FOUNDATION FOR EUROPEAN PROGRESSIVE STUDIES
FONDATION EUROPÉENNE D'ÉTUDES PROGRESSISTES

EuroVisions

The Difficult Birth of a New Treaty

Assessing the European Council of 30 January 2012

Maria João Rodrigues, Special Adviser in the European Union Institutions

For further information please contact Ernst STETTER, FEPS Secretary General at
ernst.stetter@feps-europe.eu

What has been at stake?

Treaty change has become a central issue in EU politics. A stronger "bazooka" is urgently needed to reduce spreads and to stop contagion in the euro-zone crisis. This can be a more assertive ECB, a stronger EFSF, Eurobonds or a combination of two or three of them. But there is a stumbling block: the German government is saying no. The maximum move this government can eventually accept would be an ECB decision for a larger operation in the secondary markets, directly or via the EFSF; later on, on a longer term perspective, some kind of "stability Eurobonds" might be considered.

But this German concession towards indispensable European solidarity will only come if Member States accept to partially transfer their budgetary sovereignty to the European level. The German parliament cannot be made responsible for budgetary decisions taken by other national parliaments, this is the argument made from the German side, thoughtful enough. More European solidarity will depend on more European authority. Hence, the German government is requesting some Treaty changes enshrining this transfer of sovereignty. These Treaty changes should complement the already defined ones to turn the EFSF into a permanent European Stability Mechanism, the ESM, which should be updated to take into account the recent EFSF reforms, in view of becoming a European Monetary Fund.

These stronger rules of fiscal discipline requesting a Treaty change are notably:
- (1) a stronger oversight of the budgets by the European Commission, in the spending and revenue sides, which should be previous to the discussion of the budgets in the national parliaments, particularly in the financially assisted Member States;
-(2) more automatic sanctions, also involving the European Court regarding the Member States not complying with their fiscal commitments;
- (3) a golden rule for balanced budgets to be enshrined in the national constitutions.

The political game

According to the first position of the German government, a limited Treaty revision, (maximum with a quick Convention and Intergovernmental Conference (IGC) would be enough to introduce these changes. Nevertheless, this is not the view of other Governments. The British Government claims it cannot accept such changes as they involve the transfer of more competences to the Union and argues that a normal procedure should be used, meaning a larger Convention and an IGC followed by national ratifications, which should be used to come back on other issues; in short, re-opening Pandora's box. These risks of undermining the Lisbon Treaty *acquis* are leading many key-actors to the conclusion that it would be wiser to confine the Treaty changes to euro-zone issues.

Hence, the next question is: what should be the key-elements of this Treaty change, notably deepening the content of Article 136 of the Treaty and/or Protocols 12 and 14 Treaty on the Functioning of the European Union (TFEU)? The German government would like to stick to its limited Treaty changes: just more fiscal discipline and the new ESM. Nevertheless, the French government argues that other Treaty changes are needed to better organize the

euro-zone: fiscal, tax and economic coordination, role of the EFSF/ ESM and the ECB as well as the euro-zone government, mainly on an inter-governmental basis.

For the French Government, if the negotiation of changes in the framework of the Lisbon Treaty becomes too complicated, a new Treaty could be quicker established by the euro-zone members on this inter-governmental basis, as this was the case for the Schengen Treaty. There also disturbing rumors on possible "Triple A elite clubs" reserving for themselves the issuance of euro-bonds. As this would be the direct passport for the implosion of the euro-zone and of European integration, these rumors were denied by both the German and French governments, but are being used by them to put pressure on other euro-zone partners.

As expected, the opposition from the UK led Merkel to accept Sarkozy's proposal of a new Treaty in their bilateral meeting on the 5th December. This proposal had the worst part of both proposals: the community method is being questioned and the content is only focused on austerity.

Last but not least, the last Euro-zone meeting had just recognized that EFSF leveraging solutions are falling behind what is needed to protect Italy, Spain (or France if it loses its Triple A rating). In the meantime, capital outflows are starting to undermine the euro-zone as a whole. Everybody knows that the EU has little time left to prevent a major disaster. But Merkel prefers to delay the ESM agreement and suggest that the ECB can go on with its unconventional measures. She needs a Fiscal Treaty to convince her domestic supporters to ratify the ESM Treaty.

