Congreso de los Diputados

NOTA SOBRE LA CONFERENCIA DE LA COMISIÓN EUROPEA SOBRE EL "PLAN DIRECTOR PARA UNA PROFUNDA Y AUTÉNTICA UEM: DEBATE SOBRE LA FUTURA UNIÓN ECONÓMICA, MONETARIA, BANCARIA Y POLÍTICA".

El 7 de mayo de 2013 tuvo lugar en Bruselas, en el Edificio Carlomagno, la Conferencia de la Comisión Europea sobre el "Plan Director para una profunda y auténtica UEM: debate sobre la futura unión económica, monetaria, bancaria y política". Por parte del Congreso de los Diputados acudieron el Presidente de la Comisión de Economía y Competitividad, D. Santiago Lanzuela Marina y el Vicepresidente de la misma, D. Jesús Caldera Sánchez-Capitán, acompañados por la Letrada de la Comisión, Dña. Mónica Moreno Fernández-Santa Cruz y por la Representante de las Cortes Generales ante el Parlamento Europeo, Dña. Carmen Sánchez-Abarca Gornals.

La Conferencia se inició a las 9:45 horas con la bienvenida a los asistentes por parte de **Jean- Claude Thébaut, Director General de la Oficina de Consejeros de políticas europeas (BEPA) de la Comisión Europea**, que cedió la palabra al **Presidente de la Comisión Europea, José Manuel Barroso**. Éste se refirió a la evolución de la Unión Económica y Monetaria (UEM) y a cómo la crisis financiera ha afectado a Europa, que ha aprendido de una forma severa la importancia de tener una economía y un sector financiero saneados. La UEM no puede seguir tal y como se fundó, hay que adaptarla a la realidad y evitar los desequilibrios financieros y la crisis de la deuda soberana. Si bien ésta no ha sido una crisis del euro como tal, dijo, la crisis en los países de la Unión ha puesto en jaque al euro. La crisis económica y soberana ha sido originada por la irresponsabilidad del sector financiero y la falta de competitividad entre los estados miembros.

Se refirió a las medidas tomadas hasta ahora para salir de la crisis, como el six pack o el two pack, y puso de manifiesto la necesidad de conseguir un mayor control presupuestario europeo y de los estados miembros, cuyos presupuestos deben ser equilibrados en el marco del Plan de Estabilidad y Crecimiento. Habrá que tomar medidas eficaces para garantizar la responsabilidad de los gobiernos y hacer todo lo posible para crear trabajo, creando una situación más segura jurídicamente que implicará nuevas cesiones de soberanía de los estados miembros a la Unión.

Habrá que reformar los Tratados, profundizar la UEM y garantizar la unión fiscal, económica y bancaria, refiriéndose al Blueprint presentado en noviembre por la Comisión. La unión bancaria y un mecanismo eficaz de supervisión son prioridades fundamentales que implican la revisión de los sistemas bancarios y de supervisión de los estados miembros.

Seguidamente se entró en el primer tema de debate: **"El futuro de la UEM: Profundizar en el debate"**, con **Stephen Fidler, Redactor del Wall Street Journal y del Dow Jones Newswires** como moderador. Intervino en primer lugar el **Vicepresidente de la Unión Europea y miembro de la Comisión responsable de Asuntos Económicos y Monetarios y del Euro, Olli Rhen**, que puso de manifiesto que, sin duda, lo peor de la crisis ha sido el desempleo originado por ésta. Se refirió a la necesidad de ganar confianza, incrementar la credibilidad de la política fiscal, reducir riesgos microfinancieros, corregir los desequilibrios financieros, estabilizar los mercados y mejorar la gobernanza económica, llegando a una unión bancaria que implicará importantes reformas estructurales. El principal reto a resolver, continuó, es que el crédito llegue a las empresas y a los hogares, impulsando el crecimiento, sobre todo en el sur de Europa. Para ello el Banco Europeo de Inversión ha incrementado un 40% su presupuesto. Desde el principio de la crisis se ha remodelado la arquitectura financiera en busca de estabilidad. Hay que reparar el sistema bancario en Europa y hacer algunas elecciones para el futuro, reforzando los principios de solidaridad y responsabilidad.

Jeroen Dijsselbloem, Presidente del Eurogrupo y Ministro de Finanzas de Países Bajos insistió en que el reforzamiento y avance de la UEM no puede esperar, en garantía del crecimiento y el empleo. Hay que promover la competitividad y la coordinación, impulsando el modelo social de la UE, que conllevará políticas activas en el mercado laboral, salud y educación. Todo ello, siguió, descansa sobre un sistema fiscal y financiero eficaz, devolviendo la confianza al sector bancario, para lo que es preciso conseguir la unión bancaria y un sistema de supervisión europeo sólido. En este camino, se hace preciso también reforzar las relaciones entre el Parlamento Europeo y los parlamentos nacionales, para implicar a los ciudadanos en las decisiones sobre el futuro de la Unión y dotar de amplia legitimidad democrática a los cambios que deben afrontarse.

Víctor Gaspar, Ministro de Finanzas de Portugal, se refirió a las decisiones tomadas por su país como consecuencia de la crisis, y a las causas de ésta, si bien quiso recordar las medidas que Portugal tuvo que adoptar para entrar en el euro, medidas que en países como España, Portugal o Italia implicaron bajadas de los tipos de interés que deterioraron las cuentas corrientes, incrementaron el crédito y aflojaron la disciplina financiera, llevando a desarrollos insostenibles en las finanzas públicas y burbujas en determinados mercados, como el inmobiliario. Esto debe tenerse en cuenta también para determinar las causas de la crisis y para asumir las responsabilidades que corresponden a la Unión Europea en su conjunto, más allá de culpar a uno u otro país en un claro ejemplo de falta de solidaridad. Las diferencias de cada estado miembro para financiarse han sido determinantes para las consecuencias de la crisis. La fragmentación financiera, concluyó, ha disparado los costes y ha minado el funcionamiento de la zona euro, por ello la unión bancaria es imprescindible.

Seguidamente tuvo lugar un debate en el que se pusieron de relieve los problemas para acceder al crédito de las familias y las PYMES, la necesidad de luchar contra el déficit fiscal y la importancia de la unión bancaria, el equilibrio público y privado y la consecución de empleo y crecimiento sostenible, para lo que es necesario continuar ahondando en las reformas estructurales.

A las 11.45 horas se inició el segundo debate, sobre **"La Gobernanza económica: restaurar la confianza y consolidar la estabilidad"**, moderado por **Peter Spiegel, Director de la Oficina en Bruselas del Financial Times.**

En primer lugar tomó la palabra **Marco Buti, Director General ECFIN, de la Comisión Europea**, que se refirió a la arquitectura acordada en Maastricht, centrada principalmente en la estabilidad de precios, la prohibición del déficit excesivo y el pacto de estabilidad y crecimiento, sobre una suave coordinación económica. La crisis ha puesto de manifiesto, dijo, algunos de los fallos de esta arquitectura. Tras un periodo de bajos tipos de interés se generaron burbujas que han explotado causando una crisis terrible, fallaron los controles de disciplina de los mercados y las herramientas de supervisión, por lo que es evidente que hay que mejorar la prevención de riesgos futuros y la inestabilidad financiera que sigue amenazando a la Unión Europea. Ya se han tomado una serie de medidas a nivel europeo y nacional que han implicado importantes reformas estructurales, pero aún queda por hacer. El Semestre Europeo ha sido un buen acicate para la coordinación económica y, aunque quizá se ha puesto el foco principalmente sobre el tema fiscal, hay otros desequilibrios que contemplar, precisamente a los que atiende el Blueprint, que persigue una integración bancaria y financiera, una auténtica unión económica y cambios en la responsabilidad política, con una supervisión única.

A continuación **Sharon Bowles, Presidenta de la Comisión de Asuntos Económicos y Monetarios del Parlamento Europeo**, y **Katarzyna Zajdel-Kurowska, miembro del Consejo del Banco Nacional de Polonia**, se refirieron a los principales retos que afronta la Unión Europea en los próximos años y a las lecciones que se han aprendido de la crisis.

Posteriormente, **Jorge Sicilia, Economista Jefe del BBVA** señaló la necesidad de una política fiscal común, cuya falta ha marcado siempre un punto débil de la Unión Europea, ocasionando una divergencia en competitividad entre los países miembros que ha pasado factura. Sin duda hay que reforzar los equilibrios financieros públicos y privados y sancionar las acciones que los vulneren. Una vez que lo anterior se consiga podremos comprobar si es un marco adecuado de funcionamiento para la Unión y los estados miembros en su conjunto.

Tras el almuerzo, a las 14:30 horas, se inició el tercer debate, moderado por **Caroline de Gruyter, Corresponsal en Bruselas del NRC Handelsblad**, sobre **"Unión**

Bancaria: hacia un sector bancario más estable, competitivo y resistente". Tomó la palabra para introducir el tema **Olivier Guersent, Jefe del Gabinete del Comisario Barnier**, que se refirió a la necesidad de consolidar el mercado financiero, aún fragmentado, reestableciendo la confianza. En igual sentido intervino **Yves Mersch, Miembro del Consejo Ejecutivo del Banco Central Europeo,** si bien señaló que aunque con la unidad del mercado financiero ahuyentaremos algunos problemas, otros quedarán sin resolverse y aparecerán en el futuro. **Marianne Thyssen, miembro del Parlamento Europeo,** pidió una amplia colaboración para avanzar en la unión bancaria, incluso de aquellos países que no pertenecen a la eurozona. **Kai Jan Trainer, Portavoz de la Comisión de Presupuestos y Finanzas del Parlamento austriaco,** se refirió a la necesidad de establecer un sistema único de garantía de depósitos en la UE, un sistema único de supervisión y un sistema único de rescate y reestructuración, cuando sea necesario, para cualquier banco europeo, si es que se quiere realmente un mercado financiero único. Concluyó señalando que el desempleo es un problema más grave que el déficit excesivo y ahí es donde la UE debe intervenir y advertir a un estado cuando no lo esté haciendo bien. Debemos preocuparnos ante todo de las necesidades de las personas. **Andrea Enria, Presidente de la Autoridad Bancaria Europea**, cerró el debate.

A las 15:45 horas comenzó el último debate sobre **"Legitimidad democrática y control, refuerzo a todos los niveles"**, moderado por **Brigid Laffan, Profesor de Políticas Europea del University College de Dublín**. Johannes Laitenberg, Jefe de Gabinete del Presidente Barroso introdujo el tema avalando la necesidad de una Europa más democrática, reforzando el papel del Parlamento Europeo en los asuntos económicos y la intervención de los parlamentos nacionales en mucho mayor grado, como representantes de los ciudadanos europeos, objetivos que el Semestre Europeo ha querido impulsar decididamente. Intervinieron también **Roberto Gualtieri, miembro del Parlamento Europeo, Rait Maruste, Presidente de la Comisión Constitucional del Parlamento estonio, Miguel Poiares Maduro, Profesor de Derecho Europeo del Instituto Universitario Europeo y Ministro de Desarrollo Regional de Portugaly Pierre Kroll, comentarista político belga.**

A las 17.00 horas se puso fin a la reunión.

Mónica Moreno Fernández-Santa Cruz
Letrada de la Comisión de Economía y Competitividad

COMISIÓN
EUROPEA

Plan director para una profunda y auténtica UEM:
Debate sobre la futura unión económica, monetaria, bancaria y política

PROGRAMA PROVISIONAL DE LA CONFERENCIA

Martes, 7 de mayo de 2013
Edificio Carlomagno, Comisión Europea

08:45-09:45 Inscripción

09.45-10.30 Bienvenida a cargo de *Jean-Claude Thébauld*, Director General de la Oficina de Consejeros de políticas europeas (BEPA), Comisión Europea

Discurso principal

José Manuel Barroso, Presidente de la Comisión Europea

10.30-11.45 **El Futuro de la UEM: Profundizar en el debate**

Olli Rehn, Vicepresidente de la Comisión Europea y miembro de la Comisión responsable de Asuntos económicos y monetarios y del euro

Jeroen Dijsselbloem, Presidente del Eurogrupo, Ministro de Finanzas, Países Bajos

Vitor Gaspar, Ministro de Finanzas, Portugal

Moderador: *Stephen Fidler*, Redactor Wall Street Journal y Dow Jones Newswires

11.45-13.00 **Gobernanza económica: restaurar la confianza y anclar la estabilidad**

Presentación: *Marco Buti*, Director General ECFIN, Comisión Europea

Miembros de la mesa redonda:
Sharon Bowles, Eurodiputada. Presidenta de la Comisión de Asuntos económicos y monetarios, Parlamento Europeo

Cat. Dariusz Rosati, Diputado, Presidente de la Comisión de Finanzas Públicas, Sejm de la República de Polonia

Jorge Sicilia, BBVA, Economista en Jefe

Holger Schmieding, Economista Principal, Berenberg Bank, Londres

Moderador: Peter Spiegel, Director de la Oficina de Bruselas, Financial Times

13.00-14.30 **Almuerzo**

14.30-15:45 **Unión bancaria: hacia un sector bancario más estable, competitivo y resistente**

Presentación: *Olivier Guersent*, Jefe del Gabinete del Comisario Barnier

Miembros de la mesa redonda:

Marianne Thyssen, Eurodiputada

Kai Jan Krainer, Diputado, Delegado de Presupuestos y economía, Partido Socialdemócrata, Nationalrat, Austria

Andrea Enria, Presidente de la Autoridad Bancaria Europea

Yves Mersch, Miembro de la Comité Ejecutivo del Banco Central Europeo

Moderadora: *Caroline de Gruyter*, Corresponsal en Bruselas, NRC Handelsblad

15:45-17:00 **Cómo reforzar la responsabilidad y legitimidad democrática en todos los niveles**

Presentación: *Johannes Laitenberger*, Jefe de Gabinete del Presidente Barroso

Miembros de la mesa redonda:

Roberto Gualtieri, Eurodiputado

Rait Maruste, Presidente de la Comisión Constitucional del Riigikogu, Estonia

Cat. *Miguel Poiares Maduro*, Ministro de Desarrollo Regional, Portugal

Pierre Kroll, comentarista político y humorista gráfico belga

Moderadora: *Brigid Laffan*, Cat. de Políticas europeas, University College, Dublin

EUROPEAN COMMISSION

José Manuel Durão Barroso
President of the European Commission

Opening keynote speech at the Conference on the Blueprint for a deep and genuine EMU

Check Against Delivery
Seul le texte prononcé fait foi
Es gilt das gesprochene Wort

Blueprint for a deep and genuine EMU conference/Brussels
7 May 2013

Spokespersons' Service
Service des Porte-parole

SPEECH/13/387

Dear Jean-Claude

Thank you, Minister Vitor Gaspar,

Distinguished members of the European Parliament, of national parliaments, ambassadors, distinguished guests, ladies and gentlemen,

'The most dangerous strategy,' Benjamin Disraeli once said, 'is to jump a chasm in two leaps'.

This, we must now admit, with the benefit of hindsight, is what is happening since the eurozone countries originally set up the economic and monetary union: while the leap towards monetary union was taken, the economic leg of the EMU stayed behind.

The consequences of this were not entirely foreseen at the time, which is understandable. As in all big projects of this nature, successes and shortcomings only become visible when the project is being implemented. The development of EMU also clearly shows that rather than conceptual problems, it was above all the incorrect application of the rules which lead to a malfunctioning of this EMU.

At the same time, economic reality quickly surpassed public institutions and academic thinking. Since the inception of the EMU, financial integration accelerated to a degree never seen or even imagined before. The resulting asymmetry between integrated financial markets on the one hand and a financial stability architecture still nationally segmented on the other, was to have far reaching consequences.

The hidden shortcomings of this set-up became clear with the fallout from the financial crisis.

Then the weaknesses in the initial design of the EMU became apparent. Before the crisis, monetary union had provided an unwarranted sense of security, shielding member states from the pressures of markets against their very often inept economic and budgetary behaviour. At the same time, the set-up was insufficient and the incentives too weak to motivate member states to push through the economic reforms they clearly needed. All this papered over the competitive problems and budgetary irresponsibility of some governments. It is only afterwards that Europe learned, the hard way, that the unbalanced framework and weakened rules of the EMU were unequal to the task of running the Euro area economy in times of increased interdependence and insecurity.
We must not underestimate to what an extent the global context has evolved since the conception of the EMU. Globalisation and economic interconnectedness has fundamentally changed the way we work; technology is changing the way we live and do business, financial integration has progressed on an unforeseen scale. Decisions by national governments, but also the economic health of the banking and corporate sectors, and of the households in one specific country, irrespective of its economic dimension, have a very strong impact on the situation in other parts of the EMU.

This is the new reality the crisis has brought to light. It showed that the EMU, as it was designed, had indeed become out of date. We will have to adapt our political and institutional framework to effectively deal with this reality, or it will mercilessly deal with us. We will create new certainties, or suffer uncertainty for some time to come.

We undeniably needed a fundamentally revised version, a deep and genuine economic and monetary union.

Ladies and gentlemen,

Dealing with the 'unfinished business of Maastricht', as you could call it, has proved to be difficult and demanding work.

By the time the financial crisis erupted on the other side of the Atlantic, a number of Eurozone countries had developed weaknesses that would turn the global financial crisis into a European sovereign debt crisis: they were falling behind in competitiveness, they had accumulated large private and public debts, and macroeconomic imbalances were growing beyond their control. The weak supervision of the financial sector and insufficient compliance with the criteria of the Stability and Growth Pact had allowed the situation to slip dramatically.

This rendered those economies particularly vulnerable when the crisis struck. Through contagion effects that were also underestimated at the time, this rendered the whole Euro area particularly vulnerable, but also the European Union as a whole.

In essence, this was not – this is not - a crisis of the euro, but an economic and financial crisis in individual countries that share the same currency and therefore impacts on the Eurozone as a whole.

Indeed, the euro remains a credible, stable and strong currency. And the financial crisis was also not euro-specific, for it affected countries in the Eurozone and outside, inside the European Union and outside, as the case of Iceland clearly shows. The economic, financial but also, in some cases, the deep social crisis was the result of the combination of irresponsibility of a significant part of the financial sector with aggravating unsustainable public debt and the lack of structural competitiveness in some member states. The monetary union absorbed some of the shocks – as it was intended to do - but was itself severely shaken as a result, and it is appropriate to say that while this is not a crisis of the euro area as such and was certainly not created by the European Union, it has posed very specific challenges - economically but also institutionally and politically - to the euro area and implicitly to our European Union.

So the role of the European institutions was - and is - not simply to reform themselves but to support reform in member states, both in the public and the private sector, who had indeed resisted reform for all too long. The revision of our role, responsibilities and institutions can only be seen in the light of this Bermuda triangle of private imprudence, public indulgence and economic inefficiency where our immediate growth prospects disappeared. The eventual success of our efforts will depend on the consistent progress we make on all three fronts.

I will not, ladies and gentlemen, dwell too long on the analysis of what went wrong before the crisis and on everything that has happened since. But it is important to underline that we have come a long way since then, step by step, in addressing some of the main inconsistencies and problems in the EMU. We need not be shy about Europe's response to the crisis and we have to keep in mind the relevance of and the rationale behind these steps:

The euro area has now a permanent crisis resolution mechanism, the European Stability Mechanism, with the capacity of providing financial assistance to the tune of some 700 bn euros to the countries in financial distress. Indeed one of the major shortcomings of the initial EMU construction was the inexistence of such a mechanism. Having allowed Greece to default would have had disastrous consequences for the euro area as whole. It was decided, and rightly so, to support Greece, in spite of the absence of well-defined mechanisms to do it. But it was done! And then the EFSM and the EFSF were created, as predecessors of the ESM, which now is a Treaty based institution.

Decisive steps were also given on the economic governance front. With the 'six pack', a series of measures to strengthen the follow-up and the implementation of the Stability and Growth Pact, in force since December 2011, and the 'two pack', which further reinforces control and coordination of national budgets and which will enter into force at the end of this month, we have significantly changed the way member states' economic and budgetary policies are assessed, coordinated and where necessary, revised. With the new macroeconomic imbalances procedure, situations derailing like we have seen in some member states recently would not have happened.

Instead of the incomplete system of reviewing economic policies we had before, we now have reinforced, pro-active and corrective instruments, including possible penalties, to make absolutely sure that governments act responsibly. And the European Commission is implementing and will continue to implement this new framework in a consistent and very determined way.

The European Semester of economic policy coordination that culminates with the adoption of the country-specific recommendations before the summer, allows for a comprehensive approach to the reforms needed to boost competitiveness, enhance growth and create so much needed conditions for job creation.

By signing the Treaty on Stability, Coordination and Governance, member states have legally underlined their commitment to balanced budgets and instated much stronger oversight by the Commission. It is interesting to note that even in such an instrument that was designed as an intergovernmental instrument, Member States agreed to give more competence to the Commission as a supranational institution.

