

## **The European Republic** Policy Proposals for a Future Constitution

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## **Policy Proposals for a Future Constitution**

by Stefan Collignon

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## **Introduction**

The ink on the enlargement Treaty of the European Union had not even dried, when policy-making in the new EU was already confronted by its first crisis over the common foreign policy on Iraq and relations with the USA. The division into “new” and “old” Europe is an early warning of problems the European Union will face after enlargement to 25 member states in May 2004. The heterogeneity of economies and cultures, views, preferences and policy objectives will prevent efficient policy-making, unless the future European Constitution establishes institutions and procedures that will involve European citizens in the formation of collective policy. The pace of European integration has accelerated in recent years. A single market with a single currency has produced an increasing number of collective public goods. These areas of common policy concern are Europe’s ‘*res publica*’. They require new forms of governance, which I call a European Republic. The in-depth analysis can be found in the study prepared for the Bertelsmann Foundation: Stefan Collignon, *The European Republic: Reflections on the Political Economy of a Future Constitution*. The Federal Trust, London, 2003. This text summarises the main arguments.

### **I. The Looming Crisis in the EU**

European integration has been one of the great success stories of the 20<sup>th</sup> century. Emerging from the turmoil of two world wars, its purpose has been to preserve peace and prosperity for European citizens. By integrating markets and creating common policy institutions, Europe’s citizens individually, and governments collectively, have also developed new forms of co-operation across borders. These new common practices have strengthened mutual respect and trust between European citizens, thereby contributing to the perception of common interests, if not identity, and to the convergence of broad policy objectives. Examples of this process have become apparent in the policy consensus on price stability leading to EMU, or in the recent popular opposition to the war in Iraq. But Europe has now attained a critical junction: Either it will consolidate its achievements in lasting democratic institutions, or the centrifugal forces of an enlarged Union will pull it apart again. The changing international context, the problems of collective action in large groups and the democratic frustration of Europe’s citizens require the leap to a Constitution ensuring Europe’s capacity to act. Otherwise, policy gridlock, Eurosclerosis and indecisiveness will gradually erode European integration. Without substantial increases in the democratic legitimacy of European policy-making procedures and institutions, the efficient management of Europe’s common concern’s will not be sustainable. I will first sketch out some broad trends in world developments, which will pose new challenges for policy-makers and then discuss the link between legitimacy and efficiency. Against this background we will be able to ask which forms of governance or policy-making regimes will be appropriate for meeting the challenges. In the second part I will draw the conclusions and implications for a European Constitution.

#### **The Changing Context of EU Policy-making**

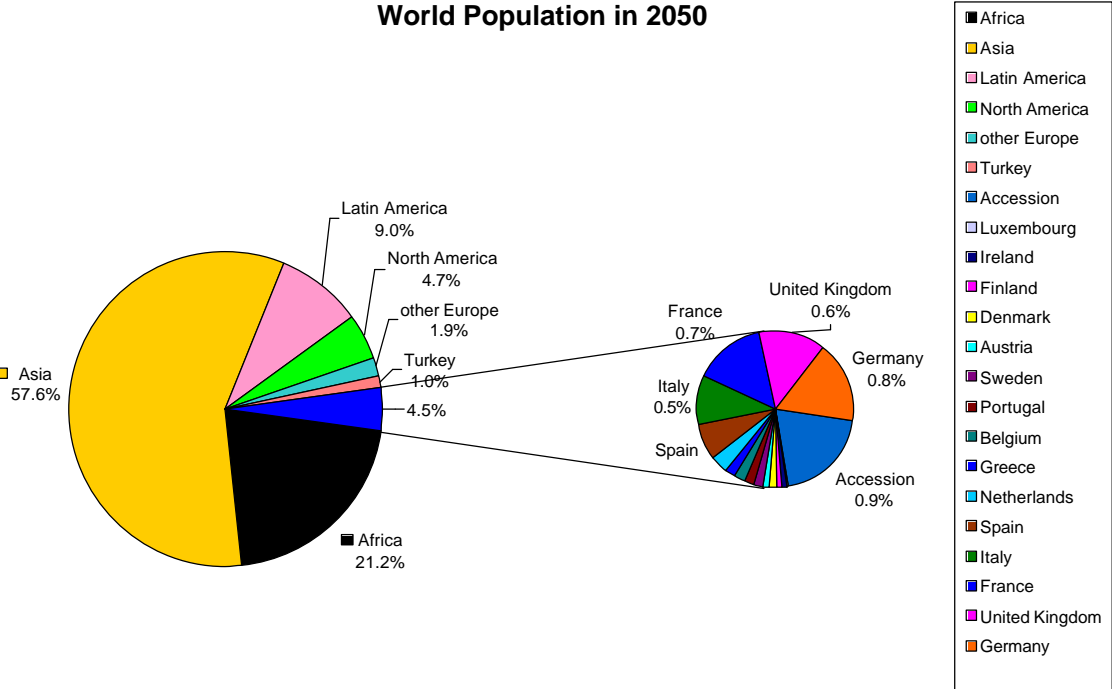
The global context within which European integration has taken place is changing. This structural transformation, due to population growth, technological change and

the dynamics of globalisation and the disappearance of the bipolar world, will profoundly affect the international power distribution.

At the end of World War II, 2.5 billion people were living on this planet. Today there are more than 6 billion and that number will increase to over 9 billion by 2050. These people need to be fed and their claims on natural resources will increase significantly. As a consequence, the number and the intensity of distributive conflicts in the world, often with recourse to military force, will also augment. Furthermore, these tendencies will cause large migrations across continents, exert disintegrating pressures on traditional cultures and societies and lead to violent and fundamentalist reactions. If Europeans want to live in peace, they will need to have the means to deal with these questions.

Population growth will not affect all regions in the world uniformly. Europe's population will shrink from 481 to 424 million. The EU15 share of the world's population will fall from 6 percent as it stands today, to 3½ percent by 2050 (8 percent to 4½ percent for EU 27, excluding Turkey). This will not only marginalize Europeans in the world, but also create serious problems at home for the distribution of income and wealth in an aging society. Moreover, technological progress and globalisation will transform economic structures, with dynamic growth poles strongly concentrated in Asia.

**Figure 1. Estimated World Population in 2050**



Yet, the most formidable challenge to European policy-making will probably result from the enlargement of the European Union. Policy-making along the current lines of intergovernmental bargaining will become increasingly complex in a Union of 25 or more members. This would be less dramatic if most member states had similar policy preferences, but the high heterogeneity in economic, political and social conditions

between the old and new members is reinforcing potential conflictuality between countries as we have recently seen in the area of foreign policy and military procurement. This danger is even larger, as US-foreign policy is no longer supporting the unification of Europe but recurs to *'divide et impera'*. Against this backdrop, the simplistic assumption that popular approval of the EU depends mainly on citizens' prosperity may easily turn out to be a strategic and counterproductive error.

Summing up the challenges resulting from Europe's changing international environment and enlargement will require a growing number of tasks and functions to be carried out efficiently only at the EU-level because individual member states do not have the means to manage them separately. In order to improve Europe's capacity to act, however, the European Union will have to improve its democratic legitimacy.

