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INTRODUCTORY STATEMENT

Economic Governance

Hearing of the Constitutional Affairs Committee of the European Parliament (AFCO) on "The institutional future of the European Union within and beyond the Treaty of Lisbon"

Tuesday, 26 May 2015

Good morning, Madam Chairwoman Hübner, and dear Members of the Constitutional Affairs Committee. I would like to thank you for inviting me to participate in this public hearing on "The institutional future of the European Union within and beyond the Treaty of Lisbon".

In the following I would like to, first, set the stage by shortly describing the framework set by the Lisbon Treaty for the "Economic Governance". After this short introduction I will focus on three main issues, namely:

1. The means of enforcement for measures taken under the EU economic governance framework;
2. The question of a euro area fiscal capacity and a euro area budget and
3. The issue of strengthening the role of the European Parliament in the economic governance framework.

SETTING THE STAGE: THE FRAMEWORK SET BY THE TREATY OF LISBON

The Treaty of Lisbon did not change the basic construction of the Economic and Monetary Union as it was introduced by the Treaty of Maastricht. The basic construction is characterised by its asymmetry. Whilst the Monetary Union is a supranational one, the Economic Union remains intergovernmental. This division is line with the traditional technocratic EU policy approach: Disciplining national democracies by a common monetary policy instead of replacing them by a common economic and fiscal policy. National economic and fiscal policies should be aligned with certain policy goals set at EU level but without any legally binding enforcement mechanism. They should be disciplined by the markets based on the assumption that, as long as the position of a Member State on the financial markets is the same as of any other private institution, markets will indicate by lowering or raising interest rates on government bonds whether a national economic and fiscal policy is convincing or not. Therefore the no-bail-out clause (Article 125 TFEU), therefore no purchase of government bonds on primary markets by central banks (Article 123 TFEU), therefore no privileged access by central governments to financial institutions (Article 124 TFEU). The coordination of Member States' economic and fiscal policies was depoliticised at EU level by definition.

The main institution in the Monetary Union is the European Central Bank (ECB) equipped with an independence vis-à-vis any other Union institution and vis-à-vis national governments and Parliaments. The main institution in the Economic Union is the Council. It coordinates, upon recommendation of the Commission, the economic policies of the Member States and it exercises the budget control under the excessive deficit procedure. The European Parliament has no major role in the supranational Monetary Union because of the independence of the ECB. It has no major role in the Economic Union either because of its intergovernmental nature. National Parliaments have no role in the Monetary Union since the monetary policy is an exclusive EU competence. And with regard to matters concerning the Economic Union national Parliaments are in an "international law modus" and, traditionally, control their governments *ex post*.

This basic construction cannot be changed outside a formal Treaty change procedure. This sets the limits for secondary law such as the "Six Pack" or the "Two Pack" regulations as well as for international treaties concluded by a subset of Member States such as the Fiscal Compact and the ESM-Treaty. The European Court of Justice confirmed this view in its "Pringle" decision on the compatibility of the ESM-Treaty with EU law when it concluded that the ESM-Treaty could enter into force even before the formal introduction of Article 136(3) into the TFEU which stated that the Eurozone Member States may establish a stability mechanism. Independently of this "Treaty change" the ESM-Treaty had to be in compliance with the EU Treaties in order to be lawful. This clear statement by the Court shows, by the way, that the ESM could also have been established within the existing Treaty framework on the basis of Article 352 TFEU.

What does the unchanged asymmetry of the EMU at the level of the Treaties mean for the future development of the Economic Governance? It means that the Treaty boundaries are reached when the coordination of Member States' economic and fiscal policies is to be supranationalised. When would there be a supranationalisation of the Economic Union? A supranationalisation can be assumed if decisions taken at European level may substitute economic and fiscal policies decisions taken at national level. Does this mean that a Treaty change is inevitable in order to strengthen the European dimension of the Economic Union? My answer to this question is: No. There is still a potential within the Treaty boundaries. In order to uncover this potential, I suggest a change of perspective from competences to means of enforcement. The possibilities to adopt guidelines for Member States' economic policies under Article 121 TFEU and for Member States' employment policies under Article 148 TFEU appear to me as a sufficient basis for the setting of common economic and fiscal policy goals for Member States. The enforcement of this policy goals is, however, highly precarious seeing the intergovernmental nature of the Economic Union.

MEANS OF ENFORCEMENT: PROPOSAL OF AN INCENTIVE-BASED ENFORCEMENT MECHANISM

What possibilities for enforcement do we have? We can distinguish five means of enforcement: *First,* there can be private enforcement. Private action builds up pressure on the non-compliant Member State and pushes the latter to modify its economic and fiscal policy decisions. *Second,* there can be public enforcement. Within public enforcement, one may distinguish several degrees of intensity. The least intense means of enforcement is "naming and shaming". A publication of non-compliance creates public pressure on the non-compliant Member State to align its economic and fiscal policies with the commonly set policy goals. There can be, *third,* sanctions for non-compliance, and, *fourth,* incentives for compliance. *Fifth,* and this is the most intense means of enforcement, European policy decisions substitute national economic and fiscal policy decisions. Non-compliance is then "sanctioned" by substitution.

Out of these enforcement means only the latter is excluded by the non-supranational nature of the Economic Union. The current choice of the Treaties is a combination of private enforcement and "naming and shaming". As already mentioned, higher interest rates on government bonds should make Member States modify their national policy choices. Publicly naming wrong policy choices should then reinforce or even trigger such private reactions. Whether this is, or let me rather call it, was a convincing enforcement mechanism for the Economic Union is a question that I leave open to your judgment.

