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# Should the eurozone be less intergovernmental?

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***Since the economic and financial crisis, the institutional landscape in the EU has changed. While no structure in the EU is perfectly intergovernmental or supranational, we have witnessed an increased tendency to introduce intergovernmental elements in the Economic and Monetary Union architecture during and after the crisis. While such an approach was warranted at the time of the crisis, it should not become a permanent feature of the economic governance framework. In order for the single currency to succeed, Member States need to reduce national biases in decision-making leading to an inefficient equilibrium and recreate a "veil of ignorance" by refocusing on their common goals and fostering trust between each other and in EU institutions.***

(*) The information and views set out in this article are solely those of the authors and do not necessarily reflect the official opinion of the European Commission.

### *1. Intergovernmentalism vs Supranationalism: which structure for the Economic and Monetary Union?*

The question whether different areas of cooperation are characterized by intergovernmental or supranational elements goes back to the inception of the European Union and the different communities preceding it. Different theories of integration attempt to explain the process and the key drivers of integration based on two different perspectives: From an intergovernmental point of view, national governments are the central actors of the integration process whereas from a supranational angle, integration triggered by sovereigns evolves independently of national governments (Bache et al. 2015).

Structures and institutions within the EU are neither purely intergovernmental nor supranational and the balance of intergovernmental and supranational features can change over time. Different areas of cooperation can therefore entail varying degrees of intergovernmental or supranational elements. In a number of areas, decisions are subject to unanimity, to preserve "vital" interests of individual Member States while discussions take place within a supranational framework. This is for example the case for common foreign and security policy (with some exceptions requiring qualified majority, e.g. appointment of a special representative), EU finances and the harmonisation of national legislation on indirect taxation.[1]

The recent economic and financial crisis highlighted the need for more coordination and brought about further integration but also revived the discussion on how competences should be divided between the EU institutions and its Member States. In this respect, the binary choice seemed to be between the intergovernmental method and the community method; the latter is characterized by the sole right of the European Commission to initiate legislation, co-decision by the Council and the European Parliament, and qualified majority voting in the Council. However, the German Federal Chancellor, Angela Merkel, in 2010 shaped the concept of a new "Union method" which she defined as "coordinated action in a spirit of solidarity"[2]. EU institutions and Member States are supposed to act in accordance with the competences assigned to them by the Treaties, with the main goal being the achievement of a common position notwithstanding which method is used.

With the EU Treaties largely unchanged through the crisis, and limited scope for action in some areas through secondary legislation, further integration led to increased policy coordination of Member States. While there has been a strengthening of supranational institutions in particular in the area of banking supervision and the implementation of the Stability and Growth Pact (Dehousse 2016), overall, the revisions in the framework of economic governance in Europe largely followed an intergovernmental approach. This led to an integration paradox and what some

[1] There is an ongoing debate whether unanimity could be overcome in some of these fields. In particular, in the area of taxation the Commission presented a Communication in January 2019 to move gradually from unanimity voting to the ordinary legislative procedure.

[2] Text of the full speech: https://www.coleurope.eu/events/mrs-angela-merkel-delivered-opening-address-opening-ceremony

scholars define as ‘***new intergovernmentalism***’: Member States pursued more integration but resisted further supranationalism (Bickerton et al. 2015).

## 2. *The “new” economic governance framework*

The recent economic and financial crisis led to a considerable improvement of the economic governance architecture while preserving the fundamental principles of the Treaty of Maastricht: centralized monetary policy and decentralized but coordinated economic policies.

***Fig 1. New economic governance framework***

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| **1. Crisis Management** | | | |
| *Crisis Resolution Mechanism* | European Financial Stability Facility (EFSF) | International Treaty | Intergovernmental |
| | European Financial Stabilisation Mechanism (EFSM) | EU regulation | Supranational |
| | European Stability Mechanism (ESM) | International Treaty | Intergovernmental |
| **2. Financial Union** | | | |
| *Banking Union* | Single Supervisory Mechanism (SSM) | EU regulation | Supranational |
| | Single Resolution Mechanism (SRM) | EU regulation and International Treaty | Supranational and intergovernmental (Financial arrangements of Single Resolution Fund, SRF) |
| *European System of Financial Supervision (ESFS)* | European Systemic Risk Board (ESRB) | EU regulation | Supranational |
| | European Supervisory Authorities (EBA, ESMA, EIOPA) | EU regulation | Supranational |
| **3. Economic surveillance** | | | |
| *Fiscal coordination* | Stronger preventive and corrective arms Stability and Growth Pact | EU regulation | Supranational |
| | Introduction of an annual process for economic and budgetary policy coordination | EU regulation | Supranational |
| | Requirements for national fiscal frameworks | EU directive | Supranational |
| | Treaty on stability, coordination and governance | International Treaty | Intergovernmental |
| | Establishment of independent advisory European Fiscal Board | Commission decision | Supranational |
| *Economic coordination* | New procedure for correcting macroeconomic imbalances | EU regulation | Supranational |
| | Establishment of National Productivity Boards | Council recommendation | Supranational |