In democracies, citizens tolerate conflict over policies and accept the frustration of their preferences because they trust that their institutions are fair. They believe that they have a reasonable chance of convincing others about their own policy objectives in the process of public policy deliberation. Yet, the institutions and processes of policy-making in the European Union today are not conducive to create this foundation of trust, because European policy deliberation takes place between governments and administrations and not between citizens. Therefore, more democracy is needed in order to create loyalty toward European institutions.

Within this context, it is fashionable today to identify more democracy with decentralisation and subsidiarity. Greater proximity of decision-making to citizens would reflect different cultural backgrounds and heterogeneous preferences. However, this approach does not address the question of potential disagreement and conflict between local communities and national political constituencies, nor how policy preferences emerge and are changed through policy debates. As a consequence subsidiarity is hijacked by national bureaucracies who try to preserve national preference heterogeneity in order to legitimise their own power. This undermines both the efficiency and legitimacy of European policy-making. In order to understand how these problems can be overcome, it is necessary to review some theoretical concepts. This will allow us to distinguish between policy competences which need to be conferred to the European level and those which can produce efficient provisions of collective goods through voluntary policy coordination between autonomous nation-states. The hurried reader, who is not interested in the foundation of my arguments, may jump to part III.

### **The Efficiency of European Policy-making**

The efficiency of governance regimes is often assessed in terms of policy output in the form of collective goods and welfare and the cost of deliberative input into decision-making. The two are linked through the *principle of equivalence*. The consequences of a policy decision should reflect the preferences of those who are affected by the decision. The *equivalence principle* states that the jurisdiction providing specific public goods should cover all those citizens who are potential consumers of these goods. All in all, this principle was realised in the traditional nation-state, although the recent developments of globalisation and European integration have started to undermine its reality: (1) policy externalities have broken the correspondence between decision-makers and affected citizens i.e. the decision

by one administration may affect citizens living in other jurisdictions. We find this phenomenon most frequently in the European context, where progress in integration makes people more dependant on each other. (2) heterogeneous preferences between groups of citizens often lead to inconsistencies in public choices, unless appropriate institutions are established. If people cannot agree on substance, they must at least agree on procedures if violence is to be prevented. Policy externalities contribute to what I call type-I-inefficiencies, while type-II-inefficiencies are related to preference heterogeneity as a consequence of the constitutional policy framework.

### *Type-I-inefficiencies*

The incidence of collective goods depends on their function. While the construction of a hospital may primarily affect the local community, the building of a highway may have consequences with larger geographical impact. Starting from this observation, the theory of fiscal federalism has provided coherent criteria for assigning competencies to different levels of jurisdiction. For our purposes we will call all those goods and policies potentially affecting all European citizens *European collective goods*, while regional goods remain restricted to national or local communities. I will also call the set of people affected by a policy the 'policy domain'. Thus, the European policy domain is determined by European collective goods. Yet, policy decisions are taken with respect to political constituencies. The principle of equivalence demands that there should be a correspondence between policy domain and political constituency. Hence, *decisions on European collective goods must be taken at the level of a European constituency and not by national governments accountable to national constituencies.*

Inefficiencies arise, when policy decisions are taken in the context of a given jurisdiction or polity, but the polity and the scope of its competences is smaller than the range of its policy consequences. By polity we mean the system of institutions, norms and rules that are set up by constitutions and represent a given constituency. The failure to take into account the cost and benefits conferred to citizens of other jurisdictions may then lower welfare.

Type-I-inefficiency in policy-making is therefore similar to the externality problem of private markets (for example when a firm causes pollution to its neighbours). But while markets allow to internalise externalities by compensating the damaged party, policy externalities need to be internalised by deliberate *ex-ante* policy co-ordination. This means effectively enlarging the polity to the extent of the policy domain. European collective goods need a European jurisdiction and therefore also a European legislator who is responsible to a European constituency. This does not necessarily mean that all European collective goods must be provided by a centralized European government. But given that all European citizens are potentially affected by European collective goods, citizens must be involved in the deliberation of their collective preferences if policies are to be democratically legitimate.

### *Type-II-inefficiencies*

However, the broadening of the policy domain is only justifiable if it includes all potentially affected citizens. This may cause another set of inefficiencies. For, if the polity remains fragmented into segregated constituencies between different member states, policy co-ordination between national governments will cause preference

frustration. The academic literature calls this fragmentation phenomenon 'multilevel governance', where the objectives of national governments reflect the preferences of their constituency, while they bargain for compromise solutions at the European level. Yet, the negotiated equilibrium solution, "minimising the loss function", will usually frustrate at least some, if not all national policy preferences. For ordinary citizens a loss is a loss, even if minimised. Hence, the system is not efficient in linking the provision of European collective goods to low cost of decision-making.

In order to overcome this dilemma, it is useful to observe how policy objectives are formed in democracies. Political preferences emerge from democratic debates on arguments, in which citizens listen to each other. Voters elect those whose claims they find reasonable. Even if this debate does not always take place in the glaring light of a European public sphere as described by Habermas, the simple fact that individuals are connected within their society and give varying weight and respect to each others' arguments will ultimately lead to a convergence of their views and preferences. I have called this phenomenon 'stochastic consensus'. It describes consensual policy preferences as a potential equilibrium view, which would be achieved after a sufficiently long process of deliberation.

Stochastic consensus does not exclude the possibility of disagreement (dissent) in societies where individuals are connected and respect each other, while the process of deliberation is still ongoing. Only if people refuse to give each other respect will communication break down and open conflict would prevail. This is exactly what European integration was supposed to overcome. However, even if open conflict is avoided, persistent dissent can cause inefficiencies for policy-making. For such disagreement makes rational choice in a strict sense impossible: because there are diverging preferences on policy objectives, one cannot choose "the" option with the highest utility. Someone must impose a solution, but this would violate the preference of others. Avoiding this violation of democracy requires consensual decision-making by unanimity, but this rule may prevent efficient decisions all together if dissent persists. The alternative is majority voting. If consensus exists on procedures such as voting, violent conflict may be avoided. Voting represents a second best method of decision-making, because decisions are taken, although by frustrating minorities. Consensual voting often implies that citizens can rationally expect to shift the policy consensus at least in the future ("the next election"). Such justified belief is the foundation of fairness that legitimates institutions.

The problem with European governance today is that the institutional arrangements make the shift of European collective preferences rather unlikely. At best it will take a long time, which is also inefficient. The reason is simple. Because policy debates take place primarily within the honey-comb of nation-state constituencies, citizens deliberate and debate policy options in view of national elections. This is where their voice is heard, where their input matters. They charge their governments to represent these national objectives at the European level. Thus, the crucial feature in this system is that European citizens are *not connected* in their policy debates and do not or hardly give respect and weight to the arguments advanced in other countries. *Consequently, the degree of policy dissent at the European level is significantly higher than at the national level and this causes type-II-inefficiencies in European policy-making.* The structure of Europe's fragmented polity leads to a structural, quasi-permanent experience of policy preference frustration. European citizens believe that decisions taken "by Brussels" do not reflect their own concerns, while



they know little of the policy debates in other countries. The declining approval of European integration by Europe's citizens (from 70 percent in the 1980s to below 50 percent today), while the range of collective goods has significantly broadened, is a telling manifestation of this trend. In the long term, it could endanger the consensus on which European integration has been built.

