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The retransformation of Europe

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The state of the Union

Prior to the more recent refugee crisis, the 'euro crisis' was the most severe crisis in the history of the EU. As the EU is often written as a history of crisis, such a statement is not made easily. However, the euro crisis occupies this position for six reasons.

First, its scale is more wide-ranging and the consequences more severe than previous crises. The failure of the European Defence Community, the empty chair crisis and the various breakdowns of earlier attempts at monetary integration did not lead to a retrenchment of the EU or to disintegration but merely prevented the EU from going further and temporarily cemented the status quo. The common currency, however, is one of the few exclusive powers of the Union. Of all the exclusive powers, it is the one that most clearly resembles a core state function (Genschel and Jachtenfuchs 2014), with the French Constitutional Council seeing it as 'vital to the exercise of national sovereignty'[1] and the German Constitution Court as a precondition for democracy.[2] A breakup of the euro would amount to a failure of the most ambitious attempt at integration so far, and in a field which is both factually and symbolically of the utmost importance. This is clearly in the minds of policy makers, most famously in Angela Merkel's often-quoted remarks before the German Bundestag: 'Europe fails if the euro fails, Europe succeeds if the euro succeeds.'[3]

Secondly, the crisis is multidimensional. The crisis is often described in this regard as one of public finances in which particular states, through bad luck, unwise choices and/or poor governance, are no longer able to pay their

1 Decision 92-308 DC, *Maastricht I*, Judgment of 9 April 1992, para. 43.
2 *Brunner* v. *TEU* [1994] 1 CMLR 57.
3 Deutscher Bundestag, Plenarprotokolle, 17. Wahlperiode, 160. Sitzung, 27 December 2012, 19078.

way. The badness of the term 'public finances' is itself unhelpful, and conceals more than it reveals. Public finance crises are not merely actuarial deficits. Direct remedial action invariably involves a mixture of cuts in public spending, most obviously to welfare, health, pensions and education; increases in taxes, often in ways which may be regressive; and garnering income through other sources, notably privatisation and the sale of public assets. In addition, international organisations and European Union institutions often perceive deterioration of public finances as a symptom of underlying weaknesses in the public administration or economy of a member state. Further remedial action may be required, therefore, in the organisation of government, labour law, industrial policy and levels of product or service regulation, or professional requirements. Public finance crises touch a multifarious variety of interests, perspectives and values in a way like no other.

This multidimensionality is, to be sure, common to all public finance crises. However, in the case of the euro-area crisis it has been further complicated by the 'sovereign-bank nexus', a vicious circle in which banks finance government debt, governments are lax on banking supervision, and governments must then rescue banks with public finances due to the wider effects on the economy of bank collapse. This nexus not only tied national governments to commercial banks in a suffocating embrace, but national governments to each other. Despite the fact that Greece represented only a small fraction of the Eurozone's gross domestic product, at the onset of the crisis neither the European Council nor the European Central Bank considered its sovereign default a feasible option because they feared a wave of bank breakdowns, bank bailouts and budget imbalances throughout Europe. The financial means involved were enormous. According to a 2012 Commission estimate, more than 4,5 trillion euros of taxpayers' money were used to rescue banks in the EU in the period of the crisis up until then (European Commission 2012a: 3).

Thirdly, the crisis has been marked by high levels of political contestation. Social hardship developed rapidly: according to Eurostat, the unemployment rates increased between 2007 and 2013 in Ireland from 6.4 per cent to 13.1 per cent, in Greece from 8.4 per cent to 27.5 per cent, in Spain from 8.2 per cent to 26.1 per cent, in Italy from 6.1 per cent to 12.2 per cent and in Cyprus from 3.9 per cent to 15.9 per cent.[4] The ability of political institutions to respond effectively was not immediately

4 http://ec.europa.eu/eurostat/statistics-explained/index.php/Unemployment_statistics.

apparent. As Jean-Claude Juncker once remarked, 'We all know what to do but we just don't know how to get re-elected once we have done it' (quoted in Hix and Høyland 2011: 271). At Union level, the crisis increased the politicisation of the Union in a manner which is unlikely to be reversed in the foreseeable future. It has also had dramatic domestic political repercussions: between 2010 and 2013, only four Eurozone governments *remained* in power (Schimmelfennig 2014: 324).

