THE EURO CRISIS IN CONTEXT: HISTORICAL AND LEGAL PERSPECTIVES

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The current concerns about the Euro and the consequences for European integration are here considered against the broad historical and legal background of the Euro. From that historical perspective it is noted that the current crisis is perhaps not so unusual.

La situation de crise que connaît aujourd'hui l'Euro et ses conséquences éventuelles sur le devenir de l'intégration européenne sont analysées à l'aune du contexte historique et juridique qui a présidé à l'instauration de la monnaie européenne. Sur ce constat, l'auteur démontre que la crise actuelle était largement prévisible.

I INTRODUCTION

European integration has become a topic of renewed interest and scrutiny of late, both within Europe itself and beyond. Uncertainty about the ability of some euro area countries to manage their accumulated sovereign debt is on-going. In the case of one member state in particular (Greece), questions are being asked about that country's chances of avoiding an orderly or, indeed, unorderly default and what, if any, repercussions this may have for the euro and for the European integration project more generally. Speculation is rife. Might it be preferable for Greece to abandon the euro and return to its national currency of old? Is it just a matter of time before Germany 'relents' and discontinues its objection to the issuing of Eurobonds? And what does one make of the situation in Spain or Italy? Surely, Italy is too big to 'fail', and therefore also too big to bail out!?

The purpose of this article is not to add to the above speculation. Rather it seeks to place the current unease about the euro, about some of the members of the euro area, and about the very future of the European Union itself in a broader, historical

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context. The main observation to be made is that European integration has tended not to follow a simple, linear path in the past. It is therefore arguable that what is being experienced today is not really unusual. Certainly, the current crisis affecting the euro is unlikely to be the last hurdle on the road to full European maturity.

This article is divided into two major parts. A first part retraces the history of the euro's introduction. Pivotal is the Treaty on European Union (the TEU), signed in Maastricht in 1992 and in effect since 1 January 1993. A second part examines the impact for the euro of the current sovereign debt problems experienced by, in particular, the southern member states of the EU. The origins of the current 'crisis' is a mixture of internal and external (the GFC!) factors. Its repercussions for European integration, however, while potentially profound, need not be entirely negative. Necessity may ultimately advance the European cause, especially where it leads to a tightening of centralised (European) control over the budgetary and fiscal policies of the participating member states.

II MAKING OF THE EURO

A The 1962 Marjolin Memorandum

The euro has been in place for barely a decade, but its introduction is the product of a gestation period that was considerably longer. The idea of a common currency first featured in a European (Commission) document of 24 October 1962. The Marjolin Memorandum, named after French Commissioner and Vice President Robert Marjolin, stressed the link between economic and monetary integration. While the

Memorandum itself was not acted upon at the time, a Committee of Governors from the various national central banks was set up in its aftermath. Established in 1964, this Committee of Governors would prove pivotal for fostering monetary cooperation among the central banks of the (then 6) EEC member states.[1]

B Articles 103-109 EEC

The precise nature of the relationship between economic and monetary integration may be open for debate. Certainly, economic integration need not lead to monetary integration. Even so, in the EU both have traditionally been treated as objectives that are closely intertwined. To be clear, the creation of a single currency did not feature expressly in the 1957 text of the Treaty establishing a European Economic Community. However, the EEC Treaty did contain a (limited) number of provisions that can be viewed, with the benefit of hindsight, as building

1 HK Scheller *The European Central Bank: History, Role and Functions* (ECB, Frankfurt am Main, 2004) 17.

blocks which could, one day, facilitate the establishment of a monetary union of sorts. Of note in this regard is Title Two of Part Three in the Treaty. The Title is headed Economic Policy and comprises separate Chapters on the need for member states to treat their "conjunctural" (ie short-term economic) policies as a matter of "common concern"[2] and to ensure the "equilibrium"[3] of their overall balance of payments. A close reading of the provisions in both Chapters (specifically arts 103-109) suggests that monetary cooperation was of concern to the Treaty drafters only in so far as it might assist in bringing about the economic integration of Europe. Put differently, in the Treaty text as adopted originally, monetary policy was subordinated to economic policy.

Articles 103-109 EEC arguably constituted an insufficient legal basis for the development of a full-fledged monetary union. Certainly, in political terms, the transfer of national sovereignty that a monetary union involves is such as to make a more explicit, unequivocal expression of the intent preferable if not imperative. The year 1969 proved pivotal in this regard. In France Charles De Gaulle had resigned as President of the Fifth Republic and was succeeded by Georges Pompidou. In that same year Willy Brandt became Chancellor of the Federal Republic of Germany. Jean Monnet – a French civil servant widely regarded as one of the founding fathers of the EEC – seized the moment by suggesting that the time was ripe for the peaceful integration of Europe to enter a new phase. Specifically, by moving towards an economic and monetary union (an EMU, in the jargon) as well as letting the United Kingdom join the European Community, a deepening as well as a widening of the integration movement could and should be achieved in his view. The six Heads of State and Government agreed as much during a summit at The Hague in December 1969.