A technical but nevertheless crucial element is the reform of the European Union statistical system. Even before the crisis, the European Commission warned that the quality and credibility of fiscal data gathered by member states sometimes left much to be desired. In 2005, during my first Commission, we put forward a proposal to strengthen the mandate of Eurostat, which was opposed and then significantly watered down by the member states at that time. The same happened with a new proposal we made in 2007, and in the end it took member states until 2012 to agree to robust rules and strong monitoring mechanisms to guarantee the independence, integrity and accountability of statistical authorities.

With the rules and tools we have today, a situation such as we have unexpectedly and unpleasantly found in Greece in 2010 need not have happened or at least not on that scale.

Ladies and gentlemen,

A lot of progress has already been made over the last two years, more than anyone would have deemed possible before, and these are certainly important steps to move towards economic union. But focusing on the individual institutional reforms we were still missing a bigger picture of the changes – or even more – a sense of purpose - to move forward on the road to complete the design of the EMU.

With its Blueprint, the European Commission fills this gap and drives the agenda for a deep and genuine economic and monetary union.

Our main purpose is to present the political vision that justifies the institutional change in the short term, builds political awareness and leverage in the medium term, and launches a public debate also on our longer term.

This vision is complemented with a description of the mechanics of the new and improved version of the EMU.

This comprehensive approach is based on key principles that need to be upheld in order to deepen the EMU while at the same time preserving the integrity of the European Union at large. This is about the EMU, but for the EU as a whole.

First, the euro area is a product of the Treaties, and its deepening should also be done within the institutional and legal framework of the Treaties. Moving outside of this framework would not only bring risks of legal fragmentation but also undermine democratic accountability, apart from increasing the overall complexity of the system and the lack of readability of many of the decisions.

Second, the deepening of the EMU should primarily and fully exploit the potential of EU-wide instruments, without prejudice to the adoption of measures specific to the euro area. Whenever legally possible, measures targeted at the current members of the Eurozone should be open for participation of other Member States. We must remember that the present configuration of the euro area is only temporary, since all member states but two are destined to become full members of the EMU under the Treaties.

And third, moves towards a genuine EMU should primarily be made through secondary legislation. Treaty change should be contemplated only where and when necessary and after careful preparation. Most of the building blocks of the EMU in the medium term, however, go beyond what is possible under the current treaty.

The Commission will, therefore, set out its views and explicit ideas for treaty change in order for them to be debated before the European elections.

These principles should provide us the much needed guidance on the way forward, especially when preparing for the longer term or addressing particularly sensitive and politically ambitious questions on the road towards a deep and genuine banking, fiscal and economic union that you will be also discussing in detail today.

The Blueprint also sets out the major questions of where we will land eventually, and how we advance on all fronts at the same time. Fiscal union, banking union and political union, all three need to move forward together, through each phase of the further development of the EMU. Because if the crisis, at this stage, has made one thing clear, it is that economic governance, democratic legitimacy and social commitments need to move forward hand in hand, keeping pace with one another.

But this can only be achieved through a fundamental public debate on how far we want to go with our political integration and how far we are willing and able to go in reforming our political institutions.

All that is the real challenge we face today, and it is quite a formidable one.

Ladies and gentlemen,

Since we presented the Blueprint on a deep and genuine EMU last November, the Commission has been working hard to prepare the next steps, the immediately necessary initiatives that can still be undertaken before the European elections, and without changes to the Treaty, to further develop our framework for economic governance and to support economic reform:

The first priority has been to build a banking union. And I'm happy that now this expression is more or less agreed. I remember at the beginning, when we spoke about this, it met with strong resistance.

With the agreement on a Single Supervisory Mechanism, entrusting the European Central Bank with the responsibility to oversee bank management throughout the eurozone, we are putting in place the first main element of a genuine banking union. Again, this is something for which there was no appetite or political momentum before the crisis, which is now becoming reality. If already in place it would probably have avoided a drama on the scale of Cyprus.

Already before the crisis, in May 2008, our EMU@10 Report stated: 'In contrast to the accelerating trend in cross-border financial activity in the EU and the euro area, financial-stability arrangements have been relatively static and remain predominantly national-based. The result is inefficiency in the framework for supervision and financial-crisis management, implying the potential for an inadequate response to contagion risks within an integrated financial system.'

Soon after, this inefficiency and those contagion risks we warned about became painfully visible. And now, we are revising the static and national-based framework, because an integrated financial system simply demands an integrated system of banking supervision and resolution.

In the same logic, we also have to go further, beyond the Single Supervisory Mechanism. The link between sovereign debt and bank debt has to be broken once and for all. We must end the vicious circle whereby the use of taxpayers' funds to rescue banks – all included, with guarantees, more than €4.5 trillion so far – weakens governments' budgets, while increasingly risk-averse banks stop lending to businesses that need funds, undermining the economy still further.

A genuine Economic and Monetary Union needs common rules, shared responsibility for policing the banking sector and joint intervention in case of banking crises. A single rulebook for financial services in the single market is now established, strengthening the resilience of the EU banking sector to absorb economic shocks.

The Single Supervisory Mechanism is agreed upon, putting in place the architecture for coordinated and coherent supervision throughout the eurozone. Building on this, we need a Single Resolution Mechanism in case better banks and better supervision should still prove insufficient, to be able to effectively stabilise the financial sector, to benefit from economies of scale, and to preclude negative externalities that result from purely national decisions. The Commission will come out with its proposal next month.

In March, we have put forward some ideas on so-called ex ante coordination of major economic reform plans in member states, in order to fully take account of possible spillover effects they may have on others.

We have also started the debate on a Convergence and Competitiveness Instrument, which is the most concrete example of combining member states' individual responsibility on the one hand, highlighted in binding benchmarks and timelines for specific reform plans, and on the other hand real solidarity with the member states under particular economic stress. This new Instrument, which could be designed on the basis of some existing tools under the reinforced economic governance, would include safeguards against the moral hazard of reforms being almost rewarded because they are overdue, but it could also help us out of the Catch-22 situation in which many countries feel themselves trapped, struggling to find funds and support for major economic reforms because they are in such a bad state economically.

Another important work strand is the social dimension of the EMU. We are working on the better integration of the social indicators and closer involvement of the social partners in the European Semester, whilst keeping the process coherent and streamlined. This involvement of the social partners in policy debates and European decision-making is critical, both through European level mechanisms and by forging links with national partners. We need to review the existing processes for consulting the social partners at EU level — the macro-economic dialogue, tripartite social summit, social dialogue committee, tripartite exchange of views and if necessary introduce new coherent forms of consultation.

The Commission will come forward with some proposals in this field before the summer.

Ladies and gentlemen,

The subtitle of our Blueprint is 'launching a European debate'.

This is important to note because we do not have either the intention or the insolence to suggest we have all the answers. No - we want to start and fuel a democratic debate with the European Parliament, members of national parliaments, governments, academics, people of culture and thinkers, citizens, on where the future of Europe should lie. We want to put all the elements on the table, in a clear and consistent way, even if some of them may sound like political science fiction today. They will be reality in a few years' time, sooner than we might think. Not only we want to be prepared for when that happens but also we have the ambition for ensuring the democratic legitimacy of the decisions taken.

That is also the role of the European Commission, to advance ideas, to prepare the ground and provide a coherent vision. I am happy to note here that the Blueprint is followed up by open debates in the Council, in the European Parliament and in a number of member states, some of which might even organise a national conference on the Blueprint, similar to this event. The fact that, for instance, last month one of Europe's most important and respected philosophers, Jürgen Habermas, referred to the Blueprint as "the first more detailed document in which the European Union develops a perspective for reforms in the medium and long term that go beyond the present" and the fact that Habermas used it as the basis for his ideas on the broader vision for Europe, strengthens my conviction that this debate will progress beyond the confines of the European institutions or beyond the confines of Brussels and Strasbourg.

A truly European public debate is necessary to underpin the intensified political union that is a key complement to fiscal and economic integration. Europe's democratic legitimacy and accountability must keep pace with its increased role and power, and I hope that the last panel later today will show the multiple ways to do this.

Further economic integration would transcend the limits of the intergovernmental method of running the European Union and the Eurozone in particular, so ensuring democratic legitimacy is increasingly a priority. In this context, the role of the European Parliament and of the national parliaments will be critical.

Above all, public support for Europe requires a change in political leaders' attitude to create a truly European political sphere. A full-grown European Union cannot do without a mature democratic debate. However difficult it may be to convince citizens in times of crisis, however hard it is to explain often technical and sometimes very unpopular decisions, there is no other option in a democracy.

Europe will be open and democratic, or it will fail.

This is why I believe the mainstream forces in European politics must seize the initiative, should leave their comfort zone to welcome and embrace this debate, rather than relinquish the momentum to eurosceptic or europhobic forces.

If you believe in the democratic resilience of Europe, if you take Europe's citizens seriously, you have to fight with rational arguments and unwavering convictions - and be convinced, as I am personally, that these will win the debate for us in the end.

Ladies and gentlemen,

The world has moved on since we set up the Economic and Monetary Union.

What 20 years ago was a big step forward, has now been surpassed by rapid evolutions in technology, in the economy and in our societies.

Europe's economic interdependence - so strikingly highlighted by the financial crisis - calls for increased political integration.

We will not get away with half-hearted solutions any more, and half-integrated institutions will no longer do. We will not regain the trust of investors if we allow the momentum for reform to slip once again. We will not serve our citizens unless we do what we have to do - all of it – and do it well.

That is the challenge we are now facing. And though it is a serious challenge, in a troublesome context and with a heated democratic debate about the decisions we need to take, I am absolutely convinced that we will succeed in transforming the European Union so that it is fit to face the demands of this 21st century.

I thank you very much for your attention. And I wish you a very rich and interesting debate.

A BLUEPRINT FOR A DEEP AND GENUINE EMU
Launching a European debate
Executive summary

1. Rationale, aspirations, and benefits of EMU

The creation of Economic and Monetary Union (EMU) and the introduction of the euro as the currency of the European Union were milestones of European integration and are crucial for the economic, social and environmental well-being of the citizens. They stand out among the EU's most far-reaching achievements and the euro is one of Europe's defining symbols at home and across the globe.

EMU is unique among modern monetary unions in that it originally combined a centralised monetary policy with decentralised responsibility for most economic policies, albeit subject to constraints as regards national budgetary policies. It has been clear since the inception of the euro that the increased interdependence of its Member States meant that sound budgetary and economic policies were of particular importance. The Stability and Growth Pact set down the rules governing the coordination of budgetary policies.

By the time of the eruption of the financial crisis in 2008 some euro area Member States had accumulated large private and public debts, losses in competitiveness, and macroeconomic imbalances. This was partly due to an insufficient observance of and respect for the agreed rules underpinning EMU as laid down in the Stability and Growth Pact (SGP). In good part these vulnerabilities stemmed from features of the original institutional setup of EMU, in particular the lack of a tool to address systematically macroeconomic imbalances.

2. The measures taken so far: a crisis response

In tackling the crisis, the Commission has taken a leading role in preserving the single market, in overhauling EMU's economic governance, in the reform of financial sector regulation and supervision, and in spearheading support to the real economy.

The totality of measures taken so far amounts to a strong response to the crisis. Yet for some of these measures to have a positive impact, they will need to be seen working well for some time. That is one reason why - despite a strong response - it has not been possible to prevent the sovereign debt crises from turning into a crisis of confidence.

In the meantime, the level playing field for businesses and households has been damaged. Diverging developments that are detached from economic fundamentals can hamper the whole project of European integration.

A fundamental response to the crisis must be able to restore confidence that the achievements of the Single Market and the Single Currency will not be undone.

3. The way forward: combining substantial ambition with appropriate sequencing

A comprehensive vision for a deep and genuine EMU conducive to a strong and stable architecture in the financial, fiscal, economic and political domains, underpinning stability and prosperity is required.

This blueprint sets out the actions the Commission believes are necessary in the short, medium and long term. The transformation cannot be completed overnight. The way forward needs to be carefully balanced. Steps towards more responsibility and economic discipline should be combined with more solidarity and financial support. This balance has to be struck in parallel and in each phase of the development of EMU. The deeper integration of financial regulation, fiscal and economic policy and corresponding instruments must be accompanied by commensurate political integration, ensuring democratic legitimacy and accountability.

Some of the required steps can be adopted within the limits of the current Treaties. Others will require modifications of the current Treaties and new competences for the Union. This must be built on the following basic principles. First, the deepening of EMU should build on the institutional and legal framework of the Treaties. Second, the Euro Area must be able to integrate quicker and deeper than the EU at large, whilst preserving convergence with future members of the Euro Area as well as the integrity of the policies conducted at 27, notably the single market. This means that, wherever appropriate, the euro area measures should be open for participation of other Member States. Indeed, while the Treaties foresee that a number of rules apply only to euro area Member States. The present configuration of the euro area is only of a temporary nature, since all Member States but two (Denmark and the UK) are destined to become full members of EMU under the Treaties.

In the short term (within the next 6-18 months), *while the immediate priority should be given to the full deployment of the new economic governance tools brought by the six-pack as well as rapid adoption of current Commission proposals such as the two-pack and the Single Supervisory Mechanism, more can still be done through secondary law, in particular in the area of banking union, economic policy coordination and support to structural reforms necessary to overcome imbalances and to improve competitiveness.*

Once a decision on the next Multi-annual Financial Framework for the EU has been taken, the establishment of an instrument within the EU economic governance framework and the EU budget, separate from the MFF, to support rebalancing, adjustment and thereby growth of the economies of the euro area would serve as the initial phase towards the establishment of a stronger fiscal capacity alongside more deeply integrated policy coordination mechanisms.

The existing framework for economic governance of the euro area should be strengthened further through ensuring greater ex-ante coordination of major reform projects and through the creation of a "Convergence and Competitiveness Instrument" (CCI) to provide a framework for commitments to and support for the timely implementation of structural reforms.

Financial support would be granted for reform packages that are agreed and important both for the Member State in question and for the good functioning of EMU. The use of financial support would be defined as part of the contractual arrangement concluded between the Member State concerned and the Commission.

The financial support mechanism would be part of the EU's budget but outside the ceilings set in the Multi-annual Financial Framework Regulation.

The "Convergence and Competitiveness Instrument" would combine deepening integration of economic policy with financial support, and thereby respect the principle according to which steps towards more responsibility and economic discipline are combined with more solidarity.

An effective banking union would not only require the setting up of a Single Supervisory Mechanism, but after its adoption also a Single Resolution Mechanism to deal with banks in difficulties. It would be in charge of the restructuring and resolution of banks within the Member States participating in the Banking Union. Where intervention by the Single Resolution Mechanism proved necessary, shareholders and creditors should bear the costs of resolution before any external funding were granted. Any additional resources needed to finance the restructuring process should be provided by mechanisms funded by the banking sector, instead of using taxpayers' money.

Building on progress achieved in the economic governance of the euro area, a strengthening and consolidation of its external representation should be pursued, aimed at streamlining and, where possible, unifying it in international economic and financial organisations.

In the medium term (18 months to 5 years), *the overhaul of the budgetary and economic governance that the euro area would have undergone with the adoption of the two-pack and the availability of the Convergence and Competitiveness Instrument would represent major steps forward in ensuring budgetary discipline, financial solidarity and economic competitiveness.*

As further steps, a strengthening of the collective conduct of budgetary policy and as regards economic policy, the euro area would benefit from deeper coordination in the field of tax policy issues as well labour markets, given the significance of labour mobility for adjustment capacity and growth within the euro area.

Building on the Convergence and Competitiveness Instrument, the fiscal capacity for the euro area should be further enhanced. It should be autonomous and rely solely on own resources. It should provide sufficient resources to support important structural reforms in a large economy under distress.

A clearly reinforced economic and fiscal governance framework could allow considering the reduction of public debt significantly exceeding the SGP criteria through the setting-up of a redemption fund subject to strict conditionality. This would warrant increased surveillance and power of intervention in the design and implementation of national fiscal policies.

The common issuance by euro area Member States of so-called eurobills - short-term government debt with a maturity of up to 1 to 2 years - could constitute a tool against the present fragmentation, reducing the negative feedback loop between sovereigns and banks, while limiting moral hazard. The introduction of such a common debt instrument would require a closer coordination and supervision of Member States' debt management in order to ensure sustainable and efficient national budgetary policies.

The monitoring and managing function for the fiscal capacity and other instruments should be provided by an EMU Treasury within the Commission.

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The further strengthening of policy coordination and enhancement of the fiscal capacity would initially start under secondary law, but would require Treaty changes at some point. The creation of a Debt Redemption Fund and the common issuance of short-term government debt would require Treaty changes.

Finally, in the long term (beyond 5 years), *based on progressive pooling of sovereignty and thus responsibility as well as solidarity competencies to the European level, the establishment of an autonomous euro area budget providing for a fiscal capacity for the euro area to support Member States in the absorption of shocks should become possible. The central budget would provide for an EMU-level stabilisation tool to support adjustment to asymmetric shocks, facilitating stronger economic integration and convergence and avoiding the setting-up of long-term transfer flows. Overall, a shared instrument could deliver net gains in stabilising power, as compared with current arrangements. How large this fiscal capacity would ultimately turn out to be will depend on the depth of integration desired and on the willingness to enact accompanying political changes.*

Also, a deeply integrated economic and fiscal governance framework could allow a common issuance of public debt, which would enhance the functioning of the markets and the conduct of monetary policy.

This would be the final stage in EMU.

Attaining a deep and genuine EMU involves incremental measures, building on what would have been achieved over the short and the medium-term and introducing further integration on a step-by-step, policy-by-policy basis.

The full EMU would therefore realize the four building blocks: a banking union, a fiscal union, an economic union, which all require, as a fourth element, appropriate democratic legitimacy and accountability of decision-making.

This final stage would require a fundamental overhaul of the Treaties.

4. Political union: democratic legitimacy and accountability

Any work on democratic legitimacy as a cornerstone of a genuine EMU needs to be based on two basic principles. In multilevel governance systems accountability should be ensured at the level where the respective executive decision is taken. This holds true for new powers on budgetary surveillance and economic policy as much as for new EU rules on solidarity between Member States. Briefly put: further financial and economic mutualisation requires commensurate political integration.

The European Parliament needs to primarily ensure democratic accountability for any decisions taken at EU level, in particular the Commission. A further strengthened role of EU institutions will therefore have to be accompanied with a commensurate involvement of the European Parliament in the EU procedures. The European Parliament, and only it, is that Parliament for the EU and hence for the euro, ensuring democratic legitimacy for EU institutions' decisions. At the same time, the role of national parliaments will always remain crucial in ensuring legitimacy of Member States' action in the European Council and the Council.

In the short term, ensuring optimal democratic accountability and governance without Treaty change should focus on practical measures, in particular those designed to foster parliamentary debate in the European Semester, such as foreseeing the involvement of the Parliament in the discussions on the Commission's Annual Growth Survey.

In the context of a Treaty reform conferring further supranational powers to the EU level, steps should be considered to ensure a commensurately stronger democratic accountability.

A further way of strengthening the EU's legitimacy would also be to extend the competences of the Court of Justice.

Finally, special challenges to ensure appropriate democratic accountability need to be addressed in case the Treaty is changed to permit the mutualisation of the issuance of sovereign debt underpinned by a joint and several guarantee of all euro area Member States.

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COMMUNICATION FROM THE COMMISSION

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Launching a European Debate

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A BLUEPRINT FOR A DEEP AND GENUINE EMU

Launching a European debate

1. Rationale, aspirations, and benefits of EMU

According to the Treaties, the aim of the European Union is to promote peace, its values and the well-being of its people. It shall work for the sustainable development of Europe based on balanced economic growth and price stability, a highly competitive social market economy, aiming at full employment and social progress, and a high level of protection and improvement of the quality of the environment. It shall promote economic, social and territorial cohesion, and solidarity among Member States. The European Union shall establish an Economic and Monetary Union (EMU) whose currency is the Euro (cf. Art 3 TEU).

The creation of the EMU and the introduction of the euro were milestones of European integration. They stand out among the EU's most far-reaching achievements and the euro is one of Europe's defining symbols at home and across the globe. The founders of the EMU pursued great aspirations with the single currency, both economic and political. Some of these aspirations have already been realised, while others remain to be achieved.