### **Subsidiarity, Community Method and Voluntary Policy Coordination**

Many academic observers and political actors have sought to overcome the dilemma of externalities versus preference heterogeneity by reverting to the subsidiarity principle: according to the EU Treaty, the European level "shall take action only if and insofar as the objectives be better achieved by the Community", and "shall not go beyond what is necessary to achieve the objectives of the Treaty". Thus subsidiarity would reduce type-II-inefficiencies, but simultaneously it would increase type-I-inefficiency. Some authors have formulated this dilemma as a trade-off between two evils, where decentralised policy-making is preferable, presumably because it carries a higher degree of legitimacy. They claim that if European policy action is then undertaken *voluntarily* by national governments, it will more easily reflect their constituencies' preferences. However, the other side of this logic is that if governments cannot agree, no decision is made and this may be inefficient.

Voluntary policy coordination has become particularly prominent since the Lisbon European Council in 2000 turned the failure of agreeing on common policies into a virtue by calling voluntary participation the 'open method of coordination'. Yet, there is a serious problem with this approach because decentralisation to lower level jurisdictions does not only increase the scope for policy externalities, but it also decreases the likelihood for European collective goods to be provided at all, or at least to an optimal amount. The reason is the so-called 'collective action problem' explained first by Mancur Olson (1971). This argument shows that for a wide range of collective goods the likelihood of their optimal provision will decrease as the number of members in a group increases. *Hence both the enlargement of the EU to new members, and the justification of the subsidiarity principle to keep policy competences at the national level would increase the number of decision-makers in the European Union and thereby reduce the EU's capacity to provide efficient policy output.*

Olson's paradox of collective action is that *large groups*, composed of rational individuals, will *not* act in their group interest. For policy-making in the enlarged EU it implies that the *voluntary policy coordination and cooperation between autonomous governments is not necessarily optimal*. The answer would be to centralise European policy-making at the EU level. Traditionally such centralisation has taken place through the conferral to community institutions (Commission, ECB) or through so-called *hard and binding forms* of policy coordination (e.g. Stability and Growth Pact). However, the argument must be qualified. There does actually exist a range of European collective goods where voluntary policy coordination may be sufficient for their efficient provision. The defining criterion is the character of their externalities. It can be shown that voluntary policy coordination can be efficient in providing so-called inclusive collective goods, while the collective action problem will prevent this for exclusive goods. In the first case, policy-making competences can be shared between Member States. In the second must the European Union have exclusive competences.

### *Inclusive collective goods*

The classical definition of public goods is that (1) they must be provided in the same amount to all the affected consumers (jointness of supply) and (2) that everyone must consume the same amount of the good (non-rivalness for consumption). However, as figure 2 shows, the concept of collective goods is larger. If only condition (1) holds but not (2), the collective good is called an inclusive club good; in the opposite case it is an exclusive common resource. Collective goods, characterised by different externalities, require different forms of governance. The crucial distinction lies in the nature of expectations formed by autonomous actors and their implications for interactive equilibria.

**Figure 2. Typology of Collective Goods**

		Consumption (Benefits)	
		Excludable/rival	Non-Excludable/non-rival
Supply (Cost)	Non-joint/rival	I. <u>Pure private goods</u>  (exclusive goods) Apples, pears.	II. <u>Common property resources</u>  (exclusive collective goods) Oil wells, fisheries, Central bank liquidity
	Joint/non-rival	III. <u>Club goods</u>  (inclusive goods) Swimming pool, EMU	IV. <u>Pure public goods</u>  (non-exclusive goods) Defence, lighthouses,

Olson (1971) has shown that the club goods in box III of figure 2 are inclusive in the sense that (below a given capacity limit) an existing club may increase the total benefit from membership by admitting new members. The recent literature on network externalities has also observed the positive correlation between benefits and the number of group members under certain conditions. For example, the value of my membership in a Tennis club may increase when I can draw on a larger pool of potential partners to play with. Similarly, a large European Union with a single currency provides greater opportunities for trade. In this case the benefits of individual members are complementary to each other.

Yet, the positive spillover of a given common policy into any individual jurisdiction will only take place, if all individual governments were sufficiently convinced that their marginal contribution to the common policy will have a positive effect on their own constituency. Otherwise, they would abstain from making the effort of producing the policy outcome. Hence, collective preferences between autonomous actors will converge, if there is sufficient information and trust about the intentions of other club members. This is exactly what the soft policy coordination regimes are supposed to achieve: increased flow of information, exchange of best practices, peer pressure are all mechanisms to “tip” a policy network away from an initial sub-optimal equilibrium and move it to a higher welfare equilibrium. This logic has two implications: (1) Voluntary policy coordination and adherence to soft guiding rules will be forthcoming,

if and only if a soft institutional structure ensures the “tipping” of the preference convergence. (2) The group of decision-makers can then also be large, as network externalities increase the incentive to provide these collective goods. Hence voluntary and soft policy coordination are the appropriate regimes for the provision of inclusive collective goods.

### *Exclusive collective goods*

However, the case is different for exclusive collective goods, i.e. common resource goods (box II in figure 2). Policy coordination for exclusive collective goods is hampered by so-called strategic substitutabilities, which cause Olson’s collective action problem. They are caused by two different forms of externalities. (1) Although consumption of exclusive collective goods is the same for all group members, their access (supply) is rival, meaning that the share of benefits for each group member falls as the number of participants increases. As a consequence, the feedback on the expectations of existing group members is negative. The individual marginal benefit for a new or deviating member of the group is positive, but for existing or conforming members it is negative. Thus, there exists an incentive to go against collective interest (such as the Stability and Growth Pact), insofar as existing members’ willingness to pay for collective goods will be reduced as the number of group members increases. Hence, the *likelihood for a large group to provide an exclusive collective good voluntarily will disappear*. (2) Because benefits are the same for all group members, but supply is rival, it is possible to externalise production costs to others and free-ride. For example, if most countries in a monetary union balance their budgets, everyone may benefit from lower interest rates. But the free-rider could benefit from low interest rates “produced” by other member-states’ collective fiscal restraint and this creates an incentive for individual non-compliance with the policy rule. Therefore hard forms of policy coordination or even, as in the case of monetary policy, conferral to a European authority are required in order to provide these collective goods efficiently. The argument applies with force to the aggregate fiscal policy stance, but also to a range of other policy coordination issues, including foreign and security policy.

The two points can interact. The zero-sum game quality attached to common resource goods provides an incentive to keep the group of collective decision-makers small, for otherwise one risks the non-provision of the collective good. But if the group is enlarged, the provision of collective goods will be reduced and ultimately cease. Hence, voluntary intergovernmental policy coordination will not be sufficient to provide large groups of countries with an efficient or optimal amount of collective goods. A consistent approach to policy coordination for such goods requires “hard” or binding regimes of governance.

