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EDITORIAL COMMENTS

Tinkering with Economic and Monetary Union

Believing that today's economic recovery is robust (evidenced by growth rates of 2% and unemployment rates at their lowest since 2008), and expecting political leadership in the aftermath of the French and German elections, the Commission issued a Roadmap indicating further steps to complete Economic and Monetary Union on 6 December 2017.[1] The impression given by this Roadmap is that every measure that was taken – in a great rush, and with significant political and legal contestation[2] – to address and contain the adverse effects of the sovereign debt crisis has been the right one, and that the next steps are self-evident. This is surprising, since economists are still puzzling about what to learn from the Eurozone crisis.[3] Nor is the package particularly radical: three of the five proposals are about institutional reconfiguration, and two aspire to wiser uses of the EU budget.

In these comments, we survey the Commission's Roadmap, and a reading key is offered to account for its unexciting nature: the attempt to tread delicately between two antagonistic visions of Economic and Monetary Union. On the one hand, there are those who consider that EMU can only become resilient through better discipline, retaining and strengthening the current systems for *ex ante* monitoring fiscal policies so as to eliminate the risk of further bailouts. Under this "regulatory" vision some might even consider that the European Stability Mechanism should inherit *ex ante* monitoring of States' fiscal policies from the EU institutions, as it might serve as an independent and robust agent to secure compliance with the stability and growth pact. Contrasting with this regulatory approach is a vision based on greater solidarity: asking for the EU as a whole to help fight the next crisis and not leaving matters in the hands of the ECB to do "whatever it takes" to save the euro. In this view, the EU should emerge with a fiscal policy to assist States

1. European Commission, Further Steps Toward Completing Europe's Economic and Monetary Union: A Roadmap, COM(2017)821 final.

2. Beukers, de Witte and Kilpatrick (Eds.) *Constitutional Change through Euro-Crisis Law* (Cambridge University Press, 2017).

3. Akerlof, Blanchard, Romer and Stiglitz (Eds.) *What Have We Learned ? Macroeconomic Policy after the Crisis* (MIT Press, 2014); Bohoslavsky and Raffer, *Sovereign Debt Crises: What Have We Learned?* (Cambridge University Press, 2017).

who suffer asymmetric shocks. Put simply, this is a tension between, respectively, a German and a French vision.[4] The institutional reforms are based largely on the former, the budget proposals largely on the latter.

Fiscal Compact Directive

It will be recalled that much legislative ink has been spilled to create the means to ensure that public finances are sound, involving monitoring, assessment and punishment of Member States. Not everyone is convinced that this has been worth it: "The 224-page Vade Mecum on implementing fiscal discipline in the EU is hopelessly complex, to such a degree that no finance minister, let alone parliamentarian, fully understands what his or her country must abide by."[5] Reasonable people might think a period of relative economic stability is an opportune time to reconsider the principles underpinning this rulebook, but the institutional proposal is merely to incorporate into EU Law those parts of the Treaty on Stability, Coordination and Governance (TSCG) that have not yet found their way there.[6] In particular, the proposal is to revise Article 3 (the so-called fiscal compact) and transform its obligations into a Directive.[7] Given that the provisions under this article have already been enacted into national laws,[8] what is the added value of the proposal other than giving the Czech Republic and Croatia the option to sign up to the fiscal compact?[9] Granted, the signatories to the TSCG had agreed to integrate the Treaty into Union Law by January 2018, but this is hardly a compelling case to avoid deeper reflections on how to optimize the governance of EMU.

In briefest outline, Article 3 TSCG establishes an obligation, to be made binding under national law, to ensure sound budgetary policies complementing obligations based on EU Law, and an automatic correction

4. Brunnermeier, James, Landau, *The Euro and the Battle of Ideas* (Princeton University Press, 2016) viewing the French and German positions as two ideal types.

5. Pisani-Ferry "The Lesser Evil for the Eurozone" Project Syndicate 27 March 2017, referring to European Commission, Vade Mecum on the Stability and Growth Pact, 2017 Edition (Institutional Paper 052, March 2017).

6. Ufficio Parlamentare del Bilancio, *The integration of the Fiscal Compact into EU law* (Flash No. 7, 4 Aug. 2017) for a helpful exposition.