As the world's second largest reserve currency, the euro is an integral feature of the global economy. It is entrenched in balance sheets around the world. Its existence has helped to open up the internal market to more than 330 million citizens living in the euro area, by enabling immediate price comparisons for goods and services across countries. By eliminating exchange rate risk and foreign transaction costs, the euro also facilitates a more efficient distribution of resources, and makes prices for goods and services fully transparent across countries. In our interconnected electronic world, this levelling of the playing field of the single market is a powerful tool for growth. The euro has demonstrably facilitated trade between euro area countries and has equally promoted physical and financial investment between Member States. The stability of the currency has made the euro area an attractive investment destination. These trade and investment gains have boosted growth and jobs. Ample liquidity provision by the Eurosystem has helped to deal with problems in the interbank market during a period of financial disruption and uncertainty. The euro area is a dynamic and open construction. Despite the crisis, membership of the euro area, which is constituted by 17 Member States and is set to increase in the future, has remained an attractive prospect: Slovakia joined the single currency in January 2009 and Estonia joined in January 2011.

Weaknesses in the initial design of EMU and adherence to rules

By the time of the eruption of the financial crisis in 2008 some euro area Member States had accumulated large private and public debts, losses in competitiveness, and macroeconomic imbalances. This rendered them particularly vulnerable when the crisis struck, with considerable contagion effects across the euro area once it turned into a sovereign debt crisis. The build-up of these vulnerabilities was partly due to an insufficient observance of and respect for the agreed rules underpinning EMU as laid down in the Stability and Growth Pact (SGP). In good part these vulnerabilities stemmed from features of the original institutional setup of EMU, in particular the lack of a tool to address systematically macroeconomic imbalances.

EMU is unique among modern monetary unions in that it combines a centralised monetary policy with decentralised responsibility for most economic policies, albeit subject to constraints as regards national budgetary policies. Unlike other monetary unions, there is no centralised fiscal policy function and no centralised fiscal capacity (federal budget)[1]. It has been clear since the inception of the euro that the increased interdependence of its Member States meant that sound budgetary and economic policies were of particular importance. The SGP[2] set down the rules governing the coordination of budgetary policies. It also foresaw action to be taken against Member States that did not comply with the rules. It was thought that this coordination would be sufficient to ensure sound policies at national level. Already in 2008, the Commission's EMU@10 report[3] presented a range of possible changes to this setup. The crisis accelerated the need for change.

The following issues have been at the heart of the challenges faced by the euro area since 2008:

(a) The SGP was insufficiently observed by the Member States and lacked robust mechanisms to ensure sustainable public finances. The enforcement of the preventive arm of the SGP, which requires that Member States maintain a strong underlying budgetary position, was too weak and Member States did not use periods of steady growth to pursue ambitious fiscal policies. At the same time, the debt criterion of the Treaty was not rendered operational in practice in the corrective arm of the SGP. The result was budgetary slippages during good times, and an inability to bring down the debt levels of highly indebted countries.

(b) The coordination of national economic policies beyond the budgetary area relied on soft instruments – peer pressure and recommendations – and had a limited impact on the action of individual euro area Member States. The instrument was therefore too weak to counter the progressive opening of competitiveness gaps and growth divergences between Member

[1] The adjective "fiscal" in this text is used in the sense of "budgetary".

[2] The EMU policy framework comprises a set of detailed Treaty provisions, which (a) establish the European Central Bank (ECB) as an independent monetary authority for the euro area; (b) elaborate a set of rules governing the conduct of national budgetary policies (such as the excessive deficit procedure, the prohibition of monetary financing and privileged access and the so-called "no bail-out clause"); and (c) govern the surveillance of economic policies more generally in the Member States.

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States. Little consideration was given to the euro area-wide spillover effects of national measures. National economic policy-making paid insufficient attention to the European context within which the economies operate. The generalised absence of risks stemming from a global economic liquidity glut contributed to this.

(c) Financial markets play an important role in creating incentives for countries to run sustainable public finances, by pricing the risk of default into the rate at which sovereigns can borrow money. With the global easing of inflationary pressure in the late 1990s, there was a rapid and sustained expansion in the money supply by central banks. Along with new approaches to risk transfer in the financial system this resulted in globalised excess liquidity, a pervasive search for yield and ultimately a severe mispricing of risk of both private and public assets. In parallel, with the introduction of the euro the European Central Bank (ECB) relied on national bonds for its open market operations, thereby conferring upon them the top-quality status required for central bank collateral. The result was strong yield convergence, considerably limiting market discipline, despite differences in national budgetary performances. This contributed, inter alia, to the significant investments on sovereign bonds made by banks. Euro area economies in a cyclical expansion and with relatively higher inflation rates tended to enjoy low or even negative real interest rates. This led in some countries to strong credit expansion fuelling significant housing bubbles.

(d) The inception of EMU saw a sharp acceleration in the pace of financial integration. While this opened opportunities for portfolio diversifications, it also accelerated the transmission of shocks across national borders. Despite the increased market integration, the responsibility for prudential supervision and crisis management remained predominantly at the national level. This asymmetry between integrated financial markets on the one hand, and a financial stability architecture still nationally segmented on the other, resulted in inadequate coordination among the relevant authorities at all stages of the current crisis. The absence of common rules and euro area-wide supervisory and resolution institutions for the financial sector was a major problem in responding to the crisis. The lack of an integrated EU-level framework and of a mechanism to mutualise the response to risks coming from the banking sector affecting several or all Member States, resulted in powerful and damaging negative loops emerging between the banking system and the sovereigns in the vulnerable countries. These loops fuelled the debt crisis further and led to a reversal in the direction of capital flows. As a result, some Member States have been excluded from market financing and there has been a risk of contagion effects affecting the euro area as a whole. In this context, the absence of an effective mechanism to provide liquidity to Member States in distress and thus to manage contagion risk and to safeguard euro area financial stability emerged as a clear inadequacy in the crisis management arrangements.

While the EU has taken decisive action to address those major challenges, EMU needs to be deepened further. This Blueprint for a Deep and Genuine EMU describes the necessary elements and the steps towards a full banking, economic, fiscal and political union.

2. The measures taken so far: a crisis response

In tackling the crisis, the Commission has taken a leading role in preserving the single market against emerging protectionist tendencies and fragmentation according to national borders, especially in the banking sector; in overhauling EMU's economic governance to address the weaknesses of economic surveillance and in putting forward important legislative proposals to initiate the reform of financial sector supervision, in ensuring EU-level coordination and oversight of bank rescue and in spear-heading support to the real economy under the European Economic Recovery Programme.

The strong support of the European Parliament has been instrumental in enabling quick progress on these initiatives, and in bringing the legislative proposals quickly into force. In 2010, the Task Force set up by the President of the European Council for strengthening economic governance enabled a swift emergence of consensus among member states in support of the proposals by the Commission. Frequent meetings of the European Council have resulted in important commitments and significant steps by the member states to respond to Europe's crisis.

All euro area Member States and most others have committed themselves to incorporating the EU rules and principles of budgetary surveillance into their national legal frameworks under the Treaty on Stability, Coordination and Governance in Economic and Monetary Union (TSCG) signed by all EU countries except the Czech Republic and the UK in March 2012. The creation of a financial firewall for the euro area and successive decisions to increase its size and flexibility of operations and to make it permanent have significantly strengthened the crisis management capacity.

2.1 Budgetary surveillance

The Commission presented a strategy for strengthening economic governance in Europe in its two Communications of 12 May 2010 and 30 June 2010[4]. These Communications were followed up by a package of legislative proposals adopted by the Commission on 29 September 2010.

As a result of efficient inter-institutional cooperation, the legislative process proceeded quickly and the European framework of economic and budgetary surveillance was overhauled in December 2011 with the adoption of a package of six legislative proposals (known as the six-pack) designed to address the weaknesses revealed by the economic and financial crisis. It comprised three Regulations strengthening the European budgetary surveillance framework (the SGP), two Regulations introducing a new surveillance procedure

[4] See the Commission's communications of 12 May 2010 (COM (2010) 250 final) and 30 June 2010 (COM(2010) 367 final), and its "six pack" legislative proposals of 29 September 2010 (COM (2010) 522 through 527 final).

for macroeconomic imbalances and a Directive imposing minimum standards for Member States' national budgetary frameworks.

The legislative package drastically reinforced the preventive arm of the SGP by introducing an expenditure rule anchoring expenditure growth to the medium-term growth rate of potential GDP. The legislation also introduced the possibility of sanctions early in the process. Countries will now face lodging an interest-bearing deposit of 0.2% of GDP if their underlying budgetary position is not strong enough. The new legislation also provides for stronger action to correct gross policy errors within the corrective arm of the SGP and a new quantified rule requiring those Member States that exceed the debt threshold of the Maastricht Treaty to reduce the excess rapidly. The launch of an Excessive Deficit Procedure (EDP) can now result from unfavourable government debt developments as well as from high government deficits. The introduction of the reverse qualified majority rule significantly strengthens the Commission's hand in decisions relating to sanctions on euro area Member States. Whereas in the past, such decisions required the support of a qualified majority in the Council, in future, a qualified majority would be required to halt the sanction proposed by the Commission.

The six-pack also included the adoption of a Directive defining minimum requirements for national budgetary frameworks to ensure that Member States' fiscal frameworks are fit to respect the EU rules. This concept, of ensuring that the national decision-making processes are set up to deliver policy in line with the European requirements is also at the heart of the intergovernmental Treaty on Stability, Coordination and Governance in Economic and Monetary Union (TSCG). Euro area signatory Member States have committed to integrating the core principles of the SGP straight into their national legal framework through provisions of binding force and permanent character which will include a national correction mechanism supervised by an independent monitoring body to ensure compliance with the budgetary targets in the preventive arm of the Pact. Although it is intergovernmental, the TSCG foresees incorporating its provisions into Union law within 5 years. The Commission is already working with the European Parliament and the Council to integrate some of the TSCG elements into EU law applicable to euro area Member States through the legislative proposals known as the two-pack, which are currently in the EU decision-making process.

The two-pack – which consists of two Regulations – was proposed by the Commission in November 2011 and aims to further reinforce both budgetary coordination and budgetary surveillance, for more targeted prevention and more effective corrective action in case of deviations from the budgetary policy requirements deriving from the SGP. All Member States of the euro area will present ahead of parliamentary adoption their draft budgetary plans for the forthcoming year to the Commission and to their euro area partners, according to a common timetable. The two-pack also strengthens the monitoring and surveillance procedures for Member States experiencing severe difficulties with regard to their financial stability or for those in receipt of financial assistance.

2.2 Economic policy surveillance

A major weakness of the pre-crisis surveillance arrangements was the lack of systematic surveillance of macroeconomic imbalances and competitiveness developments. While such developments were analysed in the context of the Commission's reports on Member States, including the opinions on the Stability and Convergence Programmes, and in the euro area's informal competitiveness reviews every two years, there was no formal instrument for their systematic analysis and follow-up through concrete policy recommendations. The six-pack introduced a new Macroeconomic Imbalances Procedure (MIP) to close this gap: a new surveillance mechanism aiming to prevent macroeconomic imbalances and to identify and allow the timely correction of any emerging competitiveness divergences. It is based on an alert system that uses a scoreboard of indicators and in-depth country studies to identify imbalances and launch a new Excessive Imbalance Procedure (EIP) where necessary. The new procedure is backed up by enforcement provisions in the form of financial sanctions for euro area Member States which do not comply with the EIP.

The various components of economic, budgetary and structural surveillance were also fully integrated as a result of changes introduced since the onset of the crisis which set up the European Semester. While these components were previously assessed separately, their surveillance is now undertaken in parallel over the first six months of each calendar year, allowing Member States to take country-specific guidance into account in their national budgetary processes over the next six months. Policy advice is given to Member States before they finalise their draft budgets for the following year.

2.3 Financial regulation and supervision

Over the past four years, the European Union has taken decisive steps in the area of financial regulation and supervision and an ambitious and substantial financial reform agenda is being implemented. The aim is to make financial institutions and markets, which have been at the heart of the crisis, more stable, more competitive and more resilient. The Commission President asked Jacques de Larosière, the former IMF Managing Director and Governor of the Banque de France, to present a comprehensive report on the appropriate measures. Drawing on the de Larosière Report, the Commission proposed a comprehensive programme of financial regulatory reform.

Stronger prudential requirements for banks have been proposed under the fourth Capital Requirements Directive and the Capital Requirements Regulation (CRD4/CRR) currently under discussion. For the first time, the capital adequacy requirements will be enshrined in a Regulation and not a Directive. The adoption of the Capital Requirement Regulation will be a significant step forward in the completion of the single rulebook for financial institutions in the European Union. The EU has also taken action in the field of governance by introducing binding rules on remuneration practices to avoid excessive risk-taking by the banks.

The EU tightened supervision of the financial markets by establishing a European System of Financial Supervisors (ESFS) composed of three European Supervisory Authorities (ESAs) – the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA) and the European Securities and Markets Authority (ESMA) – and of a macro-prudential watchdog, the European Systemic Risk Board (ESRB). The three ESAs work together with Member States' national supervisory authorities to ensure harmonised rules and a strict and coherent implementation of the new requirements. The ESRB monitors threats to the stability of the whole financial system, allowing any weaknesses to be addressed in due time.

Credit Rating Agencies, which played an important role in triggering the crisis, are now closely supervised by ESMA. Legislation adopted in 2012 will ensure that all standardised over-the-counter derivatives are cleared by central counterparty clearinghouses, reducing the risk of default of counterparties. In addition, all standardised and sufficiently liquid derivatives will be traded on regulated platforms once the legislation proposed by the Commission is adopted. The issue of short selling has already been addressed, through the adoption of legislation increasing transparency.

2.4 Crisis resolution mechanisms

A key part of the crisis resolution approach was the development of a crisis resolution mechanism that would address financial market fragility and mitigate the risk of contagion across Member States. On the Commission's initiative, in May 2010 two temporary crisis resolution mechanisms were established: the European Financial Stabilisation Mechanism (EFSM) and the European Financial Stability Facility (EFSF). The EFSM is a financial support instrument backed by the resources of the EU budget, available to all 27 Member States of the European Union, and based on the existing Treaty framework. The EFSF is a company owned by the euro area Member States, incorporated in Luxembourg, whose functioning is regulated in an intergovernmental agreement. The EFSF's lending capacity is backed solely by the guarantees of participating Member States, and is accessible only to the euro area Member States.

Faced with the further entrenchment of the crisis, euro area Member States made the existing support mechanisms more robust and more flexible; and eventually decided on the creation of a permanent crisis resolution mechanism to better protect the financial stability of the euro area and of its Member States. As a result, the euro area's permanent financial backstop, the European Stability Mechanism (ESM) was finally inaugurated on 8 October 2012, and is now fully operational following completion of ratification of the ESM Treaty by all euro area Member States. The ESM is the world's most capitalised international financial institution and the world's biggest regional firewall (€500 bn). Its creation is a key step for ensuring that the euro area has the capacity needed for rescuing Member States experiencing financial difficulties from default. On 27 November 2012, the European Court of Justice confirmed that the ESM Treaty is in line with EU law as it stands.[5]

The ECB has played a crucial role in the euro area response to the economic and financial crisis. First, the official refinancing rate has been lowered almost to zero, as the economy has slowed. In addition, the ECB has taken a range of measures to address the effects of the crisis on the functioning of financial markets when interbank market activity nearly stalled. One of the earliest of these effects was the drying-up of wholesale funding for banks, amid concerns about the quality of assets on their balance sheets. The ECB responded to this by expanding banks' access to monetary policy operations via a relaxation of collateral rules for both standard refinancing operations and for emergency liquidity assistance. In May 2010, the Eurosystem started the Securities Market Programme (SMP), purchasing government bonds in limited and sterilised interventions. As funding pressures intensified in the second half of 2011, threatening financial stability across the euro area, the ECB provided banks with access to exceptionally long-term refinancing operations (LTROs) with maturities of up to three years (compared to a maximum maturity of three months under normal procedures). The three LTRO allotments have had a powerful impact on investor sentiment and have substantially eased the pressure building in funding markets. While access to wholesale funding remains problematic for many banks, there has been recent evidence of a gradual thawing in these markets especially for larger banks.

The spread of the crisis to sovereign debt markets and the development of negative feedback loops between banks and sovereigns has resulted in a broader fragmentation of the euro area financial system and the emergence of so-called "redenomination risk" linked to fears about the reversibility of the euro. The ECB has adopted a decision as a basis to undertake Outright Monetary Transactions (OMT) in the secondary sovereign bond markets subject to strict and effective conditionality[6]. The objective is to safeguard proper transmission of the ECB's policy stance to the real economy throughout the euro area and to ensure the singleness of monetary policy. The transactions would be undertaken strictly within the ECB's mandate to maintain price stability over the medium term. A necessary condition for Outright Monetary Transactions is strict and effective conditionality attached to an appropriate European Financial Stability Facility/European Stability Mechanism (EFSF/ESM) programme. As long as programme conditionality is fully respected, the ECB Governing Council will consider Outright Monetary Transactions to the extent that they are warranted from a monetary policy perspective. They will be terminated once their objectives are achieved or when there is non-compliance with the macroeconomic adjustment or precautionary programme. The liquidity

[5] Judgment of 27 November 2012 in case C-370/12 Pringle. The Court also confirmed the validity of European Council Decision 2011/199/EU amending Article 136 TFEU and that the Member States were free to conclude and ratify the ESM Treaty before the entry into force of that Decision.

[6] ECB Press Release of 6 September 2012 on Technical features of Outright Monetary Transactions: http://www.ecb.int/press/pr/date/2012/html/pr120906_1.en.html

created through Outright Monetary Transactions will be fully sterilised. The announcement of the OMT programme, which replaces the more limited Securities Market Programme, has again had a powerful impact on investor sentiment, resulting in a significant decline in sovereign yields in the vulnerable Member States.

EMU has been overhauled, but the work is not yet complete

The totality of measures taken so far amounts to a strong response to the crisis, particularly when compared with what was considered politically feasible only a few years ago. It has taken time to put in place many of these measures, such as the overhauled instruments of economic and budgetary policy coordination or the permanent financial firewall. Also, for some of these measures to have a positive impact on confidence, they will need to be seen working well for some time. That is one reason why – despite a strong response – it has not been possible to prevent the sovereign debt crises from turning into a crisis of confidence that threatens to put into question the integrity of the euro area itself.

Another factor behind this has been the gap between the sharp acceleration of financial integration under EMU on the one hand, and the comparatively slow progress in the integration of EU-level financial regulation and supervision on the other.

The lack of strong supra-national EU-level institutions for bank supervision made the management of the crisis much more difficult and costly for the taxpayer than it otherwise would have been. More importantly, in the absence of such institutions, the crisis of confidence combined with the lack of appropriate governance of the financial sector (architecture for regulation, supervision and resolution) and the consequent public authorities' response based on national interest, resulted in a re-fragmentation of financial markets, as risk pricing based on national benchmark bonds led to distinctly different financing conditions for businesses and households in different euro area Member States, thereby wiping out many benefits of European financial integration.

This has worked as an additional drag on growth in some Member States, as credit conditions tightened in particular where activity was already slow, further exacerbating the existing feedback interactions between banks and sovereigns in the Member States concerned and further constraining their capacity to grow out of the crisis, ultimately with implications for their capacity to refinance themselves in the markets and the potential need for financial assistance. Conversely, credit conditions eased further in Member States where activity was already relatively strong.

The lack of strong integrated EU-level institutions thus effectively resulted in the reversal of integration and caused damage to the level playing field for businesses and households simply on account of their location on one or the other side of a border between two Member States of the euro area. Quasi-identical businesses within only a few kilometres on two different sides of such a border may no longer be able to finance investments on comparable terms. On one side of the border investment may stall and unemployment rise, as credits are not granted on feasible terms. On the other side, investment costs and unemployment may fall to new lows at the very same time. The same applies to the financing conditions accorded to private households. Such diverging developments that are detached from economic fundamentals and the needs of citizens and businesses can hamper the whole project of European integration.

Ultimately, the negative feedback loop between sovereigns and banks and the associated re-fragmentation of the EU's financial markets led to the emergence of a re-denomination risk, the bet by financial market participants that this development would eventually threaten the existence of the single currency.

Anachronistically, more than 50 years after the foundation of the European Union the crisis of confidence appears to be reinstating the constraining power of national borders, questioning the Single Market and threatening the achievements and as yet unfulfilled aspirations of Economic and Monetary Union. This is also a threat to the European Union's model of a social market economy.

The lessons learned in the context of the economic, financial, and sovereign debt crises since 2008 have been drivers of a major overhaul of the economic governance of Economic and Monetary Union, which has already led to unprecedented steps. This overhaul has made EMU much more robust than it was at the onset of the crisis. The crisis has clearly demonstrated how much the interdependence of our economies has increased since the foundation of EMU. It has also shown beyond any doubt that success or failure of EMU will be a success or a failure for all involved.

The threat entailed in the crisis of confidence is however much more fundamental. It therefore requires a much more fundamental response. That response must be able to restore confidence that the achievements of the Single Market and the single currency will not be undone and that their as yet unfulfilled achievements will be realised and maintained for citizens and businesses for the future.