C Economists v Monetarists

The 1969 in-principle (political) agreement notwithstanding, no real consensus existed as regards the means by which monetary union was to be achieved. Broadly speaking, two lines of thought became apparent.[4] On one hand, the so-called monetarists (including the French) favoured an immediate decision to lock in the exchange rates of national currencies in the member states. On the other hand, the

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2 Article 103.1 EEC.

3 Article 104 EEC.

4 The discussion below draws upon M Vranken *Fundamentals of European Civil Law and Impact of the European Community* (1st ed, Federation Press, Sydney, 1997) 188-192.

'economists' (including Germany) viewed monetary integration as the end result of a process of further economic harmonisation to be achieved first. The latter group cautioned against undue haste: Monetary integration in their view would require institutional change, not just in the form of the establishment of a European Central Bank, but also in terms of increasing the democratic legitimacy of the Community's decision-making processes. This in turn would require formal amendments to the Treaty of Rome.

D The Werner Report

To avoid an impasse, and in an attempt at diffusing the tension between monetarists and economists, a working group was convened with Pierre Werner, the Prime Minister and Finance Minister of Luxembourg, as its chair. The group published its findings in 1970. In essence, the Werner report provided for the gradual, three-staged establishment of a monetary union, within a time span of 10 years commencing on 1 January 1971. However, the intervention of certain external factors – the (US) dollar 'crisis' of 1971, in particular,[5] followed by the oil and economic 'crises' of the 1970s[6] – meant that the Werner report did not get beyond the first stage of its implementation. Even so, this did not prevent some, if only piece-meal, progress. Thus a European Monetary Cooperation Fund (EMCF) was set up in 1973. While membership of the EMCF consisted of the same people that made up the Committee of Governors established a decade earlier,[7] the EMCF was accorded separate legal personality.[8]

In broad terms, the EMCF's brief was to facilitate the transition to a monetary union. Of special note is that the enabling Regulation provided an official picture of what this monetary union was meant to look like.[9] Intriguingly, a common currency was but one option. An alternative of seemingly equal standing was the "total and irreversible convertibility", at "irrevocable parities", of the various national currencies vis-à-vis one another.[10] Either way, the EMCF was to promote a progressive narrowing of any margins in the fluctuation of the national currencies

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5 BME McMahon "Progress towards Economic and Monetary Union, in Commission of the European Communities" *Thirty Years of Community Law* (The European Perspectives Series, Office for Official Publications of the European Communities, Luxembourg, 1983) 397 at 405.

6 PSRF Mathijsen *A Guide to European Community Law* (5th ed, Sweet & Maxwell, London, 1990) 261.

7 See the discussion of the Marjolin Memorandum above.

8 Regulation 907/73/EEC, *OJ*, 1973, L 089/2 (art 1).

9 McMahon, above n 5, 407.

10 Regulation 907/73/EEC, above n 8, Recital 4.

against each other. To this effect the EMCF could intervene on the currency exchange markets. As the Community-set margin of fluctuation between currencies was less than that permissible by the IMF more generally, the expression snake-in-the-tunnel came about, with the Community currencies forming the snake and the outer limits as allowed by the IMF being the tunnel. Of interest is that, for accounting purposes, the EMCF's operations as regards the currencies of the member states were to occur by reference to a so-called European (monetary) unit of account or EUA. The EUA then was the lesser-known precursor to the European Currency Unit (or ECU) which in turn would be replaced by the euro one day.

E The EMS and ECU

The snake system was short-lived. McMahon records that the (then) three applicant member states of the United Kingdom, Ireland and Denmark joined the 'snake' in May 1972 only to withdraw a few months later.[11] By early 1974 it had become clear that some of the original EEC member states (Italy and France) also were unable to maintain the discipline required to remain within the 'snake', effectively reducing it to the "German dominated"[12] currencies of the Benelux countries in addition to, of course, the Deutschmark itself. In the result the second stage of the Werner plan for the gradual transition towards monetary union had to be deferred out of necessity.

