. However, it does involve national parliaments in the regular monitoring of the functioning of the SSM thus providing another layer of democratic scrutiny. This is reinforced by the remaining accountability of national supervisors to their respective parliaments, also for the tasks carried out for the SSM.[81]

The accountability framework of the SSM presents therefore a hybrid nature, comprising a special format of the Eurogroup, the European Parliament and national parliaments, which is consistent with the variable geographical jurisdiction of the SSM and its various levels of competences. Such framework is also motivated by the fact that the supervisory tasks of the SSM may have a bearing on fiscal responsibilities of member states, notably in the case of a bank failure or financial crisis. This requires a closer relation with individual member states, including their national parliaments, similarly to economic governance arrangements. For example, the TSCG provides that the European Parliament will organise with national parliaments a conference to discuss budgetary issues (see Article 13).

The answer to increasing democratic legitimacy in the case of the SSM is, therefore, involving the national parliaments at the European level, while also enhancing the role of the Parliament in parallel to the transfer of competences to the European level.[82]

[80] Article 21.1, 21.2, and 21.3, all SSM Regulation.
[81] In this sense, see Lastra (2012: 8–9).
[82] According to Article 20.9, the ECB and the Parliament should conclude appropriate arrangements on the practical modalities of the exercise of democratic accountability and oversight over supervisory tasks. The arrangements should cover, inter alia, access to information, cooperation on investigations and information on the selection

Findings: the constitutional implications of the SSM

This chapter started with the premise that the evolution of the law of the single financial market mirrors that of European integration as a whole. The research question is the extent to which the legal and institutional features of the SSM confirm the constitutional trends underlying the European responses to the crisis and what implications it may have for wider European integration. As summarised in the introduction, there are three constitutional processes at play in the responses to the crisis: the reinforcement of intergovernmental decision-making over the Community method; the development of a composite legal architecture for integration, involving instruments within and outside the Treaty and combinations of both European and national competences; and, as a result, the increasing differentiation of EMU within the EU, which challenges the legal and institutional unity of EU by leading to variable geometries of competences and configurations of member states. The findings are that the legal foundations and institutional structure of the SSM conform to a large extent to these constitutional processes. In the context of the Banking Union, similar developments are taking place with regard to the creation of a Single Resolution Mechanism and the introduction of a Financial Transaction Tax.[83]

First of all, the SSM is a centralised enforcement structure which replaces the previous decentralised governance arrangements for the provision of banking services. This corresponds to one of the processes to address the crisis, the substitution of soft governance by legally binding enforcement of European law, for example, a trend similar to the reinforcement of the Stability and Growth Pact. This confirms that 'governance' failed as the institutional model to manage market integration; it failed, in particular, to underpin an effective decision-making process that takes European interests at

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procedure of the Chair of the Supervisory Board. The ECB is also required to cooperate sincerely with any investigations by the Parliament under the TFEU.

[83] Proposal for a Regulation of the European Parliament and of the Council establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Bank Resolution Fund and amending Regulation (EU) No 1093/2010 of the European Parliament and of the Council, COM (2013) 520 final, 10 July 2013; Proposal for a Council Directive implementing enhanced cooperation in the area of financial transaction tax, COM (2013) 71 final, 14 February 2013.

heart. The ambiguity of governance arrangements, which aggregate national wills without credible enforcement at European level, may be tolerated for the management of integration in good times but soon reached its limits in situations of stress. Accordingly, the centralised enforcement of European banking law by the SSM replaced the often divergent national enforcement, which was loosely coordinated by agencies and committees.

A common denominator to the European responses to the crisis has also been the attempt to deepen integration but to the minimum necessary to address each peak of the crisis, while avoiding transferring competences to the European level, or using the Community method for such purpose, or amending the Treaty with all the political implications that would follow. This justifies to some extent the legal nature of mechanisms such as the EFSF or the ESM, or the fiscal compact, which have been established outside the Treaty (Craig 2013: 8–9; and de Witte and Beukers 2013: 847–848).

The establishment of the SSM is noteworthy as it seemingly evades this trend. It represents a very significant transfer of competences to a European institution through the activation of a provision of the Treaty. However, it may be argued that the Treaty did not allow any other legal and institutional solution. As analysed above, Article 127.6 TFEU was the only possible legal basis to transfer supervisory competences to a European authority. This is one of the reasons why the functioning of the SSM had to be adapted to the fulfilment of the preferences of member states.

There were in particular three main preferences, which influenced the design of the SSM, as indicated above: first, the implementation of a separation principle within the ECB between the conduct of supervisory tasks and monetary policy; second, addressing the mismatch between the euro area jurisdiction of the ECB and the single market by enabling the member states from outside the euro area to participate in the SSM; and, third, involving the national supervisors in the functioning of the SSM.

The pursuance of these three preferences are very much at the origin of the intricate institutional architecture of the SSM, which combines several layers of competences, including exclusive European competences, remaining national competences, oversight competences regarding national authorities, parallel competences, and other types of shared competences. The striking difference with previous multilevel governance structures in European law is that in the SSM all the levels of competences are inextricably intertwined with each other, even much more than in a traditional federal construction, which relies on the coexistence of distinct legal and institutional structures. In the SSM, all levels of competences depend on each other and are recognised as a single system, a plywood of European and national layers. This is a significant innovation, although the combination of European and national competences is also present in arrangements such as the fiscal compact (the TSCG) relating to economic governance.

The same set of preferences justifies the mechanism for extending the supervisory jurisdiction of the ECB to the member states outside the euro area. The provision of Article 127.6 TFEU is somewhat an oddity given its dual nature of relating both to EMU and to the single market. Its activation presupposed the day when, as envisaged by the construction of EMU, the euro area would coincide with the single market. Therefore, without the fulfilment of this condition, the activation of Article 127.6 TFEU was bound to create a mismatch that could be harmful for the integrity of the single market.

The contractual mechanism of close cooperation between the member states from outside the euro area and the SSM attempts to overcome such mismatch. But in doing so, it conforms with another of the trends of previous responses to the crisis: the variable geometry of many arrangements and the widespread dynamics of opting in or opting out on the part of member states. The consequence in the context of the SSM was the introduction of a quasi-decision-making body, the Supervisory Board, within the ECB to conduct the supervisory tasks in a configuration different than the decision-making bodies of the ECB, which are devoted to the euro area. The member states from outside the euro area may choose to join the SSM and also to leave it at some stage. This presents similarities to the profusion of configurations in economic governance, such as the ESM of seventeen member states, the Euro Plus Pact of twenty-three member states or the TSCG of twenty-five member states. It may even be argued that the close cooperation mechanism is a form of intergovernmental cooperation within the structure of the SSM.

Therefore, the SSM also reflects the challenge to the principles of equality of member states and unity of the EU posed by a deepening of integration around the EMU. In this context, the dual nature of Article 127.6 TFEU makes it even more prominent the centrifugal force of EMU vis-à-vis the single market.

Finally, the accountability framework of the SSM follows the trend of variable geometry, as reporting is made to Eurogroup but in the presence of the member states participating in the SSM, and also the trend regarding the involvement of national parliaments, thus matching the federal structure of the SSM.

The conclusion is that the SSM, together with the other responses to the crisis, represents another signal that the Union may be moving forward in operating the constitutional transformation from a community of benefits to a community of risks, where not only the benefits from integration are shared but also the associated increased risks, potentially leading to redistribution policies within the Union. In fact, the SSM is the direct result of a quid pro quo between the transfer of competences and the mutualisation of risks through the direct recapitalisation of banks by the ESM. It aims therefore at matching European competences with European liabilities. Arrangements such as the ESM itself, the reinforcing of the SGP, and the TSCG were manifestations of this evolution, but probably not with the significance of the SSM which involves a permanent and complete transfer of sovereignty over competences that may have a bearing on fiscal responsibilities. In doing so, the SSM operates on the basis of a formalised fusion of European and national competences, which represents an additional novelty but also challenge for European law.

At the same time, it is clear that such momentous shift, if it happens, will be largely the result of decisions motivated by the emergency in stabilising the Union and the EMU. This begs the question of its sustainability without a broader democratic legitimisation process. In the same way that soft economic and regulatory governance is at the root of the current crisis, soft democratic legitimacy may undermine the efforts to overcome it.

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Chapter 13

The beheading of the legislative power European constitutionalisation between capitalism and democracy

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In the European beginning there was not the affirmation of *peace*, the protection of which was the reason why the European Union got the Nobel-Price last year (although, at the same time, the Union or its member states are at war in several parts of the world).

However, in the beginning there was not peace but the *negation of fascism*: that is the *emancipation* of Europe from the dictatorship of the Third Reich.

In the beginning there was not the *managerial mindset* of possessive individualism and 'peaceful competitive struggle' (Marx 1869: 97).[1] In the beginning there was political autonomy.

In the beginning there was not rational choice and strategic action enabled by *rule of law* but the *emancipation from any law that is not the law to which we have given our agreement* (Somek 2012).

Martti Koskenniemi calls the latter indifference to the managerial

[1] English quoted from: <http://www.marxists.org/archive/marx/works/1852/18th-brumaire/ch01.htm> (last accessed 20 August 2013).

mindset: the *Kantian constitutional mindset* (Koskenniemi 2006; see also Koskenniemi 2008). For Kant, in his time, the scandal of so-called absolutism was not a lack of *Rechtsstaat* or rule of law. Kant had no doubt that the contemporary monarchy was a state of law. For Kant the scandal of that monarchy was its lack of political 'autonomy' and 'self-legislation', and the absence of 'structures of political representation' (Koskenniemi 2006: 26). Historically the Kantian constitutional mindset is the mindset of the French Revolution as it once was expressed strikingly by the young Karl Marx (1972: 260) in one short sentence: '*Die gesetzgebende Gewalt hat die Französische Revolution gemacht*' (The legislative power has made the French Revolution).[2]

Constituent power

Today the memory that it was the same constituent legislative power of the peoples of Europe that has made the European Union between fall 1944 (that was the last year of World War II in Europe) and 1957, has been repressed and displaced by the managerial mindset that became hegemonial already during the 1950s. However, the European unification did not begin with the Treaties of Paris and Rome in 1951 and 1957 but with the *new constitutions* that all founding members (France, Belgium, Italy, Luxemburg, Netherlands, West-Germany) had given themselves between 1944 and 1948. Moreover, the foundation of the first Communities in 1951 and 1957 was an effect of a *global revolutionary transformation of national and international law* that was as deep as that of the French Revolution (see Brunkhorst 2012):

1. All founding members had *changed their political leaders* and had *replaced great parts of the former ruling classes* with former resistance fighters or emigrants who had defected (Osterhammel and Petersson 2007: 85; Hobsbawm 1994: 185–187).[3]

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[2] Because of the *indeterminacy* of application of law, and also the application and concretisation of legal norms, is not simply a politically neutralised business of managerial experts but, as Kelsen, Merkel and Heller rightly argued already in the 1920s, that 'determining the content of the legal norm [always is] a political question' (Koskenniemi 2006: 29).

[3] To be sure, strong continuities did remain in all countries, in particular in Germany the Nazi-continuities of the elites were still strong but silenced and displaced, strikingly described by Hermann Lübbe as '*kommunikatives Beschweigen brauner Biographieanteile*'), see Lübbe (1983: 335).

2. All constitutions of the founding members were *new* or *revised* in important aspects and *more democratic than ever before*. Only now *all* of them stipulated *universal adult suffrage*.

3. All had *eliminated* the remains (or after 1918 newly invented structures) of *corporative political representation* of society (see also Jesch 1961). The German *Grundgesetz* even constituted a completely *new state* (see Kelsen 1945).

4. All constitutions of the founding members expressed a strong emphasis on *human rights* and had *opened themselves* (explicitly or implicitly) *to international law* (on the German case, which was not exceptional, see Wahl 2003; see also Di Fabio 1998).

5. Finally, and crucial for the foundation of Europe: All founding members of the European Communities bound themselves *by the constituent power of the people* to the *project of European Unification* (Fossum and Menéndez 2011: 175).[4]

In consequence, it can be concluded that, from the outset, the European Union was not founded as an international association of states. On the contrary, it was founded as a *community of peoples* who legitimated the project of European unification *directly* and *democratically* through their combined, but still national, constitutional powers. At the same time and with the same founding act, these peoples, acting in plural, constituted a single *European citizenship*. Therefore, from the beginning, the Treaties were not just intergovernmental, but *legal documents with a constitutional quality*.

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[4] The only instance of a constitution of a founding member that made no declaration about Europe, the Constitution of Luxemburg, is itself a revealing case. In this case the Luxemburg *Conseil d'État* decided in 1952 that the Constitution implicitly committed the representatives of the people to join the *European Coal and Steel Community*, and to strive for further European unification. It is argued that, even if the constitution of Luxemburg did not contain anything vaguely resembling a proto-European clause, the *Conseil d'État* constructed its fundamental law along very similar lines. When reviewing the constitutionality of the Treaty establishing the Coal and Steel Community, the *Conseil* affirmed that Luxembourg, not only could, but should, renounce certain sovereign powers if the public good so required. See the Report on the 1952 judgment of the *Conseil d'État*.

Managerial take-over

However, as one also can observe in other cases of national or transnational constitutionalisation: the constitutional moment was followed by unspectacular evolutionary incrementalism and a silent but steady process of ever denser integration. The *managerial mindset* took over soon after the first big changes. However, it has not only *replaced and repressed* the *Kantian mindset* of revolutionary foundation but also *stabilised* and *realised it step by step legally*.[5] In European law today the Kantian mindset is expressed in the reference of the preambles of the European Treaties to 'solidarity', 'democracy', 'social progress', 'human rights' and 'rule of law'. Solidarity is mentioned again and again; however, the Treaty also states that solidarity should be for free (as in David Cameron's first sentence when the crisis erupted: 'No money for the Greeks!'). But nonetheless, the Kantian mindset is implemented in many single articles and legal norms of primary and secondary European law, such as the famous Art. 6 of the Treaty of Maastricht, or the Articles 9–12 of the Lisbon Treaty.[6] Finally, the Kantian mindset found its way into numerous legal comments and treatises. As Neil McCormick rightly has observed, during the last half century a European Common Law emerged.[7]

At the end of the day, and after the symbolic re-establishment of state-sovereignty through the constitutional court of the European hegemon in Karlsruhe – the counter-hegemonial Czech constitutional court in its judgment on the Lisbon-Treaty stated that the *European Union today forms a complete and gapless system of democratic*

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[5] For an illuminating case study, see Madsen (2011: 55–59). On the general need of the 'Kantian' mindset of normative social integration for systemic and 'managerial' stabilisation, see Habermas (1981: 228) and Nassehi (2006: 126–127).

