EUROPEAN

POLICYBRIEF

WHO IS AFRAID OF TREATY REFORMS?

EMU CHOICES

PolicyBrief n. 2, February 2019

Consensus prevails that the EMU requires reforms. Economic and financial crisis measures stretched the rigid and limited legal fundaments to their utmost boundaries and provoked watering down, mutating or even circumventing the existing Treaty limits. Instead of continuing with the same pattern when pursuing further reforms we advise to not only adjust the underlying constitutional EMU framework substantively, but address also the rigidity of the EU Treaties as such by de-constitutionalising EMU law.

INTRODUCTION

The final choice for creating a common currency area was taken more than 25 years ago. With the Treaty of Maastricht the EU Member States set a milestone in the integration process. They achieved an agreement to set up a common monetary policy at Union level. By contrast, economic and fiscal policies, even if closely linked to the monetary system remained in the hands of the Member States. They were only obliged to conduct their economic policies as a matter of common concern and respect the EU rules on sound public finances and sustainability of the balance of payments.

The economic and financial crisis hit the Eurozone hard and revealed the weakness of the economic governance regime and challenged considerably the functioning of the Eurozone system. The difficulties were addressed by numerous and various measures. The Stability and Growth Pact was extensively reformed, the so-called Fiscal Compact aiming at stricter fiscal discipline was adopted, the ECB announced and deployed both conventional and unconventional monetary policy measures, the Banking Union was installed, and financial emergency assistance instruments were created. These actions,

mostly adopted under considerable time pressure, impacted decisively on the economic governance framework and the interpretation and application of the underlying Treaty rules. However, any debate about a necessary Treaty reform as such was cautiously avoided. To the contrary, the legal foundations were stirred up and several of the adopted measures entailed controversial legal contestation, including decisive courts' rulings at national and EU level.

Mostly in reaction to the crisis, it is widely recognised that further developments to ensure a robust and resilient framework for the currency union is imperative. Various reform initiatives floated both tackling short- and long- term perspectives. Remarkably, the same pattern of avoiding even to mention respective Treaty reform is repeated. We detect a constant fear of Treaty change failure.

EVIDENCE AND ANALYSIS

Stability and Growth Pact

The obligation for EMU Member States to conduct sound public finances and a sustainable balance of payments was set as a core principle of the EMU system. Still, its effectiveness proved to be rather poor. This was addressed quite swiftly by reforming the Stability and Growth Pact in the form of the so-called six-pack and two-pack legislation. Thereby, a complex set of rules evolved since their inceptions as rather lose economic and fiscal policy coordination by the Treaty of Maastricht. Certain novelties, such as the introduction of a new sanctioning mechanism for the multilateral surveillance procedure or the insertion of the reverse majority voting for EMU decision-making triggered fierce academic controversies arguing their trespassing of EU Treaty limits.

Treaty on Stability, Coordination and Governance

Distinctively more political as well as legal concerns raised the adoption of the Treaty on Stability, Coordination and Governance in 2012, which is closely connected and in support of the EMU system. Further reinforcement of national budgetary obligations to be geared towards stricter supranational budgetary limitations – most importantly a lower limit of the annual structural deficit of 0,5% of the GDP at market prices – could not be achieved under the Treaty framework due to the resistance of some Member States. As a consequence, the willing states left the EU legal sphere by adopting the so-called Fiscal Compact as intergovernmental agreement, which included an obligation to implement those limits "through provisions of binding force and permanent character, preferably constitutional". Evidence of legal concerns regarding its compatibility in particular with the national constitutions are the several motions for national constitutional review, such as in Austria, Belgium, France, Germany and Poland.