An over-dependence on the German mark and inflexibility in accommodating the weaker currencies are among the reasons cited for the snake's early demise.[13] Even so, the disadvantages and risks associated with freely floating currencies – currency speculation, distortion of competition and impairment of economic growth, in particular[14] – triggered renewed attempts at creating a zone of monetary stability in Europe. In 1978 this led to a political agreement on the general principles of a European Monetary System (EMS). The EMS became operational one year later. At its centre stood a new European currency unit: The ECU.

The ECU was designed as a basket currency, made up of the national currencies of the EEC member states weighted according to the relative economic importance of each country. Once again the various Community currencies were allowed to

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11 McMahon, above n 5, 407.

12 Ibid.

13 Ibid.

14 Ibid, at 408.

fluctuate within limited margins in relation to one another. Only this time the ECU provided a central reference point for determining when any such fluctuation became extreme. The primary vehicle for addressing excessive fluctuations was intervention by the central banks of the member states concerned. To this effect unlimited (short-term) access to credit was available from the EMCF set up in 1973.[15] A re-alignment of exchange rates was to be a means of last resort only. To the extent that fluctuations in the exchange rate of a particular national currency reflected deeper, underlying economic problems in one of the member states, that country was expected to make adjustments in its own (national) economic policy.[16]

F An (ominous) Case of Déjà Vu?

The account thus far is by no means complete. Yet some parallels with the current euro crisis begin to emerge. Then as well as now the national economies of some member states tend to outperform those elsewhere. This puts upwards pressure on the national currency of the 'stronger' economies. The economies of the 'weaker' states for their part are being held back because of the built-in rigidities that come with pegging themselves to a (currency) standard too high for their own (economic) comfort. The move to a single European currency only exacerbated the problem. Economic integration was meant to produce a levelling effect across the Union in the lead-up to monetary union. Unfortunately, several decades of regional financial assistance notwithstanding,[17] the disparities between the northern and southern parts of Europe, in particular, remain substantial.

G The SEA

Remarkably, the EMCF, EMS and ECU were all achieved without the need for formal treaty revision. Apart from the 'specific' provisions in arts 103-109 discussed earlier, the 1957 text of the EEC Treaty contained only general provisions on economic convergence. These could be found in Part One on Principles (of the treaty). In addition, there were certain 'enabling provisions' – arts 145 and 235, in particular. Pursuant to art 145 EEC the Council (of Ministers) must "ensure coordination of the general economic policies of the Member States". Article 235 EEC, for its part, created the jurisdictional basis for the residual powers

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15 See the discussion of the Werner Report above.

16 Vranken, above n 4, 190.

17 A European Social Fund was established in 1958. It since has been complemented by the European Regional Development Fund (1975) and the European Cohesion Fund (1994). Post Lisbon, the EU treaty confirms the Union's objective in "reducing disparities" between the levels of development of the various regions and "the backwardness of the least favoured regions" (art 174 TFEU). Tellingly, structural funding continues to account for one-third of the entire EU budget.

of the Council whenever Community action proved "necessary" to attain a Community objective "and this Treaty has not provided the necessary powers". It was only in the mid-1980s that the Single European Act (SEA) formally introduced the concept of monetary union in the Treaty of Rome.

The SEA effectively signified the first major occasion for amending the 1957 EEC Treaty. The SEA expressly linked monetary union to the notion of economic union. To this effect it inserted a new art 102A into the EEC Treaty. This provision then served as the basis for a relaunching of the EMU project by the then Head of the European Commission, Jacques Delors. Undisputedly the single most successful President of the Commission to date, Delors in 1989 chaired a committee entrusted with the task of investigating concrete steps to bring about this EMU.

H The Delors Report

The Committee's report, also known as the Delors report, contained similarities and even direct references to the Werner report of 1970. But it also reflected the lessons learned from the intervening two decades. Specifically, the Report confirmed the principles of a progressive (three-staged) realisation of the monetary union and the parallel advancement of economic and monetary integration. Reluctant to address the issue of a European Central Bank head on, the Report proposed the establishment of a European System of Central Banks (ESCB) instead. Because of the need for a transfer of national sovereignty in the final stage of EMU, the Delors report further called for a new treaty to amend the EEC Treaty. The Report thus set the scene for the developments culminating at Maastricht.