Fourthly, the euro crisis marks the visible end of the standard model of the euro-polity according to which the EU was strong in fields of rather technical and potentially Pareto-improving areas of market regulation and weak in issues relating to large-scale redistribution (Hix 2007; Moravcsik 2002; for a classical treatment of the distinction between regulatory and redistributive politics, see Lowi 1972). Now, the EU is engaged in massive redistribution among member states. This occurs most explicitly through the European Stability Mechanism (ESM), a €700 billion series of guarantees to support euro-area states which can no longer sustain their public finances. It has also occurred indirectly through various forms of European Central Bank (ECB) assistance and intervention (Wilsher 2013), but most dramatically through the commitments by the ECB to purchase both unlimited amounts of securities from euro-area governments which have entered EU sponsored financial support programmes (Outright Monetary Transaction (OMT) Programme)(European Central Bank 2012) and its wider monthly purchases of €60 billion of euro-area public sector securities, which began on 9 March 2015 and is envisaged to last until September 2016 (Public Sector Purchase Programme (PSPP)).[5] These measures not only redistribute wealth between member states but also between private parties. The ESM has secured the position of creditors at the expense of taxpayers and recipients of public expenditure in the debtor state who have to bear the burden of any programme to secure financial support. OMT and PSPP stoke demand for particular assets, thereby benefiting holders of those assets. While regulatory policies can, under certain conditions, be legitimated by their output and be taken by non-majoritarian institutions, the massive involvement of the EU in such redistributive policies has created visible winners and losers, something which has habitually required a strong democratic mandate (Scharpf 1999; Dawson and de Witte 2013).

Fifthly, the crisis has shifted the relationship between the different EU institutions and has further increased the EU's institutional fragmentation

5 Decision ECB/2015/10 on a secondary markets public sector asset purchase programme, Decision of 5 March 2015.

(Genschel and Jachtenfuchs 2016). For many observers, the crisis marked a decisive step for the 'new intergovernmentalism' (Bickerton et al. 2015), which is characterised by the dominance of the European Council and a diminished role for the Commission and the European Parliament, which supersedes and partly replaces the old Community method. In this view, the increased role of the European Council is not merely a phenomenon that accompanied the most dramatic years of the crisis but a long-term structural change which the crisis brought to the forefront. Moreover, the European Council is not the only intergovernmental body to acquire prominence during the crisis. The euro group, comprising the finance ministers of the euro-area states, the ECB President and the Commissioner responsible for economic and financial affairs, has been central to micro-managing many aspects of the crisis, be it draft national budgets or structural reforms, as well, in its guise as the Board of Governors of the ESM, as the central decisions governing financial support for states which have requested it as well as the central conditions surrounding that support. In the case of the Commission, these include supervision of almost all fields of economic and social policy under the guise of preventing and correcting macroeconomic imbalances. The ECB's powers to purchase unlimited amounts of securities have turned it into a lender of last resort (Buiter and Rabari 2012; Wilsher 2013). Beyond the monetary sphere, it has sought to acquire ever more regulatory powers, initially over prudential supervision but also over clearing systems, in the guise of securing monetary stability. This has resulted in new administrative resources, most notably the addition of 1,000 employees to the ECB in 2013–14 to allow it to carry out its new tasks of prudential supervision.

The relative power of these supranational institutions is facilitated by their decision-making dynamics. Despite the build-up of a more permanent administrative structure and a President, the European Council is, in essence, a forum for negotiation and deliberation which meets only several times a year for brief periods, and which has to decide mostly by unanimity. In contrast, the ECB has a fast decision-making structure, independent from direct democratic control and with a substantial administrative backup. This shaped the relative influence and roles of the institutions during the crisis. While the European Council was often divided on the issue and unable thus to make decisions, the ECB stepped in to provide substitutes, most notably financial support to stricken states, and thereby broadened its powers 'through the monetary backdoor' (Schelkle 2014). These overlapping, fluid roles between the European Council, Commission,