[6] A good explication of the Kantian democratic and even cosmopolitan mindset of the Lisbon Treaty is von Bogdandy (2012a); on the Maastricht-Amsterdam Treaty, and in particular the Constitutional Treaty that failed in 2005 but is to a large extend identical with the Lisbon Treaty, see Callies (2005: 402–404).

[7] What German lawyers observe as the emergence of an *autonomous legal doctrine* is reflected by a Scottish observer as the emergence of *European common law* that transcends the *pacta sunt servanda* validity of international law. European 'institutions and organs', Neil MacCormick (1999: 139) argues, 'have had a continuous existence over several decades and through many changes of personnel. They have become central institutional facts in the thinking of Europeans. Citizens and officials throughout Europe have interpreted the norms of and under the treaties as having direct effect on private persons and corporations as well as on states. Over more than four decades this has proceeded with impressive continuity'.

legitimisation, and rightly so (Ley 2010: 170). Legally Europe no longer has a crucial democratic deficit. It is already a full-fledged democracy on both levels: the national *and* the transnational.

The problem is that nobody knows it.

The problem is not just the managerial mindset but the *hegemony of the managerial mindset*, and the *reduction* of politics to technocracy that today allows the political and economic elites to bypass and manipulate public opinion and democratically legitimated public law *on both levels*: the European *as well as* the respective national level. At the same time as it is growing legally, the public power of the people and its representative organs is more and more deprived of real power and replaced by grey networks of *informal government* (Möllers 2005, 2003)[8]; – called 'good governance' (see Zürn 2004) instead of democratic government, called 'administrative accountability' (See Grant and Keohane 2005: 2943) instead of parliamentary responsibility, called 'deliberative democracy' instead of egalitarian decision-making.[9] In the world of informal government public contestation over real issues and substantial alternatives is just 'not helpful' (*nicht hilfreich*), to say it in the matchless managerial language of Angela Merkel. In Angela Merkel's world deliberative democracy begins when the doors are closed.

Hence, and this is my *overarching thesis*: The Kantian mindset of revolutionary foundation has been concretised and stabilised throughout the gradual evolutionary process of constitutionalisation. This evolutionary process was performed under the lead of the managerial mindset of Europe's political elites and professional experts. However, the hegemony of the managerial mindset had the paradoxical result that the Kantian mindset at the same time was *preserved and repressed* (or displaced), *constitutionalised and de-constitutionalised* – again and again on every stage of the twisted paths of European constitutionalisation.[10]

To demonstrate that, I will combine throughout the following

[8] On the accumulation of flexible and decentered power structures see Hardt and Negri (2002); Prien (2010); Fischer-Lescano and Teubner (2006). On white, grey and black networks, see Matiaske (2012).
[9] For a sound criticism of these tendencies, see Puntscher-Riekmann (2010).
[10] On the stages, see Tuori (2010).

sections Koskenniemi's Kantian inspired distinction between the two constitutional mindsets with Kaarlo Tuori's more managerial reconstruction of the constitutionalisation of Europe as an incremental evolutionary process of stages of structural coupling of law with other social systems. Through this combination, Koskenniemi's more voluntaristic distinction is transformed into a set of 'existing concepts' (Hegel) that are internal to the social evolution.[11]

Economic constitution

As Tuori has shown, Europe now has not only many national (and sub-national) constitutions but also many transnational constitutions that evolved gradually and in stages. The **first evolutionary step** was taken in 1957 with the establishment of a functional **economic constitution** that lies within the *structural coupling* of the *legal* and the *economic system*. The establishment of the economic constitution was due to German ordoliberalism. The ordoliberals were a German-Austrian group of economists and jurists at the end of the Weimar Republic. They all were (more or less) far-right neo-conservatives but, with few exceptions, anti-Nazis. The centre of the school was the University of Freiburg in south-western Germany. Members of the School were Franz Böhm, Walter Eucken, Alexander Rüstow, Wilhelm Röpke, Alfred Müller-Armack and Friedrich August von Hayek.[12]

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[11] I have tried to explain that further in Brunkhorst (2013). On the 'existing concept', see Hegel 1969: 481. On the (very one-sided) critique of the empty, or as Hegel says: 'abstract ought', see Hegel (1971: 369–372). Kant is not that far away from modern historical and evolutionary thinking as his critics since Hegel regularly assume, see also Vorländer (1921: 100). Such a concept then can work in both directions dialectically: Either as a mechanism for stabilising the so called *Sittlichkeit* (ethical life) of the *social systems* of bourgeois society that is capitalist or bureaucratic class-rule and authoritarian economic government; or (in dialectical retaliation) the existing concept of law 'can strike back' against the so called *Sittlichkeit* of capitalist domination (Müller 1997: 56). It can strike back because law, and in particular *constitutional law*, can be used by the 'have-nots', by peripheral states and lower classes as a legal principle, a legal claim, or even as a legal remedy to contradict its own interpretation and implementation that is in the service of the respective ruling classes.

[12] Most of the school were conservative opponents to Nazi-fascism. Böhm was a declared anti-Nazi, an especially early defender of the Jews, and a member of the resistance with close relations to Bonhoefer and Gördeler. Eucken was a conservative Anti-Nazi who strongly opposed Heidegger as the first Nazi-Rector of the University of Freiburg (Even in 2011 the dedication to him, dating from 1936, is still clearly visible above the main entrance). He was loosely associated with the conservative resistance. Rüstow was a member of the far-right shadow cabinet led by General Kurt von Schleicher. He engaged in a half-hearted attempt at an anti-Hitler coup

Originally the idea of an economic constitution was an invention of the German socialist left at the end of World War I, in particular Hugo Sinzheimer and his student Franz Neumann. Sinzheimer and Neumann strictly followed the Kantian presupposition that the political constitution and the parliamentary legislator should keep the supremacy over the economic constitution. The economic constitution should have a mere service function: It should improve the possibilities of the democratic legislator to subject the markets to democratic control, and in particular the private sphere of domination within the capitalist firm, under democratic control.[13]

At the end of the Weimar Republic the ordoliberals 'rather hijacked' the idea of an economic constitution from Sinzheimer and Neumann, watered it down and reversed it severely (see Tuori 2010: 16).[14] During the 1950s they turned the idea upside down, trans-nationalised the economic constitution, decoupled it from the national political constitution and subsumed the latter under the former. Now the whole society should be 'subsumed' under the 'principle of market-compliance', as the (at that time pious) former Nazi Alfred Müller-Armack wrote in 1960 (Müller-Armack 1960: 11–12, 15, my translation).[15] In 1957 treaty negotiations the German ordoliberals under the lead of Müller-Armack, and strongly supported by the American government, finally won the battle against the recalcitrant French government that, at the time, defended a constitutional project that was much closer to the original ideas of Sinzheimer and Neumann (Wegman 2010).

With the establishment of the economic constitution in 1957 a

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d'état, and he had to emigrate in 1933. Röpke was attached to the conservative 'revolution' (*Tat-Kreis*) from the early 1920s. However, he strongly opposed German fascism as early as the late 1920s, and he emigrated (as did Eucken) to Turkey in 1933. Alfred Müller-Armack was a Nazi of the first hour. Hayek took a chair at the London School of Economics (LSE) and he left the continent by 1931. He was the most radical liberal opponent of Keynes, who already at that time had a chair at the LSE. Still the best criticism of Hayek is by Kelsen (1954). As a legal theorist, Hayek was very close to Carl Schmitt. This point is made in Scheuermann (1997) and Vatter (2010).

[13] See Neumann (1978: 70–74, 79–99; in particular pages 70, 72, 74, 87–90, 95–96).

[14] The hijacking was organised by Franz Böhm in his *Wettbewerb und Monopolrecht* (Böhm 2010[1933]).

[15] For a brief and powerful criticism of the imperial tendencies of ordoliberalism see Teubner (2012: 30–34).

Schmittian constitutional *Grundentscheidung* (basic decision) was made. It consisted of the radical 'negation of a political constitution of Europe' (Tuori 2010: 15). Instead of subsuming the economic constitution under the political constitution the political constitution was subsumed under the economic constitution, and therefore *Wettbewerbsrecht* – competition law – became the 'axis of the economic order' (Wegmann 2010: 93). In case of doubt the 'concrete order' of *law and economics* trumps the formal constitution of *law and democracy*.[16] Whereas formal constitutional law still adhered to the Kantian priority of democratic legislation, the concrete order of *law and economics* became Europe's informal prerogative constitution – Europe's 'hidden curriculum'.[17] The legal link between visible constitutional law and the invisible prerogative constitution was Art. 2 TEEC[18] (Wegmann 2010: 94).[19] One of the most crucial effects of the European prerogative

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[16] *Diese Asymmetrie ist bereits in den Gründungsverträgen angelegt, was sich daran zeigt, dass im Gegensatz zu den meisten Rechtsordnungen der Mitgliedstaaten die Wettbewerbspolitik der Union verfassungsrechtlich abgesichert ist, während die Bewältigung der sozialen Folgen den Mitgliedstaaten überlassen bleibt. Auf diese Weise fallen Deregulierung und Regulierung institutionell auseinander.* Legitimationstheoretisch lässt sich das nicht begründen. *Die Aufspaltung in eine bloß formelle Legitimation des gemeinsamen Marktes und eine materielle, über die Mitgliedstaaten vermittelte Legitimation der Marktkorrektur macht angesichts der vielfältigen wechselseitigen Abhängigkeiten heute keinen rechten Sinn mehr. Will man Freiheiten über Grenzen hinweg ausdehnen, müssen auf Ebene der Union politisch hinreichend verantwortete Kompetenzen für eine Umverteilung geschaffen werden* (Franzius and Preuss 2011: 70).

[17] On the 'hidden curriculum', see Offe (2003: 463). On the distinction between the two constitutional orders, see Fraenkel (1999[1941]) and Joerges (2012).

[18] Treaty establishing the European Economic Community.

[19] Art. 2 TEEC: 'It shall be the aim of the Community, by establishing a Common Market and progressively approximating the economic policies of Member States, to promote throughout the Community a harmonious development of economic activities, a continuous and balanced expansion, an increased stability, an accelerated raising of the standard of living and closer relations between its Member States.' Today it is replaced by Art. 3 EC: 'The Community shall have as its task, by establishing a common market and an economic and monetary union and by implementing common policies or activities referred to in Articles 3 and 4, to promote throughout the Community a harmonious, balanced and sustainable development of economic activities, a high level of employment and of social protection, equality between men and women, sustainable and non-inflationary growth, a high degree of competitiveness and convergence of economic performance, a high level of protection and improvement of the quality of the environment, the raising of the standard of living and quality of life, and economic and social cohesion and solidarity among Member States.' On the term 'invisible constitution' but with a bit different meaning, see Wiener 2008. The changes of the text are massive. The *wording* of Art. 3 EC already entails everything that is needed for a democratically controlled capitalism (or even for a

constitution was the negation of any transnationalisation of the political constitution. The hegemony of the hidden curriculum stimulated and reinforced the Europeanisation of large enterprises and employers' federations, but at the same time strictly limited unions' activities and employee organisations to the sphere of the national state (see Buckel 2012: 20).

Ordoliberals today are proud of the fine differences that distinguish them from Neoliberalism. But it was indeed ordoliberalism that for Europe disclosed the historical path to the latest great transformation of globalisation that started in the 1980s. If we resume the three basic ideas of ordoliberalism, it becomes evident, that only one idea is different. Therefore, the relation between ordo- and neoliberalism resembles more a cooperative historical division of business than a fierce opposition:

- The *first* basic idea of ordoliberalism is: to *get rid of state-control of the markets*. The spectre of 'socialism' and 'communism' must be banned as long as it is haunting Europe under the mask of macro-economic state interventionism. Here ordo- and neoliberalism have always agreed. Today's representatives of the power elite, such as the President of the German *Bundesbank*, Jens Weidmann, or the former judge of the Verfassungsgericht, Udo DiFabio, are accusing even the President of the ECB, Mario Draghi, of creeping socialisation (*schleichende Sozialisierung*) and centrally planned economy (*planwirtschaftliche Zentralität*) – Dragi, the crypto-communist who learned his job at the communist cadre training centre Goldman & Sachs.[20]

- However, ordoliberalism not only distrusts the (bureaucratic) state, Marxists and Keynesians – but also big size (that is

democratic socialisation of the means of production), and the wording is already concretised partially in secondary European and national law (see Buckel 2012). However it lacks the *power* of a full-fledged implementation of the change of the hegemonic axis of Europe's economic order from the *neoliberal project of improvement of competition capacities* to the new Art.'s 2 *egalitarian democratic programme of European solidarity* (see Habermas 2013 and the quote by Franzius and Preuss in note 16 above).

[20] See Weidmann, J. 'Die Stabilitätsunion sichern', *Frankfurter Allgemeine Sonntagszeitung*, 8 July 2012, p. 33; Weidmann, J. 'Der Euro verlangt eine Stabilitätsunion', *Süddeutschen Zeitung*, 27 June 2012, p. 28, quoting Di Fabio, U. 'Das europäische Schuldendilemma als Mentalitätskrise', *Frankfurter Allgemeine Zeitung*, 22 June 2012, p. 9.

bureaucratic) capitalism and its tendency to concentration and centralisation of capital that has led to monopoly-capitalism since the beginning of the 20th century (see also Marx 1969[1890]: 650–657). Therefore the *second* basic idea of ordoliberalism is: to *get rid of monopoly capitalism*. Competition law shall keep the economic chances of *all* market participants equal *any time*. This idea is called market justice, but it is a very poor idea of justice (see Friedman 1982[1962]: 15–26, esp. 20–21). From the beginning it was ideological. In fact (as Hans Kelsen has demonstrated in his scathing criticism of Hayek already 1954), it worked in favour of the 'haves' who disposed over the 'means' of production, and at best regulated *their* competition (Kelsen 1967[1954]; Tugendhat 1992; Streeck 2012). However, *in this respect ordoliberalism is clearly different from Neoliberalism*. Neoliberalism has bluntly abolished competition law and reduced so called market justice to shareholder value that then has been identified with the common good by Milton Friedman and others (see Crouch 2011). That's why we can no longer avoid the bright lights of the latest stock market news everywhere we go.

- The *third* (and in terms of constitutional law most crucial) basic idea of ordoliberalism is: *to get rid of democratic legislative control*. Here again ordo- and neoliberals meet in applying the categorical imperatives: Give the judges what you have taken from the democratic legislator and the parliament-bound government! Promote the Judges to the guardians of functional *Ordnungsrecht* (in particular competition law)! In the words of Ernst Joachim Mestmäcker, the present head of the school: '*Die wichtigsten Aufgaben obliegen nicht der Legislative oder der Regierung, sondern der Rechtsprechung*' ('The most important decisions have to be taken not by the legislator or the government but by the judges') (Mestmäcker 2010: 9).[21] The beheading of the legislator is the true end of the French Revolution and the Kantian political

[21] The same argument seems to fit the present crisis, see Mestmäcker, 'Ordnungspolitische Grundlagen einer politischen Union', *Frankfurter Allgemeine Sonntagszeitung*, 9 November 2012, p. 12. Similarly, Milton Friedman and the Chicago School argue that the main threat to political and economic freedom 'arises out of democratic politics' and must be 'defeated by political action' (Amond 1991: 231).