I Maastricht Treaty

The 1992 Maastricht treaty on European Union introduced a new Title Six ("Economic and Monetary Policy") in Part Three ("Community Policies") of the E(E)C Treaty. In addition, a series of Protocols were annexed to the Maastricht Treaty concerning the transition to the final stage of EMU. The member states at Maastricht agreed that the move towards monetary union would be irreversible. They also decided on a date: 1997 at the earliest or 1999 at the latest. In the lead-up to D day – 1 January 1999, as it turned out - the member states were expected to get their public finances in order. Article 109e.2.b EC uses the expression of "sound" public finances in this regard. Further, art 104c.1 EC tells member states to avoid "excessive" government debts. Protocol 5 limits the maximum permissible annual government deficit to 3% of GDP and the maximum overall government debt to 60% of GDP. With the benefit of hindsight, these percentages – or, rather,

their lack of effective enforcement – would come back to hound the EU before too long. Also of interest, again with the benefit of hindsight, is some of the language used in art 109h EC. That provision sought to address scenarios where "a member state is in difficulty or is seriously threatened with difficulties" as regards its balance of payments and "where such difficulties are liable in particular to jeopardise the functioning of the Common Market". This language bears a striking resemblance to that used in later legal instruments, not only for the establishment of the European Financial Stability Facility and the European Financial Stabilisation Mechanism in 2010, but also for their 'permanent' replacement, the European Stability Mechanism, in 2012.

In terms of institutional set-up, the TEU provided for the establishment of a European System of Banks (ESCB) and a European Central Bank (ECB) pursuant to art 4a EC. Protocol 3 attached to the TEU clarifies that the ESCB is composed of the central banks of the member states and the ECB. Together the national central banks of the member states also form the European Monetary Institute (EMI), replacing the European Monetary Cooperation Fund (EMCF), pursuant to art 109f EC. Whereas the primary objective of the ESCB is to maintain price stability (Protocol 3, art 2), the EMI was charged with the broader task of preparing for the 3rd stage of EMU (Protocol 4, art 2).

J At Long Last: The Euro

Implementation of the Maastricht treaty led to the introduction of the Euro as a single currency in 11 of the (then) 15 member states on 1 January 1999. Of the four remaining member states, two (Greece and Sweden) did not fulfil the convergence criteria at the time, although one (Greece) subsequently managed to join - in 2001. Two other member states, Denmark and the United Kingdom, negotiated a 'derogation' Protocol which effectively allowed them to hold on to their national currencies regardless of fulfilling the requirements for adopting the euro. On 1 January 2002 the euro thus became a physical reality in 12 member states. Five further EU countries have since adopted the euro: Slovenia in 2007; Cyprus and Malta in 2008: Slovakia in 2009; and Estonia in 2011.

The provisions of the Maastricht Treaty have not been modified in substance by the subsequent Amsterdam and Nice treaties.[18] This state of affairs reinforces the importance of the supervision and compliance provisions negotiated at Maastricht and built upon through a so-called Stability and Growth Pact. In a nutshell, monitoring is entrusted to the Commission in the first instance. The European

18 JC Piris *The Lisbon Treaty. A Legal and Political Analysis* (Cambridge University Press, Cambridge, 2010) 303.

Commission reports to the Council who, in turn, may put any non-compliant member state on 'notice' and, as a means of last resort, impose a fine.

III UN-MAKING OF THE EURO?

A The Stability and Growth Pact – Mark I

It is useful to look at the safeguards for the Euro in greater detail. The Stability and Growth Pact (SGP) is a mechanism for monitoring the on-going compliance by member states with the Maastricht criteria – of 3 and 60% – once they have adopted the euro and for addressing any national deviations from the Maastricht criteria should these occur. The former aspect of the SGP has been referred to as its "preventive" arm, whereas the latter is said to form the "corrective" arm.[19] The preventive arm is the focus of Council Regulation (EC) 1466/97.[20] The corrective arm is the subject of Council Regulation (EC) 1467/97.[21]

Pursuant to Regulation 1466/97 member states must submit information (to the Council as well as the Commission) about their budgetary position on a regular basis. The focus is on allowing the European institutions to review the medium-term budgetary objectives of the member states. This in turn provides an opportunity for an "early warning" by the Council in order to prevent "the occurrence of an excessive deficit" in individual member states.[22] Overall, the preventive arm can be said to typify the EU's preference for "soft" procedures and, ultimately, "peer pressure" to keep member states in line.[23]

The corrective arm of the SGP, dealt with in Regulation 1467/97, is different in its approach. It relies on "stricter and more formal procedures" to ensure compliance with the Maastricht criteria.[24] Specifically, it entails the submission of

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19 R Morris, H Ongena and L Schuknecht *The Reform and Implementation of the Stability and Growth Pact* (Occasional Paper Series, no 47, European Central Bank, Frankfurt am Main, June 2006) 12.

20 Council Regulation (EC) no 1466/97 of 7 July 1997 on the Strengthening of the Surveillance of Budgetary Positions and the Surveillance and Coordination of Economic Policies, *OJ*, 1997, L 209/1.