To be effective and credible, that response must first of all deal with the pressing practical difficulties citizens, businesses, and Member States face today. A banking union would be able to end the disintegration of the EU's financial market and ensure reasonably equal financing conditions for households and business across the EU; it would help sever the negative feedback loops between Member States and banks; and it would help ensure that divergences between the business cycles across the euro area are not artificially amplified. Second, the response must set out the vision for a more deeply integrated EMU to be achieved in the future. And third, it must chart a clear and realistic path towards that ultimate ambition based on the firm commitment of the EU's institutions and its Member States.

3. The way forward: combining substantial ambition with appropriate sequencing

EMU is facing a fundamental challenge, in particular as regards the euro area, and needs to be strengthened to ensure economic and social welfare for the future. The European Council in June 2012 invited the President of the European Council, in close collaboration with the President of the Commission, the President of the Euro Group and the President of the ECB, to present a specific and time-bound roadmap for the achievement of a genuine EMU. An interim report was presented to the October European Council, and a final report is due in December 2012. The European Parliament adopted on 20 November its report "Towards a genuine Economic and Monetary Union", which outlines the Parliament’s preferences for a more deeply integrated EMU. The Commission's proposal on the way forward is outlined in this blueprint.

A comprehensive vision for a deep and genuine EMU conducive to a strong and stable architecture in the financial, fiscal, economic and political domains, underpinning stability and prosperity is necessary. In such a deep and genuine EMU all major economic and fiscal policy choices of its Member States should be subject to deeper coordination, endorsement and surveillance at the European level. These policies should cover also taxation and employment, as well as other policy areas crucial for the functioning of EMU. Such an EMU should also be underpinned by an autonomous and sufficient fiscal capacity that allows the policy choices resulting from the coordination process to be effectively supported. A commensurate share of decisions with regard to revenue, expenditure and debt issuance should be subject to joint decision-making and implementation at the level of EMU.

It is clear that the current EMU cannot be completed overnight by a transformation into a deep and fully integrated version, in particular considering the significant additional transfer of political powers from the national to the European level. In order to arrive at an EMU that can ensure its citizens stability, sustainability and welfare on a permanent basis, decisive steps towards the goal need to be launched already in the short term (within the next 6-18 months). Such steps need then to be followed by further steps in the medium and long term. The steps to be taken in the short, medium and long term must build on each other and follow from each other.

The way forward needs to be carefully balanced. Steps towards more responsibility and economic discipline should be combined with more solidarity and financial support. This balance has to be struck in parallel and in each phase of the development of EMU. The deeper integration of financial regulation, fiscal and economic policy and corresponding instruments must be accompanied by commensurate political integration, ensuring democratic legitimacy and accountability.

This chapter identifies the steps and actions required in the short, medium and long term to arrive at a deep and genuine EMU on a permanent basis, from stronger policy coordination to fiscal capacity to greater pooling of decisions on public revenue, expenditure and debt issuance.

Some of the instruments can be adopted within the limits of the current Treaties. Others will require modifications of the current Treaties and new competences for the Union. The former can therefore progress in the short term and should be completed at the latest in the medium term. The latter can only be initiated in the medium term and completed in the long term. It should however be clear throughout that the concept is a holistic one in which each stage builds on the previous one.

In the short term (within the next 6-18 months), while immediate priority should be given to the full deployment of the new economic governance tools brought by the six-pack as well as rapid adoption of current Commission proposals such as the two-pack and the Single Supervisory Mechanism, more can still be done through secondary law, in particular in the area of economic policy coordination and support to structural reforms necessary to overcome imbalances and to improve competitiveness. Once a decision on the next Multi-annual Financial Framework for the EU has been taken, the establishment of a financial instrument within the EU budget to support re-balancing, adjustment and thereby growth of the economies of the EMU would serve as the initial phase towards the establishment of a stronger fiscal capacity alongside more deeply integrated policy coordination mechanisms. Together, the next step in fiscal and economic policy coordination and the corresponding initial phase of the build-up of a fiscal capacity could take the form of a "convergence and competitiveness instrument". Following the adoption of the Single Supervisory Mechanism, a Single Resolution Mechanism for banks will be proposed.

In the medium term (18 months to 5 years), further budgetary coordination (including a possibility to require a revision of a national budget in line with European commitments), the extension of deeper policy coordination in the field of taxation and employment, and the creation of a proper fiscal capacity for the EMU to support the implementation of the policy choices resulting from the deeper coordination should be established. Some of these elements will require amending the Treaties.

The reduction of public debt significantly exceeding the Treaty criterion could be addressed through the setting-up of a redemption fund. A possible driver for fostering the integration of euro area financial markets and in particular to stabilise volatile government debt markets is common issuance by euro area Member States of short-term government debt with a maturity of up to 1 to 2 years. Both of these possibilities would require amending the Treaties.

Finally, in the long term (beyond 5 years), based on the progressive pooling of sovereignty and thus responsibility as well as solidarity competencies to the European level, the establishment of an autonomous euro area budget providing for a fiscal capacity for the EMU to support Member States in the absorption of shocks should become possible. Also, a deeply integrated economic and fiscal governance framework could allow a common issuance of public debt, which would enhance the functioning of the markets and the conduct of monetary policy. As set out in the Commission's Green Paper of 23 November 2011 on the

feasibility of introducing Stability Bonds[7], the common issuance of bonds could create new means through which governments finance their debt and offer safe and liquid investment opportunities for savers and financial institutions, as well as a euro area-wide integrated bond market that matches its US dollar counterpart in terms of size and liquidity.

This progressive further integration of the euro area towards a full banking, fiscal and economic union will require parallel steps towards a political union with a reinforced democratic legitimacy and accountability.

The progress in terms of integration will also have to be reflected externally, notably through steps towards united external economic representation of the euro area.

Box 1: The basic legal principles

In order to secure the sustainability of the common currency, the EMU must have the possibility to deepen more quickly and more thoroughly than the EU as a whole, whilst preserving the integrity of the EU at large.

This can be achieved through the observance of the following principles:

First, the deepening of the EMU should build on the institutional and legal framework of the Treaties, for the sake of legitimacy, equity between Member States and efficiency. The euro area is a product of the Treaties. Its deepening should be done within the Treaties, so as to avoid any fragmentation of the legal framework, which would weaken the Union and question the paramount importance of EU law for the dynamics of integration. Only EU decision-making rules provide full efficiency, resting on qualified majority instead of burdensome unanimity requirements and on a robust democratic framework.

Intergovernmental solutions should therefore only be considered on an exceptional and transitional basis where an EU solution would necessitate a Treaty change, and until that Treaty change is in place. They must also be carefully designed so as to respect EU law and governance, and not raise new accountability problems.

Second, the deepening of EMU should primarily and fully exploit the potential of the EU-wide instruments, without prejudice to the adoption of measures specific to the euro area. The European Semester, the internal market *acquis* and the support to competitiveness and cohesion through the EU budget provide a good basis for developing a comprehensive legal and financial framework for economic coordination, integration and real convergence. On-going efforts to make these policies more effective through e.g. macroeconomic

[7] COM(2011)818.

conditionality of the structural funds or the new governance approach of the single market will also contribute to the strengthening of EMU.

At the same time, additional financial, fiscal and structural coordination or support instruments specific to the euro area should be established whenever needed and should be designed as a complement to the EU's foundations. The Lisbon Treaty has provided a useful legal basis (Article 136 TFEU) for deepening the integration of the euro area. This legal basis has been already widely used with the successive six-pack and two-pack.

Wherever legally possible the euro area measures should be open for participation of other Member States. Indeed, while the Treaties foresee that a number of rules apply only to euro area Member States, the present configuration of the euro area is only of a temporary nature, since all Member States but two (Denmark and the UK) are destined to become full members of EMU under the Treaties.

Third, moves towards a genuine EMU should primarily be constructed using all the possibilities offered by the Treaties as they stand, via the adoption of secondary legislation. Amendments to the Treaties should be contemplated only where an action indispensable for improving the functioning of the EMU cannot be constructed within the current framework. Possible changes should be carefully prepared, so as to ensure the political and democratic ownership needed for a smooth ratification process.

3.1 In the short term (within the next 6-18 months): measures possible under secondary EU law to move towards the banking union, improve policy coordination as well as taking a decision on the next MFF and creating a "convergence and competitiveness instrument"

The deepening of EMU must address the consequences of excessive public and private debt accumulation, and thereby reduce the associated imbalances that were generated in the European economy. But adjustment is proving a long and difficult task, involving constraints in the credit supply, stretching public finances, and weak growth in the private sector as firms and households clean their balance sheets.

Commitment to budgetary discipline is an essential safeguard of the stability of the euro area, and a necessary step towards a fully-fledged integrated budgetary framework. This will ensure sound budgetary policies at the national and European levels and thereby contribute to sustainable growth and macroeconomic stability. Full deployment of the new tools for budgetary and economic surveillance and quick adoption of the current proposals should be the first priority. In parallel, the progress towards a banking union needs to start through the adoption and implementation of the proposals made on financial regulation and supervision, notably the proposal for a Single Supervisory Mechanism (SSM) for the euro area and for non-euro area Member States wishing to join.

To ensure a smooth functioning of the EMU, more should be done in the area of coordination of economic policies. The weight of the growth and adjustment challenge in the euro area contrasts with the absence of strong forms of policy coordination in the area of structural reforms. The evidence of large cross-country externalities calls for a reinforcement of the way in which economic policy must be run in the euro area. The proper functioning of the EMU requires that euro area Member States work jointly towards an economic policy where, whilst building upon the existing mechanisms of economic policy coordination, they take the necessary actions and measures in all areas which are essential to the proper functioning of the euro area. In particular, the setting-up of a procedure for the ex-ante discussion of all major economic policy reforms is necessary. This should be underpinned with the corresponding initial phase of the build-up of a fiscal capacity for the EMU, providing targeted financial support for the Member States facing adjustment difficulties.

Recalling the importance of sound public finances, structural reform and targeted investment for sustainable growth, the Heads of State or Government signed a Compact for Growth and Jobs on 28-29 June 2012, demonstrating their determination to stimulate job-creating growth in parallel to their commitment to sound public finances. The Commission is also monitoring the impact of tight budget constraints on growth-enhancing public expenditure and on public investment. In this context, the euro area should ensure that investment is kept at an adequate level in order to ensure the framework conditions for competitiveness developments and to contribute to growth and jobs.

All the initiatives presented in this section can be adopted in the short-term and within the limits of the current Treaties.

3.1.1 Full implementation of European Semester and six-pack and quick agreement and implementation of the two-pack

The completion of the current economic governance framework and its full implementation must be the first order of the day.

The introduction of the European Semester as well as the six-pack legislation has addressed central lessons learned in the context of the crisis. They included a reform of the SGP, the creation of the Macroeconomic Imbalances Procedure, and the introduction of minimum standards for national fiscal frameworks. They represent a leap forward in terms of economic policy coordination. This promises stronger policy implementation at national level, in particular for euro area Member States, and a better functioning of EMU as a consequence, thereby contributing to a return of confidence. That promise must now be delivered through the full use and strict implementation of the new tools that are already in place.

For any further steps towards a deep and genuine EMU to become possible the proposed two-pack legislation ought to be agreed by co-legislators without any further delay. The two-pack contains important instruments to sharpen budgetary surveillance and to deal more efficiently with situations of financial instability in Member States. Its swift adoption and implementation thereafter should bolster confidence in the commitment of EU institutions to complete the overhaul of economic governance.

3.1.2 Financial regulation and supervision: single rulebook and proposals for a Single Supervisory Mechanism

The euro area summit held on 29 June 2012 marked a turning point in the approach to the crisis. It recognised the "imperative" need to "break the vicious circle between banks and sovereigns" that is weakening the finances of euro area countries, to the point of threatening the very existence of the EMU. In particular, the agreement to set up a Single Supervisory Mechanism (SSM) was based on the conviction that financial fragmentation must be overcome and that the centralisation of banking supervision is necessary to ensure that all euro area countries can have full confidence in the quality and impartiality of banking supervision.

A true Economic and Monetary Union must indeed include shared responsibility for policing the banking sector and intervening in case of crises. This is the only way to effectively break the vicious circle linking Member States' public finances and the health of their banks, and to limit negative cross-border spillover effects.

An integrated financial framework, evolving over time into a full banking union, would help decisively by providing an integrated set of tools better to monitor and contain the risk in the financial system. That would lessen financial fragmentation, considerably reduce the necessity for public intervention, aid rebalancing and in so doing improve the prospects for growth. The tools are integrated because their impact will be lessened if any individual components are weak. Although some necessary parts of the system will take time to develop, that must not delay the swift implementation of those elements that can bring immediate benefits.

The Commission set out a vision of a gradually unfolding banking union in its Communication of 12 September 2012.[8] The Presidents of the European Council, the Commission, the Euro Group and the ECB have endorsed that vision in principle.[9] The European Council of 18 October 2012 confirmed the "*need to move towards an integrated financial framework, open to the extent possible to all Member States wishing to participate*."[10] In its report "Towards a genuine Economic and Monetary Union" of

[8] See Commission Communication titled "A Roadmap towards a Banking Union" outlining the Commission's overall vision for rolling out the banking union, covering the single rulebook, common deposit protection and a single bank resolution mechanism", COM(2012)510, http://ec.europa.eu/internal_market/finances/docs/committees/reform/20120912-com-2012-510_en.pdf

[9] http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/132809.pdf

[10] http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/132986.pdf

November 2011, the European Parliament calls for the adoption of the proposals of the Commission in this respect as soon as possible.

The first, crucial step on this path will be the Single Supervisory Mechanism, which must subsequently be complemented by a Single Resolution Mechanism (see 3.2.1).

A Single Supervisory Mechanism must ensure full sharing of information between supervisors about banks, common prevention tools and common action to address problems at the earliest possible stage. In order to restore confidence among banks, investors and national public authorities, it must also allow for supervision to be carried out in a strict and objective manner, with no room left for regulatory forbearance.

On 12 September 2012, the Commission made legislative proposals to create a Single Supervisory Mechanism composed of the ECB and national supervisors,[11] and to amend the 2010 regulation establishing the European Banking Authority in order to adapt it to the creation of the Single Supervisory Mechanism and ensure a balance in its decision-making structures between euro area and non-euro area Member States[12].

The Single Supervisory Mechanism as proposed by the Commission is based on the transfer to the European level of specific, key supervisory tasks for banks established in the euro area Member States and for banks established in non-euro area Member States which decide to join the banking union. Under this new framework, the ECB will be responsible for supervising all banks within the banking union, to which it will apply the single rulebook applicable across the single market. The framework proposed by the Commission ensures effective and consistent supervision in all participating Member States, while relying on the specific know-how of national supervisors. It is of crucial importance that the negotiations on the SSM are completed before the end of the year, and that its implementation starts early on in 2013. As a complement, the European Banking Authority (EBA) will be adjusted to the new framework for banking supervision in order to ensure the integrity of the Single Market.

This will pave the way towards the use of the ESM as a public backstop in order, where appropriate, and once an agreement has been reached on this instrument, to directly recapitalise banks in accordance with the conclusions of the European Council of 19 October 2012. This will further reinforce the euro area, by helping to break the negative feedback loop between banks and their sovereigns.

Depositor and market participants' confidence is paramount in resolving banks. To achieve a level of public trust that is comparable to the best resolution authorities around the world, there will need to be a credible single resolution system and a powerful financial backstop in

[11] http://ec.europa.eu/internal_market/finances/docs/committees/reform/20120912-com-2012-511_en.pdf

[12] http://ec.europa.eu/internal_market/finances/docs/committees/reform/20120912-com-2012-512_en.pdf

place. That responsibility remains national in the near term. But once the SSM is in place, and subject to the relevant guidelines, the ESM should be allowed to offer mutualised support to directly recapitalise banks that fail to raise funds in the market and that cannot be rescued by their home Member State without endangering its fiscal sustainability.

An integrated financial framework including a single supervision and subsequently a single resolution mechanism must be based on a single rulebook. Therefore, it is essential to conclude as a matter of urgency the negotiations on the Commission proposals establishing new regulatory frameworks in the areas of banking prudential rules, deposit guarantees, and bank recovery and resolution.

3.1.3 A Single Resolution Mechanism

An effective banking union requires not only a Single Supervisory Mechanism ensuring high quality supervision across Member States, but also a Single Resolution Mechanism to deal with banks in difficulties. This was recognised by the European Council on 19 October 2012, which stated that it "*notes the Commission's intention to propose a single resolution mechanism for Member States participating in the SSM once the proposals for a Recovery and Resolution Directive and for a Deposit Guarantee Scheme Directive have been adopted.*"

Following the adoption of the Single Supervisory Mechanism, the Commission will therefore make a proposal for a Single Resolution Mechanism, which will be in charge of the restructuring and resolution of banks within the Member States participating in the Banking Union. This mechanism will be articulated around a separate European Resolution Authority, which will govern the resolution of banks and coordinate in particular the application of resolution tools. This mechanism will be more efficient than a network of national resolution authorities, in particular as regards cross-border banking groups for which, in times of crisis, speed and coordination are crucial to minimise costs and restore confidence. It would also entail significant economies of scale, and avoid the negative externalities that may derive from purely national decisions.

Any intervention by the single resolution mechanism will have to be based on the following principles:

- The need for resolution should be reduced to the minimum, thanks to strict common prudential rules, and improved coordination of supervision within the Single Supervisory Mechanism.
- Where intervention by the Single Resolution Mechanism is necessary, shareholders and creditors should bear the costs of resolution before any external funding is granted, in accordance with the Commission proposal on Bank Recovery and Resolution.
- Any additional resources needed to finance the restructuring process should be provided by mechanisms funded by the banking sector, instead of using taxpayers' money.

Future Commission proposals for a single resolution mechanism will be based on these principles.

The Commission considers that, just as the establishment of an effective Single Supervisory Mechanism, the creation of a Single Resolution Mechanism can be realised by secondary law without require any amendment of the current Treaties.

3.1.4 A quick decision on the next Multi-annual Financial Framework (MFF)

The Commission proposal for the 2014-2020 Multi-annual Financial Framework represents the decisive driver for investment, growth and employment at the EU level. It also foresees to tie the funding from cohesion policy, rural development and the European maritime and fisheries policy more systematically to the different economic governance procedures. The Common Strategic Framework (covering the following 'CSF Funds': the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund) establishes a strong link between these funds and the national reform programmes, the stability and convergence programmes drawn up by the Member States, as well as the country-specific recommendations adopted by the Council for each Member State.

This will be implemented via partnership contracts/agreements between Member States and the Commission and the application of rigorous macroeconomic conditionality. In the Commission proposal macroeconomic conditionality is applied in two ways:

1. Reprogramming: this concerns amendments to the partnership contracts and relevant programmes in support of Council recommendations, or to address an excessive deficit, macroeconomic imbalances or other economic and social difficulties or to maximise the growth and competitiveness impact of the CSF Funds for Member States receiving financial assistance from the EU. Where a Member State fails to respond satisfactorily to such a request, the Commission may suspend part or all of the payments for the programmes concerned.
2. Suspension: when a Member State fails to take corrective action in the context of the economic governance procedures. In such a case, the Commission shall suspend part or all of the payments and commitments for the programmes concerned.

The partnership contracts and operational programmes will ensure that the planned investments co-financed by the CSF funds will effectively contribute to addressing the structural challenges facing Member States. In the case of Council recommendations in the context of Articles 121 and 148 of the Treaty and the corrective arm of the MIP, a reprogramming will be triggered for those recommendations that are relevant for the CSF funds and related to structural challenges that can be addressed through multi-annual investment strategies. Such recommendations cover, among other things:

- Labour market reforms that will improve the functioning of the labour market such as addressing the skills mismatches
- Measures to foster competitiveness such as the improvement of education systems or the promotion of R&D, innovation and infrastructure
- Measures to improve the quality of government such as the improvement of the administrative capacity and statistics

Through a swift adoption of the MFF and the relevant sector legislation, in particular the "Common Provisions Regulation" for the CSF Funds, incentives and support for structural reforms in Member States will be rapidly strengthened.

3.1.5 Ex-ante coordination of major reforms and the creation of a "Convergence and Competitiveness Instrument"

The fact that Member States' economic policies are a matter of common concern has been brought into sharp relief through the experience of the crisis, especially in the euro area. Slow or absent implementation of important structural reforms over long periods of time aggravated competitiveness problems and hampered Member States' adjustment capacity, in some cases significantly. This contributed to increasing these Member States' vulnerability. Short-term costs, be they political or economic in nature, often act as a deterrent to reform implementation even when the medium- to long-term benefits are sizeable. The potentially significant spillover effects associated with structural reforms in the euro area justify the use of specific instruments, as has already been done through the enforcement mechanisms introduced under the six-pack legislation. In view of these considerations, the existing framework for economic governance of the euro area should be strengthened further through ensuring greater ex-ante coordination of major reform projects and, following the decision on the next MFF, through the creation of a "Convergence and Competitiveness Instrument" to provide support for the timely implementation of structural reforms (see Annex 1 for a more detailed description of the intended setup). This instrument would combine deepening integration of economic policy with financial support, and thereby respect the principle according to which steps towards more responsibility and economic discipline are combined with more solidarity. The Commission will, in a forthcoming proposal, set out the precise terms for this instrument.