Against this complex background, what should be the way forward to tackle the euro-zone crisis?

The PES leaders in their preparatory meeting have decided:

1. To call for immediate and strong action to stop contagion without waiting for a Treaty change: strengthening the European Financial Stability Facility (EFSF) with a credit line to be provided by the ECB and, in the meantime, to let the ECB act. To accept more fiscal surveillance at European level provided, this is combined with stronger instruments to support growth: macro-economic coordination should be developed on the basis of the new macro-economic surveillance; the Community budget should be more focused on supporting investment and complemented by the EIB, particularly by using project bonds and Eurobonds for investment. A financial transaction tax should be adopted to share the burden of the recovery with the financial markets and to reduce speculation
2. If a Treaty change becomes unavoidable- and this was now quite likely:
   a) To reject a Treaty change only limited to fiscal discipline: this would not be a "Fiscal Union", even less an "Economic Union", but just a straight jacket for an economic disaster
   (b) To be against opening a larger revision of the Lisbon Treaty because, in the present political conditions, this can lead to a major setback in the European construction;
   (c)To also avoid a new Treaty on an intergovernmental basis as this would undermine the community method.

Another possibility was also referred, but not considered: to prefer a development of the Lisbon Treaty focusing on euro-zone issues, but with a comprehensive approach regarding the content and an inclusive approach regarding the participants. The negotiation of this enhanced cooperation should be opened to all Member States willing to complete and join the Economic and Monetary Union (and which can be much more than the euro-zone members). With this approach, the effect of "two-speed Europe" should be as limited as possible. A comprehensive approach to develop the Lisbon Treaty should comprise the following key-elements:

- An EFSF/ESM counting on ECB credit line and preparing a larger issuance of euro-bonds and evolving to a European debt agency/Treasury
- A European budgetary coordination to ensure fiscal responsibility, but also room for key investments to promote a new kind of growth and sustain welfare systems
- Larger European economic coordination to promote the same objectives, using the new mechanism of macro-economic surveillance on deficit/surplus countries, and activating the Community budget and the EIB to support key investments
- Supporting upward convergence for better social and environmental standards
- Coordination to introduce a new tax, a financial transaction tax
- A more effective executive power in the euro-zone including its external representation, with respect for the community method
- A new role to be given to the European Parliament on euro-zone issues, in order to enhance democratic legitimacy.

What is at stake now is to overcome a dangerous crisis of European integration by completing the Economic and Monetary Union. But this should be made in a balanced and democratic manner, otherwise it will fail.

Key issues for an assessment of the European Council of 9 December 2011

To overcome the euro-zone crisis requires an inclusive, democratic and balanced deal. The deal for a new Treaty for a "Fiscal Stability Union" defined by the European Council on 9 December fell short of these three ingredients and has opened a difficult period of the European history.

Inclusive?

Most of member States (MS) have accepted the deal for a new Treaty not by conviction but in order to avoid financial and political isolation, in face of German pressure. The British PM has presented conditions which were in fact unacceptable as they would hinder the need to regulate the financial markets. This British self-exclusion involves risks for UK but also for the EU, since this has obliged the other MS to move to a risky operation of an inter-governmental Treaty.

Democratic?

An inter-governmental Treaty, if this is achievable in political and legal terms, might undermine the community method twice, in its ratification procedure and in its content. Regarding ratification, it is up to each MS to clarify which is the required procedure, and this will be a particular problem for Ireland, also possibly for the Czech Republic, Finland, Denmark, Sweden and Hungary. There will many political and legal controversies over the possibility to mention the role of the Community institutions in an inter-governmental treaty. Sooner or later, this one would need to be integrated in the Lisbon Treaty and this should require a normal revision procedure, involving a Convention and an IGC. The more the new policy developments are integrated in an enhanced cooperation in the framework of the Lisbon Treaty, the less Treaty changes will be extensive and complicated. The lack of a convincing and balanced proposal in this direction has led to the current split of the EU framework into two different Treaties: Lisbon EU Treaty and an intergovernmental Treaty.