21 Council Regulation (EC) no 1467/97 of 7 July 1997 on Speeding up and Clarifying the Implementation of the Excessive Deficit Procedure, *OJ*, 1997, L 209/6.

22 Regulation 1466/97, Article 6.2.

23 Morris, Ongena and Schuknecht, above n 19, 12.

24 Ibid.

a formal report by the Commission to the Council,[25] followed by a Council recommendation addressed to the member state concerned.[26] Where the member state fails to respond by taking "effective" action, the Council issues a formal decision.[27] The decision itself is enforced, in the first instance, through an exercise in public shaming[28] and, as a means of last resort, through the imposition of an escalating range of financial sanctions.[29]

B The Stability and Growth Pact – Mark II

For a variety of reasons, both economic and political, the SGP was not rigorously enforced[30] and, even then, ultimately watered down.[31] Bergsten and Kirkegaard provide extensive data to show all was not well from the outset.[32] Indeed, when taken at face value, the Maastricht maxima of 3% annual and 60% overall public deficit represented "hard" convergence criteria for euro area membership.[33] In reality, the 60% rule proved difficult for many member states. Figures for 1998, the year immediately prior to the introduction of the euro currency, show that no fewer than six of the 11 original euro area members had gross debt figures in excess of 60% GDP. In worst position were Belgium and Italy, with general government gross debt in 1998 at 117.4 and 114.9 % of GDP respectively.[34] France made the cut-off, if only just (at 59.4%), whereas Germany fell short of the target, although (at 60.3%) not by much. The other countries to exceed the 60% rule were the Netherlands, Austria and Spain. Meeting the 3% rule, on the other hand, proved less problematic.[35] As Morris, Ongena and Schuknecht have commented, national governments "staked their reputations" on

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25 Regulation 1467/97, art 2.2.

26 Regulation 1467/97, art 3.3.

27 Regulation 1467/97, art 5.1.

28 The Council may decide to make its recommendations to the member state public: Regulation 1467/97, art 4.1.

29 Regulation 1467/97, arts 6 and 11-16.

30 Morris, Ongena and Schuknecht, above n 19, 15ff.

31 Ibid, 18ff. See Council Regulations (EC) no 1055/2005 and no 1056/2005, both of 27 June 2005, *OJ*, 2005, L 174/1 and L 174/5 respectively. These Regulations amend initial Regulations 1466/97 and 1467/97.

32 Bergsten, CF, and Kirkegaard, JF, *The Coming Resolution of the European Crisis* (Policy Brief, Peterson Institute for International Economics, Washington DC, January 2012).

33 Ibid, 3.

34 Ibid, 4 (Figure 1).

35 Morris, Ongena and Schuknecht, above n 19, 11 (Table 2).

bringing deficits below 3% so as to be "in time to be among the first wave" of euro area countries.[36]

The start of the 21st century was characterised by persistent slow economic growth together with what can only be described as political "consolidation fatigue".[37] In response the Commission formulated a number of proposals, in 2002 and again in 2004, that sought to refine the operation of the Stability and Growth Pact. Subsequent discussions by the national Ministers for economics and finance in the (ECOFIN) Council resulted in a decision to formally amend the regulatory framework of the SGP. Council Regulations 1055/2005 and 1056/2005 thus introduced changes to both the preventive and corrective arms of the SGP.[38]

The changes in the preventive arm aimed at acknowledging and positively accommodating national diversity within the euro area. In particular, each member state henceforth was able to formulate its own country-specific, medium-term budgetary objectives. While, of course, not giving individual member states a total *carte blanche*, country-specific structural reform (eg pension reform) could be taken into account when assessing a member state's compliance record with the Maastricht criteria. The changes to the corrective arm equally sought to introduce more flexibility by, ultimately, increasing the scope for discretion by the European institutions in holding individual member states accountable. While laudable in principle, these changes arguably also risked exacerbating an already weak enforcement scenario.[39]

If things looked poorly at the commencement of the 21st century, they were about to get a whole lot worse. The period from 2007 onwards, in particular, is perhaps best described as a rollercoaster, whether viewed in political (protracted negotiations for the Lisbon treaty), legal (the struggle to ratify Lisbon), or economic (the so-called global financial crisis followed by a contagious European sovereign debt crisis) terms.

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36 Ibid, 11.

