Notre Europe
Thinking a united Europe
Penser l'unité européenne
Policy Brief
No. 33
February 2012

160

The "Fiscal Compact": legal uncertainty and political ambiguity

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Introduction

Twenty years from now, how will the "Treaty on Stability, Coordination and Governance in the Economic and Monetary Union"[1], recently approved by the heads of state and government on 31 January, be viewed? The answer will largely depend on what follows from this decision. Will the treaty receive enough signatures to be ratified and enter into force? Will it calm market fears? Will governments actually fulfil the new obligations they are subject to? In any case, the reference to a longer time-period should also be seen as an incentive to consider the place this "fiscal compact", as it is sometimes called, will hold in the EMU's short history. After all, the Maastricht Treaty, praised in its day as a historic agreement, today seems more of an ambiguous compromise which left a certain number of fundamental questions hanging in the balance, questions which have weighed on the events of the past two years. What lies ahead for this new treaty?

At first sight, the fiscal compact is inspired by a **desire to break with the past**, which is the main rationale for its adoption. The "governance by rules" set in Maastricht was characterised by two things: first its rejection of overly strict discipline, and second, its refusal to allow supranational bodies to play a controlling role similar to that accorded them in other areas. All infringement proceedings before the Court of Justice were therefore excluded in the excessive deficit procedure framework[2], while the Commission has seen its oversight responsibilities reduced, its power being limited to merely making recommendations[3]. The weaknesses of its power were to be measured in 2003 when it attempted to use it against France and Germany, which clearly violated the stability pact. In many respects, the Maastricht Treaty was thus halfway between the community method of the "first pillar" and the intergovernmental approaches of the second and third pillars.

The **new treaty aims to remedy these structural weaknesses**. First, it will **reduce states' fiscal discretion** by establishing a "golden rule" of balanced budgets, which should be, if possible, a fundamental element of their constitutional texts (Article 3). Next, it will **strengthen the control powers of the Commission**, to which the Eurozone members are committed to lend their full support (Article 7). Finally, it will **give the Court of Justice new powers of control** (Article 8). In sum, the "fiscal compact" may appear to be the formal abandonment of the laxity that has marked the first decade of the single currency, a move that, among others, is meant to assuage market fears regarding the euro's sustainability. Reality, however, is much more complex. On the one hand turning to an "intergovernmental treaty" considerably limits reform possibilities. On the other hand, the effectiveness of the control mechanisms put into place remains uncertain.

1. Treaty on Stability, Coordination and Governance in the Economic and Monetary Union, http://www.european-council.europa.eu/media/579087/treaty.pdf
2. Article 126(10)of the TFEU.
3. Article 126(9) of the TFEU.

I. The choice of an "intergovernmental treaty"

As it is well known, the rejection by the British government of the treaty reform proposals has led to a shaky solution – a new treaty, whose coexistence with prior treaties is anything but simple.

1.1. The right to conclude a separate treaty

In principle, nothing prevents a separate agreement from being established between certain EU member states. International law allows some of the signatories of a multi-lateral treaty to conclude additional agreements among themselves, as long as it does not infringe on the rights of the parties not included.

Moreover, because the EU only has limited powers[4], **member states remain free to conclude agreements in their areas of competence**. There are several examples of treaties concluded between some EU member states only: Benelux, the Nordic cooperation, the Schengen Agreement, or the more recent treaty establishing the European Stability Mechanism signed in July 2011.

1.2. A right with many restrictions

The right to conclude a separate agreement between some EU member states is, however, subject to several restrictions.

First, the signatories of the new treaty remain bound by the obligations of the European treaties. **They may add new rules, but may not derogate from existing ones**. The centrepiece of the new treaty – balanced budgets, or the "golden rule" as outlined in Article 3 – complies with this demand: any government following this new provision will automatically abide by the Maastricht rule, which only prohibits *excessive* deficits.