European Stability Mechanism (ESM)

Certainly, the systemically most crucial and controversial development of the EMU was the instalment of financial emergency assistance instruments for Member States suffering from solvency and liquidity problems. It started with the euro area Member States together with the International Monetary Fund providing ad hoc assistance to Greece in the form of coordinated bilateral loans in 2010. Later on, temporary stability facilities, open to other Member States, were created in terms of the EU instrument of the European Financial Stability Mechanism and the European Financial Stability Facility established under Luxemburgish private law. Most controversies however were raised on the legality of the establishment of a permanent European Stability Mechanism, being in force since October 2012. Due to the limits and the rigid EU Treaty structure the ESM was created outside the EU framework, however with strong links to it, both substantially and institutionally. It was in this context that a respective Treaty amendment was adopted, in fact the only one undertaken in the course of the crisis. The introduction of the third paragraph in Article 136 TFEU, entering into force on 1st of May 2013 was claimed to be necessary to ensure legal certainty. It states, "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". The German government, not the least in the eyes of the German Constitutional Court, considered the amendment was required to accommodate the change allowing financial assistance to Eurozone members. The CJEU, by contrast, qualified in its Pringle ruling the legitimizing amendment of Article 136 TFEU as only declaratory and approved the legality of the ESM Treaty already before the entering into force of Article 136(3) TFEU. What is more, fundamental legal concerns on the compatibility of the ESM Treaty with the EU Treaties as well as national constitutional laws materialised in judicial appeals, both at national constitutional and EU level. In the end, all rulings legitimized almost all hotly debated aspects and thereby contributed to avoid a legal collapse.

It must be noted that this resulted in essential changes in the reading of the underlying rules, such as the no-bailout rule, without according adaption of the primary law. One guiding principle for the stability of the euro area is outlined as the obligation and responsibility for Member States to effectuate sound public finances and sustainable balance of payments. It is assumed that financial markets would, through eventually imposing high interest rates as 'sanctions' for excessive annual deficits and overall debts, exert sufficient pressure into the direction of sound Member States' budgets. The Treaties only foresee Union financial support for Euro area members under certain conditions in case of exceptional occurrences beyond the Member State's control as outlined in Article 122(2) TFEU. With the CJEU Pringle ruling, this market-based

paradigm comes close to being substituted by setting strict conditions to the assistance in the form of structural reforms 'enforced' by the lending states.

European Central Bank (ECB)

At the second front of EMU, monetary policy, the European Central Bank stepped in as a decisive "problem solver" during and in the aftermath of the crisis. Besides applying conventional monetary policy, such as interest rates cuts or the expansion of the collateral list, it announced and deployed unconventional monetary policy measures with the ambition of "doing whatever it takes". Its bond buying schemes in the private and public sector made the ECB the largest creditor in the euro area and affected the liability structure and its independent status. The accusation of the ECB overstepping its mandate was brought before the German Constitutional Court which in turn, in its first preliminary reference ever, asked the CJEU for scrutiny. The latter upheld the measures as legal, in approving the ECB's changing role and the broadening of its powers, argueably thereby impacting on future ECB measures in the field.

Banking Union

Furthermore, in addition to its monetary policy competence, the ECB was conferred upon prudential supervisory tasks of credit institutions within the Single Supervisory Mechanism. The ECB became the core supervisor in the Banking Union of significant financial institutions. It follows that these new functions relating to the same policy recipients in the monetary policy field, create tensions regarding the different underlying objectives, price stability on the one hand and financial market stability on the other. Thereby, the ECB's prime objective and role under the Treaties ensuring price stability was considerably modified without any adjustment of the formal rules.

In addition, the establishment of the Banking Union led to the emergence of a set of new agencies, such as the European Banking Authority, the European Systemic Risk Board or the European Securities and Markets Authority. The far-reaching delegation of both discretionary and legally binding powers to such agencies resulted in an essential change of the institutional landscape, and produced legal challenges. The CJEU accepted and arguably overthrew its previous, longstanding, and more restrictive jurisprudence in this regard.

Constitutional 'Mutation'?