> era.[22] Never again shall a legislator be able to carry out a revolution. That was Maggie Thatcher's very message.[23]

For these reasons, the implementation of the Euro without political government was not just a mistake, or the worst possible compromise – that it was, at least from the perspective of the negotiating parties (see Enderlein 2011) – but actually, seen from an observers' point of view, the implementation of the Euro was nothing else than, as Wolfgang Streeck says, a 'frivolous experiment' to realise a 'market economy emancipated' from all political bonds and to establish 'a political economy without parliament and government' (Streeck 2012: 6–8). That's why big money – the banks, hedge funds, and multinational enterprises – was so strongly in favour of the Euro. The implementation of the Euro just immunised 'the markets against democratic corrections'.[24] This immediately resulted in an increase of the social differences between the rich North and the poor South. When the crisis finally started, European *Ordnungsrecht* derogated national as well as transnational *constitutional law* (see Böckenförde 2011: 299–303; Grözinger 2012; Rödl 2012;). As a result, the social gap that is separating the North from the South grew dramatically in favour of the northern hegemon: that is, Germany.[25] Hence, by beheading the legislator, ordoliberalism has opened the evolutionary path for the neoliberal globalisation of capital beyond state-control.

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[22] For the thesis that transnational law has already mutated into a law that no longer is related to the legislative power, see Amstutz and Karavas (2006: 20). For a skeptic view, see Ladeur (2012); Albert and Stichweh (2007).

[23] In 2002 Alec Stone Sweet (2002: 193, quoted in Buckel 2012: 26) could only state that: '[in] today's multi-tiered European polity, the sovereignty of the legislator, and the primacy of national executives, are dead. I concert or in rivalry, European legislators govern with judges'. One has to add that the combined transnational and national constitutional jurisdictions have reinforced one another, and in a way the European *Verfassungsgerichtsverbund* has reserved the most basic functions of all three classical state-powers for itself – at least in normal times of incremental and managerial evolutionary constitutionalisation; see Vosskuhle (2010).

[24] On the unity of ordo- and neoliberalism, see also Scharpf (2011).

[25] Paul Krugman rightly states: 'Fifteen years ago Greece was no paradise, but it wasn't in crisis either. Unemployment was high but not catastrophic, and the nation more or less paid its way on world markets, earning enough from exports, tourism, shipping and other sources to more or less pay for its imports.' See Krugman, P. 'Greece as Victim', *New York Times*, 17 June 2012, retrieved from: <http://www.nytimes.com/2012/06/18/opinion/krugman-greece-as-victim.html> (last accessed 13 August 2013).

Ordoliberalism has done its job, ordoliberalism can go. Once Neoliberalism had taken over in the 1980s, the *great transformation* of the last thirty years could begin: the transformation *of state-embedded* and *state-controlled markets* into *market-embedded* and *market-controlled states* (Streeck 2005).

State of law constitution

For all that, economic constitutionalisation is not the only evolutionary formation of European constitutional law, and even if it remains the hegemonial constitution to date, it was and is not the last stage of Europe's constitutional evolution. The latter is, as we have seen, conducted by the managerial mindset of *law and economics*. However, and this is my very point:

- Once the Kantian mindset has been constitutionalised and integrated into the public authority of European law, it counteracts the managerial mindset of blind evolutionary adaption *as* a *normative constraint*.

- Once the Kantian constitutional mindset becomes an evolutionary normative constraint it switches from an *empty ought* to a (Hegelian) *existing concept*. Its emancipatory idea 'can be halted or inhibited. But it cannot be eliminated'.[26]

In the European constitutional history, the Kantian mindset of autonomy came back already in the early 1960s, together with the rapidly increasing volume of European regulations. It came back in the reduced and, for professional lawyers, manageable form of individual lawsuits over issues of *private autonomy*. In two landmark decisions of the European Court from 1963 (*van Gent & Loos*) and 1964 (*Costa*) the *emancipatory* side of the legal form flashed up. To establish only private autonomy, the judges (in a bold teleological interpretation of the Treaties) had to create an autonomous European *citizenship* and European *citizens' rights* as rights of an autonomous legal community (see Chalmers *et al.* 2006; Craig *et al.* 2007). The two decisions from 1963 and 1964 were therefore described emphatically (and a bit overdone) as 'the declaration of independence of Community law' (see Tuori 2010: 17).
However, the Kantian flash of the two landmark decisions would

[26] With reference to the historical concept of *emancipation*, see Somek (2012: 8).

have disappeared immediately from the trajectory of constitutional evolution, if the two decisions had not been followed by thousands of cases appealing to European Law in national courts of all member states (and the backing of the national courts by the ECJ submission procedure under Art. 267 TFEU) (see Alter 1996, 1998; Hitzel-Cassagnes 2012). In this case the old evolutionary insight became true – that not the elites but the *masses* make the evolution, and here I mean the masses of negative legal communications that filled the variety pool of the legal evolution, and finally engendered a new constitutional formation: the **second stage** in the evolution of European constitutional law was reached. European *Rechtsstaatsverfassung*, or the **juridical constitution of Europe**. The European *Rechtsstaatsverfassung* consists of the (reflexive) *structural coupling of law and law* – or may be more precise: it consists in the structural coupling of *law and subjective rights* (Tuori 2010: 18).[27]

However, all these legal advances remained limited to legal experts and individual plaintiffs. After the rule-of-law-stage-II of the constitutional evolution of Europe was reached, the Kantian mindset was *constitutionalised under private law*. The Kantian mindset became a European public authority with binding legal force – even if it remained, it's true, *privatised* – and it was big money that pocketed the profits of the newly invented rights. The dialectic of European constitutionalisation now becomes obvious. *Constitutionalisation at once advances and is de-constitutionalised by its own advances*.

> You could create rights and afford judicial remedies to slaves. The ability to go to court to enjoy a right bestowed on you by the pleasure of others does not emancipate you, does not make you a citizen. Long before women and Jews were made citizens they enjoyed direct effect.[28]
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> (Weiler 1997: 303)

[27] The European *Rechtsstaat* has finally transformed Europe into *one single*, internally differentiated legal order; negatively described as fragmented, positively described as pluralised. On the ambivalence of the fragmentation diagnosis (that is true also for all larger national states) see Möllers (2010).

[28] In cases such as *Walrave*, *Bosman*, *Viking* and *Laval* of the European Court, the basic freedoms prevail over basic rights. In an antidemocratic way *basic rights are now constrained by the four basic freedoms*, and in particular by the freedoms of big money, capital etc., and not – as it should be at least in an *egalitarian democratic society* – the other way round; see Buckel and Oberndorfer (2009: 285).

Political constitution

Nonetheless, the paradoxical coincidence of constitutionalisation and de-constitutionalisation became a driving force of further progress in the constitutionalisation of Europe. Since the middle of the 1970s the long latent conflict between the ever closer united executive powers of Europe and the parliamentary legislative bodies became more and more manifest.[29] The pressure to reduce the growing *democratic deficit that yawned between private and public autonomy*, finally urged the political and professional power elites to take into account Kantian mindset's longing for public autonomy. Again it became evident that the *Kantian mindset* of emancipation can be repressed, 'can be halted or inhibited. But it cannot be eliminated' (Somek 2012: 8) – once it is constitutionalised.

Since the first direct elections to the European Parliament in 1979 the power of the Parliament has increased persistently. The managerial mindset and stubborn incrementalism of every-day parliamentary work over a quarter-century has turned the weak and restricted European Parliament into a *controlling and law-shaping parliament* that now is one of the strongest institutions of the EU (see Dann 2002; Fossum and Menéndez 2011: 123). The final step to the *parliamentary legislative procedure*, introduced in the Treaty of Lisbon, largely completed the **political constitution of Europe** (Bast 2010). The **third stage** of structural coupling of law and politics was reached.

However, even this time the managerial mindset remained hegemonial. The abysmal dialectic of Europe's technocratic constitutionalisation did not vanish. The polling stations and the market places remained empty. To the same extent as the shaping power of the parliament increased, its public legitimacy decreased dramatically from election to election.[30] The most crucial act of the Kantian mindset: the political implementation of representative government based on fierce public debate (*Freiheit der Feder*), had the paradoxical effect of *democratic public legislation without democratic public life*. The

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[29] At the same time the European Court of Human Rights turned into an active court. Now backed by the ECJ's doctrines of *European law supremacy* and *uniform application*, it radicalised its human rights jurisdiction, see Madsen (2012: 55).

[30] See 'An ever-deeper democratic deficit', *The Economist*, 18 November 2012, retrieved from: <http://www.economist.com/node/21555927> (last accessed 14 August 2013).

increase of *constitutionalisation of public legislation* was again paid at the price of a *de-constitutionalisation of public discourse*.

Return of the repressed

However, these days, the repressed return. The *economic* crisis, and in particular the *banking* crisis, can no longer be displaced by the *budget* crisis. As a consequence, the long latent *crisis of political legitimisation* suddenly becomes manifest. The Kantian mindset gangs up in the streets, in Athens as well as in Madrid and elsewhere. The disregarded constitutional textbooks are striking back: 'Stop *law and economics*! Support *law and democracy*!', they say. They have opened the quarrel about the **social welfare constitution** of Europe that is the **fourth stage** of European constitutionalisation.[31]

As it seems, the structural coupling of law with the systems of social welfare and security can no longer be performed silently behind closed doors and at low costs. The crisis makes it evident: that there is *no modern mass-democracy* without the *rough equality of stakeholders*, at the very least (Crouch 2004).[32]

The national state looked like the big winner after the outbreak of the global economic crisis in fall 2008 (and many political theorists and analysts triumphed, such as Erich Honecker, the last prime minister of the German Democratic Republic: *Totgesagte leben länger* – 'The condemned live longer'). But in fact the state was already weak, and therefore became one of the greatest losers of the crisis. Wolfgang Streeck rightly headed an essay two years later with: *Noch so ein Sieg und wir sind verloren* ('Another victory like that and we are lost'). The great crisis of 2008 has proven that the national state already was deprived of its most basic alternatives in economic and social politics (Streeck 2010, 2011).

The national state's capacity to act and shape the future always relied

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31 On the emergence of the social welfare constitution (together with the security constitution at the external boarder of Europe), see Buckel (2012).

32 See also the quintessence of the last books of the economists Paul Krugman and Joseph Stiglitz in Hacker and Pierson (2012); with instructive statistics and observations, see Judt (2010). On rough equality of stakeholders, see Christiano (2010: 130–132); on 'rough equality' as a necessary condition of modern mass-democracy, see Crouch (2004, ch. 1).

upon the existence of *two major instruments* to keep modern capitalism under control and to enforce the legislative will of democratic majorities: either the stick of the law, or the carrot of money (see Mayntz 2010).

However, it seems that from the beginning of the present crisis the national states were no longer able to perform *macroeconomic steering* through an effective mix of stick and carrot, legislation and investment. The political actors had already lost most of the legislative power that is needed to regulate and control capitalist economy. Up to now they did not regain it at the global level. On the contrary, during the last 30 years of neoliberal global hegemony, the fragile balance of power between democracy and capitalism has dramatically shifted in favour of capitalism.

As long as modern, functionally differentiated economy (with capitalist markets) is embedded in democratically controlled state-power, the parties of the 'have-nots', either the exploited social classes, or the nations who are the losers of the global economic competition between states and regions, have two means to enforce *rough compensatory justice*.[33] They can perform macroeconomic steering in times of crisis: (a) *nationally* by legal regulation and investment, in particular by increasing taxes for high incomes and assets, and/or (b) *internationally* by devaluating their national currency (Offe 2012, 3; Streeck 2012). In today's Europe they have lost both.

- Globalisation (a') has transformed tax-collecting states into debt-depending states, hence reversed the direction of control between states and capital. The *taxing state* that is in control of capitalism has become a *borrowing state* that is controlled by capitalism (Offe 2012: 6).[34]

[33] On states as global economic actors see Ten Brink (2008).

[34] On the genealogy, see Streeck (2011). Crucial for the neoliberal triumph, and sharply recognised by Reagan and Thatcher and their economic advisers, is: that first the Unions are losing their formerly strong political influence and then their organisational power; either by direct oppression such as in the UK, the US and in the low intense democracies (these are democracies defined only by two institutions: free elections and free markets) of the so-called Third World, or by internal reform that makes them sometimes powerful, quasi council-democratic participants in globally operating industrial enterprises such as *Volkswagen*; but at the price of the general interest of the working class. On the latter, see the case study by Herrigel (2008).

- The implementation of the Euro (b′) has taken away all means of resistance poor countries have in the unequal competition with rich countries.

Franklin D. Roosevelt's New Deal administration in the 1930s was supported and pushed by *democratic class struggle*: fighting working class and young and strong Unions who had nothing to lose, organised huge strikes and stay-in strikes. Backed this way by a strong workers' movement, the new Dealers finally regulated and controlled Wall-Street, increased taxes for the rich, cut banks and industrial corporations in pieces, created public jobs, printed money. This way the social democrats and socialists in advanced societies were able to square the circle: that is, to *socialise the means of production within the capitalist mode of production*.

However, this seems no longer possible. After 2008, the tax-increase was nowhere comparable to the increase in the US and other western countries in the 1950s and 1960s. Not one of the banks too big to fail was nationalised or cut in pieces. All but Lehmann were bailed out again and again. Moreover, in Europe the common currency excluded all possibilities of currency devaluation. Deprived of its legislative power to regulate the economy, the state was left only with the alternative to perish or to spend the rest of its money (see Mayntz 2010; Streeck 2010).[35]

Therefore the state has become susceptible to blackmail, and Maggie Thatcher's lie, that there is no alternative, became true as a self-fulfilling prophecy (Beckert and Streeck 2012). Former democratic governments are now in the hands of bankers and their staff of technocrats – directly or indirectly. In states where the bankers have not yet taken the lead, their advice resembles the advice of the old Roman Senate, the *senatus consultum*. That was an advice without any legally binding force: soft law. But whoever did not follow it was already a dead man, even if he left the room alive. Therefore the national state must execute the neoliberal programme with microeconomic means and 'devalue labor and the public sector', 'put pressure on wages, pensions, labor market regulations, public

[35] See also the long time case study, Streeck and Mertens (2012).

services' (Offe 2012: 3)[36] – and then sell the whole thing as a 'reform', 'modernisation', 'new public management' and 'individual empowerment', best served by Third Way labour parties, reformed social democrats and red-green coalitions.[37]

Unfortunately neither Keynesians nor Marxists have ever tried to develop transnational continental and global alternatives to national state power. They have socialised the means of production not only within the capitalist mode of production but also within one country. They have not even made up a plan to establish a transnational *political power* that can match up with global big money and the unleashed communicative forces of the world market. The ordo- and neoliberals (and that is the historical truth of Neoliberalism) had such a plan, as we have seen, and it worked, albeit with catastrophic results. Only that explains the strange non-death of Neoliberalism – after a crisis that, following the pure Chicago doctrine, should only happen after 50.000 years.