In order to safeguard the financial stability of the euro area and its Member States, the European Stability Mechanism (ESM) was established based on an intergovernmental treaty, following its temporary precursor (the European Financial Stability Facility, EFSF). This treaty is currently under revision following an agreement by Member States to strengthen the role for the ESM in financial assistance programmes, develop further its precautionary instruments and to cater for the provision of the backstop to the Single Resolution Fund (SRF). One of the main achievements of the past years was the agreement to set up a Banking Union comprising a Single Supervisory Mechanism (SSM) and a Single Resolution Mechanism (SRM) for banks, both being part of the community framework. At the request of the Council – due to legal uncertainties related to the legal base of the SRM – the transfer of the contributions to the SRF and the mutualisation of the financial resources in the national compartments were regulated through an Intergovernmental Agreement (IGA). However, the agreement included a clause that steps would need to be taken to incorporate the IGA into the legal framework of the Union within ten years of the date of its entry into force. Economic policy coordination, as well as the underlying rules, were strengthened considerably. Heads of States and Governments of the euro area also agreed on a new Fiscal Compact, which complemented the revised EU fiscal framework. Due to the absence of unanimity among Member States to include the Fiscal Compact in the EU legal framework, including by means of a Treaty change, it was adopted as an intergovernmental treaty. The so-called Treaty on Stability, Coordination and Governance (TSCG) was signed by all EU Member States except for the United Kingdom and the Czech Republic and foresees the eventual incorporation of its substance into Union law. The Commission made a proposal to this end.

There are a number of reasons behind the shift towards an intergovernmental working mode during and after the crisis. In many instances, this approach was the only option during the turmoil since the EU Treaties and the budget did not provide the necessary competences to safeguard the stability of the euro area within a very tight timeframe and under extreme stress. This was exacerbated by the fact that changing the EU Treaties would have required unanimity. The response to the crisis was also shaped by an increased role of the European Council and the Council in economic governance. Since the start of the economic and financial crisis, the European Council has not only provided the necessary impetus for the Union's development and defined the general political directions and priorities but it also played an increased role in day-to-day politics. Furthermore, informal working methods started to prevail. Key strategic policy discussions have increasingly taken place in the Eurogroup, instead of the ECOFIN Council[3], with the latter essentially becoming primarily a law-making forum (Puetter 2012). Importantly, the use of the intergovernmental approach was also favoured since Member States pledged significant new national resources in the framework of assistance programs which needed to be matched with the adequate accountability on the national level.

### *3. Is the new intergovernmental model successful?*

Undoubtedly, the euro area crisis has laid bare multiple compromises, which were the result of the integration process and were motivated by the need to preserve the Union's unity. As Fabbrini (2014) pointed out, Denmark's and the United Kingdom's decision to stay out of the euro reflects the existence of diverse preferences concerning the economic and monetary integration and more broadly economic policies: in this case, agreement on the goals – economic growth and price stability – but not the same means. Intergovernmental agreements can therefore help to pursue integration of those willing to cooperate more closely or at different speeds and be a strategic opportunity and a catalyst for a deepened EU.

[3] This, however, has changed lately since the Eurogroup in inclusive format (all EU Member States except for the United Kingdom) has allowed EU Member States to come back to the table.