37 Ibid, 15.

38 See the full references to both European laws in n 31 above.

39 Reactions to the revamped SGP were mixed: Morris, Ongena and Schuknecht, above n 19, 22.

C Lisbon

The Treaty of Lisbon grew out of the failed attempt at producing a constitutional framework for the EU.[40] In terms of the monetary union, Lisbon seeks to improve the decision-making powers of the Council for the euro zone.[41] The Treaty on the Functioning of the European Union (TFEU), as it is known officially, contains provisions specific to member states whose currency is the euro. In particular, Article 136 TFEU provides the basis for the adoption by the Council of measures:

(a) to strengthen the coordination and surveillance of their budgetary discipline; and

(b) to set out economic policy guidelines for them, while ensuring that they are compatible with those adopted for the whole of the Union and are kept under surveillance.

Council decisions are made by qualified majority, but only euro zone countries are allowed to vote.

D Beyond Lisbon

The Treaty of Lisbon was formally signed on 13 December 2007 and entered into force on 1 December 2009. The time frame is important. It is during this period that the Global Financial Crisis took hold, with the European sovereign debt problems coming to the fore from late 2009 onwards. In response, the European Council decided to amend Article 136 TFEU by adding a new paragraph to the effect that:

> The Member States whose currency is the euro may establish a stability mechanism to be activated if indispensable to safeguard the stability of the euro area as a whole. The granting of any required financial assistance under the mechanism will be made subject to strict conditionality.

The above amendment was the result of a European Council decision taken on 25 March 2011.[42] The decision grew out of a European Council meeting held in late October 2010 during which the various Heads of State and Government of the member states agreed upon the need for a "permanent crisis mechanism" to safeguard the financial stability of "the euro area as a whole".[43] The permanent

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40 B Milton, J Keller-Noëllet with A Bartol-Saurel *The European Constitution, its Origins, Negotiation and Meaning* (John Harper Publishing, London, 2005).

41 Piris, above n 18, 305-307.

42 European Council Decision 2011/199/EU, *OJ* L 91/1, 6.4.2011.

43 Ibid, Recital 2.

crisis mechanism in question is the European Stability Mechanism (ESM). The ESM did not come about immediately. Rather, it was preceded by two temporary constructs, the European Financial Stabilisation Mechanism and the European Financial Stability Facility. Of note is that none of these institutions existed when Lisbon first was negotiated in the 1990s. This realisation serves as an indication of the speed at which the situation in the economic and financial markets has been evolving of late.

E The EFSF and the EFSM as Temporary Firewalls

According to Angel Gurria, Secretary-General of the OECD, the GFC created an atmosphere of uncertainty beyond parallel and with effects that could be felt world-wide.[44] The flow-on effects for Europe in terms of what has since been labelled a sovereign debt crisis became an issue of concern from late 2009 onwards. In May 2010, following the activation of an EU/IMF bail-out package for Greece with an initial loan in the order of 45 billion euro, the Council of the EU agreed to the establishment of a European Financial Stabilisation Mechanism (EFSM) together with a European Financial Stability Facility (EFSF).

The legal basis for the EFSM is Council Regulation 407/2010 of 11 May 2010.[45] This Regulation in turn is based on Article 122(2) TFEU to the effect that, where a member state is in difficulties or is seriously threatened with severe difficulties caused by "natural disasters or exceptional occurrences beyond its control", financial assistance may be granted "under certain conditions". The nature of these 'exceptional circumstances' is elaborated upon in the preamble to the Regulation. Specifically, a "serious deterioration in the international economic and financial environment"[46] and, in particular, the "unprecedented global financial crisis and economic downturn that have hit the world"[47] are said to have led to "a severe deterioration of the borrowing conditions of several Member States"[48]. Of course, if all euro-zone members had complied with the Maastricht criteria in the first place, the impact of the GFC might have been easier to handle. As for Regulation 407/2010, it simply states that, in order to address this 'exceptional'

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44 A Gurria "The Global Financial Crisis" (2008) 33(6) New Zealand International Review 17.

45 *OJ* L 118/1, 12.5.2010.

46 Ibid, Recital 2.

47 Ibid, Recital 3.

48 Ibid, Recital 4.

situation, a "stabilisation mechanism" is to be established and activated in the context of "joint EU/IMF support".[49]

Regulation 407/2010 stresses that any assistance to individual Member States is not provided for altruistic reasons but rather it occurs with a view to preserving the overall financial stability of the European Union.[50] A member state seeking assistance must discuss its needs with the Commission. While the Commission defines and monitors the general economic policy conditions to be attached to any financial assistance in order to maximise the chances of the recipient member state getting back on its own (financial) feet, the ultimate decision to grant assistance is taken by the Council acting by a qualified majority.[51] Financial assistance by the Union can take the form of a loan or a credit line. To raise the necessary funds the Commission is authorised to borrow on the capital markets or from financial institutions. Any costs associated with the provision of financial assistance are to be borne by the member state concerned.[52]