ECB and the euro-Group raise questions not only about institutional coordination and cooperation, but also accountability, transparency and representation as this varies significantly between the institutions (Bovens and Curtin in this volume). These issues have been further stirred by the presence of processes which do not have a formal institutional presence but have significant equivalent effects. The most visible of these is the 'Troika' of the International Monetary Fund (IMF), the European Commission and the European Central Bank, which is responsible for negotiating the details and overseeing the implementation of those programmes which are a precondition for ESM financial support. In practice, this has allowed it to impose demands and oversee almost all aspects of those states' economic and social policies in a highly unaccountable manner. It has, thus, become the symbol of far-reaching and deeply intrusive adjustment policies from a technocratic informal association without democratic credentials, with its removal being a central demand of the incoming Greek Syriza government in January 2015.

Sixthly, and finally, the crisis set tremors through domestic constitutional settlements. The only formal requirement was that euro-area states entrench a commitment to balance their budgets 'in provisions of binding force and permanent character, preferably constitutional'.[6] Arguably, a greater transformation is that EU law now claims a continual oversight and legal authority over elements which are at the centre of many domestic constitutions, be these budgetary powers, the social state, or citizenship. As the demands of EU law have intensified and shifted during the crisis, this has, in turn, put corollary pressures on established domestic understandings of sovereignty, citizenship and parliament–executive relations. It is, thus, unsurprising that it has led to a series of responses in national constitutional courts (Chalmers in this volume). Furthermore, the constitutional resettlement taking place is not that advocated by some exponents of European constitutionalism in which the disciplines of EU law or the image of Europe leads domestic settlements to take more account of interests or values historically poorly represented within them (Joerges 2014a). Instead, it is one in which asymmetries of financial power are protected from political correction with private creditors of euro-area states insured against the risk of bad investments and creditor states within the ESM given greater power to dictate policy terms to debtor states (Dawson and de Witte 2013).

6 Article 3(2) TSCG.

The continuation and amplification of structural features of the Union by the crisis

To be sure, the six developments outlined in the previous section transform the European Union. They stretch and challenge the pre-existing modus operandi, set up new constellations of conflicts and make European Union policies a much more salient and divisive presence. However, for all this change, the institutional responses to the crisis represented very much a continuation of a Union way of doing things. By this, we argue that the evolution of the crisis was not merely a result of economic and fiscal policy choices but reflected broader structural features of the European Union construction which the crisis exposed. These structural features are marked by enduring and persistent characteristics. They are not impossible to change or to deal with but evidence frequent potentially powerful and entrenched effects which are endemic to the EU in that they settle and institutionalise their effects. The following seem particularly important to us.

A concern with scale

A recurring feature of Union responses to its challenges – be they realising collective goods, dealing with externalities, strengthening institutional capacity or reimagining political community – is the assumption that sizing upwards will offer solutions that would otherwise not be available. This is most explicit in the subsidiarity principle, which links the justification for Union action to the effects or scale of a problem. It is also present in the granting of significant powers to centralised non-majoritarian institutions, most notably the Commission as the central agenda-setter for law-making and policy, and the ECB as the pre-eminent institution in managing the economic policy of the euro area. The rationales are that these have a purview and a freedom from sectoral or national interests that domestic institutions do not have. It exists within the hierarchy of norms within the Union, whereby international law binds the Union, EU law has primacy over national law, and national governments are assigned responsibility for all that takes place on their territory on the assumption that central domestic legal law can suborn other legal orders within the territory. It is, of course, present territorially, not only in the concern with the expansion of the Union but also in its neighbourhood and other policies which seek to extend the effects of Union norms beyond its frontiers (Lavenex 2014; Scott 2014). Notwithstanding certain benefits,

this privileging of scale generates many tensions and conflicts. There are dangers of administrative centralisation, imperfect knowledge, the effects of poor policies being magnified, and insensitivity to local concerns. Furthermore, as Majone has observed in this volume, collective action theory suggests that, the greater the number of participants in an enterprise, the more likely it will be that the agreed outcome will deviate from what is optimal for the majority.