*Hence the nature of collective goods decides which form of European governance is most efficient. Inclusive collective goods can be provided optimally by voluntary policy coordination and shared competences between EU member states, exclusive goods require exclusive competences at the European level. The efficient assignment of policy competences does not depend on taste. It is dependent on the nature of the collective good.*

In practical terms, the distinction is not always easy. It seems that most of the policy areas covered by the Lisbon Process and the Open Method of Coordination fall

under the heading of inclusive goods. But the literature on fiscal federalism has also clearly established that aspects of macroeconomic stabilisation policy (price stability, interest rates, exchange rates and, in Euroland, the definition of the aggregate fiscal policy stance) are dominated by the strategic expectations related to exclusive collective goods. However, if exclusive competences at the EU-level may increase the efficiency of policy-making, they also pose a major challenge for the democratic legitimacy of policy-decisions at the EU-level. This has important implications for the drafting of a European Constitution.

## **II. The Democratic Challenge**

Efficient policy-making in the European Union requires forms of governance that eliminate or at least minimise the two types of inefficiencies described above. We will now look at how this can be achieved.

### **Shifting the Trade-off between Type-I and Type-II Inefficiencies**

Our discussion of type I and II inefficiencies has shown that the structure of the European polity determines the nature and size of policy inefficiencies. If the polity is fragmented and reflects the preferences as they are deliberated in unconnected national constituencies, as proposed by the subsidiarity principle, the policy-making process may well appear 'close to the people', but the resultant large externalities will prevent the sufficient provision of exclusive European collective goods. Hence subsidiarity will minimize type-II-inefficiencies and maximise type-I-inefficiencies. Alternatively, if the externalities are 'internalised' by intergovernmental policy coordination in a 'two-level governance' process type-I-inefficiencies will be minimised, but democratic preference frustration will undermine the legitimacy of the institutions.

A poignant example of this dilemma is the debate around the Stability and Growth Pact (SGP), which has assigned fiscal policy competences to the national level, while Euroland stabilisation policies require the definition of an aggregate European fiscal stance as a benchmark for stability orientated monetary policy. By stipulating that each government should keep its budget position 'in balance or surplus' over the medium term, the SGP effectively determines the aggregate stance to be equally 'in balance or surplus'. However, this poses a problem to democratic legitimacy. In recent years an increasing number of national governments have been elected with programs which are inconsistent with the commitment to balanced budgets. It seems inconceivable that the rigid budget rules of the SGP are sustainable in the long run, for a fundamental tenet of democracy is: 'No taxation without representation'. Voting citizens will not accept for ever, that they vote for one thing and get another because some previous government has committed them to different policy options. As we saw, the possibility of preference change is inherent to fair and democratic institutions. To preclude preference change means violating the norms on which European unification is built. The dilemma results from the fact that preference change only takes place in the context of national constituencies, while national policy decisions would affect everyone else.

The answer is to unify the national polities by forming a single European constituency, within which the policy preferences for European collective goods are

formed. This integrated polity would assume the competences to deal with all policies which potentially affect all European citizens. This implies the *European Constitution must establish a proper European government capable of taking decisions with regard to all exclusive European collective goods exercising the shared competences for spillovers between national and European goods. National authorities unwilling to confer their competencies seem to be unaware that they have already lost a large part of their power because of the widespread policy externalities in an integrated economy.*

Does setting up such a government imply the creation of a European 'super state'? Not, if we mean by that the coercive imposition of an uncontrolled Leviathan. Private spheres need to be protected by fundamental rights and the public sphere must be freely and equally accessible to each citizen. But when externalities of exclusive public goods exist, they need a system of governance, which is *able to police deviating behaviour consistently*. The solution to the dilemma of collective action consists in appointing a democratically accountable government that is itself subject to sanctions by voters (the sovereign) if it does not sanction others. As a consequence, the European constitution must clearly stipulate that it is *European citizens and not national governments who are the primary source of political legitimacy*.

### **Creating Structures for Democratic Policy Deliberation**

It is often asserted that a European democracy is not possible because a European *demos* does not exist. 'People' – rather than 'citizens' – are characterised by the cultural background and historic traditions in which they live. It is claimed, that this "identity" prevents them from agreeing on collective European preferences. However, people also change. Human beings are capable of learning. They listen to each other, evaluate new evidence and change their prior views and assessments. In order to make this process of deliberation an instrument of European integration, a constitution must create institutions which structure political debates such that a European-wide policy consensus can ultimately emerge. As I pointed out above, this requires that individual citizens are connected and extend mutual respect to each other.

A democratic polity creates exactly these conditions. Governments are accountable to their voters and compete with opposition parties for the trust of their constituency. Citizens are connected through their rights as the voting (and sanctioning) sovereign and through the public debates and deliberations that precede the election. Consequently, constitutional arrangements determine the speed of preference change leading to policy consensus. How should a European polity be structured? It can be shown that in a stylised *intergovernmental system*, national polities and constituencies are separate and only connected through government representatives at the European level. Hence, policy disagreement between member states is highly persistent. Alternatively, in a *European Republic* with a single constituency all citizens are directly connected because they need to elect a European government that manages their collective goods. Here, policy consensus emerges most rapidly. Today's '*community method*' is a hybrid intermediary case, where the European Commission facilitates the flow of information and the degree of trust between governments, but derives no direct legitimacy from citizens. This arrangement is useful for the provision of inclusive collective goods, when network externalities

provide the potential for convergent policy action. But it is inappropriate for exclusive collective goods, when national preferences are not converging. A unified approach is then required to provide the collective goods.

The need to elect a common government would automatically broaden the chain of respect and trust among citizens across borders, because the policy debates in other regions would become relevant to every individual's assessment of different policy options. Even if dissent on substantive policy issues prevailed – as it does in most democracies – the efficiency of European policy-making would be strengthened by a European-wide constitutional consensus about procedures, because it would bring individual citizens into the deliberation process. The alternative model of making states – rather than citizens – the ultimate source of political legitimacy would not only perpetuate policy disagreement between 'people', but it is also founded on pre-democratic norms and forms of government.

### **III. Practical Implications for the European Constitution**

Our analysis has a number of practical consequences for the drafting of a democratic European Constitution. Some of these conclusions may appear too radical for today's intellectual climate, but at least they can serve as benchmarks giving direction to smaller pragmatic steps. I will first outline some of the more ambitious orientations, and then present some concrete steps for implementation.

#### **The Value Content of Europe's Constitution**

One issue is the normative content of a European Constitution. Although there seems to be consensus that the democratisation of institutions is desirable, there is disagreement as to the need of going beyond procedural rules. From the political left there is a demand to enshrine the model of a social market economy, or a Social Union in the constitution. The political right resists such attempts.