Ex-ante coordination of major reforms

The current EU economic surveillance framework already provides a basis for economic policy coordination. This framework, however, does not provide for systematic ex ante coordination among the Member States of national plans for major economic policy reforms. Ex ante discussion and coordination of major reform plans, as envisaged in Article 11 of the TSCG, would allow the Commission and Member States to assess the potential spillover

effects of national action and comment on the plans before final decisions are taken at national level. In a forthcoming proposal, the Commission will propose a framework for the ex-ante coordination of major structural reforms in the context of the European Semester.

A Convergence and Competitiveness Instrument: contractual arrangements and financial support

The proposed Convergence and Competitiveness Instrument (CCI) would encompass contractual arrangements underpinned by financial support.

The implementation of structural reforms in the euro area Member States would be facilitated by the set-up of contractual arrangements to be agreed between them and the Commission. This new system would build on the existing EU surveillance framework, namely the procedure for the prevention and correction of macroeconomic imbalances (the Macroeconomic Imbalances Procedure or MIP)[13]. Such arrangements would be negotiated between individual Member States and the Commission, discussed in the Euro Group and concluded by the Commission with the Member State. They would be compulsory for euro area Member States subject to an Excessive Imbalance Procedure and the corrective action plan (CAP) they have to submit under this procedure would constitute the basis of the arrangement to be negotiated with the Commission. For the euro area Member States subject to a preventive action as regards their macroeconomic imbalances, the participation would be voluntary and would involve the presentation of an action plan similar to that required under the Excessive Imbalance Procedure.

The arrangements would therefore be always based on the country-specific recommendations emanating from the MIP, which typically focus on enhancing adjustment capacity and competitiveness and promote financial stability, i.e. factors critical to the good functioning of the EMU. The MIP therefore establishes a sensible filter for major reforms eligible to be accompanied by financial support in view of the associated externalities present in a currency union.

The action plan presented by the Member State would then be assessed by the Commission and a final set of reforms and measures and the timeline for their implementation would be adopted as an arrangement. This arrangement would thus set out the more detailed measures which the Member State commits to implement after having obtained the endorsement of its national parliament where appropriate under national procedures. This system of negotiated arrangements would enhance the quality of the dialogue between Commission and Member States as well as the Member States' commitment to and ownership of their reforms.

The reforms taken up in the contractual arrangements would be financially supported, as a complement to the discipline requirements already introduced by the six-pack. The aim of

[13] Regulation (EU) N° 1176/2011

such support would be to lead to timely reform adoption and implementation by overcoming or at least lessen political and economic deterrents to reform. By promoting structural reforms that enhance the adjustment capacity of a Member State the CCI would improve the economy's capacity to absorb asymmetric shocks through enhancing market functioning.

Financial support would only be granted for reform packages that are agreed and important both for the Member State in question and for the good functioning of EMU. The financial support would be supporting the efforts of a Member State and in particular provide support in cases where the emergence of imbalances happened in spite of full compliance with previous country-specific recommendations addressed to the Member State concerned..

The financial support will have a clear signalling effect recognising both the cost of reform for the Member State in question as well as the benefit of national reforms accruing to the rest of the euro area given positive cross-border externalities (which may not be sufficient though to lead to reform impetus by Member States). Where the Commission finds ex post that a Member State has not fully complied with the contract, the financial support can be withheld.

The financial support should be designed as an overall allocation to be used to contribute to financing measures flanking difficult reforms. For example, the short-term impact of reforms raising the flexibility in the labour market could be accompanied by training programmes financed in part through support provided under the CCI. The use of financial support would be defined as part of the contractual arrangement concluded between the Member State concerned and the Commission.

To support this mechanism of financial support a special financial instrument could be set up in principle as part of the EU budget.

The instrument would be established by secondary legislation. It could be construed as part and parcel of the MIP reinforced by the contractual arrangements and financial support as outlined above and thus be based on Article 136 TFEU. Alternatively one could envisage having recourse on Article 352 TFEU, if necessary by enhanced cooperation (coupled with a decision pursuant to Article 332 TFEU on expenditure being included in the EU budget).

The financial contributions necessary to the instrument could be based on a commitment of the euro area Member States or a legal obligation to that effect enshrined in the EU's own resources legislation. Contributions should be included in the EU budget as assigned revenues. Being financed through assigned revenue, the instrument would not be placed under the ceilings set in the MFF Regulation. Only contributing Member States would be in a position to enter into a contractual arrangement with the Commission and benefit from the financial support. Support through the CCI would be coherent and consistent with the support from the Structural Funds, in particular the European Social Fund. The volume of the instrument could remain limited in the initial phase but could become larger over the medium

term provided that the support mechanism proves to be effective in promoting rebalancing, adjustment and thereby sustainable growth in the euro area.

The Commission will in forthcoming proposals set out the precise terms for this "convergence and competitiveness instrument" based on contractual arrangements and financial support.

3.1.6 Promoting investment in the euro area

Structural reforms supported, first, by the MFF and, second, the Convergence and Competitiveness instrument will be essential to improve the medium-term growth potential of euro area members and their adjustment to shocks. Credible and growth-friendly consolidation that improves the efficiency of the tax structure as well as the quality of public spending will contribute to stimulating growth. As recommended in the Annual Growth Surveys 2012 and 2013, the Member States should strive in particular to maintain an adequate fiscal consolidation pace while preserving investments aimed at achieving the Europe 2020 goals for growth and jobs.

The EU fiscal framework offers scope to balance the acknowledgment of productive public investment needs with fiscal discipline objectives.

Public investment is one of the relevant factors to be taken into account when the fiscal position of a Member State is being assessed in the report foreseen under Article 126(3) TFEU that precedes the launch of an EDP.[14] The importance of relevant factors, such as public investment, for the assessment has considerably increased with the recent reform of the SGP. Under certain conditions, consideration of relevant factors may lead to not placing a Member State in EDP[15]; and relevant factors should be taken into account in formulating recommendations for correcting the excessive deficit, including the deficit reduction path.

In the preventive arm of the SGP, public investment is taken into consideration in the new expenditure benchmark, which is used alongside the structural balance to assess the progress towards the medium-term budgetary objective. Specifically, general government gross fixed

[14] Specifically, according to Article 126(3) TFEU: "The report of the Commission shall also take into account whether the government deficit exceeds government investment expenditure and take into account all other relevant factors (...)".

[15] First, consideration of relevant factors may lead to not placing a Member State in EDP despite a breach of the deficit criterion when the debt ratio is below the reference value. Second, a breach of the debt reduction benchmark should result in the opening of an EDP only after the assessment of the relevant factors.

capital formation is averaged over a number of years, in order to avoid that Member States penalised because of annual peaks in investment[16].

The Commission will explore further ways within the preventive arm to accommodate investment programmes in the assessment of Stability and Convergence Programmes. Specifically, under certain conditions, non-recurrent, public investment programmes with a proven impact on sustainability of public finances could qualify for a temporary deviation from the medium-term budgetary objective or the adjustment path towards it.[17] This could apply, for example, for government investment projects co-financed with the EU, consistently with the framework of macro-conditionality.

While a fully-fledged framework would have to be worked out to render operational such conditions (notably in terms of information/definitional requirements), a specific treatment of public investment could only lead to a temporary deviation from the medium term budgetary objective (MTO) or the adjustment path towards it. The Commission will issue a Communication on the appropriate path towards the MTO in Spring 2013.

Specific provisions for investment projects should not be confused with a 'golden rule', which would allow a permanent exception to all public investment. Such an indiscriminate approach could easily put in danger the prime objective of the SGP by undermining the sustainability of government debt.

3.1.7 External representation of the euro area

Building on progress achieved in the economic governance of the euro area, a strengthening and consolidation of its external representation should be pursued. This can be fully achieved on the basis of the current Treaties (Article 17 TEU and Article 138 TFEU).

[16] Also, expenditure on EU programmes, and thus also investment expenditure, to the extent that it is fully matched by EU funds revenue, is also excluded from the expenditure considered for assessing the compliance with the expenditure benchmark.

[17] The SGP embeds specific provisions that allow for such a possibility. Regulation 1466/97 - Article 5(1): "...When defining the adjustment path to the medium-term objective for Member States that have not yet reached this objective, and in allowing temporary deviation from this objective for Member States that have already reached it, provided that an appropriate safety margin with respect to the deficit reference value is preserved and that the budgetary position is expected to return to the medium-term budgetary objective with the programme period, the Council and the Commission shall take into account the implementation of major structural reforms which have direct long-term positive budgetary effects, including by raising potential sustainable growth, and therefore a verifiable impact on the long-term sustainability of public finances..."

Such strengthening is necessary to ensure that the euro area is represented in a manner commensurate with its economic weight, mirroring the changes taking place in the internal economic governance. The euro area must be able to play a more active role both in multilateral institutions and fora as well as in bilateral dialogues with strategic partners. This should result in delivering a single message on issues such as euro area economic and fiscal policy matters, macroeconomic surveillance, exchange rate policies and financial stability.

To achieve these objectives will require agreement on a roadmap aimed at streamlining and, where possible, unifying the external representation of the euro area in international economic and financial organisations and fora.

The focus should be on the IMF, which through its lending instruments and surveillance is a key institutional pillar in global economic governance. As the crisis has shown, it is of utmost importance for the euro area to speak with a single voice in particular on programmes, financing arrangements and the crisis resolution policy of the IMF. This will require a strengthening of coordination arrangements of the euro area in Brussels and Washington on EMU-related matters, to mirror changes in EMU internal governance and to ensure consistency and effectiveness of the messages provided.

Enhancing the euro area representation in the IMF should be done through a two-stage process. In a first stage, the country constituencies should be rearranged so as to re-group countries into euro area constituencies which could also include future euro area Member States. In parallel, observer status in the IMF executive board should be sought for the euro area [18].

These measures should prepare the ground for the euro area seeking, at a second stage, a single seat in the IMF bodies (the executive board and the IMFC). The Commission will in due course make formal proposals under Article 138 (2) TFEU to establish a unified position to achieve an observer status of the euro area in the IMF executive board, and subsequently for a single seat. The appropriate institution to represent the euro area in the IMF, in accordance with Article 138 TFEU, would be the Commission, with the ECB being associated in the area of monetary policy. More details on this aspect of deepening EMU are found in Annex 2.

3.2 The medium term: Enhanced economic and budgetary policy integration and steps towards a proper fiscal capacity

The medium term should see the establishment of further budgetary coordination (including the possibility to require a revision of national budgets in line with European commitments),

[18] I.E., the EU representing the euro area Member States in accordance with the Treaties.

the extension of deeper policy coordination to the fields of taxation and employment and the creation of an autonomous, proper fiscal capacity for the EMU to support the implementation of the policy choices resulting from the deeper coordination. Some of these elements will require amending the Treaties.

The reduction of public debt significantly exceeding the SGP criteria could be addressed through the setting-up of a redemption fund. A possible driver for fostering the integration of euro area financial markets and in particular to stabilise volatile government debt markets is common issuance by euro area Member States of short-term government debt with a maturity of up to 1 to 2 years. Both of these possibilities would require amending the Treaties.[19]

3.2.1 Reinforcement of budgetary and economic integration necessitating Treaty changes

The overhaul of the budgetary and economic governance that the euro area would have undergone with the adoption of the two-pack and the availability of the Convergence and Competitiveness Instrument would represent major steps forward in ensuring budgetary discipline but also economic competitiveness.

However, moving towards more mutualisation of financial risk would require bringing the coordination of budgetary policy one step further by ensuring that there is collective control over national budgetary policy in defined situations.

In particular, the innovations brought by the two-pack and especially the possibility of a Commission opinion on draft budgetary plans, and in extreme cases, the possibility to request a new draft budgetary plan in case of serious violation of the Member State's obligations under the SGP, are reaching the limit of what is possible under the current Treaties in terms of coordination and intervention from the EU level in the national budgetary process. With the two-pack, once adopted, the EU will largely have exhausted the limits of its legislative competence in these respects.

Moving further in terms of national budgetary policy control, for example by setting up a European right to require a revision of national budgets in line with European commitments, would require a Treaty change.

The following (non-exclusive) avenues could be considered:

- First, an obligation for a Member State to revise its (draft) national budget if the EU level so requires in case of deviation from obligations of budgetary discipline previously set at EU level. This would involve changing the nature of the opinion on national budgets foreseen in the two-pack from a non-binding to a binding character.

[19] See Judgment of 27 November 2012 in case C-370/12 Pringle, points 137 and 138.

- Second, building upon the tighter monitoring and coordination process set up by the two-pack, in certain particularly serious situations to be defined, a right to require a revision of individual decisions of budget execution in line with European commitments which would result in a serious deviation from the path of budgetary consolidation set at EU level.

- Third, a clear competence for the EU level to harmonise national budgetary laws (along the lines of the Treaty on Stability, Coordination and Governance in Economic and Monetary Union[20]) and to have recourse to the Court of Justice in case of non-compliance.

As regards economic policy, tax policy can support economic policy coordination and contribute to fiscal consolidation and growth. Based on the experience to be gained with the structured discussions of tax policy issues which focus on areas where more ambitious activities can be envisaged, one might in future consider in the context of a Treaty change providing scope for legislation on deeper coordination in this field in the euro area. Another area of similar importance where such progress could be considered is labour markets, given the importance of well-functioning labour markets and in particular labour mobility for adjustment capacity and growth within the euro area.

Coordination and surveillance of employment and social policies should be reinforced within the EMU governance, and convergence promoted in these areas. The current Broad Economic Policy Guidelines and Employment Guidelines could be reinforced by merging them into one single instrument.

These changes would provide the basis for developing a proper fiscal capacity for the euro area to support structural reform on a large scale as well as for enabling forms of debt mutualisation to facilitate the solution of the problems of high debt and financial segmentation that are among the legacies of the crisis.

3.2.2 A proper fiscal capacity for the euro area

Building on the experience of systematic ex-ante coordination of major structural reforms and the CCI, a dedicated fiscal capacity for the euro area should be established. It should be autonomous in the sense that its revenues would rely solely on own resources, and it could eventually resort to borrowing. It should be effective and provide sufficient resources to support important structural reforms in a large economy under distress.

[20] In any event, the substance of that Treaty should be integrated into Union law as foreseen in its Article 16.

This proper fiscal capacity for the euro area could initially be developed under secondary law, as explained in section 3.1.3. Its enhancement would however benefit from new, specific Treaty bases which would be necessary if the capacity had to be able to resort to borrowing.

3.2.3 A redemption fund

A clearly reinforced economic and fiscal governance framework could allow addressing the reduction of public debt significantly exceeding the SGP criteria through the setting-up of a redemption fund subject to strict conditionality.

The initial proposal of a European Redemption Fund (ERF) as an immediate crisis tool was developed by the German Council of Economic Experts (GCEE) as part of a euro area-wide debt reduction strategy.

In order to limit moral hazard, and to ensure the stability of the structure as well as the redemption of payments, the GCEE proposed several supervisory and stabilising instruments, such as: (1) strict conditionality, similar to the rules agreed within EFSF/ESM programmes; (2) immediate penalty payments in case of non-compliance with the rules; (3) strict monitoring by a special institution (e.g. Court of Justice of the EU); (4) an immediate stop of debt transfer to the fund during the roll-in phase in case of non-compliance with the rules; (5) pledging of Member States' international reserves (foreign exchange or gold reserves) as a security against their liabilities and/or assignment of (possibly newly introduced) taxes to cover the debt service (e.g. VAT revenues) to limit the liability risk.

The Commission agrees that a strong economic and budgetary framework is a pre-requisite for a workable redemption fund. Increased surveillance and power of intervention in the design and implementation of national fiscal policies would be warranted as discussed in the previous section. The credibility of the adjustment plans would require appropriate fiscal conditions to be set when a Member State enters the system. Strict observance of the adjustment path towards the medium-term objective as proposed by the Commission would represent a minimum in this respect.

A European Redemption Fund under such strict conditionality (see also Annex 3) could thus provide an anchor for a credible reduction in public debt, bringing the level of government indebtedness back below the 60% ceiling as foreseen in the Maastricht Treaty.

The introduction of such a framework could give another signal that euro area Member States are willing, able and committed to reduce their debt levels. This could in turn lower the overall financing costs of over-indebted Member States. By assuring the funding of the reduction of the "excess debt" at sustainable cost, in combination with both incentives and continuous monitoring of its reduction, it could provide euro area Member States with the possibility to gear debt reduction in a manner that could facilitate investment in growth-supporting measures. Furthermore, such a framework could contribute to debt reduction

being done on a transparent and coordinated basis across the euro area, thereby complementing the coordination of budgetary policies.

The setting up of such a debt redemption fund could only be envisaged in the context of a revision of the current Treaties. For accountability reasons, the act creating such a fund would need to be framed with great legal precision, as regards the maximum transferrable debt, the maximum time of operation and all other features of the fund, to guarantee the legal certainty required under national constitutional laws.

A possible model ensuring appropriate accountability for a debt redemption fund thus designed would be as follows: a new Treaty legal base would allow the setting up of the fund through a decision of the Council, adopted by unanimity of the euro area members with the consent of the European Parliament, and subject to ratification by Member States under their constitutional requirements. That decision would set up the maximum volume, length and conditions of participation in the fund. A European debt management entity within the Commission, accountable to the European Parliament, would then manage the fund in accordance with the rules set up by the Council decision.

3.2.4 Eurobills

An important effect of the crisis has been the reassessment of sovereign-credit risk within the euro area. After more than a decade during which Member States could borrow at almost identical conditions, markets started again to differentiate risk premia across countries. Government securities issued by the weaker euro area Member States have been traded at considerably higher yields, with adverse consequences for the sustainability of public finances for the sovereigns concerned as well as for the solvency of the financial institutions holding those government securities as assets. This segmentation of credit risk together with the "home bias" that characterises financial institutions has proved to be a powerful engine of financial fragmentation in the euro area. Banks overexposed to weaker sovereigns find it increasingly difficult to refinance and credit conditions for the private sector have become significantly diverse according to the location of the borrower. At the same time, segmentation of the financial market hinders the transmission of monetary policy and easing at central level does not translate into an appropriate improvement of lending conditions where it would be more warranted.

In light of this situation, there is a strong argument for the creation of a new euro area sovereign instrument. A possible driver for fostering the integration of euro area financial markets and in particular to stabilise volatile government debt markets is so-called eurobills. This common issuance by euro area Member States of short-term government debt with a maturity of up to 1 to 2 years would constitute a powerful tool against the present fragmentation, reducing the negative feedback loop between sovereign and banks, while limiting the moral hazard. Additionally, it would also help restoring the proper transmission of monetary policy. Eurobills could progressively replace existing short-term debts, and not expand the overall amount of national euro area short-term debt.

These so-called eurobills could contribute to completing European financial markets by creating a large integrated short-term securities market in the euro area. Given the important role of short-term papers for cash management and the short-term nature of bills, these securities typically enjoy a particularly high credit quality. At the same time, the revolving, short-term nature of such bills makes it possible to adjust the funding schemes quickly to national fiscal behaviour, thereby setting incentives for fiscal discipline.

The common issuance would strengthen financial stability insofar as it would ensure a ready supply of short-term liquidity for all euro area Member States. It would also create a pool of safe assets across the euro area, which would greatly facilitate the liquidity management of financial institutions and thereby reduce their often strong home bias, which proved very detrimental in crisis situations. The eurobills would also help greatly for the conduct of monetary policy in the euro area, as the transmission channels would be strengthened and harmonised. Eurobills would thereby be fully compatible and complementary to the concept of a redemption fund.

Due to their character as financial instruments requiring joint and several guarantees by the participating Member States, changes to the Treaties would be required to allow these instruments to be developed. Eurobills are not a substitute for improved economic governance and fiscal discipline. The implementation of such a common debt instrument would require a closer coordination and supervision of Member States' debt management in order to ensure sustainable and efficient national budgetary policies. This monitoring and managing function could be provided by an EMU Treasury within the Commission.

3.3 A longer-term vision for EMU

In the longer term, the European Union should move towards a full banking union, a full fiscal union, a full economic union, which all require, as a fourth element, appropriate democratic legitimacy and accountability of decision-making. Major Treaty reform will be required on this path.