7. Proposal for a Council Directive laying down provisions for strengthening fiscal responsibility and the medium-term budgetary orientation in the Member States COM(2017)824 final.

8. Report from the Commission presented under Article 8 of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union COM(2017)1201 final.

9. These are the two Member States that are not yet parties to the TSCG. Art. 4 provides that Member States whose currency is not the euro may send a notification to the Commission that they wish to be bound by the Directive.

mechanism should the target not be met. The proposed revision of Article 3 requires States to abide by a rule whereby the medium-term objective in terms of structural balance is to achieve a ratio of debt to GDP at or less than 60 per cent. The Directive would retain the duty to activate, automatically, a "correction mechanism" (read: "make budget cuts") should there be a deviation from the medium term objective.

To ensure these obligations are met the Directive would require that independent bodies be set up to monitor compliance. The budget – that most political of national instruments – is now regulated by national bureaucrats so as to render governance of the EMU "effectively legitimate and democratic."[10] The tension in this passage echoes Dani Rodrik's trilemma: one cannot pursue greater economic integration (the aim of EMU governance) whilst retaining both a high degree of democracy and national sovereignty.

A European Monetary Fund

The European Stability Mechanism (ESM) is fêted for rescuing the euro area, but it is perhaps less appreciated by the Member States that received its assistance. Yanis Varoufakis puts it graphically: "groups of technocrats dispatched by the IMF, the European Commission and the ECB had arrived at Athens airport, from which they had been driven at high speed under police escort in a convoy of Mercedes-Benzes to the various ministries, where they had proceeded to interrogate elected ministers and dictate to them policies that affected the lives of millions."[11]

Before one gets too excited at the prospect of the ESM being replaced by a more benign-sounding EMF, the current proposal largely subsumes the ESM, as it is, into the EU legal order.[12] The major substantive proposal is to allow the Fund to serve as a backstop to the Single Resolution Fund: this makes sure that markets view a bank's assets as safe since in case of failure and an absence of sufficient private funds, public money is available.[13]

Another proposal of potential significance for States is the option for the EMF to develop financial instruments that might be used for offering "precautionary financial assistance", meaning that the Fund can intervene to

10. Roadmap, cited *supra* note 1, p. 7.
11. Varoufakis *Adults in the Room: My Battle with Europe's Deep establishment* (Penguin Random House 2017) pp.165–166.
12. European Commission, Proposal for a Council Regulation on the establishment of the European Monetary Fund, COM(2017)827 final.
13. See Schoenmaker, "Why we need a fiscal backstop to the financial system" 30 Aug. 2014 (available at <voxeu.org/article/why-we-need-fiscal-backstop>).

prevent crises.[14] This echoes the views that the ESM should have been called on sooner by Member States in need.[15] However, this would have to come with safeguards that an early call on the Fund does not stigmatize the beneficiaries, weakening their positions on the financial markets. Menacingly, an ECB opinion on this aspect of the proposal suggests that even precautionary assistance must come with "adequate conditionality."[16] It is hoped that these conditions would be along the lines of assessing the country's economic policy design, and affording access to funds if the State has carried out adequate reforms, rather than *ex post* requests for budget cuts.

The need for better design of future Memoranda of Understanding is recognized in a call for a "social impact assessment", although one might have wished for more attention to the adverse effects that these conditions yield and for a codification of the role of this assessment in the Articles of the Regulation.[17] Here, an internal reform of the ESM to improve its approach to lending and designing conditions would probably achieve more than the proposed legislative initiative. Finally, the proposal appears to end the close working relationship with the IMF, which has led to certain frictions, but may well have been essential to ensure the establishment and the operation of the ESM.[18]

The key institutional change is that the Council would endorse the decisions taken by the European Monetary Fund, which would become a "unique legal entity under EU Law."[19] The Commission takes the view that this construction is necessary to respect the boundaries set by the *Meroni* doctrine. Yet, quite what the advantage is of bringing an institution established outside the Treaties within them, only to ascribe a unique status to it under EU law is unclear. More prosaically, since the Board of Governors of the ESM and the new EMF is the Eurogroup, and the Regulation provides that "the votes of members of the Council representing Member States whose currency is not the euro shall be suspended", it is simply the same people wearing different hats.[20] That Article 352 TFEU provides a clear legal basis for this proposal

14. Proposal cited *supra* note 12, recitals 43–44.

15. Independent Evaluator appointed by the ESM Board of Governors, *EFSF/ESM Financial Assistance Evaluation Report* (European Stability Mechanism, 2017).