The political values of modernity are expressed in the universal values of the republic: *liberté, égalité, fraternité*. Even if this is a French articulation, their essence is incorporated in all modern democracies. Yet, these three slogans do not only establish the dimensions of the modern political space, they also formulate a ranking of these values which is relevant for the economy. Individualism and markets are based on the predominance of two fundamental principles: freedom and equality. They are derived from the norms of modern contractual economies. Without freedom and equality neither contracts nor individual rights are possible and all social relations would be subject to the principle of hierarchy. By contrast, the value of *fraternité* (brotherhood) reflects traditional, holistic ideologies. They survive in the modern context either as communitarian values, often with reference to ethnic or cultural communities, or in the hierarchical institutions of the state. European integration is clearly grounded in the principles of a market economy and a European Constitution must therefore reflect the values of modern society as they emerged from the enlightenment philosophy. This does not imply disrespect for references to religion and other cultural traditions, but these pre-modern values must remain secondary to the political affirmation of the republican principles of freedom and equality. It is therefore consistent with the political objectives of the European Union to affirm human dignity, liberty, democracy, the rule of law and respect for human rights as the

Union's values, but the principle of equality of citizens should also be cited here explicitly. (The draft EU Constitution only mentions the equality of citizens in article 33). Furthermore, the integration of the Charter of Fundamental Rights of the individual citizen is also an expression of and not, as argued by some, a contradiction with the economic principles of a monetary market economy. Hence, *a Constitution that protects European citizens against holistic claims by governments and communities, whether national or European, and protects the formal and substantive equality of their individual rights must be part of the normative content of a European Constitution.*

By embracing individual freedom and equality as the fundamental norms, a democratic European Constitution does not necessarily have to take a position with respect to these twin principles of modernity. Traditionally, these have been the guiding stars of the political right and the political left in democratic societies. Economic liberals emphasise the freedom of entrepreneurship, while social-democrats emphasise the substantive equality between individuals that is easily lost under the dynamics of unfettered markets. Thus, for the political right a European Constitution must preserve the functioning of efficient markets. For the left, high levels of employment and social protection are a substantive condition of political equality and economic freedom. In modern democracies, policy preferences swing between these two major poles reflecting the outcome of different weights of arguments in public policy deliberations. It would be wrong to limit the outcome of these deliberations by constitutional norms, although it is essential that both fundamental norms are acknowledged by the Constitution. For only respect for the freedom and equality of citizens allows consensual policy preferences to emerge.

### **The Question of Borders**

Another open question is where the borders of the Union are to be drawn? Often this is addressed in terms of geography. Some claim that geo-strategic objectives of stabilising Europe would require the accession of Turkey first, followed by the Ukraine, Russia and others later. Undoubtedly, these are countries in need of stability. But it may be wise to remember Napoleon who had learned a lesson when he said:

“Empires die of indigestion.”

The limits of the European Union appear by the auto-selection of those who want to play by Europe's constitutive rules. These rules must be structured in such a way that they enable coherent and efficient policy-making by providing desired collective goods and legitimacy into the policy process. Those who do not like these rules should not be part of the republic.

### **Setting up a European Government**

*A European constitution must establish an European Government, democratically elected by a unified constituency and able to decide on European collective goods and policies in an efficient way. As a consequence, political debates and policy deliberation are focussed on the election of this government. Naturally, the Commission should assume this function and be elected by and accountable to the European Parliament.*

However, this only makes sense if it has powers to act and a President who provides orientation for the general policy direction. Otherwise, why should European citizens bother to vote? It is therefore incompatible with a modern constitution that the President of the Commission is pre-selected by the European Council. Such practices belong to pre-democratic aristocracies, where the Upper House controlled the Commons. The right to legislate and grant or withhold public goods must be subject to universal suffrage of the citizens concerned.

Furthermore, the Commissioners must be responsible for the provision of specific European collective goods. The Commission's services and staff are the administration of such a political executive. It therefore should be the responsibility of the Commission President and not the Council to establish who is in charge of what and whether regional interests are sufficiently represented and balanced by the composition of this body.

### *The European Parliament*

If the Commission is to become a European executive, it needs democratic control. This is the key task for the European Parliament. It must therefore have the right to vote the Commission in and to revoke it. For only the European Parliament has a proper European constituency. Policy debates in this Parliament would not only *directly* reflect the policy preferences of European citizens, they would also contribute to their formation. In order to support this process, political equality between all citizens needs to be ensured. It is therefore desirable that the *same electoral law* applies to all member states. Of course, the accountability of Commissioners to Parliament would contribute to politisation of European policy-making. But this is a desired side-effect, for it is likely to increase public participation in policy debates throughout Europe. Founding the legitimacy of the European government on the European Parliament is therefore simultaneously creating and reinforcing a European public sphere and ultimately the European identity.

### *The Council*

Even if there are European collective goods, which can clearly be distinguished from national goods, there is also a wide range of interdependences and spillovers from national to European goods. Here is the role for the European Council and the Council of Ministers. The *Council should become a second legislative chamber*, co-deciding with the European Parliament on European laws. However, the executive orders and directives of this European legislation should be left to the authority of the European Commission, which is accountable to the European Parliament but may delegate its implementation to national authorities. This would greatly simplify the procedures of European legislation by taking away the bureaucratic bargaining between national administrations over the detailed application of European legislation that contributes to much over-regulation and bureaucratisation in the European Union today.

A difficulty in the delimitation of tasks between a new-style Commission and member-states relates to *joint tasks*, when there are spillovers from one level to the other. This is therefore where the European Council and the Commission could jointly assume certain executive functions. But who would be the driving force? Traditionally, this has been a function of the EU Presidency. Several ideas have been



put forward for the reform of the EU presidency. The essential question is: Which system is most likely to strengthen Europe's constitutional consensus? The present system of rotating presidencies in the EU has the advantage of re-enforcing mutual respect across Europe, as each presidency makes special efforts to prove its European commitment. In peripheral countries, this is a beneficial side effect and helps mobilizing public interest for European affairs. However, the short durations (six months) are a handicap. A more permanent administrative structure may be needed for policy issues requiring continuity, which is best provided by the administrative services of the Commission, although certain political decisions may be reserved to the European Council. In this case one could preserve the rotating presidencies of the EU to allow member-states to provide impetus into certain policy areas.

### *The Congress*

A European government must be in charge of European collective goods. However the delimitation between European and national collective goods is not always clear. Given the changing nature of collective goods, policy competences may change character over time. The draft EU Constitution assigns 'the flexibility' clause to the European Council acting unanimously on a proposal from the Commission after assent from the European Parliament. Using an alternative approach, one might assign the responsibility for deciding at which level policy decisions should be taken to a *European Congress*, consisting of an equal number of members of national and European Parliaments. This Congress would therefore be the authority of last resort in constitutional rule setting and have the competence of competence transfers. The function of a Congress is also important in case the Constitution now under discussion does not go far enough to guarantee efficient policy-making. The Congress could then authorize constitutional amendments without having to entirely re-write the Constitution. This approach would give the Congress a clearer mission than the presently envisaged Congress of the Peoples of Europe.