3.3.1 Full banking union

Over the longer term, the logic of aiming for a full banking union for all banks is compelling. The direct supervision by the ECB applying the single Rulebook and the standards developed by EBA ensure a consistently high quality of supervision across the euro area. In combination with euro area level macro-prudential policy tools, there will be an effective system to monitor and contain both micro- and macro-prudential risks in the financial system.

That system and a common system for banking resolution, combined with effective and solid deposit guarantee schemes in all Member States, will lastingly place the banking sector back

on a solid footing and contribute to keeping up confidence in the sustainable stability of the euro area. To maximise public trust, there will also need to be a credible and powerful financial backstop. That could ultimately be facilitated by the development of a euro area safe asset.

Combining all these elements, a full banking union is a key part of a long-term vision for economic and fiscal integration.[21]

3.3.2 Full fiscal and economic union

Arriving at a full fiscal and economic union would be the final stage in EMU. As a final destination, it would involve a political union with adequate pooling of sovereignty with a central budget as its own fiscal capacity and a means of imposing budgetary and economic decisions on its members, under specific and well-defined circumstances. How large this central budget would be will depend on the depth of integration desired and on the willingness to enact accompanying political changes. Such a deep degree of integration would have created the conditions for a common issuance of debt through Stability Bonds as set out in the Commission's 2011 Green Paper.

The absence of a central budget with a stabilisation function has long been identified as a potential weakness of the euro area in comparison with other successful monetary unions.

Central Budget providing for a fiscal capacity with a stabilisation function

The current EMU architecture relies on decentralised national fiscal policies under a rules-based framework. The stabilisation function of fiscal policy in this setting is expected to be already exerted at national level, within the limits of the rules of the Treaty and the SGP. Indeed, a traditional view of EMU arrangements assigns to national fiscal policies the task of responding to country-specific shocks, and to monetary policy the task of ensuring price stability and in so doing stabilise EMU-wide macroeconomic conditions. Moreover, national automatic stabilisers carry a significant potential for stabilisation in EMU countries, given the relatively large size of welfare states.

Building on the fiscal capacity, an EMU-level stabilisation tool to support adjustment to asymmetric shocks, facilitating stronger economic integration and convergence and avoiding the setting up of long-term transfer flows, could become a component for a genuine EMU. Such a mechanism would need to be strictly targeted to address short-term asymmetries and

[21] See Commission Communication titled "A Roadmap towards a Banking Union" outlining the Commission's overall vision for rolling out the banking union, covering the single rulebook, common deposit protection and a single bank resolution mechanism", COM(2012)510, http://ec.europa.eu/internal_market/finances/docs/committees/reform/20120912-com-2012-510_en.pdf

cyclical developments in order to avoid permanent transfers over the cycle. It must be supportive of structural reforms and be subject to strict political conditionality to avoid moral hazard.

A common instrument dedicated to macroeconomic stabilisation could provide an insurance system whereby risks of economic shocks are pooled across member states, thereby reducing the fluctuations in national incomes. Second, it may help improve the conduct of national fiscal policies throughout the cycle. In particular, it may encourage fiscal retrenchment during economic booms, while providing additional room for manoeuvre for a supportive fiscal stance in downturns. Overall, a shared instrument could deliver net gains in stabilising power, as compared with current arrangements.

Depending on the design, the mechanism could focus on asymmetric shocks or also comprise shocks that are common to the euro area. However, this second approach, while more encompassing, would require strong safeguards to maintain fiscal credibility, as increased stabilisation power against common unfavourable shocks could only be obtained by effectively increasing the total borrowing flow of the euro area in these periods, and thus would have to be financed by higher surpluses in good times. Under this approach, the central budget should probably be given the capacity to borrow and issue bonds. Moreover, monetary policy would still remain the primary instrument to address common shocks.

In its simplest formulation, a stabilisation scheme to stabilise asymmetric shocks could require monetary net payments that are negative in good times and positive in bad times. For example, a simple scheme would determine net contributions/payments of countries as a function of their output gap (relative to the average). No further requirements would be made on the use of the payments received from the fund.

Alternatively, schemes may require that the payments from the fund be earmarked for a defined purpose, with counter-cyclical effects (as e.g. in the US unemployment benefit system where a federal fund reimburses 50% of the unemployment benefits exceeding standard duration up to a given maximum, conditional on unemployment being at a certain level and rising). While earmarking transfers might enhance stabilisation properties, the risk that governments offset the impact of the transfers via fiscal measures with opposite effects cannot be fully prevented.

Schemes should operate in such a way to avoid "permanent transfers" across countries. In other words, they should be designed in such a way to avoid that, over a too long period of time, any country is a net loser or gainer from the scheme. A necessary condition is that cross-country differences in net transfers to the scheme do not depend on absolute income differences but rather on differences in cyclical positions. Income level differences may persist over decades, while relative cyclical positions are likely to change sign in the course of a decade. There is a trade-off between the extent to which transfers are obliged to be

temporary and the degree to which asymmetric long-lasting demand shocks (e.g. capital outflows cum deleveraging) could be addressed.[22]

Institutional considerations

Treaty amendments providing the legal bases for such a fiscal capacity with a stabilisation function could, inter alia:

- create a new explicit legal basis allowing to set up a fund serving objectives more broadly defined than is currently possible under Article 136 TFEU, including for macroeconomic stabilisation purposes;
- create a corresponding, dedicated budgetary and own resources procedure;
- create a new taxation power at the EU level, or a power to raise revenue by indebting itself on the markets (presently barred by Articles 310 and 311 TFEU);
- provide for an EMU Treasury within the Commission;
- and finally if wished, allow other Member States to freely opt in to such a fiscal capacity, as a step in preparing their joining the euro area.

Attaining a deep and genuine EMU involves incremental measures, building on what would have been achieved over the short and the medium-term and introducing further integration on a step-by-step, policy-by-policy basis. In this way deeper economic and budgetary policy coordination accompanied by financial support instruments for implementing jointly agreed policy priorities could eventually be followed by the emergence of a central budget with common stabilisation mechanisms, by the integration of the ESM into the EU Treaty framework and by steps towards the mutualisation of issuance of sovereign debt between the Member States.

The progress towards a deep and genuine EMU would over the medium term necessitate a structure akin to an EMU Treasury within the Commission to organise the shared policies undertaken with the common fiscal capacity to the extent that they imply common resources and/or common borrowing. Such a Treasury would embody the new budgetary authority and manage the joint resources. It would need to be headed by a senior member of the Commission such as the Vice President responsible for Economic and Monetary Affairs and the euro, in appropriate coordination with the Budget Commissioner, and supported by appropriate collegiate structures.

[22] Some existing analyses assess econometrically the contribution of existing transfer schemes available in federal states on the absorption of asymmetric shocks. For example, estimates on the stabilisation capacity of transfers across US States vary from 10% to 30% of the shock offset by the transfer for the US.

While it would not be excluded to integrate the ESM into the EU framework under the current Treaties, via a decision pursuant to Article 352 TFEU and an amendment to the EU's own resources decision, it appears that, given the political and financial importance of such a step and the legal adaptations required, that avenue would not necessarily be less cumbersome than operating an integration of the ESM through a change to the EU Treaties. The latter would also allow the establishment of tailor-made decision-making procedures.

All the different steps mentioned above imply a higher degree of transfers of sovereignty, hence responsibility at the European level. This process should be accompanied by steps towards political integration, to ensure strengthened democratic legitimacy, accountability and scrutiny.

4. Political Union: Democratic legitimacy and accountability as well as enhanced governance in a deep and genuine EMU

4.1. General principles

Any work on democratic legitimacy as a cornerstone of a genuine EMU needs to be based on two basic principles. First, in multilevel governance systems, accountability should be ensured at that level where the respective executive decision is taken, whilst taking due account of the level where the decision has an impact. Second, in developing EMU as in European integration generally, the level of democratic legitimacy always needs to remain commensurate with the degree of transfer of sovereignty from Member States to the European level. This holds true for new powers on budgetary surveillance and economic policy as much as for new EU rules on solidarity between Member States. Briefly put: Further financial mutualisation requires commensurate political integration. This section sets out preliminary and non-exhaustive avenues for further work.

It follows from the first principle that it is the European Parliament that primarily needs to ensure democratic accountability for any decisions taken at EU level, in particular by the Commission. A further strengthened role of EU institutions will therefore have to be accompanied with a commensurate involvement of the European Parliament in the EU procedures. At the same time, whatever the final design of EMU, the role of national parliaments will always remain crucial in ensuring legitimacy of Member States' action in the European Council and the Council but especially of the conduct of national budgetary and economic policies even if more closely coordinated by the EU. Cooperation between the European Parliament and national parliaments is also valuable: it builds up mutual understanding and common ownership for EMU as a multilevel governance system; concrete steps to further improve it, in accordance with Protocol N° 1 of the EU Treaties and Article 13 of the TSCG, are thus welcome. Interparliamentary cooperation as such does not, however, ensure democratic legitimacy for EU decisions. That requires a parliamentary assembly representatively composed in which votes can be taken. The European Parliament, and only it, is that assembly for the EU and hence for the euro.

The maxim of ensuring a legitimacy level commensurate to sovereignty transfers and solidarity within a political Union leads to two general considerations.

First, the issue of accountability arises in fundamentally different ways as regards short-term action, which can be undertaken through EU secondary law, and the further stages which involve Treaty change. The Lisbon Treaty has perfected the EU's unique model of supranational democracy, and in principle set an appropriate level of democratic legitimacy in regard of today's EU competences. Hence, as long as EMU can be further developed on this Treaty basis, it would be inaccurate to suggest that insurmountable accountability problems exist. Conversely, discussions on medium and long-term Treaty amendments as envisaged in sections 3.2 and 3.3 will need to include reflections on adaptations to the EU's model of democratic legitimacy.

Second, serious accountability and governance issues would however arise if intergovernmental action of the euro area were significantly expanded beyond the current state of play. This would in particular be the case if such action were used to influence the conduct of Member States' economic policies. Such an avenue would first raise problems of compatibility with the EU's primary law in this area. As confirmed by the Court of Justice, the Treaty attributes the task of coordination of the Member States' economic policies to the Union; the ESM is in line with the Treaties precisely because its object is not to achieve such coordination but to provide a financing mechanism and because it contains express provisions by virtue of which the conditionality foreseen by the ESM Treaty - which is not an instrument of economic policy coordination - ensure that the ESM's activities are compatible with EU law and the EU's coordination measures. Moreover, intergovernmental action could entrust only limited tasks to the Union's institutions, such as the Commission and the ECB, which may be tasks of coordination of a collective action or management of financial assistance, to be exercised on behalf of the Member States and which must not denature the functions attributed to those institutions under the Treaties.[23] In any event, one fails to see how parliamentary accountability could be organised for an intergovernmental European level seeking to influence economic policies of individual euro area Member States.

To the extent that a need arises for reinforced governance structures in a deepened EMU, these should therefore be devised, with efficiency and legitimacy, as part of the Union's institutional framework and in line with the Community method.

4.2 Optimising accountability and governance in the short term

Bearing in mind the above principles, the discussion on how to ensure optimal democratic accountability and governance without Treaty change should focus on practical measures, in particular those designed to foster parliamentary debate in the European Semester.

The starting point in this respect should be the Economic Dialogue which has been recently set up by the six-pack and which provides for discussions between the European Parliament, on the one hand, and the Council, the Commission, the European Council and the Eurogroup on the other hand. Thus, one could foresee the involvement of the Parliament in the discussions on the Commission's Annual Growth Survey and that, in particular, that two debates in Parliament be held at key moments of the European Semester, namely before the European Council discusses the Commission's Annual Growth Survey and before the adoption by the Council of the country-specific recommendations (CSRs). This could be achieved through an inter-institutional agreement between the European Parliament, the Council and the Commission. The Commission and the Council could also be present at

[23] See the judgment in Case C-370/12, Pringle, at points 109 – 111 and 158 - 162.

inter-parliamentary meetings to be held between representatives of the European Parliament and of national parliaments during the European Semester. Moreover, to facilitate the task of national parliaments, members of the Commission could attend debates within such parliaments, on their request, on the EU's CSRs.

The application of the comply-or-explain principle, according to which the Council is publicly accountable (in practice mainly to the European Parliament) for any changes it introduces to the Commission's economic surveillance proposals, such as the CSRs, should be reinforced in practice.

In a deepened EMU, the Parliament should also be more directly involved in the choice of the multiannual priorities of the Union as expressed by the Integrated Guidelines of the Council (Broad Economic Policy Guidelines and Employment Guidelines).

The European Parliament should be regularly informed of the preparation and implementation of the adjustment programmes concerning Member States receiving financial assistance, as foreseen in the two-pack. It should be underlined that this economic policy conditionality vis-à-vis the Member States concerned is framed by the economic policy coordination pursued within the EU framework.

Furthermore, the European Parliament has the possibility of adapting its internal organisation to a stronger EMU. For instance, it could set up a special committee on euro matters in charge of any scrutiny and decision-making pertaining especially to the euro area.

Similarly, some further practical measures can still be taken without Treaty change to improve the functioning of the Euro Group and its preparatory instance, in line with the euro area summit statement of 26 October 2011.

Finally, and without this being a point specific to EMU, a number of steps of significant importance can be taken to foster the emergence of a genuine European political sphere. This includes, in the context of the European elections of 2014, most importantly the nomination of candidates for the office of Commission President by political parties, as well as a number of pragmatic steps that are possible under current EU electoral law. Moreover, the proposal recently tabled by the Commission for a revised statute for European political parties should be rapidly adopted.

4.3 Issues for discussion in case of Treaty amendment

In the context of a Treaty reform conferring further supranational powers to the EU level, the following steps should be considered to ensure a commensurately stronger democratic accountability:

First, for the sake of visibility, transparency and legitimacy, the current Broad Economic Policy Guidelines and Employment Guidelines (currently presented together as "integrated guidelines" but based on two distinct legal bases) should be merged into one single instrument expressing the Union's multiannual priorities, and crucially, that instrument should be adopted through the ordinary legislative procedure providing for co-decision by the European Parliament and the Council.

Second, to be appropriately legitimised, a new power of requiring a revision of a national budget in line with European commitments, if considered necessary, could be taken as a legislative act by co-decision. This solution, ensuring maximum democratic legitimacy, is justified given that Member States' annual budgets are also adopted by their parliaments, usually with legislative character. To ensure speedy decision-making, a Treaty amendment should create a new special legislative procedure consisting of only one reading.

Integration of the ESM into the EU framework, as called for in this blueprint, would allow it to become subject to proper scrutiny by the European Parliament.

Institutional adaptations might also be considered:

A "euro committee" established within the European Parliament could also be granted certain special decision-making powers beyond those assigned to other committees, e.g. a greater weight in the preparatory parliamentary stages or even a possibility to perform certain functions or take certain acts in lieu of the plenary.

Within the Commission, any steps designed to reinforce even further than today[24] the position of the Vice President for Economic and Monetary Affairs and the euro, would require adaptations to the collegiality principle and, hence, treaty changes. They could be contemplated in the long run to allow for political direction and enhanced democratic accountability of a structure akin to an EMU Treasury within the Commission. In this context, a special relationship of confidence and scrutiny between the Vice President for Economic and Monetary Affairs and a "euro committee" of the European Parliament could be

[24] It should be recalled that, in October and November 2011, the position of the Commissioner for Economic and Monetary Affairs was already significantly strengthened by several acts adopted within the limits set by the current Treaty rules, in order to guarantee the independence, objectivity and efficiency in the exercise of the Commission's responsibilities of coordination, surveillance and enforcement in the area of the economic governance of the Union and of the euro area. In particular, following an amendment to the Commission's Rules of procedure, Commission decisions in this area are adopted upon a proposal from the Vice-President responsible for Economic and Monetary Affairs and the euro by a special written procedure allowing for a more objective and effective decision-making. The Vice-President is also empowered to adopt, acting in agreement with the President, decisions on behalf of the Commission in several areas relating to the 'six-pack' and in relation to economic adjustment programmes in the framework of the EFSM, EFSF and ESM. Finally, all Commission initiatives which have a potential impact on growth, competitiveness or economic stability require the prior consultation of the Vice-President's services.

created. Their design should however be carefully pondered. The collegiality principle applies to decisions across all policy areas for which the Commission has competence, from competition to cohesion policy. It stands for a system of collective internal checks and balances which contributes to improving the legitimacy of the Commission's action.

Sometimes a call is also made to strengthen the Euro Group further by making it responsible for decisions concerning the euro area and its Member States. This would require Treaty change, since the purely informal character of the Euro Group as set out in Protocol n° 14 implies a mere forum for discussions without decision-making powers. That said, the current Treaties, in Articles 136 and 138 TFEU, have already created the model of the Council adopting decisions with only its euro area members voting. In this blueprint, the Commission makes the case for creating further Treaty legal bases following this model. The main practical difference between it, and a Euro Group endowed with decision-making powers, would be that, in the second case, delegates from non-euro area Member States would be excluded not only from voting but also from deliberations and from preparatory work carried out at instances below the ministers' meetings. That would however be undesirable in the Commission's view, since it would in reality lead to building up a "euro area Council" as a separate institution without adequately taking into account the convergence between existing and future members of the euro area.

Furthermore, a specific point to be addressed by Treaty change would be to strengthen democratic accountability over the ECB insofar as it acts as a banking supervisor, in particular by allowing normal budgetary control by the European Parliament over that activity. At the same time, Article 127 paragraph 6 TFEU could be amended to make the ordinary legislative procedure applicable and to eliminate some of the legal constraints it currently places on the design of the SSM (e.g. enshrine a direct and irrevocable opt-in by non-euro area Member States to the SSM, beyond the model of "close cooperation", grant non-euro area Member States participating in the SSM fully equal rights in the ECB's decision-making, and go even further in the internal separation of decision-making on monetary policy and on supervision). A Treaty change creating a special status for Agencies in the field of financial regulation, strengthening the supranational character of these Agencies, and their democratic accountability could also be considered. Not only would this very significantly enhance the effectiveness of the ESAs, but it would significantly facilitate the establishment and working of the Single Resolution Mechanism to be created.

A further way of strengthening the EU's legitimacy would also be to extend the competences of the Court of Justice, i.e. by deleting Art. 126 paragraph 10 TFEU and thus admitting infringement proceedings for Member States or by creating new, special competences and procedures, although one should not forget that some of the issues do not lend themselves to full judicial review.

If a Treaty reform were to extend beyond EMU matters, it should include the objective of generalising the ordinary legislative procedure, i.e. making applicable co-decision by the

European Parliament and the Council, voting by qualified majority, instead of the currently remaining instances where special legislative procedures apply.

Finally, special challenges to ensure appropriate democratic accountability would arise in case the Treaty is changed to permit the mutualisation of the issuance of sovereign debt underpinned by a joint and several guarantee of all euro area Member States. The underlying accountability problem is that such a joint and several guarantee, if claimed by creditors, may result in considerable financial burden for one individual Member State's finances, for which that Member State's parliament is accountable, although the burden is the result of policy decisions that have been made over time by one or several other Member States under the responsibility of their parliaments. As long as the EU level is not granted very far-reaching powers to determine economic policy in the euro area and the European Parliament is not responsible for deciding on the resources of a substantial central budget either, this fundamental accountability problem cannot be overcome simply by entrusting the management of mutualised sovereign debt to an EU executive even if it is accountable to the European Parliament.

In contrast, that problem would no longer arise in a full fiscal and economic union which would itself dispose of a substantial central budget, the resources for which would be derived, in due part, from a targeted, autonomous power of taxation and from the possibility to issue the EU's own sovereign debt, concomitant with a large-scale pooling of sovereignty over the conduct of economic policy at EU level. The European Parliament would then have reinforced powers to co-legislate on such autonomous taxation and provide the necessary democratic scrutiny for all decisions taken by the EU's executive. Member States would not be jointly and severally liable for each other's sovereign debt but at most for that of the EU.

If the Treaty were changed so as to allow, as an intermediate step, the issuance of short-term eurobills, combined with reinforced powers of economic governance, an accountability model resting both on the EU and national levels would have to be devised. The European Parliament would provide the necessary accountability for decisions of management of the eurobills to be taken by an EMU Treasury within the Commission. However, there should also be Council decisions, adopted by unanimity of the euro area Member States with the consent of the European Parliament, on the first establishment and subsequent periodic renewal of the eurobills scheme. Member States could provide, within their national constitutional systems, the degree of accountability through their national parliaments that they deem necessary for consenting to these establishment and renewal decisions.

The proposal for a debt redemption fund raises accountability issues of a distinct nature. To design a model ensuring appropriate accountability for a DRF would presuppose that its legal basis can be framed with great legal precision, as regards the maximum transferrable debt, the maximum time of operation and all other features, to guarantee the legal certainty required under national constitutional laws. If this could be ensured, then a new Treaty legal base might be imagined that would allow the setting up of the fund through a decision of the Council, adopted by unanimity of the euro area Member States with the consent of the

European Parliament, and subject to ratification by Member States under their constitutional requirements. That decision would set up the maximum volume, duration and precise conditions of participation in the fund. The Commission, accountable to the European Parliament, would then manage the fund in accordance with the precise rules set up by the Council decision.