The starkest manifestation of this concern with scale was the Commission's 'blueprint for a deep and genuine economic and monetary union' which acted in many ways as the template for reforms in response to the crisis (European Commission 2012b). This called in particular for a more centralised economic and monetary union. This would include a banking union in which there would be a single Union rulebook for the financial services industry, the ECB would acquire significant powers of prudential supervision, and a European Resolution Authority (now a Single Resolution Board) would establish a recovery and resolution regime for insolvent banks within the euro area. The rationale provided for this are assertions that a lack of strong supranational institutions exacerbated the crisis, led to a reversal of integration and the lack of a level playing field for businesses and households (European Commission 2012b: 9). The blueprint also sought harmonisation of national budgetary laws, increased fiscal capacities for the Union and greater Union oversight of employment and tax law. The rationale was, once again, that lack of supranational oversight and power had led to weak national performance in these fields which had contributed to the crisis (European Commission 2012b: 2–3 and 6). The diagnosis is thinly substantiated, but, even if it were correct, does it warrant the prognosis? All the concerns of capture, amplification of risks of poor decision-making, sub-optimal choice of collective preferences, and poor local knowledge are present in the blueprint. Furthermore, federations experience cycles of power moving upwards or downwards between levels. More than 60 years after its foundation, if the EU were such a federation, a downward cycle would be likely and no fundamental threat. Even such a characterisation does not take account of the current political debate in Europe in which elites and mass public are increasingly attracted by narratives which argue that European integration in general is the problem and not the cure (Majone 2014). This is not to argue that there is not a place for arguing that scale has certain benefits. It is simply to argue that these are neither questioned sufficiently nor are the risks and costs sufficiently thought through.

A weak political centre and administrative system of justice

For all its attempts at legal and administrative consolidation, the European Union has weak central resources relative to its competencies. Compared to other political systems, there are limited central financial resources; a small bureaucracy; no extensive administrative system of justice; weak political authority; and considerable checks and balances hemming in central decision-making. This leads to the Union having to rely strongly on national administrations, legal systems and resources to secure its policies. This results in a double bind. On the one hand, the Union can externalise the costs of applying and implementing its policies onto national actors. Unless it is highly attuned – and this is unlikely – to the extent, incidence and nature of these costs, there will inevitably be a danger that it externalises costs which are seen as excessive, unequally distributed and culturally insensitive. This has led to increased concerns with tools such as impact assessments (European Commission 2009), but the scale and heterogeneity of the Union makes sensitivity to its diversity very difficult indeed. On the other, the independence of national actors becomes a source of suspicion as it can be used to frustrate and negate Union policies. The Union is, thus, marked by a variety of tools used both to police national administrations and to induce them to realise Union policies – be they financial sanctions administered by the Court of Justice; litigation before national courts by private parties affected by non-compliance; naming and shaming; reporting duties; or benchmarking.

To be sure, during the crisis the Union acquired new capacities. Most notably, the ECB's unlimited purchasing power turned it into a de facto lender of last resort. Its weak central authority and resources shaped its dominant strategy to the crisis, which was to adopt a regulatory style. Central long-term goods were set out to be protected, notably fiscal discipline, return to the financial markets, and balanced economic performance. Protection of these goods justifies regulation by non-majoritarian supranational institutions to protect against their being damaged by domestic legislative or governmental excess or neglect. The sacralisation of these goods has been taken furthest in the Treaty on Stability, Co-ordination and Governance (TSCG) stipulation that a duty to balance the budget across the economic cycle should be put in a permanent and binding norm preferably of a constitutional character.[7] This is notwithstanding that there is no tradition since the Second World War of balancing the budgets in

7 Article 3(2) TSCG.

Europe, let alone a constitutional one that elevates it above other imperatives in these fields. As Chalmers observes in this volume, these norms then justify an institutional system of oversight, discipline and sanctions which is analogous to that found in fields where regulatory agencies are deployed. There is no tradition of this in the field of fiscal or welfare policy (Chalmers 2012). It has allowed the Union, however, to externalise the central costs and political responsibilities of adjustment onto national administrations. This has, in turn, proved to be an Achilles Heel for the Union. National administrations both become vehicles for securing its goals and the central impediment to realising them. Having cast them as unreliable actors to justify its intervention in the first place, the crisis led it – in both the 'Six Pack' and 'Two Pack' – to set out ever more detailed legal constraints on the exercise of domestic fiscal and economic policy. However, it has no administrative machinery to enforce these constraints effectively. More powerful states can thus game these constraints by exacting greater leeway as a price for cooperation.