### **Voting and Equality**

Political equality implies, every country's voting rights would represent its population share, so that each individual has the same weight. In the EU, this is not the case. The EU has a bias in favour of small member states. Malta and Luxembourg with less than half a million people and less than one per mille of the EU27 population have over ten times as much voting power in the Council and over eight times the representation in the European Parliament than they deserve for their population share. Germany with 19 percent of the population has only half that weight in the Council and only 13.5 percent of the seats in Parliament. How serious are these distortions?

One way to measure inequality is the Gini coefficient.<sup>1</sup> Table 3 shows that political equality is fairly evenly distributed in the EU, although the Gini coefficient for Council representation is nearly twice as high as for the EP. This fact emphasises our point that the *Council is a representation of national administrations, not citizens*. The inequality is justified if, and only if, the Council represents member state

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<sup>1</sup> This coefficient ranges from 0 to 1, where 0 represents perfect equality, and 1 total inequality. Thus, 'one (wo)man, one vote represents a coefficient of zero, 'all communities are equal' implies a coefficient of one.

governments and their interests, rather than citizens and their preferences. The Council should therefore have *legislative competencies that are relevant to national collective goods and their interdependence with European policies*, not for policies that are relevant for the provision of European collective goods over the entire European policy domain.

Whether this inequality justifies changing the voting weights at some future point should be open for debate. But the proposal of introducing an unweighted double majority of member-states and population as the criterion for qualified majority voting in the Council would certainly increase the efficiency of the decision-making process. However, a simpler and more transparent legislative procedure would be to obtain a simple majority in the (legislative) Council and the European Parliament for co-decision between these two bodies. This would guarantee a double majority of countries and citizens, and improve the transparency of arguments in the process of policy deliberation.

**Table 3. Gini Coefficient for Political Inequality**

Gini Coefficient	Council	European Parliament
EU15	0.291	0.149
EU27	0.282	0.160

**IV. Implications for an Efficient Economic Governance**

Our analysis of European collective goods has shown that inclusive goods with network externalities can be provided efficiently by voluntary cooperation between governments. The Open Method of Coordination, which was part of the Lisbon Strategy, is the appropriate instrument to deal with these goods. It applies to policy areas where joint action is an incentive to participate, for example in developing the knowledge society, e-Europe etc. However, the range of policies, where national preferences are persistent and collective goods are exclusive, is far more extensive than often acknowledged. It covers in particular most aspects of macroeconomic stabilisation policies in the single currency area, but also many structural reforms where selective incentives on a national basis prevent policies that would benefit the Union as a whole. Hence a strengthening of Europe’s economic governance is required and I will now discuss some of these aspects.

**Europe’s Future Financial Constitution**

Establishing the European Commission as a proper European government necessitates that it has command over its own resources. Because in democracies there can be ‘no taxation without representation,’ a financial constitution for the European Union requires:

1. *Full budget authority for the European Parliament*, on both the income and expenditure side. This does not exclude the possibility that the Council may have co-decision rights with respect to certain

issues, but the autonomy of a European government is indispensable for the efficient provision of European collective goods.

2. *The European Parliament must have the authority to authorise the Commission to raise European taxes.* The principle of jurisdictional congruence requires such taxing capacities to be subject to full accountability to the representation of European citizens at the level of the European Parliament. A European tax does not necessarily imply heavier tax burdens for European citizens. Part of the funds raised for a European budget would substitute transfers that were previously coming from national budgets. They may therefore even reduce the tax burden in some countries, especially when they are net-contributors to the EU budget. *The Council is the forum where distributional transfer issues must be discussed and decided jointly with the Commission.*

The criteria for choosing the *appropriate tax base* must be related to the European single market with the purpose of avoiding distortions. In practical terms, this refers to goods and capital markets:

1. On goods and services, a proportion of VAT could be assigned to the European level while member states collect the other part. The European VAT rate would be uniform throughout the single market (say 2 percent) whilst national rate variations would reflect local policy preferences.

2. The uniform taxation of highly mobile factors of production, such as capital, is also imperative in order to prevent distorting and unfair tax competition. However, other taxation can and should remain under the authority of national governments, as harmful tax competition is unlikely to take place in this domain. Decisions of occasional reallocations of the tax base between the European and the national level would be decided by the European Congress.

## **Macroeconomic Governance**

With the advance of monetary integration a large share of Europe's collective goods relates to stabilisation policies. Because macro-economic policies and financial stability resemble exclusive collective goods, economic theory has long argued that stabilisation policy and financial regulation must be operated at the central level. This principle has been applied to monetary policy by the creation of the European Central Bank and therefore there is no need to change the institutional arrangements in this area. However, because of the collective action problems discussed above, an independent intergovernmental structure will not produce optimal results for economic and budget policy. These tasks should be conferred to the European Commission, which would be accountable to all European citizens.

Yet, even if the European Commission controlled its own budget, its size will remain too small for the foreseeable future to become an efficient tool of stabilisation policy. Hence a more efficient mechanism for the determination of the optimal macroeconomic policy mix is required.

### *Defining aggregate fiscal policy*

The *definition of the aggregate fiscal policy* stance, i.e. the determination of aggregate European expenditure and revenue programs, is an exclusive collective good because liquidity borrowed under the single currency constraint is a common resource. But *the allocation of government spending* is a different matter. Most of the expenditure by public authorities concerns local and national collective goods whose benefits do not necessarily spill over into other countries. It is true that there are some large-scale European investment projects like transport networks, strategic research or expanding information and communications technology, but the bulk of spending is on public goods which are consumed in a local or regional environment. Fiscal federalism has assigned the *allocation function for such goods to decentralized levels, while macroeconomic stabilization is to be decided centrally*. In Europe a large EU budget does not seem politically feasible, nor is it necessary. What matters for the optimal policy mix is the amount of government net spending, wherever it may originate. This means that the *allocation of collective goods is not necessarily a European function, although the financing restriction makes the aggregate fiscal stance an exclusive European good*. Hence, the budgeting may be done bottom up from the national and regional level, while the aggregate fiscal policy stance needs to be set at the European level (top down).

The main problem is how to allocate the different expenditure and income shares to national governments. My suggestion to solve the policy mix problem is to *confer the function of setting the macroeconomic fiscal policy stance to the European government and leave the formulation of the specific spending (and revenue) chapters to national governments*. The idea of separating the two functions is already part of budget practices in several European countries, notably France and Italy. France's Parliament first votes for a given macroeconomic stance, then proceeds to so-called *arbitrages* between the different titles. In Italy, Parliament first votes the *Documento di Programmazione economico-finanziaria* (DPEF), indicating the targets of budgetary policy over the following three years and their relevance for inflation, growth and employment. A few months later, budgetary policy is implemented by the *Legge Finanziaria* (Finance Act), containing the provisions of the national budget and implementing legislation (*appunto di accompagnamento*). The coherence of the aggregate fiscal policy stance in Europe could be achieved by developing the Broad Economic Policy Guidelines into a 'European DPEF' in the form of a "European framework law".

### *The process of fiscal policy-making*

Fiscal policy-making in Europe would then be a process going through several steps.