ANNEX 1: The Convergence and Competitiveness Instrument

Steps towards a genuine EMU in the area of economic policy coordination should build on the current system while further reinforcing the process. National ownership of the reforms in this setup would be key, as well as a gradual increase in the intrusiveness of euro area-level guidance when Member States fail to take appropriate action. Larger spillover effects within the currency union call for such a more stringent process of economic policy coordination for euro area Member States. On the basis of the current Treaties, the legislator could therefore set up an integrated framework for the surveillance of economic policies consisting of two elements: 1) a mechanism for systematic ex ante coordination of all major reform projects of Member States in the context of the European Semester, envisaged in Article 11 of the TSCG. 2) A Convergence and Competitiveness Instrument (CCI) in the framework of the Macroeconomic Imbalances Procedure (MIP) based on contractual arrangements between Commission and euro area Member States coupled with the possibility of financial support.

This framework would complement the MIP and the existing framework for the surveillance of the budgetary situation of the Member States (the SGP). Its objective would be twofold: first it would reinforce the existing procedures in particular by strengthening ex ante coordination of major economic reforms; second, it would strengthen the dialogue with the euro area Member States to enhance national ownership through the introduction of contractual arrangements to be concluded between the Commission and Member States. It would be coupled by a dedicated system of financial support, representing the initial phase of the build-up of a fiscal capacity for the EMU. The contractual arrangements together with the financial support would be bundled into a CCI for theEMU.

The Commission will in forthcoming proposals set out the precise terms both for the mechanism for ex ante reform coordination and the CCI, which is based on contractual arrangements with financial support. The Commission proposals will also aim to streamline the existing procedures that have been created over the time (European Semester, National Reform Programmes, MIP etc.).

<u>*The envisaged process would develop as follows:*</u>

The innovations to the European Semester would consist of the introduction of a systematic ex ante coordination of major economic reforms; stronger dialogue with the Member States; the introduction of contractual arrangements to be agreed by the Commission and euro area Member States; and financial support attached to the implementation of the contractual arrangements.

1. The Commission publishes the AGS and a proposal for integrated guidelines: Broad Economic Policy Guidelines (BEPGs) and Employment Guidelines (EGs). These would set out the priorities and objectives (quantified or not) for the coming year both for the policies of the Member States and for the EU level. The EU-level measures could include concrete proposals where the co-legislators would need to act once agreed and launched. The European Parliament would be consulted (this is currently obligatory only for the EGs; a political agreement would be concluded to consult the EP on the whole guidelines package). In parallel, the Commission presents the Alert Mechanism Report, which identifies Member States that are considered to be affected by imbalances and which will then be subject to an in-depth review (to assess whether those imbalances exist and if so, whether they are excessive).

2. On the basis of this guidance, each euro area Member State submits a National Reform Programme, a single document containing proposals for policy measures central to improving its growth and competitiveness, and a Stability Programme which presents its fiscal plans for the medium term.

3. The Commission assesses the programmes and presents its evaluation in a series of Staff Working Documents which also highlight remaining challenges. These documents would be published earlier than currently to enable a dialogue on the analysis. In parallel, the Commission writes a horizontal appraisal of the proposed major economic reforms in the euro area countries. This horizontal document and its conclusions are discussed in the Euro Groupand the ECOFIN Council in view of systematically coordinating ex ante the major reform plans.

4. After this, the Commission comes forward with a proposal for country-specific recommendations (CSRs) setting out the specific policy measures agreed as well as the envisioned timeframe for implementation. In parallel, the Commission presents for the Member States with excessive imbalances a recommendation establishing the existence of such an excessive imbalance and recommending that the concerned Member States take corrective action. Thanks to the process of informal dialogue on the policy analysis, country-specific recommendations will be more detailed, policy-specific and time bound. The country-specific recommendations would focus on a small number of key elements related to growth and adjustment weaknesses in the Member State concerned. This increased focus and specificity could give a greater impetus to reform efforts in Member States.

5. After the adoption of the country-specific recommendations including the MIP recommendations by the Council, Member States under the preventive and corrective arm of the MIP submit (on a voluntary basis for the former and on a mandatory basis for the latter) a contractual arrangement proposal including specific policy action they

intend to implement and a timetable for those actions, based on the aforementioned recommendations. For Member States under the corrective arm of the MIP, the Corrective Action Plan would correspond to the contractual arrangements to be set up with the Commission. For Member States under the preventive arm of the MIP, the contractual arrangements would consist of an action plan similar to that required under the corrective arm.

For Member States under the corrective arm, the negotiation of the contractual arrangements corresponds to the approval of the Corrective Action Plan, so Articles 8 to 12 of Regulation 1176/2011 apply.

For Member States under the preventive arm, a similar procedure and deadlines should also apply, including on the monitoring and assessment of the implementation of the measures foreseen in the contractual arrangements. However, sanctions are not applicable.

Each year, the Member States would report on the progress in implementation of their contractual arrangements in their National Reform Programmes.

6. The contractual arrangements would be accompanied by financial support. They would be related to the CSRs emanating from the MIP, which focus on strengthening Member States' adjustment capacity and competitiveness, i.e. areas where reforms would lead to large positive spillover effects to other Member States and hence are necessary to ensure a smooth functioning of EMU.

The financial support would consist in a lump sum to be attributed per contractual arrangement, not earmarked to specific reforms. The definition and use of the amounts involved and of the disbursement (which can involve more than one tranche) will depend on the conditionality (measures/reforms to be implemented by the Member States) and should be also specified in the contractual arrangements.

In addition to the sanctions and underlying procedure applicable to Member States under the corrective arm (as envisaged by regulation 1174/2011), contractual arrangements could then be enforceable in that the Commission can issue warnings (by the use of 121.4 TFEU) if a Member State does not meet the contractual arrangements. These warnings, which the Commission can issue autonomously, could include a call for Member States to correct the deviation, including a timeline. When this is not met, the financial support can be withheld.

The financial support will be financed by a special fund/financial instrument, as mentioned in the main text. Euro area Member States will be required to contribute to that fund, based on a contribution key dependent on GNI.

When the Commission presents its proposal on reinforcing and streamlining the existing procedures, it will also address the risks of potential unintended consequences of introducing such financial support, such as moral hazard (e.g. rewarding relatively poor performers) and deadweight losses (reforms that would anyway have been implemented even without additional incentive).

ANNEX 2: External representation of the euro area

The progress that will be agreed on further integration will have to be reflected externally, notably through progress towards united external economic representation of the EU and of the euro area in particular. A strengthened voice of the Economic and Monetary Union is an integral part of the current efforts to improve the economic governance of the euro area.

One of the key lessons of the crisis is that, when faced with a global shock for which a collective response is needed, it is the size of the euro area that matters in influencing the type of policy responses that will be taken in international financial institutions and fora. Over the past few years, the Union, especially because of the euro, has become the natural counterpart of major economic powers when global growth, financial assistance or financial regulation are discussed. However, because of the current fragmentation of its representation in international financial institutions and fora, the euro area does not have an influence and leadership commensurate to its economic weight.

The efforts to strengthen the economic governance of the euro area need to be accompanied by a move towards a more unified and coherent external representation of the euro area in order to be fully effective. Such a step should mirror the significant strengthening taking place in the internal economic governance.

The external representation of the euro area[25] should be strengthened to allow it to play a more active role both in multilateral institutions and fora as well as in bilateral dialogues with strategic partners. This should result in delivering a single message on issues such as economic and fiscal policy, macroeconomic surveillance, exchange rate policies, and financial stability.

To achieve these objectives will require agreement on a roadmap aimed at streamlining and unifying the external representation of the euro area in international economic and financial organisations and fora.

The focus should be on the IMF, which through its lending instruments and surveillance is a key institutional pillar in global economic governance. At the moment, the 17 euro area Member States are spread across eight constituencies and chairs and have up to five Executive Directors. Currently, the presence of Union institutions in the IMF is very limited. The European Central Bank is an observer on the IMF Executive Board and the IMFC. The European Commission only has observer status at the IMFC.

Article 138 (2) TFEU foresees the adoption of appropriate measures to ensure unified representation within international financial institutions and conferences. The objective

[25] I.E., the EU representing the euro area Member States in accordance with the Treaties.

underlying this Treaty article was to achieve a stronger and unified representation of the Union for the euro area Member States in such institutions and conferences, given that the effectiveness of the current informal arrangements for representing the euro area was deemed unsatisfactory.[26]

It is necessary to step up the euro area coordination infrastructure in Brussels and in Washington. The euro area coordination process should be improved, and Member States should follow common messages on a compulsory basis. Constituencies should be rearranged so as to re-group countries into euro area constituencies for the IMF which could also include future euro area Member States. In parallel, an observer status in the IMF Executive Board should be sought for the euro area. This requires negotiations with the IMF. Euro area members share a single currency, a single monetary and exchange rate policy, and the management of members' external reserves by the European System of Central Banks. The recent changes in euro area governance have fundamentally changed the way fiscal and economic policies are coordinated at European level. In euro area matters, the European Commission has become a natural interlocutor of the IMF. In addition, more recently, the Commission and the ECB have worked closely together with the IMF in negotiating the financial assistance packages for euro area and EU Members and by collaborating in general with the Fund on surveillance. Against this background, conferring observer status on the euro area, represented by the European Commission with the European Central Bank being associated in the area of monetary policy, is essential to increase the synergies of the cooperation between the IMF and the institutions that are at the core of the daily management of the euro area.

To reach the longer-term aim of a single seat of the euro area in the IMF, one should envisage a gradual approach that would allow all actors involved to make the necessary institutional arrangements to accommodate a single euro area seat.

In terms of concrete steps forward, the European Commission:

- will submit a roadmap with steps for consolidating the euro area representation in the IMF over time into a single seat.
- will in due course make formal proposals under Article 138 (2) TFEU to establish a unified position to achieve an observer status of the euro area in the IMF for an observer status in the IMF executive board, and subsequently for a single seat.
- will put forward a proposal for improving the coordination amongst Member States on IMF issues related to EMU.

[26] See also Final Report of the European Convention's Working Group VI on Economic Governance, WG VI 17, 21.10.2002, p. 8. Cf. equally Final Report of Working Group VII on External Action, WG VII 17, 16.12.2002, pt. 66.

- Will consider making use of the possibilities under Art. 138 (1) TFEU to propose common positions on matters of particular interest for economic and monetary union within the competent international financial institutions and conferences.

- will foster further the representation of the euro area in the context of bilateral relations with major economic partners. The setting of the discussions with China on macroeconomic and exchange rate issues (which are dealt with by a euro area delegation[27]), could serve as a model.

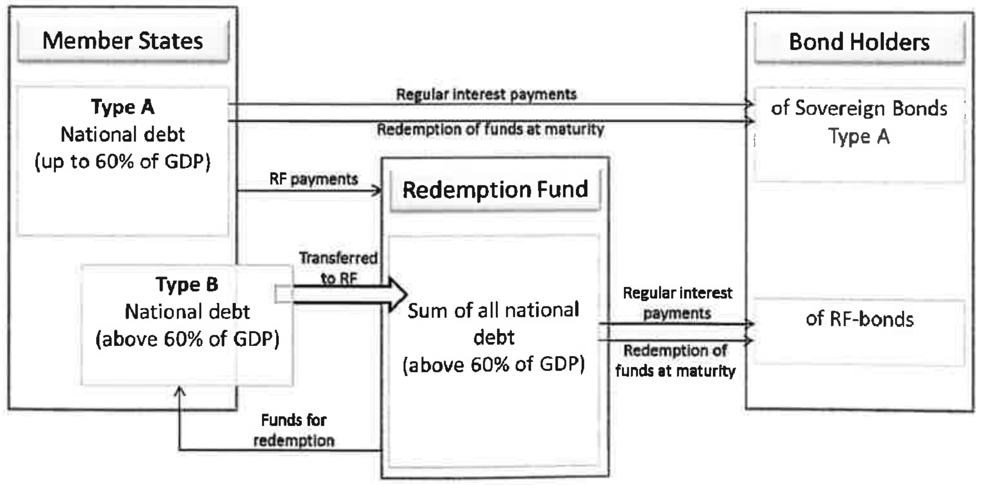
[27] This delegation is composed by the Commissioner for Economic and Monetary Affairs accompanied by the President of the Eurogroup and the president of the European Central Bank

ANNEX 3: A European Redemption Fund

The concept of the Redemption Fund (RF) was first presented in 2011 by the German Council of Economic Experts. The key idea of the RF is to provide a framework for bringing the euro area Member States' public debt to sustainable levels by lowering their overall financing costs in exchange for additional commitments to fiscal governance.

As a basic approach, the Member States' public debt would be divided into two parts: (1) one part is equivalent to 60% of GDP, which is the threshold stipulated by the Stability and Growth Pact; this part would remain each single Member State's responsibility; and (2) a part consisting of public debt above the 60% of GDP threshold, which would be transferred and pooled into a RF, and therefore be owned by the RF, though Member States would be obliged to autonomously redeem the transferred debt over a special period of time (e.g. 25 years). The RF would finance itself by issuing its own bonds, which would be serviced on a pooled basis by all participating Member States. In order to make these RF bonds attractive and marketable, investors would need sufficiently strong assurances about their credit quality. Therefore, the RF bonds would ideally be backed by a joint and several guarantee of all euro area Member States. The joint and several guarantees on RF bonds would result in a relatively low cost of financing for participating Member States thereby easing their overall debt-servicing burden. The repayment schedule for every Member State will have to be precisely specified and follow a transparent calculation key specifying the type of instalments (equal over time, or dependent on the economic situation, e.g. as a percentage of GDP, which would adapt the annual payments to the economic cycle). The scheme of this framework is depicted in Figure 1.

Figure 1: Scheme of the European Redemption Fund



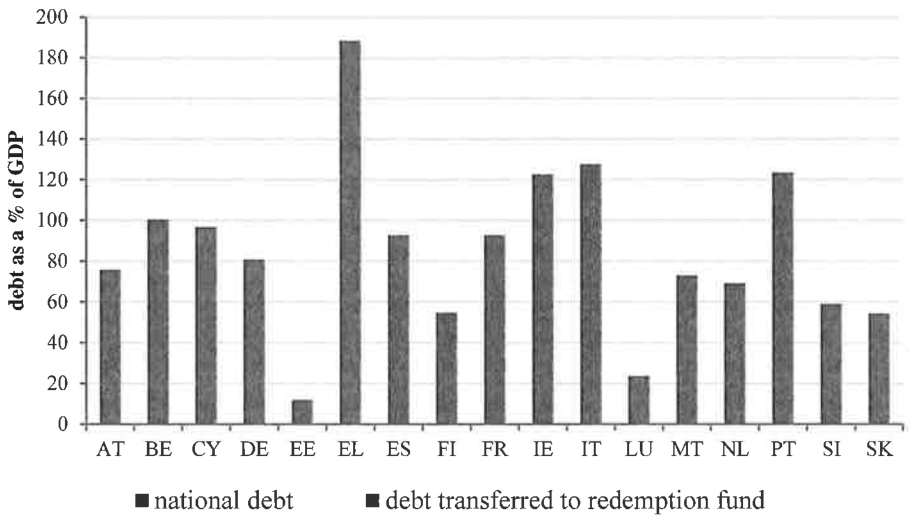
A problem of moral hazard is inherent to the RF approach, as the joint and several guarantee and ensuing lower financing costs for Member States could create unintended incentives for incurring further debt. This risk of moral hazard would need to be addressed by additional commitments by Member States in the area of economic governance. As a pre-condition for participating in the RF, a path for budgetary consolidation and structural reform would be laid down for each Member State, which would oblige the Member State to redeem autonomously the transferred debt over a certain period. Consolidation and reform agreements are a crucial condition of credibility and could include: (i) earmarking of tax revenue specifically for payment obligations to the redemption fund, (ii) depositing collateral,

(iii) mandatory commitment to previously agreed structural reforms and consolidation measures. In case of non-compliance, the transfer of national debt to the redemption fund could be immediately stopped.

From a practical point of view, the redemptions of maturing debt and new financing needs of participating Member States would be financed with the money received from the sale of RF bonds[28] until the transferred liabilities reach the agreed amounts. A clear and strict legal framework/contract governing this transfer of debt would be required, which would regulate in particular: (i) the maximum amounts to be transferred[29], (ii) the repayment scheme, as well as (iii) the seniority of bonds issued by the RF over national bonds.

As a result of the transfer to the RF, a country's total debt would be divided into two parts - national debt and bonds issued by the RF[30] (see Figure 2).

Figure 2: Member States' debt structure under a Redemption Fund scheme



Source: European Commission Autumn 2012 forecast, debt figures forecast for 2013

The establishment of a RF would pose several challenges. Firstly, although the entire euro area would benefit from a decline of sovereign and systemic risk due to reduction of overall debt levels and particularly debt levels in more vulnerable countries, high-credit quality Member States would seem to benefit relatively less from the Fund. Therefore, incentives for participation by these Member States would need to be created. Secondly, as excessive debt would be covered by joint and several guarantees it would be converted into a relatively low-risk asset. Hence, the market-disciplining effect would be substantially weakened. In fact, the disciplining task would be transferred entirely to the co-guarantors. Thirdly, the RF is intended as a way of bringing the debt levels down and Member States should not have incentives to prolong unnecessarily the participation in the RF only to benefit from lower financing costs. Finally, from a market perspective, a limited duration of the scheme would

[28] The management of the RF would be entrusted to a dedicated institution to be established under the Treaty, i.e. a European Debt Management entity within the Commission, accountable to the European Parliament.
[29] The contract should also specify clearly that the agreed amounts to be transferred are not expandable.
[30] The overall size of the RF could reach EUR 3 trillion. Calculation done on the basis of the European Commission Autumn 2012 forecast.

reduce market liquidity towards the end of the scheme. This would put in question the role and use of the commonly issued bonds as a benchmark and also the likelihood of establishing proper derivative markets. After the expiry of the common issuance, the euro area government bond market would be as little integrated as now and none of the potential benefits of common issuance would be achieved.

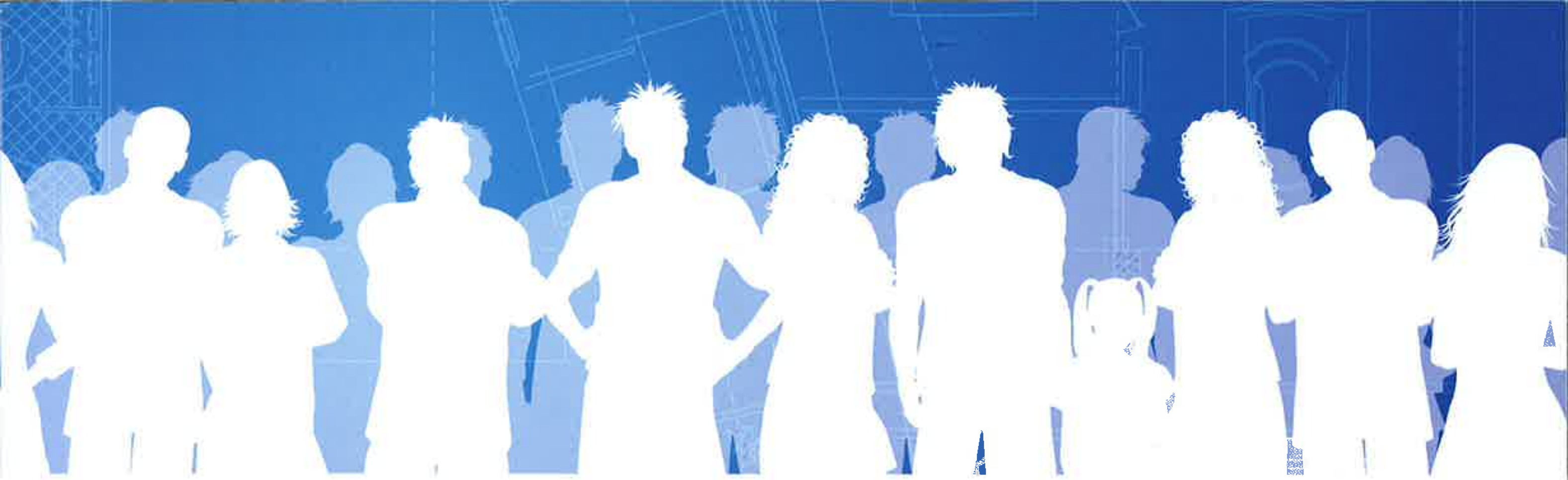
European Commission

Blu€print for a deep and genuine EMU:

Debating the future economic, monetary, banking and political union

Speakers

Brussels 7 May 2013



José Manuel BARROSO

In 1980 José Manuel Barroso joined the Social Democratic Party (PSD). He was named President of the party in 1999 and re-elected three times. During the same period, he served as Vice-President of the European People's Party. As State Secretary for Foreign Affairs and Cooperation he played a key role as mediator in the signing of the peace accords for Angola in 1991, and as Minister for Foreign Affairs he was a driving force in the self-determination process in East Timor between 1992 and 1995. Under his leadership, the PSD won the general election in 2002 and he was appointed Prime Minister of Portugal in April of that year.