Now national state power is over, at least as the power of the so called sovereign state. To take up a metaphor of Eyal Benvenisti (an Israelian international lawyer):

> In the process of globalisation the state politically, legally, economically and culturally has been transplanted completely from a detached villa into a condo in the middle of a house of 200 condos with many different and overlapping forms of real estate ownership.
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> (quoted from von Bogdandy 2012b: 8).

However, the network of transnational public law and politics, and the already emerging formation of transnational statehood (Albert and Stichweh 2007), are by far too weak to establish control over global markets again. Coordinated state powers together with international organisations can at best *make* the global market (negative integration) but are nowhere near to being able to *constrain* it

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[36] See also Scharpf, W. 'Rettet Europa vor dem Euro!', *Berliner Republik*, 2/2012..

[37] See Somek (2012); Brunkhorst, H. 'Raus aus der Neuen Mitte! Umrisse einer künftigen Linken', *Die Zeit*, 25 March 1999, p. 28; Brunkhorst, H. 'Schluss mit der Kritik! Die Generation Berlin und der Affekt gegen den Egalitarismus', *Die Zeit*, 4 November 1999, p. 54; Brunkhorst (2007).

normatively: that is, in the general interest of all of us (positive integration) (see Offe 2003: 457).[38] In thirty years of globalisation the most powerful states of history – the Western democracies – have been turned, as Wolfgang Streeck (2011: 28) writes, 'into debt-collecting agencies on behalf of a global oligarchy of investors, compared to which C. Wright Mills's "power elite" appears a shining example of liberal pluralism'.[39]

The only way out seems to be the *reinvention of democratic class struggle* on the transnational level. The chances are very small but these must not be overseen. For the first time in history, the Unions of southern Europe are beginning to act and strike transnationally and beyond borders. Together with the European Parliament, that for the first time is becoming publicly visible, they could finally trigger a new democratic class struggle for profane aims: a European unemployment assurance to solve the biggest social problem of Europe today – the highest unemployment rate of the young people of the south ever since the great depression of the late 1920s and 1930s.[40] The next step could be a massive diversion away from the deadly ailment of neoliberalism that is called austerity. There is a simple and effective alternative to cutting expenditures, and that is raising taxes (Offe 2012:13).[41] The chances seem small but without renewed democratic transnational class struggle, there is no way out of the crisis, and no way towards a political union of Europe that is worth the name 'Democracy'.

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[38] On the concept of solidarity as the general or universal interest of all of us, see Brunkhorst (2005); on normative constraints see Brunkhorst (2013); on the distinction between 'positive' and 'negative integration', see Scharpf (1999).

[39] As a consequence popular sovereignty has been fragmented and marginalised, beyond and within the national state, see Prien (2010).

[40] This goes back to a suggestion of Claus Offe after a highly pessimistic lecture of Wolfgang Streeck on a conference at the New School for Social Research and the German Research Foundation on 'Social Research in a Transforming World: Transatlantic Conversations', 28 February 2013, New York.

[41] Offe (2012: 15) concludes: '(The) rich countries of Europe dictating the poorer ones the austerity cure in order for them to regain the trust of the financial industries. They do so in spite of all the evidence that austerity is a highly poisonous medicine, an overdose of which will kill the patient (rather than stimulate growth and expand the tax base), in which case the weakest Euro zone members (and eventually all of them) become ever more dependent on lenders and allow them to charge ever higher and ever more unsustainable rates. It becomes ever more difficult to envisage the bootstrapping act by which European political elites might escape from this vicious circle'.

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Chapter 14

On the parliamentary control of a reformed monetary union?

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Introduction

In his famous critique of the limits of reason in politics, Michael Oakeshott eloquently argued that it is in the nature of the human condition that we 'sail on a boundless and bottomless sea; there is neither harbour nor shelter nor floor for anchorage, neither starting place nor appointed destination. The enterprise is to keep afloat on an even keel' (1962: 133). This image may have been suggested to Oakeshott by the philosopher Charles Sanders Peirce who likewise argued 'we must rebuild our ship on an open sea, never able to dismantle it in dry dock and to reconstruct it out of the best materials' (See Scheffler 1974: 57).

For certain, much of the recent rebuilding of monetary union has had to be done at sea, without the safety of a dry dock or of a firm anchorage. Whether the best materials are being used in the retrofit is more open to debate. This chapter aims to contribute to that debate by discussing one particular institutional 'material', namely, arrangements for the parliamentary control of a redesigned monetary union. I argue that some form of multi-level parliamentary process should be included in the retrofit. A redesigned monetary union should not, in other words, be controlled either by the European Parliament (EP) alone or by individual national parliaments. Rather, parliamentary powers should be distributed between the levels, which should, in turn, operate co-operatively for some purposes, and individually, for others.

I develop the argument in the following stages. The first section identifies a role for parliamentary scrutiny in reconciling the independence of the European Central Bank (ECB) with standards of democratic control and uses it to argue that the ECB has duties of justification to both the European and national parliaments. Secondly, I discuss the advantages of giving both national parliaments and the European Parliament some control over new powers that are being conferred on the European Council, Council of Ministers and Commission as part of a re-designed monetary union. The third section argues that the case for a multi-level form of parliamentary control is further reinforced by the probability that the performance of a reformed monetary union will not just depend on single institutions but on the 'policy mix' implied by their several actions. Finally, the last section draws overall lessons for both the distribution and co-ordination of powers of parliamentary control between the European and national levels.

Democratic legitimacy and the European Central Bank

Many believe that independent central banking and parliamentary politics are incompatible, and should be kept as far apart as possible. As it happens, this is not the position that the EU has taken in the design of its monetary union, and for very good reasons, or so I will argue here. In particular, I will argue that it is possible to achieve important elements of parliamentary control without undermining the arguments for independent central banking. However, it is easier to reconcile these two requirements with some forms of parliamentary control than others. Clarifying why this is so, will help me make my overall argument that monetary union calls for a distributive form of parliamentary control with contributions from both national parliaments and the European Parliament. First, though, it is important to say something about the form of independent central banking that the European Union (EU) has adopted, and about the ECB's place in the EU's political system. For, the difficulties and options of reconciling independent central banking with parliamentary control are, to some degree, specific to political systems. Here the

EU presents some unusual difficulties, as well as some unusual possibilities too.

The powers of the ECB are extraordinary in at least two ways. On the one hand, the ECB is unusually powerful and independent in comparison with other European Union institutions. As Kenneth Dyson has remarked: 'What is novel and distinctive about the European Central Bank is that it has the potential to play an active role as a supranational "executive" body that exceeds the autonomy of action available to the European Commission' (2000: 11). Indeed, most Union institutions are usually constrained several times over. First, powers over most decisions are usually distributed across several institutions. Most matters – and not just legislation – need to be more or less co-decided by several institutions under rules that require high levels of agreement within and across those institutions. Second, the Union, in any case, rarely enjoys its own exclusive competence in which it is free to decide what it wants without regard for what national and sub-national authorities are attempting to do in the same policy field. Sure the Union claims that its laws take priority over any national measures that conflict with them. But that only leads on to the third constraint. The Union may claim primacy for is laws, but its decisions have to be implemented by national or sub-national authorities, over which the Union only has limited coercive resources.

In contrast, these constraints are weak, or even non-existent, in the case of the ECB. It acts in one of the few areas where the Union does have exclusive competence. Within the eurozone it has monopoly control over monetary policy. Moreover, it decides monetary policy on its own initiative and without having to concern itself with any other veto holders amongst the other Union institutions. Finally, the ECB's implementing agents are not national governments, but national central banks, themselves part of the tribe; or, to put the point both more technically, and more politely, the epistemic community of independent central banking. Indeed, national central bankers are themselves the dominant part of the ECB's governing Council.

Yet, there is a further way in which the ECB powers are exceptional. It does not just enjoy exceptional independence in comparison to other Union institutions. It also enjoys remarkable independence in comparison with other central banks. In setting out how it intended to exercise its own Treaty rights to discuss monetary policy with the

ECB, the European Parliament remarked that the ECB was probably the 'most Independent Central Bank in the World' (European Parliament 1998). Indeed, it is arguable that the ECB is even more independent than it needs to be. Economists distinguish between the independence with which central banks can define their own goals (goal independence) and the independence with which they can decide how to achieve those goals (operational independence) (Rogoff 1985). It is arguable that it is both desirable and possible to achieve the goals of independent central banking without delegating full goal independence to central banks. Provided the operational independence of central banks is sufficient for a credible commitment to price stability, then there would seem to be little case for them having goal independence too. After all, specifying exactly what is meant by price stability and how it should relate to other goals involves decisions about social preferences – indeed, value preferences – that should ideally be defined within a political and democratic process. What, of course, can undermine this argument is that operational independence may be far from sufficient where democratic majorities are too free to manipulate definitions of price stability to their own advantage. Yet, even that difficulty can be solved from within the political process. It all depends on the nature of the political system, and the means available to it of constraining majorities, yet taking decisions that are acknowledged as democratic all the same.

Against this background, there are two legs to the argument that the ECB may be more independent than it needs to be. On the one hand, the Treaty leaves the ECB with near complete goal independence, and not just operational independence. It merely stipulates that the ECB shall achieve price stability. Otherwise it leaves all secondary questions in the definition of that goal – the level of inflation to be targeted, the question of whether over-shooting or under-shooting the target is to be treated as equally undesirable, the question of how quickly and painlessly the euro area should return to the target in the event of deviations from it – to the Bank itself, without any explicit requirement of any input from the political process. Yet, to repeat, each of these questions can only be answered by making assumptions about social preferences, which should, arguably, be the role of political representatives than of central bankers, provided the political system is of a kind that makes it possible for to define goals.

That brings us on to the second point. The EU's political system is in some ways well suited to giving a substantial role to political actors in defining goals of price stability, whilst leaving the ECB with a largely operational form of independence. Imagine a Treaty change that confirmed the present commitment to price stability, whilst allowing for the further specification of that goal by the ordinary legislative procedure, failing which the ECB would, continue, as present, to define it for itself. No one majority would be able to manipulate the goal to its advantage. Any departure from the *status quo* would require a proposal from the Commission, whose role it is to filter out narrowly partisan or manipulative options. Possible veto coalitions in the Council would almost certainly include combinations of governments with strong preferences for price stability. Any legislation that was blatantly incompatible with the Treaty commitment to price stability would be open to a challenge in the European Court of Justice. Yet, proposing such legislation, and reviewing it at regular intervals, would be an occasion for those who hold different preferences on how price stability should be specified to justify their views in relation to one another. Not only would governments be very likely to hold different preferences, but Members of the European Parliament would be able to table amendments representing a range of social preferences in the expectation that many of those preferences will then be considered and compared in committee, plenary and even 'inter-institutional dialogue' with the Commission and Council.

However in a sense my argument has already begun to move too quickly. Regardless of whether the ECB is more or less independent than is necessary, we have to answer the deeper question of whether the far reaching delegation of powers needed to achieve *any* form of central bank independence is justifiable in liberal democracies societies, where it is assumed that democracy is the only form of legitimacy available (Habermas 1996: 448)?

There is, of course, much discussion within democratic theory of conditions under which it might be justifiable to delegate powers away from the day-to-day control of electoral or parliamentary majorities. One classic justification is that such delegations may be needed to safeguard the democratic process itself. Another justification is that the 'majority' is not, in any case, equivalent to the 'people', who can sometimes better secure such values as impartiality by delegating responsibilities to bodies that operate independently from particular political majorities (Rosanvallon 2008: 10–21).

However, it is impossible to evaluate arguments for central bank independence without ‘triangulating’ economic theory and political philosophy. Economic arguments for independent central banking cannot be persuasive on their own unless they are also sufficient from a point of view of known standards for the legitimate delegation of powers to independent authorities. Philosophical evaluations cannot do justice to the arguments that economists make for independent central banking without understanding the exact basis on which those claims are made.

The core economic argument for independent central banking rests on the so-called ‘neutrality of money’. According to those who believe in the neutrality of money there is no enduring benefit to be had from manipulating the quantity of money. Over the medium term, output and employment will be much where they would have been in the absence of policy intervention. The only thing that will be different is that inflation will be higher (Lucas 1972). Whilst, however, the ‘neutrality of money hypothesis’ implies that short-term attempts to manipulate the supply of money to achieve outcomes other than price stability is a pure welfare loss to voters, it can allow elected politicians to create an illusion of improved output and employment at the time of their re-election. Worse, since it is known that elected politicians can behave in this way, even honest politicians will be unable to achieve the best possible trade-offs between employment and growth on the one hand and inflation on the other (Kydland and Prescott 1977). Financial markets will demand higher interest rates – and workers will demand higher wages – to cover the risk that politicians might create surprise inflation during the course of a loan or a wage contract.

If this argument is correct, the strongest democratic case for independent central banking might run as follows: transferring responsibility for monetary policy from elected politicians to an independent central bank would allow publics to achieve a combination of outcomes – lower inflation and higher growth and employment – that is both desirable from all points of view and unattainable through normal majoritarian politics. Such a delegation would also be a benefit to the democratic process itself, since it would remove an opportunity for governments to manipulate the terms of their own re-election by managing the economic cycle to coincide with the political cycle.

More things can be said in response to this argument than can be considered in the limited space available here. However, the most important point is this: if all public power must ultimately be democratically justifiable, some means have to be found of delegating central banking powers away from normal processes of democratic competition without delegating them away from *any* kind of public control that citizens can exercise as equals if independent central banking is to be justifiable. What are the possible ways of squaring this circle? The key requirement, it seems to me, is that any decision to give control of monetary politicians to central bankers, rather than elected politicians, should, as it were, be justifiable as the people's own act. However, there are several difficulties with this, each of which is magnified in the specific case of the EU.

First, it presupposes some agreement on who are the people, or, in other words, exactly who can get together to delegate powers to an independent central bank in a manner that is acknowledged as binding on all. In the case of the EU, the delegation probably has to be understood as a delegation from the people*s* of the European Union, though conceivably with the caveat that those peoples may understand themselves as having acquired some obligations to one another through their common membership of the Union. Whilst I cannot pursue this caveat here, it is nicely developed in the debate on *demoicracy* (Weiler 1997), as well as in the work of John Erik Fossum and Agustín Menéndez (2011) on constitutional synthesis. Either way a multi-state and multi-people delegation to a single central bank creates new challenges of continuing democratic control. Even a segmented understanding of who are the peoples of Europe raises the question of whether they can severally control a process they have mandated jointly. A more *demoicratic* understanding of the peoples of the European Union raises the converse question whether they might owe a bit more to one another than can be achieved by each making their own separate attempts to control delegations to Union institutions separately.