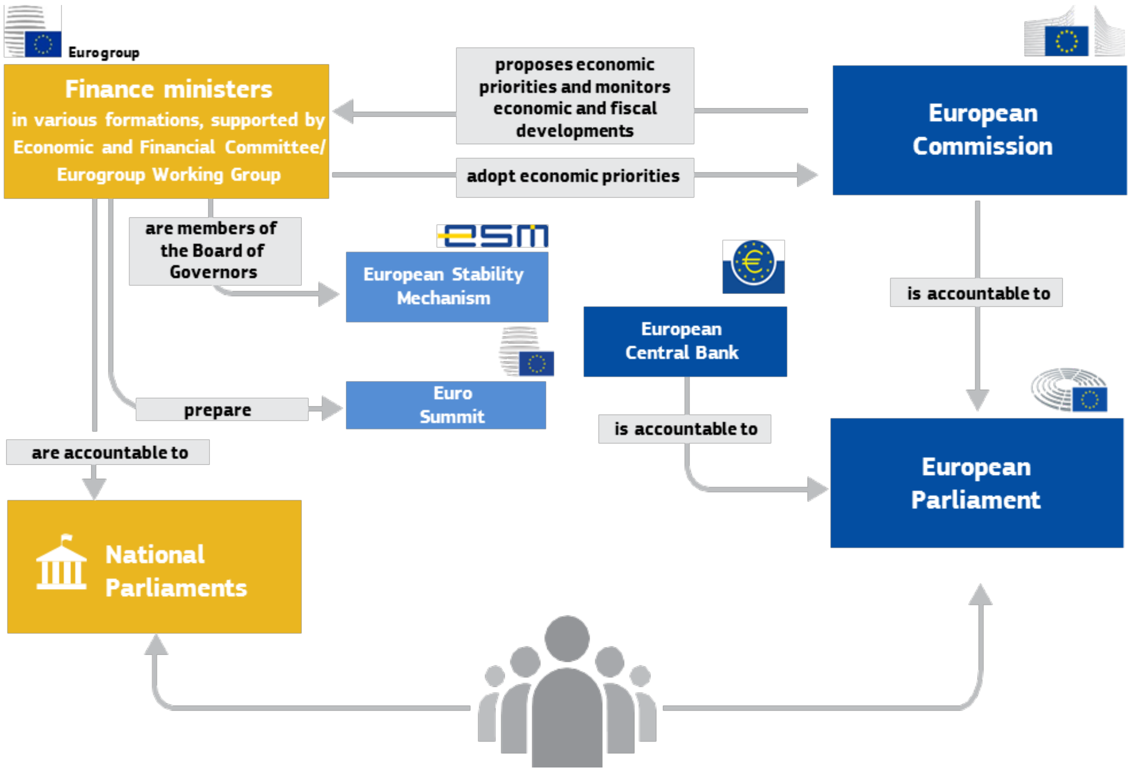
Various scholars advocate for a multi-speed Europe consisting of different clubs or clusters in particular in light of a further enlargement of the EU. Schmidt (2019a) suggests an EU "***as soft-core of multiple clusters of Member States, in which any duo or trio of Member States would take leadership in any given policy community***". Member States could therefore intensify cooperation in policy fields in which they have an interest in working together while participation in the Single Market and the respect of fundamental social and democratic rules as well as common institutions and legal systems are a perquisite. Voting would be restricted to policy areas in which Member States participate. Similarly, Demertzis et al. (2018) presented a new structure for Europe that should break the existing stalemate. Member States would be part of a "bare-bones EU" consisting of a set of policies and could then choose to integrate further and participate in multiple clubs open to all.

Challenges related to differentiated integration can be eased if such a cooperation is organized within the EU legal framework. However, under certain circumstances enhanced coordination outside the EU legal framework can be beneficial if it follows the notion of "intergovernmental avant-garde". This means that that intergovernmental agreements should fulfil the following criteria: all Member States have the opportunity to join, the role of EU institutions is strengthened, no new parallel institutions are set up outside the EU legal framework and there is the willingness to integrate such structures into the EU framework as soon as possible (Emmanouilidis 2012). Looking at the reform initiatives of the past years, not all the intergovernmental structures fulfill the last two criteria. While intergovernmental features have been and will continue to be a part of the EU framework, the question arises whether the current economic governance framework works efficiently and whether the status-quo should be preserved.

We see several drawbacks linked to this system.

**(1) The new system is perceived as being complex and difficult to understand.** Due to the reforms in the past years, the current system is criticised as too complex and opaque and therefore difficult to apply (Tuori and Tuori 2014). Whereas monetary policy is centralized and assigned by the EU Treaties to the ECB which regularly reports to the European Parliament, economic and fiscal policy is decentralized. Economic and fiscal policy remain national competences although thoroughly coordinated at the Union level in various fora often with the involvement of different stakeholders: these fora and institutions have their own Chairpersons and Presidents, their own accountability and in some cases accounting systems (European Commission 2017).

*Fig 2. Stakeholders in the economic governance framework*




*Source: European Commission 2017*

(2) **The decision-making, including the principle of unanimity, might delay or hamper processes.** The decision-making process under an intergovernmental method usually requires a consensus, and often involves additional national procedures which make it difficult to reconcile with the speed needed for ensuring an effective crisis management. This is illustrated by the use of the European Financial Stability Mechanism (EFSM), a temporary crisis mechanism backed by EU budget guarantees, to provide bridge finance to Greece in July 2015: amending an EU Regulation and deciding to use it proved in practice to be quicker than taking an ordinary ESM decision of disbursement.