Excessive reliance on government by law

A consequence of these weak central resources is a high dependence on those which remain available to the Union, most notably legal resources, to further its objectives. Law remains the central instrument both for realising integration and for allowing the Union to govern. In this, one sees not so much a Union rule of law. EU legal constraints on Union institutions are often patchy and EU law in a way claims to rule over private activities within the Union (Chalmers and Chaves 2014). Instead, there is government by law. Intervention is, above all, by use of legal instrument. This has resulted in an overstretching of EU law. As EU law is the central tool for the realisation of EU policies, a failure to meet the ambitions of these policies is frequently condemned as an act of illegality because these policies have been formalised within the substantive norms of EU law. This had a number of effects. It has led to an instrumentalisation of EU law, whereby EU legal pre-commitments are not only associated with unpopular or ill-conceived policies but seen as an instrument for masking debate about these behind requirements that the law be observed (Herdegen 1998). It has, in some cases, led to over-formalisation whereby the rigid structures of the law are unable to adapt with sufficient suppleness to the needs of the policy-sector and those affected by it. Finally, it has led to a desiccation of legal authority. In order to manage law's inflexibilities, an ever wider array of legal or quasi-legal instruments has been developed. Alongside the Regulations,

Directives, Decisions and Recommendations mentioned in the original Treaties, a number of other instruments have emerged which include, inter alia, Resolutions, Guidelines, Framework Directives, Action Plans, international agreements, common positions and Declarations. If these are less constraining than EU law, which is formally binding or directly applicable, the central features of law remain intact. It is difficult to change legal instruments, and legal normativity requires conduct not to deviate from the law for legally impermissible reasons. These features constrain the flexibility that can be offered, and it is obtained often at a cost, most notably in the form of uncertainty as to the impact and incidence of non-binding law.

The crisis extrapolated these features through both legal expansion and legal dispersion. It has generated a lot of EU law. The 'Six Pack' and 'Two Pack', the post-crisis secondary legislation governing the budgetary and macroeconomic policies of states, combine to make up seventy pages of *Official Journal*. However, alongside this, there has been a hollowing out of EU law and a move to other forms of law. The former is best seen with regard to assessments of whether a state has a macroeconomic imbalance. This is gauged against a Scoreboard which, in April 2015, comprised 16 headline indicators and 34 auxiliary indicators.[8] None of these indicators can be said to qualify as legal norms. It is difficult to know how they are read by the Commission to guide its assessment, but it is doubtful that it does this through interpreting these indicators as legal texts, although they do, nonetheless, combine to form a legal term, 'excessive macroeconomic imbalance', which can be deployed to act as a trigger for legal procedures and sanctions. The latter, the use of other forms of law to serve Union objectives, is seen most vividly with the three central treaty responses to the crisis. The European Financial Stability Facility (EFSF) Treaty, ESM Treaty and TSCG are all characterised as international agreements between member states which must comply with EU law, notwithstanding that the ESM required an amendment to Article 136 TFEU to allow its ratification[9] and it is anticipated that the TSCG will be integrated into the EU Treaties by 1 January 2018.[10] The implications of this go beyond the formal designation of the legal instrument (Chiti and Texeira 2013; Peers 2013). The ESM Treaty, for example, breaks from the established principle that the member states treat each other as equals by requiring that the granting of financial assistance

8 http://ec.europa.eu/economy_finance/indicators/economic_reforms/eip/#/headline/.
9 Decision 2011/199/EU amending Article 136 of the TFEU with regard to a stability mechanism for member states whose currency is the euro, OJ L 91, 6.4.2011, 1.
10 Article 16 TSCG.