A second difficulty with the view that a central bank can receive all the legitimation that it needs from a delegation from the people is that, with the passage of time, the public that live under the decisions of any one bank may be very different from the public whose representatives authorised that independent central bank. Thus, in the case of most eurozone countries, authorisation of the ECB dates back to treaties ratified by publics and parliaments twenty years ago. If this is not a form of 'rule by ancestors' then the principles and practices of independent central banking either have to amount to a series of eternal truths that are universally agreed, or there have to be some means of reviewing and revisiting them. The former possibility can, of course, be ruled out. As already partially suggested, at least the following controversies have been stimulated by independent central banking and the ECB's own approach to it: is a short sharp monetary tightening preferable to a gentle but drawn-out response to unexpected inflation? Should inflation targets by symmetric, or, in other words, should the risk of inflation falling below its target be considered as undesirable as the risk of it exceeding its target? Should the central bank target asset prices such as house prices and share prices, given that 'bubbles' in these prices can endanger whole financial systems? In sum, independent central banking involves 'real-time' and 'value-specific' controversies, not eternal truths.

This leads straight into the third difficulty. The idea that an independent central bank can be democratically authorised by a delegation from the people plainly works best where most of the decisions can be traced to the initial act of delegation. Yet, the crisis has revealed precisely how difficult it is for a central bank to restrict its decisions to what has been explicitly authorised in its mandate and to avoid more discretionary choices. Indeed, the crisis, arguably, only become a crisis because the ECB has had to wrestle with the difficulties of becoming a discretionary decision-maker for which it has neither mandate nor inclination. If a central bank can only guarantee a currency against self-fulfilling market panics where it is known to have unlimited ability to print money and buy key financial assets such as government bonds, then it will unavoidably have to make discretionary decisions. If it is to act as a firefighter, it will need to have the discretion to direct its resources where the fire directs, and not where its mandate directs. Worse, back-stopping a financial system by buying public debt does not just require Central banks to make discretionary judgements. It also requires them to behave as political actors. Central banks need to be able to indicate to governments on what terms they are prepared to buy and hold government debt in so far as they also have a duty to publics to avoid losses. As Agustín Menéndez has put it, all this

> makes the ECB a political actor, as proven by the famous letter sent by Trichet and Draghi to Zapatero and Monti, rendering explicit the kind of reforms the ECB regarded as necessary to see implemented in Spain and Italy, days within the ECB expanding its securities market programme to Spanish and Italian debt.
>
> (Menéndez 2012: 59)

Surely, these various limitations to the notion that an independent central bank can be adequately authorised by a single delegation from the people surely imply the need for some continuing form of public control? But is it really possible to subject an independent central bank to public control without compromising the very justifications for independent central banking in the first place? It seems to me there are two ways forward, which I can only present here as possibilities that deserve further reflection, not as options that any one has yet really thought through. If, however, they do have any merit, they have important implications for what forms of parliamentary control maybe best for the ECB.

Terry Moe once observed that it is possible to delegate powers to a public body and then spread out surveillance of that body between several other institutions and actors in such a way that 'no one controls the agency and yet the agency is controlled' (1990: 143). Moreover, dispersing controlling powers between multiple bodies each of which represents different majorities in different ways has many attractions in systems where any one majority only has a flimsy basis for representing the whole. As Pierre Rosanvallon puts it, a majority may only be a chance agglomeration of minorities rather than a 'general will': a majority at one particular moment, at one level of aggregation, and according to just one method of counting votes (2008). In the case of the ECB multiple practical dependencies and reporting obligations could conceivably require it to justify itself and maintain the active co-operation of individual governments, the Commission, the Council of Ministers, the European Parliament and national parliaments, and even the Court, without any one of those bodies being in a position to compromise the independence of the bank.

My second thought is that independent central banks should, as it were, be exempted from democratic politics as a form of political competition, but not from democracy as a structure of justification. Arguments for independent central banking – such as the time inconsistency – only argue for freeing monetary policy from dependence on electoral cycles. They do not provide any justification for freeing independent central banks from normal obligations in a democracy to justify decisions to individual citizens on whose behalf collective decisions are made. Now, in using the rather odd phrase 'democracy as a structure of justification' (Forst 2007), I really do want to suggest that there are structural characteristics of democracy that structure the kind of justifications that any public body needs to provide. Each individual – and each point of view – must presumably have an equal right to a justification, given that democracy is a relationship of political equality. Justifications must presumably take the form of 'public reason' (Rawls 1993: 212–254). They must in, other words, be interpretations of the needs and values of citizens. They cannot, as Philip Pettit puts it, be solely based on, the '*arbitrarium* (the pleasure or whim) of decision-makers' (Pettit 1997: 55). If publics or their representatives are to be the judges of the quality of justification they must presumably be free to weigh justifications in a free and open public debate that puts no restrictions on arguments beyond what the public itself takes to be standards of good argument (Habermas 2003: 107).

Yet justification also needs a site. Although it is essential that much public debate is open, spontaneous, and even, as Habermas puts it, 'wild' and 'anarchic' (1996: 307), it is no less important that some of it should be formally structured. Thus however many other audiences public bodies address, it would seem important that they should also justify themselves to parliaments. Unlike other bodies, parliaments are formally elected on a basis of universal and equal suffrage. They can also link justification to legislation. Their judgements on how well public bodies justify themselves can affect their attitudes to future legislation on those bodies.

As an aside, the ECB is open to one large criticism for how well it justifies its decisions, since its minutes are not published for 16 years (Blinder *et al.* 2001). Yet, some interesting possibilities are suggested by the ECB's relationship to the European Parliament. In deciding how it was going to operationalise its powers under the Treaty on

European Union (TEU), the EP followed its normal habit of putting a maximal interpretation on its treaty rights and of linking them together to increase their cumulative impact. It billed its right to be consulted on the appointment of the executive board of the ECB as full 'confirmation proceedings'. Each nominee was required to fill in a written questionnaire and appear in person before the Economic and Monetary Affairs Committee of the Parliament (EMAC). A mechanism for requesting the withdrawal of nominees was also written into the EP's own rules of procedure. During the 'confirmation hearings'. To allow for more 'trial by public debate' (Manin 1995) the EP reached a further agreement with the incoming President, Wim Duisenberg, that regular hearings with EMAC would be held every three months on top of the annual hearing stipulated in the Treaty.

Beginning with the 'confirmation proceedings' the aim was to press the ECB into ever close specification of its targets, forecasts and policy rules, and for members of the European Parliament (MEPs) then to use those statements as criteria to judge the ECB in each subsequent hearing. It was thus hoped that the ECB's relationship with the EP could be turned into a form of self-appraisal on the part of the Bank, made all the more devastating by the impossibility of dismissing it as a political interference, whose assumptions derived from anywhere else than the independents central bankers themselves. It was finally made clear that grave or persistent failure to live up to the standards that the ECB had set itself would be grounds for the EP to use its treaty rights to request an unscheduled meeting with the EP. Such a move, the EP believed, would be publicly perceived as a 'summons' (For all this see European Parliament 1998 and Lord 2003).

More recently, ECB Presidents have also appeared before committees of national parliaments. Assuming duties of public justification to both the European and national parliaments corresponds to different forms of public interest in the ECB's decisions. On the one hand it has an obligation set out in its own mandate to make policy judgements that aimed delivering price stability for the eurozone as a whole. Thus it needs to justify itself to a representative body that is most likely and able to judge it on whole. On the other hand, no holistic understanding of monetary union can remove the fact that one-size-fits-all monetary policies will have very different impacts on individual member states. Indeed, that is, arguably, the core structural problem of any monetary union. National parliaments thus surely have every right to represent their views on what the policies of the ECB have for them and to receive justifications for how far their own circumstances have been weighed in overall policy judgements.

Of course, much of what I have said is open to the objection that, in making so much of the procedures that would encourage and require the ECB to justify its decisions to representative bodies at the European and national levels, I have not really said anything serious about parliamentary control. However, it seems to me that the objection is mistaken. There is no reason why the need for a central bank to justify itself to representative bodies should not be considered an important ingredient of what we know central banks care about most, namely, their credibility.

The democratic legitimacy of Monetary Union beyond the Central Bank

Before the financial crisis it might have been reasonable to conclude a discussion of the parliamentary control of monetary union at the end of the previous section on the European Central Bank. In Kenneth Dyson's words the TEU agreed an 'ECB-centric' (2000) form of monetary union. Sure, other institutions acquired some responsibilities for the co-ordination of national fiscal policies. The TEU required the Commission and Council to establish broad economic policy guidelines (BEPG) for the Union as a whole. Member states also entered into a continuing agreement to keep their annual deficits to 3 per cent of national income and their total borrowing to 60 per cent. In 1997, they also agreed a Stability and Growth Pact (SGP) to enforce the limits on annual deficits. However, the BEPG were just guidelines, and, the SGP was effectively abandoned as soon as it threatened to constrain the national fiscal policies of the larger member states.

In contrast, changes wrought by the crisis have challenged the original model of monetary centralisation and fiscal decentralisation. In effect, the combined effect of the European Semester and Fiscal Compact is to transform the European Commission and the Council of Ministers into something of a common budgetary authority for the euro-area, albeit as part of a shuttle in which detailed proposals will move to and fro between the Community institutions and member states. How far this will intrude into, and constrain, the budgetary autonomy of national democracies will vary. Member states which are comfortably within the agreed fiscal rules will more or less be able to decide their taxation, borrowing and spending as they want. Once, however, there is any uncertainty as to how far a member state can sustain compliance with the fiscal rules, 'mutual surveillance' – by other member states, acting on the initiative of the Commission – is likely to have an ever more constraining effect on its economic policies, beginning with recommendations and warnings and culminating with fines. Indeed, during the crisis, member states in need of bailing-out have had to accept a kind of semi-guardianship in which large parts of their internal affairs are, for a period, co-decided between their own governments and a 'Troika' of the International Monetary Fund (IMF), the European Commission and the European Central Bank.

Note, though, that even where the European semester does little to constrain the substance of national budgetary authority, it will entail new procedural constraints. Agustín Menéndez has pointed out:

> the whole procedural structure of national budgetary process gets to be determined by supranational law. In particular there is a shift from the one-year budgetary process which has been a core of national democracy to five-year budgetary perspectives, which may be hard to reconcile with national electoral times, and may dilute national parliamentary control over governments.
>
> (Menéndez 2012: 57)

Moreover, new arrangements for fiscal co-ordination do not just extend the powers of Commission-Council tandem into new areas of fiscal co-ordination. They also change both the substance and procedures of the Community method. Recalling the distinction between policies aimed at regulation, redistribution and macro-economic stabilisation (Majone 1996), they certainly involve the Union in assuming new responsibilities for the latter. Decisions may also become more redistributive, explicitly so if the eurozone develops a 'fiscal capacity that is able to counter economic shocks with inter-state transfers, implicitly so if it continues to collectivise risk.

The procedural changes to the Community method are no less radical. The introduction of Reverse Majority Voting (RMV) means that some Commission proposals will be automatically adopted unless a majority – of 55 per cent of the member states representing

65 per cent of the Union's population – can be found *against* them. This will increase the Commission's agenda-setting powers and reduce the protection that any one member state can normally expect from majority decision-making. In effect, a norm that requires over-sized majorities for decisions binding on member states is to be replaced by a rule that will allow important Commission proposals on fiscal matters to be adopted by a minority of the Council. Moreover, this procedure will be used precisely where fiscal co-ordination will involve new forms of coercion. Fines on member states will be automatic unless reverse majorities can be found for forgiveness.

In addition to extending and changing the Community method, the crisis has also transformed the role of the European Council into a kind of emergency decision-maker. This may turn out to be more than a temporary change. Quite apart from any 'crisis tendencies' that may be inherent in any attempt to run a single currency, there are, as already seen, limits to how far the Treaties of a treaty-based union can offer guidance for what to do in a crisis. As the body that represents the authors of the Treaties the European Council would seem to be the body with most authority to make emergency decisions that go beyond the Treaty.

In sum, then, greater fiscal co-ordination and more emergency decision, means that there are new powers that need to be subject to parliamentary control. Now, I take it for granted that much of that control will need to be exercised by national parliaments. Given, that taxation, borrowing and spending will remain national competences, it is hard to see how the challenge could be anything other than one of reconciling greater fiscal co-ordination with control of budgets by national parliaments. Whilst, however, that is surely necessary, it is unlikely to be sufficient, for at least the following reasons:

Completeness. In his great work on Representative Government, John Stuart Mill remarked that parliamentary control can take many forms. However, whatever form it does take, the public's representatives should be able to exercise control in 'all its completeness' (1972 [1861]: 228). By this he meant that there should be no institution, agency or procedure that cannot ultimately be controlled by representative bodies. Yet control by national parliaments – acting individually – would leave two large gaps in the control of new arrangements for fiscal co-ordination. First, individual national parliaments can only control the behaviour of their own governments in the Council, and not the Council as a collective decision-making body. I will expand on this difficulty in the next point about *faits accomplis*. Second, national parliaments have minimal control over the Commission. Yet, as seen, the Commission will be an unusually powerful agenda setter under new procedures for fiscal co-ordination, and even the *de facto* decider where the Council cannot achieve a reverse majority against some of its proposals. In contrast to national parliaments, the EP can dismiss the Commission. Although it rarely even attempts to do this, the possibility of a censure is an important background factor in the relationship between the Commission and the EP (Lord 2004: 146). Nor to be forgotten is that new procedures for fiscal co-ordination have been established under co-decision. Legislative authority for changes to those procedures will require the Commission to return to the Parliament with new proposals.

Faits accomplis. One reason why it may be difficult for individual national parliaments to control the Council as a collective decision-making body through their relationship with their own governments is that even the powerful domestic institutions of powerful member states may sometimes feel constrained from re-opening decisions agreed at the European level (for a fascinating example from the case of defence co-operation see Wagner 2006). Factors that might deter individual parliaments from 'unilateral' opposition might plausibly include a) concern to maintain the overall credibility of co-operative frameworks, b) concern to maintain the reputation of their own country as a reliable negotiating partner, c) patterns of reciprocity and d) the bargaining costs of re-opening agreements which have been negotiated with difficulty.