All in all, the crises revealed that the initial EMU architecture is imperfect by focusing on the prevention of financial distress but neglecting the case of difficulties. These shortcomings were admitted and addressed in particular in reaction to the crisis. By means of secondary law, intergovernmental treaties and political agreements, a complex system of economic governance emerged. As outlined, both substantial as well as institutional changes were adopted. Quick solutions were found, however, arguably at the price of circumventing the EU legal framework or exceeding the given EU rules. The fear of tackling Treaty reforms led to stretching the law to the outmost,

sometimes neglecting, sometimes violating it, but neither properly enforcing nor amending it, as it should be. This puts the rule of law, a fundament of the EU Treaties under stress and creates remarkable uncertainty, as reflected in the numerous constitutional challenges before national and EU courts.

A Persistent Policy of Muddling-Through

The same pattern of avoiding any Treaty revision can be witnessed in the communications and reports for EMU reforms tabled by EU officials. The message of the Four Presidents' report and the Commission's Blueprint of 2012, the 2015 Five Presidents' report and the White Paper and Reflection Paper of 2017 indicate only the general direction of reforms towards completing the EMU. The Commission's legislative proposals of the Saint Nicholas package of 2017 finally suggest a first comprehensive package of legislative proposals and initiatives. However, it is to be critically observed that just as the crisis management measures any respective Treaty change is still cautiously avoided even though the reform initiatives touch upon the fundamentals of the EMU. To the contrary, the assumption prevails that the transformation of the ESM into a European Monetary Fund, the creation of a euro area fiscal capacity or new structural convergence tools are fully in line with the existing Treaty framework. Other initiatives such as the installation of a European Minister of Economy and Finance certainly make the impression of being a strong further step, however when examined more precisely the initiative is rather cosmetic by refraining from equipping it with any new and significant competences.

In addition, several specific proposals of the past, such as the installation of Eurobonds or a Redemption Fund and Pact, legally not feasible under the existing framework, were dropped at all.

The resulting danger is obvious: Refraining from proposing amendments of EMU-related Treaty provisions leads to half-hearted reforms. They may not achieve the 'completion' of the EMU while they might nevertheless stretch or even overstretch the legal fundaments. The consequence might not be the stabilisation aimed at but continuing with a destabilising 'muddling-through-policy'.

POLICY IMPLICATIONS AND RECOMMENDATIONS

As outlined, the crisis management measures as well as reform initiatives reveal certain hindrances for desired developments in the field of the EMU. In fact, what can be learnt from the past is that the rigidity of the Treaty amendment process, requiring all Member States' consent and ratification according to the national laws, is a 'constitutional' deadlock for further integrative steps in the field. The veto position given to each Member State easily impedes necessary developments. Treaty revisions have become

a rocky endeavour as can be witnessed by the Lisbon Treaty in 2009 being postponed after failure of ratification in Ireland or the failed ratification of the Constitutional Draft Treaty of 2004 in France and the Netherlands. As a consequence, the institutional and substantive provisions in the field are frozen and the fear of Treaty change failure seems to prevail impacting heavily the economic and monetary union framework.

Admittedly, substantial Treaty revisions may be difficult to achieve, however before the explicit objective to complete the EMU by 2025, this needs to be tackled.

Thus, we suggest addressing and advancing the existing 'constitutional' system by terminating the mechanisms of facile blockage for each Member State and provide for feasible reform options by majority decision.

We recommend, especially after years of turmoil, a clear call and postulate for adaption of the EMU Treaty provisions. As mentioned, several related issues led to legal controversies and uncertainty as reflected in numerous judicial review applications and rulings before national courts as well as the EU courts.

The substantive leap forward towards a completion of the EMU should go hand in hand with constitutional reform both at EU but also at national level. It should address the very detailed but limited economic governance provisions in the EU Treaties.