Regulation 407/2010 binds all 27 member states of the EU. In addition, the 17 member states of the euro area agreed to establish a so-called Special Purpose Vehicle[53]: the European Financial Stability Facility (EFSF). Technically, the EFSF is a Luxembourg-based company owned by the euro-area member states. Its objective is to preserve financial stability by providing temporary financial assistance to euro-area member states in need. In practical terms, if a euro-area member state experiences difficulty when borrowing money in the financial markets, the EFSF can be used as an intermediary to raise the funds required. To this effect the EFSF can issue bonds backed by a guarantee of the euro-area member states. Countries to have received assistance in this fashion are Ireland (in November 2010) and Portugal (in May 2011). The 2010 bail-out of Greece was not financed through the EFSF, but rather it was the result of a bilateral commitment by the euro-zone countries and the IMF.

F The ESM and the TSCG as Permanent Firewalls

It did not take long for it to become clear that the economic and financial markets considered temporary solutions to what was seen as a structural problem in

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49 Ibid, Recital 5.

50 Ibid, art 1.

51 Ibid, art 3.

52 Ibid, art 7.

53 Special Purpose Vehicle is the expression used by in Press Release 9596/10, issued by the Council of the EU, following an extraordinary meeting of the EU Ministers for Economic and Financial Affairs in Brussels on 9/10 May 2010.

EU governance to be inadequate. Two post-Lisbon treaties specifically aim at addressing the current European 'sovereign' debt crisis in a more permanent fashion. They are the Treaty establishing the European Stability Mechanism (the ESM Treaty) and the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (the TSCG). The ESM treaty was signed on 2 February 2012 and the TSCG, also known as the fiscal compact, one month after that. At one stage it was anticipated that the ESM treaty could enter into force as early as July 2012, ie one year ahead of schedule. However, in view of a constitutional challenge currently before the German *Bundesverfassungsgericht*, this date has proved elusive.

While open for accession by other EU member states upon application,[54] the ESM Treaty applies to the 17 members of the euro area in the first instance. It is these 17 countries who signed the text of the Treaty, a first time on 11 July 2011 and, following modification of the text to incorporate subsequent decisions by the Heads of State and Government "aimed at improving the effectiveness of the mechanism",[55] again on 2 February 2012. The text itself is a modified version of the original document agreed to in July 2011. Technically, the ESM – not unlike the EFSF - is an international financial institution[56] with its seat and principal office based in Luxembourg.[57] Its task is to provide financial assistance to (euro-area) member states "where needed"[58] and subject to "strict conditionality".[59] This financial assistance can take the form of a credit line[60] or a loan.[61] It also may involve the purchase of bonds from the member state concerned.[62]

The ESM Treaty clarifies the exceptional circumstances required for intervention. It does so by emphasising that ESM support must be "indispensable" to safeguard the financial stability of the euro area as a whole (again, rather than

54 ESM Treaty, Article 44; see also Recital 7: "All euro area Member States will become ESM Members".

55 Factsheet, *Treaty establishing the European Stability Mechanism*, 2 February 2012, EN, 1.

56 ESM Treaty, art 1.

57 ESM Treaty, art 31.

58 ESM Treaty, Recital 1.

59 ESM Treaty, Recital 2.

60 ESM Treaty, art 14.

61 ESM Treaty, art 16.

62 ESM Treaty, art 17-18.

individual countries).[63] The conditions attached to ESM support can range from the imposition of a macro-economic "adjustment" programme to "continuous respect of pre-established eligibility conditions".[64] The latter are not spelled out in the ESM Treaty itself. However, it does bring to mind the conditions for joining the euro in the first place: maximum annual budget deficits of 3% and overall public debt of 60% of GDP. In addition, the ESM Treaty expressly stipulates that it and the TSCG – to be discussed immediately below - are complementary.[65] For any member state seeking financial assistance under the ESM Treaty this means that it is expected to ratify the TSCG as well as the ESM Treaty itself. This in turn commits the relevant member state to implement the balanced budget rule as specified in the TSCG. Furthermore, the ESM is stated to "cooperate very closely" with the IMF - both at "technical and financial" levels; as a rule, any euro area members seeking assistance from the ESM must also approach the IMF.[66]

The ESM Treaty takes effect upon ratification by all 17 euro area member states. At July 2012 this was still to occur.