16. Opinion of the ECB of 11 April 2018 on a proposal for a regulation on the establishment of the European Monetary Fund (CON/2018/20) p. 2. The ECB is also concerned that the renaming of the fund would be confusing (monetary policy is for the ECB) and, more importantly suggests that the Bank's role in the ESM/EMF be clarified.

17. Proposal cited *supra* note 12, recital 26.

18. Henning, *Tangled Governance: International Regime Complexity, the Troika, and the Euro Crisis* (OUP, 2017).

19. Proposal cited *supra* note 12, p. 5.

20. Ibid. Art. 3(4).

may be doubted:[21] since it must be shown under this Article that EU legislation is "necessary" to attain a Treaty objective, and nearly everyone agrees that the ESM is already serving to safeguard the financial stability function while operating outside the Treaty, how necessary is law reform?

Redeploying and expanding the EU budget

The budget of the EU is relatively modest (amounting to 1% of the EU's GDP). Its basic philosophy is to serve as an investment budget for common EU policies, with limited redistribution functions.[22] At the same time, it was (belatedly) recognized that during the crisis spending to assist Member States was necessary, with some welcome initiatives established.[23] The December 2017 proposals consider novel spending options, some of which would be rolled out before 2020, the rest for the next budget cycle.[24] In the Roadmap, emphasis is placed on what money would be spent on, since the post-2020 Multiannual Financial Framework discussions are now under way and the revenue side of budget discussions will raise a host of issues, including the budget shortfall resulting from the exit of the UK.[25] Hopes for any success in the proposals below being funded should not be too high: "stabilization policy in a EMU raises far more divisive institutional and budgetary questions than the Union has faced in the past."[26]

The first proposal is for a "new policy delivery tool" whereby, if Member States commit to undertake the sort of economic reforms which are judged to make a significant contribution to the resilience of the national economy and

21. The Commission cites Case C-370/12, *Pringle,* EU:C:2012:756, para 67. However, it is not clear that this paragraph really helps: it merely states that Member States are not obliged to create the ESM using Art. 352 TFEU, without taking a position on whether it would have been an appropriate legal basis.

22. High Level group on Own Resources, *Future Financing of the EU* (December 2016) p. 6.

23. E.g. the Structural Reform Support Programme, and see Proposal for a Regulation of the European Parliament an of the Council amending Regulation (EU) 2017/825 to increase the financial envelope of the Structural Reform Support Programme and adapt its general objective COM(2017)825 final.

24. European Commission, New Budgetary Instruments for a Stable Euro Area within the Union Framework COM(2017)822 final. The fourth element of this Communication, the fiscal backstop to the banking union, is discussed under the EMF proposal *supra*.

25. EU budget: Commission proposes a modern budget for a Union that protects, empowers and defends Brussels, 2 May 2018 (Press Release IP/18/3570).

26. Laffan, *The Finances of the European Union* (Macmillan, 1997), p. 254 writing, presciently, before EMU.

thereby lead to positive spillovers for the EU as a whole, then some of the funds available under this new budget head may be used.[27] It is linked to the European Semester and to the regulatory paradigm for EMU: to ensure that these funds are not misused, the proposal foresees National Reform Programmes to be agreed *ex ante* and their implementation to be monitored *ex post* by the Commission. This proposal contains a "pilot phase" for the period 2018–2020 (achieved by amending the Common Provisions Regulation),[28] followed by a more systematic roll-out. This approach has affinities with the approach to State aid, where measures that are perceived to benefit the EU are given a smoother procedural pathway *ex ante* and are subjected to *ex post* reviews. This regulatory approach is also proposed for cohesion funds, here linking access to these funds to respect for the EU's fundamental values.[29] This latter kind of conditionality is particularly controversial; moreover, it must be ensured that all the conditions retain a modicum of consistency.