Capabilities and incentives. There may be limits to how far decisions taken in the institutions of one political system (in this case decisions of the Commission and Council on fiscal co-ordination) can be politically controlled through the institutions of other political systems (in this case national parliaments). Research has shown that the power of representative bodies is overwhelmingly related to their capacity to overcome asymmetries of information that otherwise put them at a disadvantage to the very executive bodies they seek to control (Krehbiel 1991). National parliaments face the difficulty that in order to control decisions bargained in EU institutions they may sometimes have to acquire expertise specific to the Union's political system. That may, however, involve opportunity costs. Time and resources spent scrutinising EU matters are time and resources not spent scrutinising domestic matters.

Political Equality. National parliaments are unequal in their controlling powers on EU matters. A few, of course, have legal or political powers to mandate their governments. Others are more likely to be controlled by their own governments than *vice versa*.

Collective action problems. The whole point of fiscal co-ordination is to prevent a monetary union from turning into a nightmare of negative externalities, free riding and irresponsible risk taking. National parliaments will not however have obvious incentives to constrain these behaviours where it is their own member states that are likely to profit from them. Basing a redesigned monetary union on control by national parliaments would thus create a predicament. The problem cannot be fully elaborated here, but, in rough summary, it is as follows: a well-managed macro-economic framework – in which no one can impose negative externalities on any one else and everyone can enjoy the benefits of a stable currency that provides a reliable store of value – is a public good. If things work out well, they will work out well for everyone. No one will be excluded from the benefits of the framework.

However, public goods go under-provided where individual actors have incentives to free ride on the efforts of others to provide them. Sure, it is possible for powers over collective actions to remain decentralised in the hands of the very individual actors who are in a position to free-ride or impose negative externalities on others (Coase 1960). But only where those actors accept that the manner in which they exercise control has itself to be compatible with the overall provision of macro-economic stability as a public good. Given transaction costs, the individual actors are quite likely to conclude that the only way they can reliably do this is by delegating at least some powers to an independent arbiter and enforcer, which has the power to over-ride them in individual cases, even if it derives its general authority to do that from the very actors it disciplines and constrains.

Indeed the concept of a binding arbiter seems to me to offer the solution to what would be a complete and stable structure of parliamentary control for a system of fiscal co-ordination. National parliaments should control the authoring of rules of fiscal co-ordination. But they should do that as part of a shared process of deciding what are generally fair rules for dealing with negative externalities, avoiding moral hazard and providing macro-economic stability as a public goods. However, their control over the day-to-day administration of the rules cannot have the effect of 'putting the sharks back in charge of the swimming pool', or, in other words of re-introducing the very problem from which we started out, namely that national parliaments may themselves have interests in negative externalities, irresponsible risk taking and free-riding. Of course, the administration of shared rules cannot go uncontrolled by any democratic body. Thus it would make sense for national parliaments to delegate the task to a common parliament, whose composition is co-extensive with the whole area over which any public good of macro-economic stability is provided, without remainder for negative externalities (see esp. Collignon 2003).

Public Sphere. Following on directly from the previous point, it is, arguably, a 'constitutional defect' (Joerges 2006) of democratic states that their representative institutions only have incentives to consider the interests and views of those who vote for them, and not for all those who are affected by their actions (see also Grant and Keohane 2005). Given that members of a monetary union can impose costs and risks on one another, it may be difficult to hold the view that membership entails *no* responsibilities to other participating states and their citizens. For example, James Bohman has argued that closely interdependent societies should at the least form a trans-national public sphere of national public spheres. Those who can be adversely affected by others should be able to put their concerns on to their neighbours' political agendas and have them fairly considered on a basis of reciprocity (2007). Thus in a monetary union in which there are likely to be negative externalities it would be important that any scrutiny by national parliaments should include some sensitivity to debate in other member states.

And a problem of many hands?

So far I have discussed two important matters separately from one another: namely the parliamentary control of the ECB on the one hand and that of the new powers that the European Council, Council and Commission seem to be acquiring in a redesigned monetary union. But this leaves the problem of how to control outcomes that are not directly attributable to any one institution, but arise, instead, from interactions between them. Of course, this is an old problem. As Max Weber noted long ago, democratic control is always difficult where there are so many hands that it is hard to attribute responsibility.

The problem is, however, acute in the case of monetary union. The public has a strong interest in the 'policy mix' between monetary and fiscal policy (Enderlein 2006). Yet responsibility for the two kinds of policy is divided between the ECB and the member states. Wim Buiter explains the difficulty: 'Where communication, co-operation and co-ordination between the central bank' and budgetary authorities 'are seriously impaired, central bank independence can do more harm than good. The costs of non-co-operation are apt to be especially serious if the dominant macro-economic problem is unwanted deflation' (2006).

Maybe the problem of 'many hands' reinforces the observation in the previous section that it is important to aim at a complete structure of publicly control. Where outcomes are jointly determined by several institutions, large differences in how far those institutions are publicly controlled may obviously entail an element of 'power without responsibility'. Publics or their representatives will be put in the invidious position of heaping all the blame for things that go wrong on those institutions that are answerable or accepting that some failures may never be adequately sanctioned.

However, even where a complete structure of public control ensures there is no public agency that is not accountable to some representative body, there can still be difficulties in apportioning responsibility for outcomes that are jointly determined by different actors. Two ways of coping with this problem are worth mentioning.

One is to distinguish forms of accountability based on 'logics of appropriateness' from those based on 'logics of consequence'. As James March and Johan Olsen have argued, difficulties in assigning responsibility for outcomes do not preclude holding actors responsible for how far they follow norms that are designed precisely for cases where consequences are jointly determined and difficult to attribute to individual actors (1995).

Second, the problem of 'many hands' can even be turned to the advantage of public control. It might appear that it is best to delegate to just one body with clear and unambiguous responsibility. However, this is not necessarily so. As seen, publics and their representatives may face huge asymmetries of information in exercising public control. By delegating to just one agent they risk creating bodies that are in a position to dominate through a monopoly of expertise. By delegating to several agencies, they allow several bodies to develop expertise that they can then use to criticise one another. The secret may be to delegate to multiple bodies that have mixed interests in co-operating with one another to solve common problems whilst competing somewhat for the confidence of the principal: that are equally well informed members of a policy community, yet, if need be, mutually suspicions of the claims of others to represent the professional beliefs of that community (Strøm: 2003). Representative bodies can thus benefit from complex structures of delegation. Indeed, the same holds for publics themselves in determining delegations to representative bodies. They too may be better off delegating to more than one representative body that can evaluate and criticise one another's arguments: that can compete as well as co-operate. Once again, this seems to point to a distributed solution in which both national parliaments and the European parliament have powers over new forms of fiscal co-ordination in monetary union.

Conclusion

I have argued that the parliamentary control of monetary union should be distributed between the European Parliament and national parliaments. However, I have not really dealt with the question of how far parliamentary control should be co-ordinated between the levels. That is a question for a further paper. However, for the moment it is worth labouring the point that the distribution and co-ordination of parliamentary powers in a multi-level political order are two distinct questions. It is possible to believe that powers should, indeed, be distributed between the levels, but *not* co-ordinated. Anticipating what might be a justifiable balance, it seems to me that there are two strong arguments for co-ordination and one against it.

First, the national parliaments of a shared undertaking such as monetary union might plausibly come to understand themselves as having some duties to one another that imply some measure of co-ordination. Recall, for example, Bohman's argument that democracies that want to remain as self-governing as possible, even where they are in a position to impose negative externalities on one another and in need of one another to provide public goods, might plausibly be understood as at least having a responsibility for allowing other democracies to put their views about the external effects of actions on to one another's political agenda and to receive justified responses. If that is a general obligation that follows from interdependence between democracies, it surely applies even more strongly where the democracies in question have deliberately institutionalised a common undertaking, such as monetary union, from which there are neither easy exit options nor ways of avoiding choices that are likely to have profound effects on the life chances of individuals, as well as the allocation of values, in different member states. To the extent that the right to put views on the political agendas of other member states is best done through the formal political agenda of parliamentary debate, that right might imply some obligation on national parliaments to co-ordinate their procedures accordingly.

Second, parliamentary control at the European and national levels may itself have 'public goods characteristics'. It may, in other words, be difficult to exclude other parliaments from the benefits of at least some scrutiny undertaken by any one parliament. Given inequalities between the powers of parliaments, there may even be scope for an element of surrogate representation (Mansbridge 2003) in which stronger parliaments can get answers to problems that are also of concern to weaker parliaments. Indeed, parliaments should co-operate to produce one particular kind of good: namely, network goods which are 'complementary in consumption'. In other words their consumption does not diminish what is available to others. It 'adds to the benefit others can draw from the good' (Köllicker 2001: 131). Where, for example, single parliaments use information in their scrutiny whilst also pooling it in an information network available to others, they do not diminish the information available to others. They add to it.

In contrast, parliaments at the European and national levels should not co-ordinate in ways that reduce the plurality of voices or of parliamentary checks on monetary union. The aim of co-ordination should not, in other words, be to create agreement on monetary union at the expense of reasonable and justified disagreement. Recall Moe's argument that one way to reconcile public control with a need to delegate some decisions to independent agencies is to parcel out control to several controlling bodies such that no one of those bodies controls the agency and yet the agency is controlled. Such an arrangement would hardly be compatible with the controlling bodies colluding too closely with one another. Recall too arguments that the structure of public justification needs to be open and critical, and that there are important structural reasons why the European and national parliaments should see themselves as having distinct roles, the one in debating how far a policy mix is justified for the Union as a whole, the other in debating how justified it is in giving different weights to the often conflicting interests of particular member states in a one-size-fits-all policy. National parliaments neither should – nor are likely – to develop a *pensée unique* on monetary union at the expense of the need to demand these two quite different forms of justification.

Much of this is anticipated in the idea of a parliamentary field developed by Ben Crum and John Erik Fossum. In other words parliaments have a certain isomorphism in their normative and functional roles (2009) and they should co-ordinate where that helps them deliver those roles and refrain co-ordination where it does not. What is for certain is that debate on how the parliamentary control should be distributed and co-ordinated is central to whether the 'rebuilding of monetary union at sea' ends up by widening or narrowing the democratic deficit. Without adequate parliamentary control the reform of monetary union could massively aggravate what is in many ways the classic definition of the democratic deficit: namely, a tendency towards a form of executive federalism in which executive power is increased at both levels (national governments, the Commission and the ECB) at the expense of the controlling powers of representative bodies at both levels (national parliaments and the European Parliament) (Habermas 2012; Weiler *et al.* 1995).

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Part IV

Political science matters

Chapter 15

The crisis
A challenge to representative democracy in the European Union?

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Introduction

This chapter focuses on how the crisis affects representative democracy in the European Union. The first purpose is to shed light on the nature of the structure of representation that has emerged in the EU. EU democratisation has occurred along two dimensions: a vertical dimension pertaining to the effort to establish representative arrangements at the EU-level, most closely associated with the development of the European Parliament; and a more horizontal dimension relating to the effort to stabilise democracy across Europe (including through a system of democratic entrance requirements).[1] The point of departure is that this two-dimensional effort to establish and/or reinforce representative democracy unfolds in a distinctive manner and unleashes a process of reconfiguring national representative structures, in order to take the new EU-level constituency properly into account. The upshot is that this structure has taken on a

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[1] Cf. article 49 of the Treaty of European Union.

distinct and unprecedented form in the EU. The first purpose of the chapter, then, is to provide an overview of the nature of this structure as it emerged in the period prior to the crisis.

The second purpose is to provide an assessment of how the present EU (not only financial but also institutional and constitutional) crisis has affected this representative structure. The crisis appears to have greatly weakened parliaments in relation to executives; at the same time the crisis response (consider in particular the European Semester of budget coordination) also appears to make inter-parliamentary coordination more relevant and necessary.

The third and final purpose of the chapter is to assess the democratic implications of these developments. That assessment must run through the entire analysis because the democratic quality of the structure of EU representation pre-crisis is not only a matter of contention, but also quite a challenge because of its complexity and unprecedented nature. Paying attention to the status pre-crisis helps to render more explicit how significant the democratic implications of the crisis are.

In the following pages, I first establish what is meant by democracy and discern a set of criteria that inform the democratic assessment. Thereafter I provide a brief overview of the distinctive features of the structure of EU representation as it appeared in the period prior to the crisis. As we will see this system has emerged in a highly dynamic manner, and without a clearly delineated template or familiar *leitmotif*. Even if bits and pieces of member state representative arrangements have been copied onto or emulated at the EU-level the overarching structure has no precedents, because it has emerged in a situation where there has been a constant tension and struggle between two distinctly different conceptions of organising Europe: through supranational integration on the one hand and through interstate coordination and cooperation on the other.[2] Both conceptions are baked into the present EU structure, which means that the structure of EU representation has been set up to serve both, and is affected by their uneasy interaction. Then I provide an overview of

[2] Lionel Jospin summed it up: 'Europe is an original political structure, a unique precipitate, an indissoluble mixture of two different elements: the federalist idea and the reality of European Nation States' (2001: 6).

the crisis, what type of crisis it is, and what it has done to the integration process. As part of both assessments, attention is paid to the democratic implications that we can discern from these developments.

Democracy conceptualised

Democracy must be understood foremost as a higher-order legitimation principle (Eriksen and Fossum 2000). As such, it is a principle that spells out the requisite conditions for justification. Laws must be justified to those affected by them. In that sense democracy serves as a critical standard, which in turn also places deliberation at the centre of democracy; deliberation is necessary to get political results right. This reading of democracy does not exclude the use of voting; it underlines that the relevance of such decision-making procedures must be explained and justified.

The two core criteria of democracy can be said to be *autonomy* and *accountability* (Eriksen and Fossum 2000, 2012a, 2012b). Autonomy refers to the notion that those who are affected by laws should be authorised to make them. Accountability is both about making an account and holding to account. It is about 'a justificatory process that rests on a reason-giving practice, wherein the decision-makers can be held responsible to the citizenry, and where, in the last resort, it is possible, to *dismiss*, incompetent rulers' (Eriksen and Fossum 2012a: 20). These principles require representative democratic arrangements and explicit sanctioning mechanisms. The link to representation becomes clearer once we recognise that 'the opposite of representation is not participation. The opposite of representation is exclusion. And the opposite of participation is abstention' (Plotke 1997: 19). That on the one hand means that we cannot pin autonomy on a notion of direct participation because no modern political system can deliver the requisite level of direct participation. On the other hand it means that representation is not inimical to autonomy; when appropriately devised systems of representation can serve autonomy. In modern democracy representation is deliberatively encoded and is fashioned in such a manner as to be in line with the basic principles and values in the democratic constitutional state (freedom, basic rights, rule of law, and democracy). In actual fact, it should be added that democratic representation is what is generally understood as that form of democracy and that form of institutional arrangement that best ensures democracy in a modern context. With David Plotke we could say that '[r]epresentation is crucial in constituting democratic practices' (Plotke 1997: 19).