Unlike the ESM Treaty, the TSCG has been agreed to by (almost) all EU member states. The text of the TSCG, formally signed on 2 March 2012, is the result of an agreement reached among 25 of the 27 EU member states (excluding the UK and the Czech Republic) at a European Council meeting held on 9 December 2011. The TSCG is scheduled to enter into force on 1 January 2013, upon ratification by 12 euro area countries. This novel technique avoids the possibility of a single member state holding the collective to ransom by refusing to ratify. As any member state failing to ratify cannot avail itself of the financial assistance available under the Treaty, a clear incentive to ratify exists. In Ireland ratification was approved by a popular referendum on 31 May 2012.

The TSCG introduces rules as regards a so-called fiscal compact.[67] It obliges the parties to the compact to maintain a balanced budgetary position.[68] Excessive deficits trigger an "excessive deficit procedure".[69] The TSCG further provides for regular meetings of the various Heads of State or Government from the euro area.

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63 ESM Treaty, Article 12.1.

64 Ibid.

65 ESM Treaty, Recital 5.

66 ESM Treaty, Recital 8.

67 TSCG, Title 3.

68 TSCG, art 3.

69 TSCG, arts 4-5.

These "Euro Summits" are meant to be informal occasions for exchanging views concerning the governance of the euro area.[70] They are attended by the Presidents of the European Commission and, upon invitation, the ECB and the European Parliament.

G Towards a Single Banking Regulator?

In the early hours of 29 June 2012 a political agreement was reached to allow European bailout funds to be provided to struggling banks in the member states directly rather than through the member states. As reported in the general media, in exchange the member states committed to more centralised supervision and regulation of their banks through a newly to be established euro bank regulator.[71] The language used in the official EU press release is distinctly tentative. While acknowledging the importance of breaking "the vicious circle between banks and sovereigns", the only firm commitment is for the Commission to prepare proposals for a single supervisory mechanism "shortly" with a request for the Council to consider these proposals "as a matter of urgency by the end of 2012". Once an "effective" single supervisory mechanism is in place, which will involve the ECB, a direct recapitalisation of banks in the euro area by the ESM becomes a "possibility" subject to "appropriate conditionality".[72]

IV SUMMING-UP

The euro effectively replaced the national currency of 11 EU member states on 1 January 2002. At that stage the euro had been in place as a 'virtual' currency for accounting purposes and cash-less payments for three years already. The build-up to the introduction of the euro goes back even further in time. The immediate forerunner of the euro, the European Currency Unit or ECU, dates from the late 1970s; its introduction has a political history that can be traced back to the late 1960s. It is therefore clear that the development of a monetary union for the EU has had a gestation period stretching more than four decades.

In creating the euro the EU plainly did not wish to be unprepared. It tried to avoid the risk of stepping onto one-night-old ice, so to speak. And yet, things did start to unravel in more recent years. In seeking answers for the current woes of the

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70 TSCG, art 12.

71 Shanahan, L, 'Eurozone Deal lifts Hopes of End to Debt Crisis' *The Australian*, 2 July 2012.

72 Euro Area Summit Statement, Brussels, 29 June 2012.

euro, it has been useful to go back over the key developments of the past half century or so. That is where the seeds of the euro's current woes lie.

Since 1 January 2002 six further EU member states have joined the euro club. The initial euphoria notwithstanding, two different but related problems have arisen. A first problem is internal. Member states did not follow the club's rules as regards public deficit and debt limits. This has now come to haunt some of its (mainly southern) members. A second problem is external. The GFC has brought into the open the first problem; it also has exacerbated it. To fix the problem creative thinking will be required. Any attempt at doing precisely this is hampered by the need to preach austerity without stifling economic recovery. In all of this German Chancellor Angela Merkel plays a pivotal role. Her caution is understandable, laudable even, especially when viewed against the backdrop of the euro's chequered history to date. The slow pace of change need not be an issue for concern per se. After all, incrementalism is a traditional hallmark of European integration.

Jean-Claude Piris, the immediate past Director General of the Legal Service at the Council of the EU, asks how an ever larger EU membership base affects the pace of European integration.[73] While acknowledging the possibility of a two-speed Europe developing, Piris argues that this need not result in a two-class Europe.[74] Even more unequivocal is his considered opinion that Europe, and indeed the world at large, will continue to need a strong EU in the foreseeable future.[75] Further integration then may be the answer to the current euro crisis. Only time will tell how intimately the future of the euro is linked to the future of the EU itself.

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73 J-C Piris *The Future of Europe: Towards a Two-Speed EU?* (Cambridge University Press, Cambridge, 2012).

74 Ibid, 6-7.

75 Ibid, 8ff.