The second and third proposals are technically distinct but politically conjoined: a convergence facility for States "on their way to joining the euro" and a stabilization fund for Eurozone States. Since EU budget discussions are zero-sum games this approach tries to avoid winners and losers; but it remains unclear whether the benefits to the two groups will be of similar size. The most intriguing and forward-looking proposal is that for Eurozone States.[30] Three options are on the table for what this slice of the budget could cover: a European Investment Protection Scheme, which would support projects that have already been planned (e.g. infrastructure and skills development) and for which States need extra financing given an economic downturn; a European Unemployment Reinsurance Scheme to support national unemployment schemes; a more generic "rainy day fund" which lacks further specification.[31] Finding a legal basis for these will be tricky, because the EU has limited

27. Communication on new budgetary instruments for a stable euro area within the Union framework, COM(2017)822, pp. 9–11.

28. Proposal for a Regulation amending Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006 as regards support to structural reforms in Member States COM(2017)826 final.

29. A Modern Budget for a Union that Protects, Empowers and Defends The Multiannual Financial Framework for 2021–2027 COM(2018)321 final, p. 4. This is phrased quite delicately, intimating that weak rule of law may impair the financial interests of the Union, but the political message implied is much sterner.

30. On the need for a Eurozone budget generally, see Hennette, Piketty, Sacriste and Vauchez, *Pour un traité de démocratisation de la zone euro (T-Dem)* (Éditions du Seuil, 2017).

31. Communication cited *supra* note 27, p. 14.

competences when it comes to social affairs; and the absence of solidarity in the construction of EMU should be recalled.[32]

The Commission realizes that if macroeconomic stability is to be pursued via the EU budget, then this might require much bigger funds than may be obtained even from a successful expansion of own resources, so it suggests that funding might also come from the European Monetary Fund, and that States might consider the construction of a dedicated fund outside the EU budget to serve as an insurance mechanism. These disparate sources of finance might be merged by a "dedicated vehicle" managed by the Commission. It is perhaps paradoxical that whilst the Fiscal Compact and the ESM are re-patriated into the EU legal order for the sake of legitimacy, clarity and effectiveness, the same batch of proposals suggests that a different approach – outside the EU framework – is necessary to ensure effective delivery of macroeconomic stabilization.

Furthermore, the proposal suggests that access to stabilization funds depends on "eligibility criteria and an agreed mechanism to trigger its use."[33] What might these two elements mean? Consider these in case of unemployment reinsurance, a policy that has been under official consideration in the distant past and again more recently.[34] The trigger mechanism requires careful design lest access to these funds can be "gamed" by the would-be beneficiary. For example, proposals for unemployment reinsurance would require that access to these funds is available when a clearly measurable event occurs which is beyond the control of the parties, e.g. an increase in unemployment above a set rate. Such a high unemployment rate would stretch national budgets and require additional assistance.

In terms of eligibility criteria, one might wonder whether the same types of conditions that were prescribed by the ECJ in *Pringle,* when it gave the green light to the ESM Treaty, would also apply here. It will be recalled that the Court circumvented the no-bailout clause because ESM funding addressed a widespread risk (financial instability of the euro area) and the funds were subject to strict conditions. Since a request for funding to supplement national unemployment insurance schemes would also amount to a sort of bail-out (funds would only be dispensed once the State exhausts its resources) one wonders if EU law requires conditions to be attached. This is particularly so because the kind of unemployment reinsurance scheme that is planned is

32. For a helpful discussion of possible legal bases, see Steinbach, "Insurance-type cooperation mechanisms under EU law", 27 *Swiss Review of International and European Law* (2017), 19.

33. Communication cited *supra* note 27, p. 13.

34. Marjolin et al., Report of the Study Group "Economic and Monetary Union 1980" (1975), and back on the table now: European Commission, COM(2017)291, Commission's Reflection paper on the deepening of the Economic and Monetary Union of 31 May 2017, p. 25.

designed to afford macroeconomic stability, and is not motivated by the desire to improve national schemes. That is, States with less generous schemes will receive funds to ensure these schemes have funds, but there is no interest in harmonizing national schemes to an optimal amount. Irrespective of whether unemployment reinsurance is tantamount to a bail-out, it would be prudent to attach some conditions lest Member States free ride on these funds and fail to make the necessary provisions in their national policies. Parameters pertaining to adequate economic reforms or economic performance in the period before the asymmetric shock could be considered. Notice, however, how this approach means that the solidarity in the proposals is not redistributive: it is not the bonds among citizens of different nations that motivate transfers; rather, solidarity is grounded on avoiding negative spillovers, and it is conditional on the beneficiary's fiscal prudence.