The two core criteria of democracy require institutions and procedures, which must ensure that citizens will be able to affect law-making processes and must provide citizens with opportunities for evaluating whether they find the justifications behind the laws and the decisions to be acceptable. In that sense democracy in the deliberative trapping that I espouse here presupposes a set of arrangements that include: (a) a constitution with a set of inalienable rights; (b) forums for public debate; and (c) institutional mechanisms that are capable of transforming political initiatives into collective commitments in a representative manner.[3]

It follows from the above that whereas democracy is fundamentally a justification principle, in the modern state context it has developed into an institutionalised arrangement with explicit presuppositions for how human beings should relate to each other, and how they should address problems and issues that concern them all, individually and collectively. Democracy is associated with a conception of the relevant community, or *demos*; there are therefore also associated presuppositions of membership (and citizenship); that is, of who are part of the community and of how and in what sense they are part; of identity (people need to identify with the community for this to make up a community in the first place); and of legitimacy, as people must believe that the community's basic norms are just and valid for this to make up a democracy. Such additional presuppositions are necessary, for at the core of democracy there is a fundamental ambiguity: democracy cannot itself determine the *demos*; that is, spell out precisely who the people shall be. Thus, whereas democracy requires other additional arrangements to establish the specific popular make-up, it not only depends on but also places particular – democratic – requirements on membership (citizenship), identity, and legitimacy.

At the same time, precisely because democracy is essentially a justification principle, all the criteria for establishing the demos have

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[3] For more details on this institutional version of deliberative democracy, see Eriksen and Fossum (2012b).

to be open to constant contestation. That means that a central precondition for a democratic order is a viable public sphere. With that is meant a communicative space (or spaces) in which relatively unconstrained debate, analysis and criticism of the political order can take place (Habermas 1989).[4]

This conception of democracy also entails that democracy should not be seen as strictly tied to the state form. There is a strong historical argument for such a link but it is contingent. The state form has no doubt been able to deliver arrangements that can sustain democracy within a given territory. But there is no need to confine democracy to this particular institutional form or historical configuration. In this connection it should be added that the state plays a central role in sustaining a profound paradox in today's world, namely that the successful entrenchment of democracy in the internal affairs of states is coupled with 'a lust for power [that] marks the relations among countries in which the stronger dominate the weaker' (Archibugi 2008: xiii). One distinctive trait of the EU experience is precisely the attempt to surpass this situation, with the main instrument being a complex tapestry of representative democratic structures.

EU democratisation pre-crisis – a brief overview

In order to understand the nature and impact of the structure of democratic representation that has emerged in the complex multilevel EU configuration, the normal point of departure would be the familiar assumption that EU-level democracy is being embedded in two distinct channels of representation that address citizens in their capacity as individual members of a European constituency (embodied in the EP), and in their capacity as members through holding citizenship in a member state (with national constituencies represented in the Council structure). At first glance the relevant image would be that of a rather conventional two-channelled structure of representation – similar to the kind of structure we find in such federal states as Germany. From this we might surmise that EU democratization would be mainly a matter of 'uplifting' national democracy to the EU-level.

[4] For assessments of the EU's public sphere, see for instance the various contributions in Fossum and Schlesinger 2007.

This image is however somewhat misleading. Although we see two broad institutional patterns in the EU, they take on a distinct shape. One channel connects the EU directly to the citizens through the EP, and is a vertical process of EP parliamentarisation.[5] This process is far from complete and has its own distinctive features. The structure in place at the EU-level falls well short of parliamentarianism, in the sense that the European Parliament election procedure offers no clear safeguard for European citizens' voting preferences through parliamentary elections to carry direct implications for the composition of European government and the Commission as a non-elected body is endowed with a formal monopoly of proposing legislative acts. It is obvious that insofar as we can talk of a European constituency, the structure in place is imbued with serious autonomy defects: European citizens cannot understand themselves as self-legislating persons under this structure.

The other collective channel actually connects citizens to the EU through two sets of collectives: the main one through the many council formations, and another through national parliamentary involvement (and interparliamentary interaction).

Council Formations: Chameleons or shape-shifters?

With regard to the Council, it has legislative functions, but deviates in certain respects from a second legislature or upper chamber. Joseph Weiler has noted that:

> Community and Union governance perverts the balance between the executive and legislative organs of the state. The executive branch, government ministers, are reconstituted in the Community as the principal legislative organ with […] an ever widening jurisdiction over increasing areas of public policy.
>
> (Weiler 1997: 274)

[5] For a comprehensive account of the development of the EP, see Rittberger (2005). See also Hix *et al.* (2007); Smith (1999).

It is questionable whether more transparency has done much to alter this (see Naurin, 2014). In this connection it should also be added that the Council has explicit executive functions.[6]

Part of the reason for the distinctness of the Council structure is that it has roots in or is at least still endowed with significant vestiges of such institutional arrangements and procedures that we associate with international diplomacy rather than domestic representative democracy. That in turn has rendered it particularly germane to distinctive representative roles, such as for instance the notion of 'shape-shifting representation'. With shape-shifting is meant that representatives adopt distinct representative roles that they strategically adjust to the particular settings they are addressing or relating to (cf. Saward 2012). I propose here to extend the notion from the level of representative to the level of body, in order to claim that certain bodies are almost shape-shifting by nature. The European Council and the Council configurations receive and mediate between two sets of institutional inputs, one from the European level and the other from the member state level (individual member states and the collective of member states). Naurin (2014) citing Wallace (2002: 342) labels the Council a 'complex and chameleon-like beast' and notes:

> It is both-and, and depending-on: Both executive and legislative in its functions, both national and European in its interests and incentives, both intergovernmental and supranational in its procedures, much depending on the policy area and the policy agenda of the day.
>
> Naurin (2014)

A similar argument applies to the European Council, which lacks the legislative role but still occupies a range of different roles directed to different constituencies: as a strategic driver of the integration process and directed to the European constituency; as a national champion because each head of government is elected by and responsible to its respective national constituency; and as a second-order constitutional agent because it is the key body in charge of constitution-making and at the same time the aggregate of national constitutional agents each of which has a veto over constitutional

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[6] See for instance Curtin (2009); Curtin and Egeberg (2008).

change proposals. The many roles that the Council and the European Council are supposed to fulfil in relation to their various contexts leave considerable scope for representatives for shape-shifting – how much scope depends on the specific elements of the representative relationship, such as whether they are instructed to act as delegates or are more free, to act as trustees. The Danish representatives face the strongest national constraints (with clear instructions from the national parliament) and are considered delegates. Other representatives with weaker national constraints can more easily play the role of trustee and adapt that role strategically to the several contexts they relate to. It is obvious that such bodies are notoriously difficult for citizens to programme and to hold to account: given that they serve several constituencies. To whom should they (and do they) give accounts, and what should (and do) these accounts contain?

Inter-parliamentary coordination

The other form of collective representation pertains to a growing web of arrangements that increasingly tie national parliaments to the decision-making processes at the EU-level. In today's EU national parliaments are increasingly tied together with the institutions at the EU-level (notably the Commission and the EP) through formal arrangements such as the provisions in the Lisbon Treaty on national parliaments and subsidiarity, and the so-called Early Warning Mechanism.[7] There are specific arrangements for collecting and publishing information, such as the Inter-Parliamentary EU information eXchange (IPEX) and the European Centre for Parliamentary Research and Documentation (ECPRD). There are specific arrangements that secure on-going parliamentary interaction, such as the Conference of Parliamentary Committees for Union Affairs of Parliaments in the European Union (Conférence des Organes Spécialisés dans les Affaires Communautaires, COSAC). We also find a range of informal arrangements where parliamentarians meet, interact and exchange information and knowledge. There is, not the least, considerable interaction among parties at different levels.

[7] For overviews of these, consult for instance Neunreither 1994; Crum and Fossum 2009; and various contributions in Crum and Fossum (2013). Ian Cooper (2012) argues that the Early Warning Mechanism can be understood as a kind of 'virtual third chamber' for the EU.

This structure contributes on the one hand to bringing national parliaments closer into contact with what is taking place at the EU-level. The structure makes it possible to express national concerns through parliaments at the EU-level and not only through the executives that occupy the Council structure. In that sense the structure leaves more space for representing a multitude of national positions at the EU-level.

The best manner of conceptualising this system is not to think of it as an added – third – channel but rather through the notion of multilevel parliamentary field that encompasses the EP and the national parliaments (MLPF) (Crum and Fossum 2009: 2013). This notion implies that parliamentary systems share certain structural similarities and are connected across states and levels of governance. They have the same overarching function, namely to represent their citizens. What marks this field is that it unites horizontal and vertical processes. The notion of field helps us to understand how they work together, or at least relate to each other.

What we see then is that since the Maastricht Treaty the process of democratising the EU has exhibited an ever greater set of horizontal features, in line with the development of a number of formal and informal arrangements for promoting stronger relations of cooperation, coordination and learning among national (and to a far more limited extent sub-national) parliaments. In this manner the EU system is in the process of establishing a structure that links citizens and the EU system, through direct representation in the EP as well as through two forms of collectives, the Council formations and national parliamentary involvement. These, especially the EP and the national parliaments, are becoming increasingly interwoven or imbricated. That in turn reflects how a distinctive feature of the integration process, namely what we may term the fusion of levels[8] has worked its way into the representative-democratic dimension: the process wherein representative bodies try to catch up with executives and integration is one that weaves representative bodies more closely together – both across levels and across states.

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[8] The theory of institutional fusion brings this out very clearly. See Wessels (1997); Wessels and Rometsch (1996).

Within this field structure, national parliaments become more readily activated in relation to what is taking place at the EU-level. That in turn might increase accountability. At the same time, this structure of representation also lends itself to *cooptation*. Since national parliaments are consulted by the Commission and directly involved in what goes on at the EU-level – they can prevent an issue from being dealt with at EU-level – national parliaments come to assume co-responsibility for those decisions that are made at EU-level. Even if an issue ends up being decided at the EU-level, national parliaments have been consulted, and can in that sense also be said to be co-responsible for EU decisions. That in turn complicates or dilutes the lines of accountability back to the citizens.

To sum up thus far, we see that whereas the EU system in the period pre-crisis was made gradually more subject to representative-democratic procedures; these were not programmed in a traditional parliamentary manner, or according to the key tenets of a division-of-powers system. It appears more reasonable to consider this a comprehensive system of consultation, interaction, and sounding out. As already noted, a distinctive feature of multilevel EU representation is that it increasingly involves national parliaments in EU-level decision-making.

When we look at the broader context, we see that the EU integration process was skewed in favour of executives and experts, as is generally the case with internationalization of politics. EU democratisation has always been a matter of catching up with that dynamic integration process.

Further, it is important to recall that the European integration process takes place in a setting of already existing states, and EU democratisation unfolds within this system of states. Democratisation accompanies polity formation; the two processes proceed in parallel (at least they have been doing so for a considerable period of time). It is *not* a matter of democratising an already established and existing system, but of establishing and democratising a supranational system at the same time. That supranational system is such configured as to remain solidly anchored in the member states, many of which prefer interstate interaction and cooperation over supranational integration. The strong member state presence in the institutions at the EU level also structure the integration process: it is a matter of fusing levels

(EU and member state) and sharing competencies more than singling out a distinct European level of government with exclusive competencies. States cede sovereignty not to a distant entity but to a common unit that they all participate directly in.

These observations go to show that it is difficult to offer a fast and ready assessment of how well this system delivered on the two criteria of autonomy and accountability pre-crisis because the EU failed to settle conclusively that it was a matter of supranational polity formation rather than a highly distinct version of international organisation. If we are to take this EU experiment seriously we cannot simply rely on domestically-derived conceptions of autonomy and accountability but must be willing to 'stretch' these notions. At the same time and in particular since the EU affects national systems so deeply we need to be clear on how EU developments affect nationally based democracy. In retrospect, it appears that it was quite commonplace to suspend final judgment on the quality of the system as long as there appeared to be a positive link between integration and democratisation and defects were being addressed.

The critical issue now is if the crisis undermines that assumption. If we can no longer assume a positive relationship between integration and democratisation, it is no longer possible to suspend judgment on the defects of the structure in place. It might even be that the crisis and how it has been handled has amplified these defects and brought in new problems.

The crisis and Europe's conundrum

The first thing to establish when considering the effects of the crisis is to clarify what kind of crisis it is. It is clearly not only a financial or even a public debt crisis; any designation of the crisis in economic terms would ignore the important political and institutional – even constitutional – dimensions of the crisis. The crisis is therefore far more and different from a mere response to an externally generated problem in the global financial markets; it reflects deeper structural faults built into the EU construct. It should be added that its handling has not only exposed, but also exacerbated, structural flaws in the EU (Scharpf 2010).[9]

The crisis has deleterious democratic effects. Some also argue that democratic failures are among the root causes of the crisis. Miguel Maduro has recently noted that 'the origins of the financial and economic crisis of the Euro system are state and market based democratic failures that the original regime of Euro governance did not adequately address' (Maduro 2012: 1). Two widely espoused accounts attribute much of the responsibility to national representative democracies. One of these accounts attributes failure to some states' inability to pursue responsible fiscal policies which in turn has generated negative externalities for other states. In other words, the representative systems in these countries have rewarded politicians that have pursued fiscally irresponsible policies. This account locates the democratic problems basically within debtor states and a lack of fiscal prudence.[10] The EU in turn has shown itself incapable of addressing these problems. The other account holds that the crisis is a combination of market forces and states' inability to control capital flows; the source of the problem stems mainly from financial markets and creditor states' supply of cheap capital. Both accounts underline member states' inadequate recognition of, as well as inability to handle, complex interdependence and integration. The obvious solution is to reform the system of EU governance to rectify these shortcomings.

There is a bit of truth to both accounts. With regard to the first some countries have pursued fiscally irresponsible policies, if we use the Maastricht convergence criteria and the Growth and Stability Pact as the benchmark, but then Germany and France also violated these (and precipitated their change). But it is hard to pin these problems to working representative systems without taking properly into account deeper structural failures, as appears to be the case with Greece, of

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[9] Many of the measures are set out in the intergovernmental Treaty on Stability, Coordination and Governance T/SCG/en 1 of 2 March 2012 and the so-called 'Six-Pack', a bundle of five regulations and one directive that cover fiscal surveillance and macroeconomic surveillance under the new Macroeconomic Imbalance Procedure.

[10] This account is at most a partial explanation and is not a very credible explanation of the crisis as such. For one there is no one-on-one relationship between fiscal prudence and severity of crisis. The central government of Spain is a case in point.

significant structural failures in the Greek state that exceed well beyond its representative system (and were known outside but not addressed), and biases and limitations in the EU, as well. The deeper question that is better addressed in the second account is whether democracy plays any causal role in the crisis, or is better thought of as the main casualty of the crisis.