Along the same lines, **the new rules cannot hinder the work of EU institutions**. This principle is particularly important where the new treaty is concerned. Contrary to the Schengen Agreements, which dealt with a relatively unexplored area, **the new "Fiscal Treaty" falls under a policy sector which is thoroughly covered by previous texts,** be they European treaties, the stability pact or, more recently, the legislative package adopted in November 2011 to strengthen economic governance[5] (known as the "Six-Pack" in Euro-speak). This latest package puts surveillance mechanisms into place which are relatively complete, and which the new mechanisms must not weaken. Thus, when Article 2 affirms that nothing in the new treaty should be interpreted as an encroachment on community law, this is simply a matter of restating an obvious fact.[6] Legally speaking, this reminder is redundant, yet understandable in its policy aims. Its primary purpose is to alleviate certain misgivings of community method supporters, who feared that the choice in favour of an intergovernmental approach could weaken the powers of supranational institutions.

Finally, in, principle, the **prior agreement** of the 27 EU member countries should be obtained before the common institutions can be given new responsibilities, in order to protect the institutional acquis. This had been the case at Maastricht with the Social Policy Protocol, which was approved by 11 members once the British government gave their go-ahead. In reality, practices are somewhat lax on the matter. In the past, the Court of Justice has seemed to consider that an informal agreement sufficed, as long as it was unanimous.[7] The Treaty on the Functioning of the European Union (TFEU) has been amended to create the European Stability Mechanism; but this was mainly because the very idea of solidarity with those States threatened by default was disputed: The new Article 136 has no specific clause formally enabling the new agreement to have new missions given to the Commission or the Court.

4. Article 4 of the TEU.

5. Official Journal of the European Union, L 306, Volume 54, 23 November 2011, http://eur-lex.europa.eu/JOHtml.do?uri=OJ%3AL%3A2011%3A306%3ASOM%3AEN%3AHTML
6. Is it because of its obvious nature that the reference to the primacy of Community law in case of conflict with the provisions of the new treaty, included in the first drafts of the same treaty, was removed, or is it rather because it could appear to reduce the symbolic importance of the new agreement?
7. See, for example, the judgment *Parliament v Council and Commission* of 30 June 1993, Joined cases C-181/91 and C-248/91, ECR1993, I-3713.

II. Uncertainty regarding the control of national policies

The choice of an "intergovernmental treaty" alongside the European treaties has considerably reduced the range of possibilities. Two articles demonstrate the uncertainty surrounding the new compact: Article 7, relative to controlling excessive deficits, and Article 8, which deals with the role of the Court of Justice.

2.1. Rejection of automatic sanctions

With regard to Article 7, the TFEU states that decisions in the excessive deficit procedure are made by the Council, acting by a qualified majority on a Commission recommendation[8] – a measure that has shown its limits because it enabled a minority of states to avoid condemning the French and German governments in 2003.The reforms adopted in November 2011 under the "Six-Pack" framework have significantly strengthened the EU's powers of control, in particular concerning the establishment of a mechanism to prevent excessive deficits by focusing on reducing public debt and expanding the scope of oversight to a series of macro-economic indicators, experience having shown that fiscal virtue can hide other imbalances. Accordingly, **in order to consolidate the Commission's powers, its recommendations can only be rejected by a qualified majority in the Council**. Although this hardens the rule set out by the treaty, **one seems to have considered that this poses no problem as long as it applies to measures that are not explicitly foreseen in the treaty. However, this *a contrario* reasoning does not allow the same rule to be applied for the sanctions** listed in Article 126.[9]

The "fiscal compact" tries to tighten the procedure by regulating the behaviour of national governments. When the Commission's proposals and recommendations concerning Eurozone countries are debated in the Council, according to Article 7 the members of the zone in question are committed to supporting them. If that were all there was, it could have been argued that the "fiscal compact" managed to impose stricter discipline without contravening to Article 126.However, because the French government has refused to accept automatic sanctions, the new commitment contained in Article 7 no longer stands if a majority of member states oppose the Commission's conclusions. This qualification not only weakens the credibility of the threat, but substitutes a rule (reversed qualified majority) for one that exists in the TFEU whereas, as was seen, an intergovernmental treaty may in no way contradict the principles contained in the European treaties. True no government has opposed this. But who is to say that this will be the case tomorrow if the Commission proposes sanctions against a member state? In other words, **the rejection of overly strict community control results in an uncertain legal solution**.