Finally on these budgetary reforms, is there not a certain interchangeability between the funds here and those proposed for the EMF? The Commission's vision appears to be as follows. First, with sufficient internal discipline, Member States can be guided by the European institutions to develop a sustainable economic model. Second, should this good behaviour not suffice to address a particularly serious economic distortion, then the EU budget, possibly combined with the EMF and extra-EU finds can come in to prevent a sovereign debt crisis. Third, when even this fails, then the EMF arrives as a last resort mechanism. Could the EMF not suffice to serve as a funding source for stabilization at stages two and three? Irrespective of this, it is not surprising that, by showing the economic linkages between prevention and rescue, the Commission proposes a European Minister of Finance to manage these combined elements.

A European Minister of Economy and Finance

The buzzword here is synergies: these would be obtained by merging the role of the Commission Vice-President in charge of the Economic and Monetary Union with that of President of the Eurogroup as well as the Chair of the European Monetary Fund. A single person would thus: coordinate national economic policies in the interest of the EU, be in charge of surveillance of national policies, coordinate euro area budgetary instruments, and have a say in EMF rescue packages.[35]

35. Communication on a European Minister of Economy and Finance, COM(2017)823 final.

The opposite of synergy is conflict of interest: can one person be loyal to both the Member States (within the Eurogroup) and the Commission?[36] The same issue concerning the High Representative of the Union for Foreign Affairs and Security Policy was addressed explicitly in the Treaties (Art. 18 TEU). Can this new minister, with a comparably important brief be created just by dint of a change in the Eurogroup's working methods?[37] Moreover, it has been suggested that such a Minister might require the establishment of parliamentary accountability in a forum which includes reporting simultaneously to the European Parliament and national parliaments given the impact of his or her decisions.[38] Finally, is it good governance for the person in charge of overseeing compliance with Member States' fiscal prudence also to chair the group that sets the general economic direction of the EU, and also to be in charge of disbursing funds to Member States in trouble?[39]

Beyond tinkering

One would, of course, not expect the Commission to preface the launch of this policy initiative by echoing the late Rudi Dornbusch's view that EMU is a bad idea.[40] At the same time, bringing the two international treaties that supplement the EU rules governing monetary union within the EU legal order seems to bring little added value; increasing the capacity for solidarity with a larger budget is to be welcomed, but may be tricky to achieve in the current political climate, to say the least. One should seize today's relative economic calm to consider different paths and better policies for the long term sustainability of EMU.[41] This is of course best achieved at EU level. However, given the timidity of the proposals outlined in December 2017, an alternative site for such reform might, provocatively, be through a reform of the ESM Treaty: a revision of this treaty has already been suggested by an external review,[42] and States could take this as an opportunity to discuss the basis upon which this treaty might be redesigned, and identify the appropriate mix between discipline and solidarity. This vision might then be transmitted to the

36. Both organs would appoint (and may dismiss) this Minister.
37. Communication cited *supra* note 35, at footnote 15.
38. Enderlein and Haas, *What would a European Finance Minister do? A Proposal* (Jacques Delors Institute, Berlin, 2015).
39. See further Patrin, "A European Finance Minister: Form follows function, but is it legal?" (forthcoming).
40. Dornbusch, "Euro Fantasies" (1996) *Foreign Affairs*, 110.
41. See e.g. Sandbu, *Europe's Orphan: The Future of the Euro and the Politics of Debt* (Princeton University Press, 2015) Chs. 8 and 9; Stiglitz, *The Euro: How a Common Currency Threatens the Future of Europe* (Norton & Company, 2016.) Chs. 9–12.
42. Report cited *supra* note 15.

EU legal order. Of course this would very much be a second-best, given the lopsided balance of power within the ESM and its weak forms of accountability and transparency, but it could create the space to begin a conversation on how to reform EMU more radically.