Financial sanctions were introduced by the "Six Pack" for Eurozone Member States. Regulations based on Articles 121, paragraph 6 and 136 TFEU provide for interest-bearing deposits in case of a violation of the preventive arm of the Stability and Growth Pact or in case of a non-correction of excessive macroeconomic imbalances. The latter can even be topped up by fines. The legality of those sanctions is doubtful. This follows from the fact that Primary law provides explicitly in Article 126(11) TFEU for sanctions against non-compliant Member States within the corrective arm of the Stability Growth Pact. This means in turn that there cannot be sanctions for Member States where Primary law does not provide for it and, consequently, that they cannot be introduced by Secondary law. In addition to this legal argument one may question the meaningfulness of a financial sanction with a view to persuade a Member State in economic and financial troubles to modify its economic and fiscal policies.

This brings me to the last remaining enforcement mechanism which are incentives. This possibility is not yet explored by the Union legislator. Instead of sanctioning non-compliance, one may reward compliance. A regulation based on Article 121(6) TFEU may provide for financial incentives for the adjustment of a Member State's economic and fiscal policies to policy goals set by Union guidelines. Such a regulation would not infringe Primary law. In contrast to sanctions, refusing payment of financial incentives in case of non-compliance does not worsen the position of a Member State. Prior to a possible adoption of a regulation on financial incentives a Member State would have no right to claim financial assistance as it has no right to claim it after the adoption of such a regulation in case of non-compliance.

OWN RESOURCE FOR THE EUROZONE: DIFFERENTIATION IN EU BUDGET LAW

The hereby raised issue of payment of financial support to Member States triggers the follow-up question on the budgetary implications of such a mechanism and leads us to the second part of my presentation on the possibilities of a Euro area budget. Assuming that there would be an incentive-based enforcement mechanism established on the basis of Articles 121(6) and 136 TFEU for the euro area, can there be a euro area budget to finance these incentives? The answer to this question is to be found in EU budget law. The Lisbon Treaty refers in this respect to the general principle of unity of the EU budget and its completeness. This means that *all* revenues and expenditures of the Union are part of *one* EU budget which is complete and includes therefore *every* predictable revenue and expenditure of the Union. Financial assistance in form of incentives for compliance is therefore covered by EU budget rules. Yet, EU budget law provides for more flexibility than one may think. This flexibility can be found with regard to expenditure as well as to revenue. The Union budget may contain a budget line that is dedicated to expenditure which is geographically limited to a subset of Member States. More important (especially when we recall the awkward debates about the multi-annual financial framework) is the question whether there can be revenue from a subset of Member States which falls outside of the MFF. In principle, the annual budget of the Union shall comply with the MFF. Yet, the MFF regulation has an interesting recital in this regard. According to recital No. 8 the "MFF should not take account of budget items financed by assigned revenue within the meaning" of the Financial Regulation. This refers to specific items of expenditure for which a Union act explicitly defines the revenue that has to be used in order to finance this expenditure. In short, every revenue which is earmarked by a Union legal act and explicitly assigned to a certain expenditure is not covered by the MFF ceilings. Such revenue has not, by definition, to be financed by all EU Member States. This can be seen by an article in the title on Enhanced Cooperation. According to this article, expenditure "resulting from implementation of enhanced cooperation, […] shall be borne by the participating Member State". This confirms that differentiation with regard to the origin of Member States' financial contributions is legally possible under EU budget law. Yet, even differentiated financial contributions are to be considered as "own resources" in terms of the Own Resources Decisions and Article 311 TFEU.

In sum, the current Treaty framework allows the establishment of a Euro area budget outside of the ceilings of the MFF as long as financial contributions from Eurozone Member States are explicitly assigned to certain expenditure items for the benefit of Eurozone Member States. Those additional financial contributions would be new own resources wherefore the Own Resources Decision would have to be amended in accordance with the procedure foreseen by Article 311 TFEU.

ENHANCING LEGITIMACY: THE ROLE OF THE EUROPEAN PARLIAMENT

Let me now turn to my third and last point which concludes my presentation: The involvement of the European Parliament. In the current economic governance framework the European Parliament has no strong role assigned. This is, of course, linked to the intergovernmental nature of the Economic Union. There are, however, ways to increase the European Parliament's involvement the coordination of Member States' economic and fiscal policies beyond the European semester. First, one may think about the extension of the ordinary legislative procedure to matters of economic and fiscal affairs. A coordination of national economic and fiscal policies can also be achieved by the harmonisation of important areas of those policies such as tax law (based on Article 113 TFEU concerning indirect taxes and Article 115 TFEU concerning direct taxes) and social law (based on Article 153 TFEU). Yet all those legal bases provide only for a consultation of the European Parliament. The ordinary legislative procedure can, however, be extended to these legal bases either by the simplified Treaty amendment procedure or by making use of Article 333(2) TFEU which enables the Council to switch, for the purpose of an enhanced cooperation, to the ordinary legislative procedure.

Second, participation rights of the European Parliament can be strengthened by introducing a "de-facto co-decision" via Interinstitutional Agreements. The Commission could, for example, inform the European Parliament about its proposals for recommendations and decisions of the Council on matters relating to the economic governance. Amendments by the European Parliament could subsequently be included into the proposal by the Commission before it submits its proposals to the Council.

CONCLUDING REMARKS

In order to sum up, Madam Chairwoman, dear Members of AFCO committee, there is still potential for strengthening the Union level in economic governance and the role of the European Parliament therein. It is rather a question of political will than of legal boundaries whether this strengthening can be achieved. I did not address possible Treaty changes deliberately. In my view, a future Treaty change should overturn the asymmetry of the Economic and Monetary Union and should recognise the European Parliament as the main source of legitimacy for a supranational economic governance. Whether these changes can be achieved, is even less of a legal question than a question of political will in a future European Convention. I hereby want to conclude my introductory statement and I am very much looking forward to the upcoming debate of this hearing.