(3) **Democratic accountability is not always ensured at the appropriate level.** The basic principle of democratic accountability is that accountability should be ensured at that level where the respective executive decision is taken, while taking into account the level where the decision has an impact (European Commission 2012). As Buti and Lacoue-Labarthe (2016) show, it is hard to achieve effective democratic checks and balances when decisions affecting the euro area as a whole are taken by national institutions. While democratic accountability of intergovernmental institutions such as the ESM is ensured on the national level, albeit not in a uniform way across countries, the ESM only has an informal relationship with the European Parliament although decisions on granting financial assistance affects the euro area and its Member States as a whole.

(4) **Intergovernmental features can lead to imbalances between state equality and state power.** The community method tries to reconcile the principle that all states are equal while acknowledging the role of larger states and, through various checks and balances, normally delivers an agenda in the interest of all. The increased role of the European Council and hence intergovernmentalism changed that balance by providing room for the domination of larger states (Fabbrini 2015). However the dividing line did not only run between small and large Member States but also between conflicting preferences of debtors wanting more risk sharing and creditors pushing for more risk reduction. The outcome of negotiations in an intergovernmental setting is directly related to the bargaining power which favoured creditor countries since the immediate consequences resulting from the crisis would have hit debtor countries much more. Furthermore, intergovernmental negotiations are characterized by brinkmanship bargaining behavior leading to delaying rescue initiatives and adjustment policies (Schimmelfennig 2015). In the absence of a unified view on how to improve the architecture of the EMU, Member States adopted a piecemeal approach, fixing the parts of the architecture of the Economic and Monetary Union essential for its "survival" instead of agreeing on a roadmap for its medium term evolution (Pisany-Ferry 2015) which would be in the common interest of all. The current framework therefore reflects an accumulation of decisions based on 'ultima ratio'.

(5) **Intergovernmental institutions and bodies do not have the same transparency standards that are in place for EU institutions.** According to Article 15 of the Treaty on the Functioning of the European Union, "***the Union's institutions, bodies, offices and agencies shall conduct their work as openly as possible***". This means that citizens have the right of access to documents of the institutions unless disclosure would undermine the protection of the public interest as regards the financial, monetary or economic policy of the Community or a Member State or the privacy and the integrity of the individual amongst others. Such requirements are not in place for example for intergovernmental institutions and bodies.

## 4. Way forward: recreating the "veil of ignorance"

As Schmidt (2019b) highlights politicization of the EU – defined as the process of political awareness and the engagement in politics – has increased over time which expanded the influence of national politics on the position of Leaders in the European Council. However, there is a conflict between national interests mainly between creditor and debtor countries on the distribution of the adjustment burden (Delatte 2018) which together with a lack of trust between countries as well as in the EU institutions (Demertzis, 2018) can stall necessary reform efforts, produce an inefficient equilibrium and lead to outcomes and structures that are in many instances complex, lack transparency and democratic accountability is based solely on national institutions. Intergovernmental negotiations fail to give convincing and durable responses to challenges, which in turn lead to additional integration steps to correct deficiencies related to previous action (Piattoni 2017). The result is a "failing-forward" approach (Jones et al. 2016) leading to institutional incompleteness because agreements are based on the lowest common denominator. Advancing integration through a sequence of incomplete reforms can make the economic adjustment more difficult and lead to permanent output losses. In turn, the weaker economic performance undermines public support for the European project in the long-run and influences national preferences on which basis decisions are taken in the European Council.

In order to overcome this problem, Member States need to recognize and acknowledge the links and benefits between the national and the EU level and revert back to the community method. Against this background, the Commission has proposed a number of reforms in the past years to address the deficiencies related to the current system. The aim of the reforms was to favour solutions within the Treaties, in order to deliver democratic accountability at all levels and they contributed to the euro area speaking with one voice. In December 2017, the Commission presented a proposal to develop the ESM into a European Monetary Fund anchored within the EU's legal framework and to integrate the substance of the Treaty on Stability, Coordination and Governance into EU law. Furthermore, it presented a Communication to establish a European Minister of Economy and Finance who could serve as Vice-President of the Commission and chair the Eurogroup and who would amongst others pursue the general interest of the EU/euro area economy. In the past few months, intense discussions have taken place on the issues addressed by the Commission, but only in some cases the supranational approach has been followed.

The use of intergovernmental solutions was certainly unavoidable during the crisis. However, an ad hoc model of integration based on an ultima ratio approach, which does not rely on the EU Treaties and does not use the EU institutions, contains important risks for its stability. As Buti et al. (2019) have pointed out, a shared narrative is necessary to rebuild trust. In this respect, recreating Rawls' "veil of ignorance" can help Member States to revert to the common goals and leave behind their national resentments and narrow self-interest. The cooperative approach on which the Community method is built can bring wins for all.

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