1. The European Commission would formulate the fiscal policy stance for the whole of the Euro-area in view of the requirements of the business cycle, inflation perspectives, the international environment, economic growth etc. It may therefore flexibly adjust deficit levels to the business cycle. This aggregate deficit may also reflect different national debt positions, and allows therefore greater regional flexibility than the present Stability and Growth Pact.

2. To ensure that this document will indeed reflect the collective policy preferences of the European constituency, the integrated European budget plan, formulated as a

“framework law”, would have to be debated, amended and voted by the European Parliament. Because all proposals and amendments are public, this would fuel a European-wide debate on the policy orientations and provision of collective goods. Institutionally, however, the process of deliberation would by definition transcend the national framework and connect citizens. Hence, transparency would contribute to the emergence of collective European budget preferences.

3. After the vote in the European Parliament, the fiscal framework law goes to the Council for approval. At this point, arbitrages between national governments under the constraint of the aggregate position are possible. But given that the overall revenue and spending levels are now fixed, one government could only have a larger share in spending and deficits, if another country accepted a smaller share. Hence, the European Government, with the approval by the *European Parliament*, fixes the overall ‘envelope’ of public finance, but the execution is left to national authorities. It is the aggregate fiscal stance that is then relevant for monetary policy and the European Central Bank.

4. At this point, the *question of budget share allocation* arises. Three different approaches for assigning national deficit quota are possible: intergovernmental bargaining, a transfer union or a market solution.

(1) With intergovernmental bargains the Ecofin Council would become a clearing house for different national claims. The drawback is that the annual haggling for budget shares is messy and would hardly contribute to a coherent pan-European view of fiscal policy or to the strengthening of the legitimacy of political choices.

(2) Alternatively the European Union’s budget could be expanded to the size of a federal budget, as in most developed federations. Such arrangement does not necessarily imply a large budget at the level of central government, but it requires at least a system of intergovernmental grants and transfers. This solution does not seem to find much support in the EU.

(3) A third solution would be the creation of tradable deficit permits, as suggested by Casella (1999, 2001). The idea is derived from the experience in environmental markets where fishing or pollution rights are traded. These markets create property rights for exclusive public goods. Public authorities in EMU-countries would be allowed to trade rights to deficit creation after an overall ceiling (the aggregate policy stance) and an initial distribution of permits (for example corresponding to GDP-shares) has been agreed. The virtue of the scheme lies in the definition of property rights for deficits, allowing the internalisation of fiscal externalities and creating an incentive to minimize costs. Such an arrangement fits perfectly into the idea that a European government should be in charge of defining the aggregate fiscal policy stance (a collective good), while national governments are responsible for allocating taxes and expenditure. If any individual jurisdiction, be it a national government, or a regional or local authority or the European government, wishes to issue more debt than is initially allocated, it would have to buy permits from another authority which does not wish

to use its own quota. Hence, buying permits carries costs that need to be compared with the political costs of domestic fiscal consolidation. *This is exactly the debate that should be going on in national or local parliaments.* Hence, the 'envelope approach' would allow for the flexible adjustment of the aggregate ceiling in accordance to changing economic requirements. The *stabilization function* of public finance would be centralized at the European level, as postulated by the theory of fiscal federalism. The *allocation* through the market mechanism distributes the responsibility for fiscal rectitude in the most efficient manner across different countries at minimum cost.

### **Practical first steps**

The recommendations made in this report may seem too ambitious and far reaching for a full implementation today. The constitutional consensus has not sufficiently converged to make governments accept the conferral of their sovereign powers to a European Government. If this is politically not feasible today, the European Constitution should at least create structures that open the way in this direction. Three minimum requirements are:

(1) The European Union has to obtain the status of a single legal personality that makes policy decisions within a unified legal framework. This framework must contain a Charter of Fundamental Rights of European Citizens. EU laws should be passed by the European Parliament in co-decision with the Council where appropriate. Secondary legislation on implementing policies should be left to the Commission, but could be delegated to national authorities where appropriate.

(2) The European Commission President should be elected by the European Parliament by simple majority. The President should nominate Commissioners for task-orientated portfolios, not as country representatives. The Council may approve of them, but not appoint them. Parliament should be elected by a uniform electoral law.

(3) The Commission must have its own financial resources. Both revenue and expenditure ought to be approved by the European Parliament. Certain items may be subject to co-decision with the Council.

With respect to Europe's economic governance, some simple steps allow to go beyond the closed shop of intergovernmental policy-making. By making co-decision between the Council and the European Parliament the dominant principle, policy decisions would become more transparent and policy debates focused on the European Parliament would contribute to a more rapid convergence to a European policy consensus. For this reason, I suggest making the existing Broad Economic Policy Guidelines, article 99 (2,4), the emergency clause, article 100 (1,2), the no bail-out clause, 102 (2), 103 (3), the excessive deficit procedure 104 (6,7,14) and some provisions in ECB statutes, 107 (6) subject to co-decision (see annex).

## Resumée

The main points of this report are simple.

1. The changing international and European context requires that a European Constitution creates efficient structures for the governance of European collective policy goods.
2. Voluntary cooperation and coordination between autonomous governments is unlikely to provide European citizens with the collective goods they desire because of the so-called “collective action problem”. Only a limited range of inclusive goods with network externalities will be supplied by this approach.
3. The principle of subsidiarity and the enlargement of the European Union are likely to exacerbate this problem.
4. The solution is more centralisation and *conferral* of European policy-making to the EU-level. But this can only be justified if a European Government (i.e. the Commission) is fully accountable to European Citizens – rather than governments. Hence, the Commission must be elected by the European Parliament alone. Efficiency and legitimacy go together.
5. A desired side-effect of the creation a European Government is the politicisation of policy debates that will help to create a pan-European policy consensus. Hence, decision-making will become more efficient, as national governments are less likely to hold up the legislative process.
6. These changes are of particular relevance for the economic governance of European Monetary Union, as stabilisation policies are clearly a matter for centralisation. The Commission must take over the responsibility of defining European policies. Citizens must have the right to sanction the Commission if it does not reflect their preferences. National governments (or the European Council) cannot fulfil this function as they are not accountable to the European constituency as a whole. A final remark applies to the ratification of the Constitution.
7. Given that constitutional consensus is the most important foundation for efficient European policy-making, the ratification procedures must support the emergence of such consensus. Several models are imaginable.

(1) The ratification of the European Constitution can be submitted to national referenda. But if votes are only counted at the level of member state constituencies, as has been customary in previous EU-treaty referenda (Denmark, France, Ireland, UK), this method reinforces the communitarian honey-comb logic. The European Union will be perceived as belonging to member-states, rather than to its citizens.

(2) Alternatively, the constitution could come into force after a pan-European referendum has approved it. The Constitution would automatically become valid in countries that have approved it. If this

is in contradiction to national constitutions, parliamentary ratification procedures would follow after the pan-European referendum. If the population of a specific country does not vote in favour of the new constitution, it should have the right to participate nevertheless, if a minimum threshold of EU member states is reached, or to opt out. Of course, this requires appropriate procedures to deal with the opt-outs.