Balanced?

- There is a German pressure to limit the new Treaty as much as possible to fiscal discipline. That is why this is already called the "Fiscal Compact Treaty" or the "Treaty for a Union of Fiscal Stability". A new target of 0.5% of structural public deficit should be enshrined in the national constitutions or equivalent, with an implementation to be enforced by automatic sanctions. Moreover, the Member States under financial assistance should be monitored by stronger surveillance and correction procedures.
- Besides the new concept of "European economic policy", there is nothing relevant about economic coordination, even less references to growth, investment, jobs creation or convergence. The developments already adopted concerning the institutional dimension of the euro-zone governance will not be included in the new Treaty.
- The references to common issuance of debt (Eurobonds) and the banking equivalence of the European Stability Mechanism (ESM) which had been included in the first version of the conclusions were withdrawn from the final one. The German veto was fully kept in spite of a large majority of PMs in favour of these necessary developments. Some of these PMs secretly hope that the German veto on Eurobonds will be lifted
- Once a stronger fiscal discipline is put on track. Under this very uncertain assumption, they have accepted an unprecedented deal which is completely unbalanced and which reduces the euro-zone crisis to a problem of lack of fiscal discipline.

Finally, the two improvements regarding ESM will be just included in another ESM Treaty which has been under negotiation: the principle of partial sovereign default will be excluded and the decision-making process no longer requires unanimity - showing that two big mistakes of the last months are finally recognized. Otherwise,

the resources of the EFSF-ESM remain limited to 500 Billion Euros, and the ECB should not buy sovereign bonds in the secondary markets, despite its new role to back EFSF-ESM in technical but not financial terms, and its new capacities to support banks capitalization. Last, but not least, the EU insists on looking for its international partners support, by providing fresh resources to the IMF- something which will weaken the European international status and strategic autonomy.

To sum up, something extraordinary has happened: the EU which is now confronted with a new recession has just decided to tighten the belt. From the viewpoint of the outside world and even of most of the financial markets, this is now probably considered a "lost case". From the viewpoint of many of European citizens, this will mean the ruin of the European project. The disaster was so evident that Merkel and Sarkozy are now already planning for a new Euro plus Summit in January to discuss growth and jobs.

Swift decision by the members of the European Council on the 30th January 2012

This special meeting of European Council's members was the first to introduce the terms "growth-friendly consolidation and job-friendly growth". It has also introduced some first measures to support SMEs and to address the dramatic increase of youth unemployment. Yet, the main focus of this meeting was to commit the maximum number of Prime Ministers with a draft Treaty which has been prepared with intensive work over Christmas time, by a specially convened Forum composed by two representatives from each government and three representatives of the European Parliament.

This Treaty has changed its title several times, reflecting the internal disputes, starting with "International Agreement on a Re-enforced Economic Union" and finishing as inter-governmental "Treaty on Stability, Coordination and Governance in the Economic and Monetary Union". In the end, all Prime Ministers, except the British and the Czech have announced they would sign the Treaty in the European Council of March 2012. However, it is important to note that the Treaty itself is setting that a number of just twelve Member States ratifying would be enough to ensure its entry into force. This was a mechanism to prevent the risks of a new negative referendum in Ireland or, who knows, to put some pressure on the emerging candidate in the Presidential elections in France –Hollande- who was announcing he would re-negotiate the Treaty.

Maria João Rodrigues has been a special advisor in the European Union institutions, working directly with Prime Ministers in the EU Presidencies and with European Commissioners. She was in the coordinating teams in charge of designing and implementing the European strategy for growth since 2000 and of negotiating the Lisbon Treaty in 2007.
She has also been involved in the preparation of several summits between the EU and its strategic partners such China, Russia, Brazil and USA. Finally, she has been member and chair of several high-level groups to prepare EU political initiatives. She is also professor of European economic policies in the Universite Libre de Bruxelles and in the Lisbon University Institute.
Building on her experience of preparing meetings of the European Council for twelve years, she provides a special insight on the context, background and critical assessment of these meetings where the EU political direction is shaped. European politics need to be debated to be better understood and to become more relevant for European citizens. This is the purpose of these comments.