2.2. A limited role for the Court of Justice

More caution was shown with regard to the Court of Justice, but the final solution adds nothing substantial to the existing mechanisms. The problem is two-fold: A legal basis needed to be found that allowed the Court to intervene, while also taking into account the Maastricht acquis, which prohibits infringement proceedings, a classic instrument used in community law, under the excessive deficit procedure.[10] The authors of the new treaty have found a possible source of jurisdictional control in **Article 273 of the TFEU, which authorises the Court's intervention to rule on "any dispute between member states which relate to the subject matter of the treaties, if the dispute is submitted to it under a special agreement between the parties"**. As the balanced budget clause is a new rule, it can be argued that it does not fall under the exclusion clause of Article 126(10).But it would be difficult to say the same about the rest of the fiscal compact. This is why, after some hesitation, it was finally decided that **the Court's control would be strictly limited to the "golden rule"**.

This solution has, however, significantly reduced the Court's scope of intervention. It may only rule on issues related to the transposition of the balanced budget principle into national law. For all other issues, i.e. the decisions taken each year by the budgetary authorities, the principles set out in Maastricht are not affected: there is no room for judicial enforcement of the decisions taken by the Council where oversight of national budgetary procedures is concerned. This is quite far from the possibility of a veto on national budgets that had been suggested. Furthermore, the intervention of the Court remains even more uncertain than in traditional infringement proceedings, the deterrent power of which largely rests on the Commission's right to act independently against reluctant states. Article 8 gives member states the right to bring possible violations of the "golden rule" before the Court, with the Commission being restricted to drafting reports on the way by which the states fulfil their obligations. Yet experience over the past few years has shown the limits of "mutual surveillance" between states in fiscal matters. Too often, governments have chosen to look the other way concerning other states' "weaknesses", out of fear

8. Article 126(13) of the TFEU.
9. Article 126(11) of the TFEU, in particular the possibility to require from the member state to make a make a non-interest-bearing deposit with the Union.
10. Article 126(10) of the TFEU.

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of being judged themselves by their peers. We are dealing with the results of such behaviour today.

While it is true that Article 273 does not mention the Commission, recognising its power to intervene in "disputes between member states" that could arise when applying the golden rule would not have been a bolder innovation than the reference to possible financial sanctions as set out under Article 8. Why has this solution not been adopted? The most likely answer is that **the reluctance to accept overly strict supranational checks remains as strong today as it was in the past**.

Conclusion

These two examples demonstrate the **ambiguity of the new treaty.** To be fair, legal difficulties were plentiful and it is no easy task to create an effective treaty that can stand alongside the TFEU. Additionally, this legal complexity was further magnified by some governments' ambivalence regarding transfers of sovereignty, which are however a cornerstone of the construction of Europe.

These limits must not cause us to lose sight of the **progress made in the agreement**. Given the significant amount of financial transfers that have been agreed upon over the previous months, it was important to obtain a formal commitment for fiscal responsibility from the Eurozone member states. The consecration of the Eurozone summit can help provide more stable economic governance that has often been lacking over the past few years. The fact that the new treaty can enter into force as soon as it is ratified by 12 signatory states is an important precedent, and underlines that none of them alone can oppose the progress desired by a sufficient number of member states.

Nevertheless, there is a clear contradiction between the relatively modest scope of the agreement and the formal shape it was given.

The choice of a treaty entails exposure to **various risks**. As a reminder, **in the ratification procedures, the number of veto holders is higher than the number of states**. In most countries, several parliamentary assemblies are generally called upon to intervene. Constitutional courts may find reasons to object, as may the head of state; and it is easy to imagine that a referendum on fiscal discipline would be hard to win. Reforms are not simply a question of approving major principles around a conference table; the **conditions for their successful implementation** must also be considered. It is most certainly at this level that the European Council's decisions appear the weakest.

With the support of the European Commission
Europe for Citizens Programme

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design: *Notre Europe*

ISSN 2103-8635