(3) Another option would be ratification of the constitution by a European Congress, consisting of an equal number of national and European parliamentarians. This solution gives national parliaments a greater say in important European policy decisions. However, the drawback of this method is that it does not necessarily mobilize cross-border public debate, deliberation and commitment, unless it is linked to a major election, say of the European Parliament. Also, given that this method may be incompatible with national constitutions, it may have to be reserved for constitutional amendments *after* the new constitution has been ratified.

Non-ratification of the Constitution should be treated as a voluntary withdrawal from the Union.



## Annex

### Proposal to strengthen the co-decision right of the European Parliament in the section on economic and monetary policy

In what follows, first the old article based on the existing treaties and amended by the Convention's legal service is quoted. A short explanation is given as to why the old text in the Treaty on European Union needs to be changed. This is then followed by the proposed new wording.

**Art. 99 (2) old text:** "The Council shall on a recommendation from the Commission, formulate by a qualified majority a draft for the broad guidelines of the economic policies of the Member States and of the Union, and shall report its findings to the European Council."

- The proposal of the working group on economic governance (CONV 357/02, p.5) recommended:  
*"...It shall act after consulting the European Parliament."*

However, art. 13 (1) of the Draft of Articles 1 to 16 of the Constitutional Treaty (CONV 528/03) states: *"The Union shall coordinate the economic policies of the Member States, in particular by establishing broad guidelines of these policies."* The Union means not only the Member State but also participation of the European Parliament. Therefore the co-decision procedure has to apply.

Proposed new text...

*"On the basis of this recommendation, the European Parliament and the Council in accordance with the legislative procedure, shall adopt a recommendation..."*

**Art. 99 (4) old text:** "Where it is established, under the procedure referred to in paragraph 3, that the economic policies of a Member State are not consistent with the broad guidelines referred to in paragraph 2 or that they risk jeopardising the proper functioning of economic and monetary union, the Council may, on a recommendation from the Commission, adopt by a qualified majority the necessary recommendations, which it shall address to the Member State concerned. The Council may on a proposal from the Commission, decide by a qualified majority to make its recommendation public.

The President of the Council and the Commission shall report to the European Parliament on the result of the multilateral surveillance..."

- The participation of the European Parliament is necessary to ensure that the common interest is taken into account (Art. 13 (2) of the Draft of Articles).

Proposed new text...

*“...the European Parliament and the Council in accordance with the legislative procedure may, on a recommendation of the Commission, adopt the necessary recommendations...”*

**Art. 100 (1) old text:** “Without prejudice to any other procedures provided for in the Constitution, the Council on a proposal from the Commission, may adopt by a qualified majority the measures appropriate to the economic situation, in particular if severe difficulties arise in the supply of certain products.”

- The co-decision procedure has to apply to enhance transparency.

Proposed new text...

*“...the European Parliament and the Council in accordance with the legislative procedure on a proposal from the Commission, may adopt the measures...”*

**Art. 100 (2) old text:** “Where a Member State is in difficulties or is seriously threatened with severe difficulties caused by natural disaster or exceptional occurrences beyond its control, the Council on a proposal from the Commission, may adopt by qualified majority a European decision granting, under certain conditions, Union financial assistance to the Member State concerned. The President of the Council shall inform the European Parliament of the decision taken.”

- Instead of only informing the European Parliament the co-decision procedure should apply due to a question concerning the EU budget.

Proposed new text...

*“...the European Parliament and the Council in accordance with the legislative procedure on a proposal of the Commission, may adopt a European decision...”*

**Art. 102 (2):** “The Council, on a proposal from the Commission, shall adopt by a qualified majority the measures specifying definitions for the application of the prohibition referred to in paragraph 1. It shall act after consulting the European Parliament.”

- This proposal is in line with the recommendation of the working group on simplification. The consultation procedure can be applied to this provision due to its eminently technical nature (CONV 424/02, p.16).
- However, the process of setting up the rules demands transparency and thus the co-decision procedure should apply.

Proposed new text...

*“ The European Parliament and the Council according to the legislative procedure, on a proposal from the Commission, shall adopt the measures...”*

**Art. 103 (2) old text:** “The Council on a proposal from the Commission, may adopt by a qualified majority measures specifying definitions for the application of the prohibition referred to in (Art. 101) and in this Article. It shall act after consulting the European Parliament.”

- This proposal is in line with the recommendation of the working group on simplification. The consultation procedure can apply to this provision due to its eminently technical nature (CONV 424/02, p. 16).
- However, the process of defining the application of the prohibition in Art. 101 demands transparency.

Proposed new text...

*“ The European Parliament and the Council according to the legislative procedure, on a proposal from the Commission, may adopt measures...”*

**Art. 104 (6) old text:** “The Council shall, on a recommendation from the Commission, having considered any observation which the Member State concerned may wish to make and after an overall assessment, decide by a qualified majority whether an excessive deficit exists.”

- The risk of Member State hold-ups is reduced and the common interest ensured by engaging the European Parliament with the co-decision procedure.

Proposed new text...

*“ The European Parliament and the Council according to the legislative procedure, on a recommendation from the Commission, having considered...decide whether an excessive deficit exists.”*

**Art. 104 (7) old text:** “The Council, on a recommendation from the Commission, shall adopt by a majority of two-thirds of the votes of its members, weighted in accordance with (Art. 205 (2)), excluding the votes of the representative of the Member State concerned, the European decisions and recommendations referred to in paragraphs 8 to 12.”

- The risk of Member State hold-ups is reduced and the common interest ensured by engaging the European Parliament with the co-decision procedure.

Proposed new text...

*“ The Council, on a recommendation from the Commission after the assent of the European Parliament, shall adopt by a majority of two-thirds of the votes of its members, weighted in accordance with (Art. 205 (2)), excluding the votes of the representative of the Member State concerned, ...”*

**Art. 104 (14) old text:** “The Council, on a proposal from the Commission, shall adopt unanimously the appropriate measures to replace the said Protocol. It shall act after consulting the European Parliament and the ECB.”

- The change of the rules about the excessive deficit procedure is such an important issue of common concern that it has to be decided by co-decision.

Proposed new text...

*“ The Council, on a proposal from the Commission after the assent of the European Parliament, shall adopt unanimously the appropriate measures to replace the said Protocol. They shall act after consulting the ECB.”*

**Art. 107 (6) old text:** “The Council shall adopt the measures referred to in Articles 4, 5.4, 19.2, 20, 28.1, 29.2, 30.4, and 34.3, of the Statute of the *ESCB*. It shall act by a qualified majority, either on a proposal from the Commission after consulting the European Central Bank, or on a recommendation from the European Central Bank after consulting the Commission. In both cases, it shall act after consulting the European Parliament.”

- Transparency demands to apply the co-decision procedure concerning these measures. However the change to the co-decision procedure means that the ECB would lose its power of recommendation under the current procedure.

Proposed new text...

“...The European Parliament and the Council shall act according to the legislative procedure, on a prior recommendation of the European Central Bank, after consulting the Commission.”

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