The debate about a Treaty reform should be started now, instead of eventually further circumventing or watering down the given Treaty limits and thereby also threatening the essential rule of law principle being a fundamental EU value explicitly anchored in Article 2 TEU. The immediate start of a public debate is elementary in order to achieve the explicit objective to complete the EMU by 2025. Given that what is at stake certainly requires an ordinary revision procedure under Article 48(2)-(5) TEU, a powerful initiative would be a joint undertaking of those 'in charge' under this provision: governments of Member States – a coalition of the 'frontrunners' advocating deepening the EMU would be desirable – together with the European Parliament and the Commission. The more, the better. However, if such a joint effort should be beyond reach, also a smaller group should not be afraid to propose what appears to be well founded on the basis of past experience and conceptual reflection. Do we always have to wait for the next crisis to get things moving? Academia should advocate a more rational approach.

Instead of launching deficient proposals not meeting the needed substantive reforms or triggering legal controversies and uncertainty regarding their conformity with the Treaties, we recommend a debate on changing the rigid and limiting current Treaty framework as such. We advocate the creation of an adequate legal basis, which allows for swift action in times of crises, and the option of policy adjustments without immediately triggering the need of a Treaty change. Why, if broad consensus affirms the necessity of substantive reforms, should it at the same time be impossible to achieve a Treaty change if it can be established that reforms would remain deficient

without it? Why should it be impossible to convey this message in a public debate? At least from an academic point of view, this question has to be raised again and again.
In this sense, we suggest moving towards de-constitutionalising the economic governance provisions. The detailed economic governance provisions in the Treaties should be replaced by more flexible ones allowing for swift and deliberate change without cumbersome Treaty revision. The economic and monetary system being exposed to rapid economic changes requires a corresponding capacity for dynamism and adaptability of the regime. Inspiration should be drawn from Article 126(14) TFEU allowing the Council, by a special legislative procedure, instead of a Treaty amendment, to unanimously replace or specify single or all provisions and aspects of the Protocol No 12 on the Excessive Deficit Procedure. In this vein, but going even further, the EMU should be equipped by a supranational governance system which would be fully integrated into the existing EU framework. This would involve increasing qualified majority voting to enhance the dynamics of the integration process, as it had been done, long time ago, in the field of the internal market. It goes without saying that this would have to include the European Parliament on equal footing with the Council in all instances of legislation.

RESEARCH PARAMETERS

Complementary to the political science research, the legal part of the EMU Choices project assesses the legal feasibility of economic and fiscal integration against the backdrop of EU law as laid down in the Treaties since the Treaty of Maastricht. It includes the investigation of the monetary, fiscal and economic related integration measures adopted since the Treaty of Maastricht, in particular in the events of the crisis. Furthermore, the respective reform scenarios, in particular those outlined by the EU institutions, are subject of the legal research. Moreover, further research focus is put on the national constitutional laws and systems, which is fundamental for the scrutiny of legal feasibility of EMU integration measures.

PROJECT IDENTITY

PROJECT NAME

The Choice for Europe since Maastricht. Member States' Preferences for Economic and Financial Integration (EMU_SCEUS; see www.EMUchoices.eu). Horizon 2020 funded project - Grant number 649532.

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It is based on Elisabeth Lentsch (2017), Report on the institutional consequences of fiscal and economic integration, Elisabeth Lentsch (2018) Report on the compatibility of reform scenarios with the EU Treaties and Stefan Griller and Elisabeth Lentsch (2019 forthcoming), Why the EU's Constitutional Deadlock is hampering EMU Reforms, and how this could be Resolved.

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EUROPEAN NETWORK OF NATIONAL CONSTITUTIONAL LAWYERS

FUNDING SCHEME

Horizon 2020 Framework Programme for Research and Innovation (2014-2020), EURO-1-2014: Resilient and sustainable Economic and Monetary Union in Europe

DURATION

July 2015 – June 2019 (48 months).

BUDGET

EU contribution: EUR 2,150,794.00

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FURTHER READING

www.EMUchoices.eu/publications