Democracy appears foremost as a victim of the crisis; there is little credence in accounts that hold democracy as part of the cause. It is also important to note that the two accounts are inadequately attentive to the institutional context, and the distinct features of democracy in the multilevel constellation that makes up the EU, that I have highlighted in the above. Maduro's main democratic recommendation, namely to render the Commission more directly accountable to the EP through establishing closer links between the Commission's composition and the outcome of EP elections is intended to strengthen EU-level democracy and to leave more space for EU politics. But when considered in light of the structure of representation already in place in the EU it is also implicitly a recommendation to strengthen the multilevel parliamentary field and not only the EP, precisely because Maduro's recommendation is tailored to the present EU (no need for treaty changes). The following assessment of the democratic effects of the crisis seeks to pay attention to the complex and composite system of democratic representation that has already been instituted in the multilevel EU configuration.

There is no doubt that the crisis, and how it has been handled to date, has had negative effects on EU democracy and on democracy in the member states. The European Parliament has noted that 'the democratic credibility of European integration has suffered enormously from the manner in which the euro crisis has been dealt with to date […]'[11].

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[11] European Parliament (2011) Report on the European Semester for Economic Policy Coordination (2011/2071(INI)), 15 November 2011, retrieved from: <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//NONSGML+REPORT+A7-2011-0384+0+DOC+PDF+V0//EN> (last accessed 14 April 2014).

The first point of note is that the crisis has in many instances weakened the role and political influence of parliamentary assemblies, notably but far from exclusively, in the eurozone. Their ability to serve the interests of their citizens has clearly been weakened, as has their citizens' ability to hold those who are really responsible for the policies that afflict them also weakened. The pattern is however far from even across member states in the eurozone; it is clearly more so in debtor than in creditor countries. Several debtor countries have seen technocrats temporarily taking over governments. In Germany, a creditor country, the German Constitutional Court has bolstered the power of the Bundestag, even if the German Bundestag is also facing the short deadlines and market and executive 'imperatives' that emanate from the handling of a complex, multifaceted and highly dynamic crisis.

From a democratic perspective, what is also important to keep in mind is that some creditor state parliaments (notably Germany's) de facto determine many of the operating conditions of debtor state parliaments (notably Greece, Portugal, and Ireland) (Benz 2013). This expands some democratic constituencies' decision-making ability beyond their authorised bounds and procedures, whilst at the same time delimiting others', with potentially profound implications for citizens' ability to govern themselves across Europe. It is difficult to understand this as anything but dominance. It violates the democratic requirement of autonomy – that those that are affected by laws should be authorised to make them.

Other measures with negative bearings on citizens' autonomy can be seen in those instances where eurozone debtor countries' parliaments, especially those needing bail-outs, are subject to very stringent EU and troika (the European Commission, the European Central Bank (ECB), and the International Monetary Fund (IMF)) budgetary requirements, coupled with demands for deep budget cutbacks and deeply unpopular fiscal restraint measures. The economic philosophy underpinning much of the crisis management, coupled with the lopsided monetary union, generate policies with strong distributional effects (wage reductions, welfare and pension reductions). All member states are subject to strict budget requirements that constrain their parliaments' leverage, place strong constraints on budgetary policy, and subject them to sanctions in cases of non-compliance. This system is now coordinated at the EU-level under the so-called European Semester procedure. The EU and the eurozone coordinate their budgetary and economic policies *ex ante*, and based on this, specific policy recommendations are issued to each state. This has reduced the budgetary scope for national parliaments, which in turn constrains their citizens' autonomy. The EP's role in this system is quite marginal, which also delimits the autonomy of EU citizens. Given its limited role the EP will not be able to control these processes at the EU-level. Thus, for parliaments to re-assert themselves in such a structure, inter-parliamentary coordination appears necessary (and is also listed in Article 13 in the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union, TSCG).

Second, the onus on instituting constitutional spending brakes, if necessary at the national level (cf. Article 3.2 TSCG) is not only a major imposition, but raises questions of constitutional authority and legitimacy. What constitutional authority can the European Court of Justice (ECJ) claim to justify sanctions against member states that are in violation of the spending brakes? Without a properly democratically authorised constitution at the EU-level ECJ action would constitute a clear violation of citizens' autonomy, as spelled out in their respective member state constitutions.

Third, is that the crisis leads to a further strengthening of the role and salience of executives and experts at the behest of legislatures. As such, the crisis appears to reinforce certain built-in path dependencies in the EU structure, in particular in terms of executive prominence or even dominance.[12] The crisis also appears to reinforce greatly the role of technocracy, or government by experts, not only within the Union (through strengthening the ECB, the ECJ and the Council structure), but through the central role of such international bodies as the IMF (as part of the troika). The prominent role of technocrats in turn suggests that the crisis and its handling will, due to framing effects, be described and assessed as technical issues, with a strong onus on market imperatives and efficiency considerations. Such accounts tend to distort or conceal fundamental issues of political accountability. That in turn means that parliaments – if they are to bounce back and

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[12] Fossum and Laycock (2012); Habermas (2012: viii) discusses this latter aspect as a form of executive federalism.

operate as chaperons of citizens' autonomy and as enforcers of political accountability – must actively consider such framing effects and propound alternative crisis interpretations and ways of handling it. If not, their role will be further marginalised and their legitimacy in the eyes of increasingly disgruntled citizens will likely be further diminished.

Fourth, the crisis appears to be ushering in a general relative strengthening of the European Council. When coupled with a strong onus on handling the crisis through intergovernmental means (the so-called Merkel method[13]), including fashioning intergovernmental treaties (cf. Treaty on Stability, Coordination and Governance in the Economic and Monetary Union), and striking informal intergovernmental bargains through extensive summitry (including bilateral meetings between Germany and France),[14] the net effect is to weaken the integrity of the supranational Community system and the EP's ability to subject it to democratic requirements.

The more informal intergovernmental approach to crisis handling appears to weaken the supranational structure by making it more transgovernmentalised.[15] That would not only weaken the credibility and legitimacy of the supranational structure but also render it more readily accessible to and serving of certain core governments, to carry out their particular conceptions of how the crisis is to be dealt with. It clearly exposes the Commission, which is attributed with a very salient role, including in instituting sanctions (according to the undemocratic reverse quality majority voting system[16]) to such fissiparous pressures.

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[13] Spiegel International 18 November 2011, retrieved from: <http://www.spiegel.de/international/europe/phoenix-europe-how-the-eu-can-emerge-from-the-ashes-a-797626.html> (last accessed 7 April 2014).

[14] For an overview of types and frequency, see Dinan (2012).

[15] Transgovernmental 'connotes the greater intensity and denser structuring […] where EU member governments have been prepared cumulatively to commit themselves to rather extensive engagement and disciplines, but have judged the full EU institutional framework to be inappropriate or unacceptable, or not yet ripe for adoption' (Wallace 2005).

[16] European Commission (2012) 'Six-Pack? Two-Pack? Fiscal Compact? A Short Guide to the new EU Fiscal Governance', retrieved from: <http://ec.europa.eu/economy_finance/articles/governance/2012-03-14_six_pack_en.htm> (last accessed 7 April 2014).

The negative implications we can discern from this strengthening of the more intergovernmental portions of the EU do not only apply to the EP but also to national parliaments (NPs). When much of the crisis is handled through intergovernmental bargains – to deal with issues that are either outside of the treaties, or where the treaties are not considered helpful to fashion adequate responses and are therefore effectively violated – law's bite is reduced.

It might be added that this intergovernmental turn has in some instances been a matter of moving forward when certain member states (notably the UK) veto treaty changes. But it is also exposing a deeper structural problem,[17] namely the discrepancy between the problem structure and the decision-making structure. Simply put, the 18-member eurozone relies on the 28-member EU institutions to foster binding decisions. It raises the question of how, and in what respect, non-euro member states should participate in decisions pertaining to the euro, which clearly will affect them, but differently from the manner in which euro countries will be affected. One problem is how to sort out what are common concerns and what are concerns specifically pertaining to the eurozone. Another is that of representation: how to devise a democratic decision-making structure that can accommodate these different concerns? How to render such a structure accountable?

A fifth and readily apparent element is a great increase in citizens' distrust and rising opposition. As part of this we see a rise in extreme left and right-wing populism. Representative democracies may find themselves increasingly enmeshed in a highly toxic mixture of market-oriented technocracy and extreme populism.

Sixth, even before the crisis struck, the politics leading up to and the nature and status of the Lisbon Treaty have increased uncertainty and ambiguity as to the EU's constitutional nature and status (Fossum and Menéndez 2011). That has arguably made it easier for leaders to violate and/or sidestep legal provisions in their efforts to handle the crisis. That combined with the intergovernmental way of handling the crisis and the general trend towards

[17] José Manuel Durão Barroso, 'State of the Union 2012 Address', Speech/12/596 Plenary session of the European Parliament, Strasbourg, 12 September 2012.

transgovernmentalisation of the EU structure is altering the EU's constitutional construct.

Towards permanent differentiation?

A final observation is that the crisis appears to raise fundamental questions about the nature and direction of the European Union. This does not necessarily mean that the crisis has brought up these questions. It might equally well be that the main effect of the crisis is to expose and highlight features that have marked the EU well before the crisis but that have not been adequately recognised as problems before the crisis struck. One such is the differentiated nature of the EU. Whereas a core tenet in the *acquis communautaire* has been that the same policies should apply in the same way at the same time in all participating countries; differentiation is legion and takes many forms and shapes (Leuffen *et al.* 2012).[18] The most notable elements today are monetary union, where only 18 out of the EU's 28 member states are full members, and Schengen where only 22 out of the 28 are full members.[19] EU democratisation is thus not only legally encoded and takes place within a densely institutionalised system of interstate coordination and cooperation, this system is far from uniform.

This problem is, if anything, exacerbated by the crisis because it raises questions as to whether the EU is moving from a situation where differentiation is mainly a matter of different speeds,[20] based on the assumption that all states are integrating, but at different rates, to a situation where differentiation may instead be a matter of permanently different statuses. States, for various reasons, have obtained exemptions, but they are generally not thought of as *permanently* different roles. The crisis, however, compels us to think of an EU composed of states with different *statuses* within the

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[18] The authors depict differentiated integration through three sets of categories: level of centralisation; functional scope; and territorial extension.

[19] There is a provision for 'constructive abstention' under CFSP. There are provisions for reinforced co-operation in the Treaties. Lots of decisions are subject to derogations, and differential transition periods. Further, *non*-member states may also participate in Union policies. This applies to the EEA. It also applies to the Customs Union. Some states have special association agreements with the EU. Other states form part of the Neighbourhood policy. Others participate in the CFSP; and others in Schengen.

[20] For different versions of differentiated integration considered in terms of multiple speeds, see Piris (2011).

European order. In addition, we also see efforts at renegotiating relationships with the EU, as is notably the case with the UK. Thus, rather than further integration, we may see the rolling back of integration, or even dis-integration (including a still possible break-up of the eurozone). When efforts of reinforcing integration within the eurozone combine with efforts at renegotiation of membership status, we face a situation of simultaneous differentiated integration and differentiated disintegration. There is integration and there is rolling back, and both processes vary according to country or issue-area. There are many possible combinations of such processes. The following table provides an illustration of these different possible combinations.

Table 15.1 Different developmental trajectories for the EU

	Integration	Disintegration
Uniform	1	3
Differentiated	2	4

Cell 1 depicts the standard integrationist assumption. Cell 2 depicts a situation of differentiated integration. Cell 3 depicts a process of rolling back the EU, whether partially or completely, but across the EU and in the same manner across all issue-areas. Cell 4 depicts a situation of differentiated disintegration, meaning that some member states in some issue-areas disintegrate more than other ones.

Much of the EU debate has tended to focus on the dominant pattern as that of cell 1, but some have also discussed the scenarios in cells 2 and 3. Recent developments, in particular, compel us to pay more systematic attention to cell 4, and different possible cell combinations. The comments above on the effects of the crisis suggest the need to consider more carefully what happens when there is a combination of cells 2 and 4: differentiated integration combined with differentiated disintegration.

This combination in particular but also other ones raise thorny democratic challenges. How for instance to ensure autonomy and accountability in a situation where there is differentiated integration combined with differentiated disintegration, that is, when there is a combination of cells 2 and 4?

I have already suggested that the crisis forces us to rethink the core assumption that has animated research on the EU, namely that of a positive relationship between democratisation and integration. Which of the scenarios and combinations of scenarios that we can discern from the table will help to sustain that assumption and which ones will undercut it? Which scenarios are most likely to result from the crisis? What does appear clear is that a move in the direction of greater permanent differentiation – whether through a combination of cells 1 and 3 (through the singling out of a hard core and a periphery along all functional domains) or through various combinations of 2 and 4, differentiated integration and differentiated disintegration – raises fundamental questions pertaining to autonomy and accountability. Who authorises decisions in a system where voter control is differentiated according to territory and function? Who is to hold whom accountable for decisions within such a structure? These are fundamental questions for political and normative theory.

Conclusion

The above analysis has revealed that EU democratisation is a matter of establishing a system of representation at the EU-level; the process in turn redirects and reprograms national systems of representation. The process is distinct, given that it is both about establishing supranational representative democracy, and rendering interstate relations democratic, because the EU has a built-in tension between supranationalism and intergovernmentalism. Faced with such a configuration we cannot establish the EU's democratic quality simply by relying on standard ways of conceiving of autonomy and accountability, as these principles have been devised and applied for the domestic realms of political systems. The development of the EU's representative structure and its multilevel parliamentary field represents a dynamic process of constituency construction and reconstruction. The process opens up scope for manipulation, with representatives shifting blame to others, and it opens up space for co-optation. But it also opens up scope for parliaments to capitalise on their unique deliberative qualities, which may be enhanced through such systems of inter-parliamentary interaction.

These observations pertaining to putative democratic merits of the EU's multilevel representative structure, we have seen, are being challenged by the present crisis. At this stage it is clear that the crisis has seriously weakened and perhaps even undercut the process of

EU democratisation. As suggested above, a critical benchmark would be the assumption of a positive relationship between integration and democratisation. The key question is whether that has been undercut or whether it can still be rescued. We have seen that the crisis has weakened parliaments, enhanced the role of experts and executives, has reinforced transgovernmentalism at the behest of supra-nationalism, and raised the prospect of added complexity through greater differentiation.

These comments suggest that we need to pay more systematic attention to the democratic implications of increased differentiation. Can for instance the 18/28 tensions be reconciled in a democratic manner? These observations underline the need to subject to close ongoing scrutiny what the crisis does to the EU, not the least what it does to the complex representative configuration that is presently marking the EU.

With regard to how the EU system appears to be handling the crisis, there appears to be a penchant for greater multilevel parliamentary imbrication. Such a penchant must also be made subject to close critical scrutiny. What is clear is that such a configuration, were it even to become occupied with viable parliamentary systems at all relevant levels, will still raise serious questions pertaining to developing viable representative structures that are sufficiently attentive to the criteria of autonomy and accountability.

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