In July 2004 he was nominated by the European Council and elected by the European Parliament to the post of President of the European Commission. In June 2009 the European Council unanimously nominated him for a second mandate, and he was re-elected to the post of President of the European Commission by an absolute majority in the European Parliament in September 2009.

Jean-Claude THEBAULT

In 1984 Jean-Claude Thébault entered the European Commission as an Administrator and then became Principal Administrator in charge of agricultural spending in the Directorate General for Financial Control. In 1988 he helped to create the European Antifraud Office (now OLAF), before becoming Head of the "Common Agricultural Policy" unit of DG Budget. From 1995 to 2000 he was Deputy Head of Yves-Thibault de Silguy's Cabinet, European Commissioner for Economic and Financial Affairs. In 2000 he was nominated Director of the Forward Studies Unit directly linked to the President of the Commission (now known as BEPA). In June 2000 he became Director of Financial Institutions at DG Internal Market.

In 2004 he became Principal Advisor in the Cabinet of European Commission President José Manuel Barroso, and was nominated Deputy Head of Cabinet in 2006. In 2009 he was nominated Deputy Secretary-General of the European Commission's Secretariat-General. Since May 2010, he has been Head and Director General of the Bureau of European Policy Advisers of the European Commission (BEPA).

Stephen FIDLER

Stephen Fidler has been Brussels Editor of The Wall Street Journal and Dow Jones Newswires since October 2009, running a bureau of 11 journalists, leading coverage of the European Union and the euro-zone debt crisis, and writing a weekly column and other articles.

Before joining the Journal, he spent more than 20 years with the Financial Times in senior roles, including international capital markets editor, Latin America Editor, defence and security editor, and U.S. diplomatic editor based in Washington DC.

He spent almost a decade as a correspondent for Reuters in London, New York and the Middle East. He holds a degree in economics from London University, and was formerly a senior consulting fellow for the International Institute of Strategic Studies.

Olli REHN

Olli Rehn joined the current college of Commissioners in February 2010 as European Commissioner for Economic and Monetary Affairs, and in October 2011 he was appointed Vice-President of the Commission responsible for Economic and Monetary Affairs and the Euro. Before that he served as Commissioner for Enlargement (November 2004 – February 2010) and Commissioner for Enterprise and Information Society (July - November 2004). He was the Head of Cabinet of Commissioner Erkki Liikanen between 1998 and 2002. In 2002-2003 Olli Rehn worked as Professor at the Department of Political Science, University of Helsinki. He was a member of the Finnish Parliament from 1991 until 1995, when he also chaired the Finnish delegation to the Council of Europe. He was a member of the European Parliament in 1995-96. He was deputy chairman of the Centre Party in 1988-94 and chairman of the Centre Youth in 1987-89. Olli Rehn has a D.Phil. in international political economy from Oxford University (1996) and MA in political science from the University of Helsinki (1989). In 1982-1983 he studied economics, international relations and journalism at Macalester College in Saint Paul, Minnesota.

Jeroen DIJSSELBLOEM

Mr Dijsselbloem has a degree in agricultural economics from Wageningen University. In 1992, he worked as an assistant to the Dutch Labour Party (PvdA) MEPs in Brussels and in 1993 joined the staff of the parliamentary PvdA in the Hague. He was a member of the Wageningen municipal council between 1994-97. In 1996, he became a political-administrative adviser to the Minister of Agriculture, Nature Management and Fisheries. Between 1998 and 2000, he was Deputy Head of the ministry's advisory section. He was elected to the House of Representatives in 2000 and became a Minister in 2002. He was party spokesperson on educational matters. He became the Deputy Leader of the PvdA parliamentary party in 2008 and was a member of the party's election programme committee in 2010 and 2012. In November 2012, Mr Dijsselbloem was appointed Minister of Finance in the Rutte-Asscher Government. In January 2013, he was appointed President of the Eurogroup and in February 2013, the Board of Governors of the European Stability Mechanism (ESM) elected him as Chairman.

Vitor GASPAR

Vítor Gaspar holds a PhD in Economics from Universidade Nova de Lisboa. He was Head of the Bureau of European Policy Advisers of the European Commission from January 2007 to February 2010. From September 1998 to December 2004 he was Director-General for Research at the European Central Bank. From October 1994 to September 1998 he was Director of the Research Department at Banco de Portugal. From January 1993 to October 1994 he was Advisor to the Board at Banco de Portugal. From 1989 to 1992 he was Director of the Economic Studies at the Ministry of Finance. Throughout his career, he has been associated with European integration. He was alternate member of the Monetary Committee from 1989 to 1998 and representative of the Finance Minister in the Inter-Governmental Conference leading to the Maastricht Treaty. He has published several books and articles in economic journals.

Peter SPIEGEL

Peter Spiegel is the Brussels bureau chief for the Financial Times, overseeing the London-based newspaper's coverage of the European economic crisis and Europe's role in global affairs. In 2012 and 2013, Peter and his team received annual Society of American Business Writers and Editors awards for their coverage of the eurozone debt crisis. Peter returned to the FT in August 2010 after spending nearly five years in Washington covering national security issues for the Los Angeles Times and the Wall Street Journal. In both jobs, Peter's coverage focused on the wars in Iraq and Afghanistan, travelling frequently to both war zones. While at the Los Angeles Times, he was co-winner of the newspaper's top internal journalism award, the 2008 Editor's Prize, for his coverage of the Bush administration's surge in Iraq.

Marco BUTI

Marco Buti has been Director-General for Economic and Financial Affairs at the European Commission since December 2008, after a 6-month period as acting Director-General. After studies at the Universities of Florence and Oxford, Mr Buti joined the European Commission in 1987. He held various posts as an economist in DG ECFIN and the Commissioner's private office before taking up a post as an economic adviser to the Commission President in 2002-03. In 2003 he returned to DG ECFIN as Director for the Directorate for economies of the Member States, and in September 2006 was appointed Deputy Director-General. Mr Buti has been a visiting professor at the Université Libre de Bruxelles, the University of Florence and the European University Institute, and has published extensively on Economic and Monetary Union, macroeconomic policies, welfare state reforms, and European unemployment.

Sharon BOWLES

Sharon Bowles has a scientific and mathematical background having completed her doctorate at Oxford University. She later trained and worked as a Chartered and European Patent Attorney setting up her own practice in 1981. Sharon has been active in politics since the mid-1980s. She became a member of the European Parliament for UK South East region in May 2005 and was re-elected in June 2009. Sharon has been a full member of the Economic and Monetary Affairs Committee (ECON) since her arrival as an MEP and was elected as Chairwoman in July 2009. Sharon has also been a substitute member of the Legal Affairs committee since January 2007. During the previous mandate, Sharon´s work focused on Payment Services, Solvency II, Capital Requirements, Deposit Guarantees and Level 3 Committee funding, and on the reports on Hedge Funds and Private Equity, and Transparency of Institutional Investors.
She was also rapporteur for the report on tax fraud, and for the setting up of the Statistical Governance Advisory Board. As Chair of ECON, Sharon presides over each Committee meeting, as well as the trilogue negotiations between Parliament, Council and the Commission, and she is currently the ALDE group´s shadow rapporteur on CRD4 (Capital Requirements Directive), CSDR (Central Securities Depositories), PRIPs (retail investment), state aid procedural regulation, and the forthcoming Securities Law Directive

Dariusz ROSATI

A specialist in the field of macroeconomic policy, European integration, finance and international trade. Since 1990 titular professor in Warsaw School of Economics. In 1986-1987, he was a visiting professor at Princeton University. Founder (1985) and the first director of the Institute of World Economy at the Warsaw School of Economics. Between 1988-1991, he was the Director of the Institute of Business Cycles and Foreign Trade. From 1989-1993, a partner at consulting TKD - Ernst & Young Poland. Between 1991-1995, he worked at the United Nations Economic Commission for Europe in Geneva as head of the countries of Central and Eastern Europe. From December 1995 to October 1997, he served as Minister of Foreign Affairs. Between 1998-2004, he was a member of the Monetary Policy Council. From 2004-2009 he was a Member of the European Parliament. In 2011 elected as a Member of Parliament, since 2011 he is the Chairman of the Public Finance Committee of the Sejm.

Jorge SICILIA

Jorge Sicilia is Chief Economist of BBVA Group and Director of BBVAResearch. He leads a global team of economists distributed around Europe, US, Mexico, South America and Asia devoted to economic, financial and regulatory analysis. Prior to this, Jorge Sicilia was BBVA's Chief Economist for North America supervising the teams conducting economic analysis on the US and México, Principal Economist in the Monetary Policy Stance Division at the European Central Bank (ECB) in Frankfurt, Monetary and Financial Markets' Chief Economist at BBVA in Madrid, Head of the Department of Economic and Monetary Studies in Argentina, Head of Economic and Market Analysis in Analistas Financieros Internacionales (AFI) and Economist in the Economic Studies Department of the Spanish Antitrust Committee. He has given lectures on macroeconomics, financial markets and financial systems at CUNEF and Carlos III Universities in Madrid, as well as at post-graduate institutions, academic conferences, and central banks fora. He obtained the Degree in Quantitative Economics at Universidad Complutense de Madrid in 1992, and an MsC in Economics and Finance at CEMFI in 1994. He is author of several economic and financial papers published in specialized magazines, a member of BBVA Bancomer´s foundation, the Financial Studies Foundation at the ITAM and a member of the Private Creditor-Investor Committee for Greece.

Holger SCHMIEDING

Dr Holger Schmieding is Chief Economist at Berenberg Bank in London.
Before joining Germany's oldest private bank in October 2010, he worked as chief Economist Europe at Merrill Lynch, Bank of America and at Bank of America-Merrill Lynch in London.
Having studied economics in Munich, London and Kiel, he holds a doctorate from the University of Kiel.
Before taking up his first role as financial market economist in 1993, he also worked as a journalist at "Westfälische Nachrichten" in Germany, as head of a research group on east-central Europe at the Kiel Institute of World Economics and as a desk economist at the International Monetary Fund in Washington, DC.

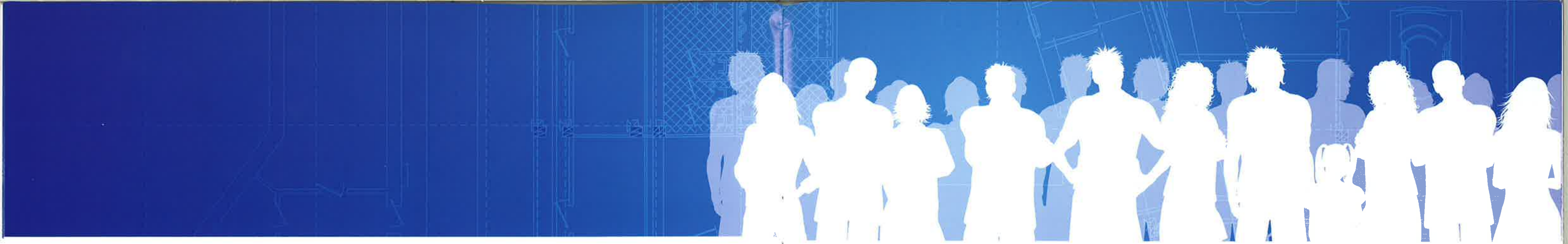
Caroline de GRUYTER

Caroline de Gruyter is the Brussels correspondent for the leading Dutch newspaper NRC Handelsblad. She is mainly following the financial and political aspects of the crisis in Europe. She was previously based in the Gaza strip (1994-1996), Jerusalem (1996-1999), Brussels (1999-2004), and Geneva (2004-2008).

In the early nineties de Gruyter won the Dutch Golden Pen Award ('Het Gouden Pennetje') for a series of articles on the war in the former Yugoslavia. She is the author of two books. In 1997 she wrote 'The Coffee House of Mohammed Skaik; Impressions from a Toy State Gaza'. In 2006, her book 'The Europeans; Living and Working in the Capital of Europe' was published, which was nominated and shortlisted for the M.J. Brusse Award 2008.

Olivier GUERSENT

Graduated with distinction from the "Institut d'études Politiques de Bordeaux" in 1983. After 8 years in the French Civil Service, Olivier Guersent joined the European Commission in 1992. Olivier Guersent took over the Commission's fight against cartels as Director in the Directorate General Competition of the European Commission (DG Competition) in April 2009. For the previous two years (2007-2008), he had served successively as Head of Merger Unit and Acting Director for "Transport & Other services" (since September 2007) also in DG Competition. Prior to this, he was Deputy Head of Cabinet of Competition to Commissioner Neelie Kroes (Nov 2004 Dec 2006). Previous positions include: Head of the "Decision Scrutiny and Enforcement Priorities" Unit (Nov 2002-Nov 2004) and Deputy Head of the Cartel Unit, (May 2001-Oct 2002) both in DG Competition. He had previously been Advisor to Commissioner Michel Barnier (Sept 1999 –May 2001) and Advisor to Commissioner Karel Van Miert (Oct 1996 – Sept 1999). His academic activities include frequent lectures in postgraduate studies in several French universities. Olivier Guersent is an active Board Member of the non-profit organisation "Aremis" that provides home medical care as a substitute for hospitalisation for heavy pathologies (Cancer, AIDS, Degenerative Genetic Diseases, etc) in the Brussels area.



Marianne THYSSEN

Marianne Thyssen has a Law degree, from the Catholic University of Leuven (KUL), 1979. She was Assistant lecturer in the faculty of law, Catholic University of Leuven (1979-1980). Head of a research department and Secretary-General at UNIZO (organisation for the self-employed and SMEs) (1988-1991). Party president of CD&V, the Flemish Christian Democrats (2008-2010). Member of the European Parliament (since 1991). Leader of the Belgian delegation in the EPP Group (since 1999). First Vice-Chairwoman of the EPP Group (2004-2009). Member of the Committee on Economic and Monetary Affairs in the European Parliament. Substitute Member of the Committee on the Environment, Public Health and Food Safety in the European Parliament. Rapporteur on the report of the Presidents of the European Council, the European Commission, the European Central Bank and the Eurogroup "Towards a genuine Economic and Monetary Union". Rapporteur on the proposal for a Single Supervisory Mechanism for credit institutions.

Kai Jan KRAINER

Kai Jan Krainer has been a Member of the Austrian National Council (Nationalrat) since 2002. Since 2007, he has been Spokesperson for Financial and Budget Affairs coordinating the Social Democratic Party's agenda concerning finance and budget policies in the Nationalrat. In the recent legislative period, this included working towards a growth-friendly fiscal consolidation of the Austrian budget as well as promoting legislation towards banking regulation and oversight. He is known for advocating employment and an integrated framework for banking regulation in the European Union. For Kai Jan Krainer, this means one regulation, one supervision, one deposit insurance scheme and one resolution scheme.

Andrea ENRIA

Mr Andrea Enria took office as the first Chairman of the European Banking Authority on 1 March 2011. Before that date he was the Head of the Regulation and Supervisory Policy Department at the Bank of Italy. He previously served as Secretary General of CEBS, dealing with technical aspects of EU banking legislation, supervisory convergence and cooperation within the EU. In the past, he also held the position of Head of Financial Supervision Division at the European Central Bank. Before joining the ECB he worked for several years in the Research Department and in the Supervisory Department of the Bank of Italy. Mr Enria has a BA in Economics from Bocconi University and an M. Phil. in Economics from Cambridge University.

Yves MERSCH

Yves Mersch is a member of the Executive Board of the European Central Bank (ECB). His eight-year term started on 15 December 2012. He was Governor of the Banque centrale du Luxembourg from 1 June 1998 to 14 December 2012. He has been a member of the Governing Council and the General Council of the ECB since its creation in 1998. He is the longest-serving founding member of the General Council. After obtaining post-graduate degrees in international public law and political science, Mersch started his career at the Luxembourg Ministry of Finance in 1975. Before joining the Permanent Representation of Luxembourg to the United Nations in New York in 1980, he was seconded to the International Monetary Fund in Washington. Upon his return to Luxembourg in 1981, he worked at the Ministry of Finance. From 1985 to 1989 he was Government Commissioner in charge of oversight of the Luxembourg stock market. Between 1983 and 1999 he was a member of the Council of the Luxembourg Monetary Institute, Luxembourg's banking supervisory authority. As Personal Representative of the Minister of Finance, Mersch contributed to the design of the Maastricht Treaty. Born in Luxembourg on 1 October 1949, Yves Mersch is married with two children.

Brigid LAFFAN

Brigid Laffan is Professor of European Politics in the School of Politics and International Relations (SPIRe), University College Dublin (UCD). She was Vice-President of UCD and Principal of the College of Human Sciences from 2004 to 2011. She is a member of the Advisory Council of the Robert Schuman Centre for Advanced Studies, the Fulbright Commission and is the 2013 Visiting Scientist for the EXACT Marie Curie Network. In March 2004, she was elected as a member of the Royal Irish Academy and in 1999 she was the founding director of the Dublin European Institute UCD. In December 2012, Professor Laffan was awarded the THESEUS Award for outstanding research on European Integration. She has published widely on European Integration including Ireland and the European Union (2008), Renovation or Revolution: new territorial politics in Ireland and the United Kingdom, (2005), Europe's Experimental Union. Re thinking Integration (1999) and The Finances of the Union (1997).

Johannes LAITENBERGER

A lawyer by training, he started in the General Secretariat of the Council of the European Union on 1996 and joined the European Commission in 1999, starting as a case-handler in the Directorate-General for Competition. When the Prodi Commission took office later that year, he was appointed to the cabinet of Ms Viviane Reding, member of the Commission responsible for education, culture, audiovisual, youth and sports. He became Head of Cabinet in 2003 and served in this capacity until the end of the mandate in the autumn of 2004. In November 2004, he became a member of the Cabinet of President J. M. Barroso. He was appointed as the Head of the Commission's Spokesperson's Service and Spokesman of the Commission by President J.M. Barroso with effect from 21st November 2005, and served in this capacity until 31st October 2009. He was appointed head of the cabinet of the President J.M. Barroso with effect from 1st November 2009.

Roberto GUALITIERI

Roberto Gualtieri graduated in literature and philosophy. He has a research doctorate (PhD) in contemporary history. He is currently an Associate Professor in Contemporary History, at 'La Sapienza' University, Rome and is the Deputy Director of the Gramsci Institute Foundation.

At the European Parliament, he is the Progressive Alliance of Socialists and Democrats (S&D) Group coordinator on the Committee of Constitutional Affairs. He has been a member of the European Parliament negotiating team for the setting-up of the EEAS (2010) and the Fiscal Compact (2011) and he is currently a member of the Van Rompuy working group for a genuine EMU.

Rait MARUSTE

Date and place of birth: 27 September 1953, Pärnu, Estonia
Marital status: married, one son and one daughter
Education: Leningrad State University, Candidate of Juridical Science 1984; Tartu State University, law 1977; Pärnu-Jaagupi Secondary School 1972
Career: XII Riigikogu 2011–; Judge of the European Court of Human Rights 1998–2010; Chief Justice of the Supreme Court 1992–1998; University of Tartu, lecturer 1977–1991, Associate Professor 1986–1991
Party affiliation: Reform Party 2010–
Membership in representative bodies: XII Riigikogu
Social activities: Estonian Academic Law Society; Tartu Rotary Club; Pärnu Yacht Club; "Acta Societatis Martensis", Editor-in-Chief
Creative activities: published specialist articles; book "Konstitutsionalism ning põhiõiguste ja -vabaduste kaitse" (Constitutionalism and Protection of Fundamental Rights and Freedoms) 2004
Awards: 2nd class Order of the White Star 1999
Hobbies: skiing, golf, sailing

Miguel Poiares MADURO

Miguel Poiares Maduro was born in 1967. He is Director of the Global Governance Program and Professor of Law at the European University Institute in Florence, Italy. He is also Visiting Professor at the Faculty of Law at Yale University in the United States of America. Advocate-General at the European Court of Justice in Luxembourg from 2003 to 2009. Having been Fulbright Visiting Research Scholar at Faculty of Law at Harvard University, USA. Doctor in Law by the European University Institute, he won the Purpose Prize Europe for the best PhD thesis of that year. Lecturer at numerous institutions, including: College of Europe, Catholic University of Lisbon, New University of Lisbon, London School of Economics, University of Chicago Law School, Centre for Political and Constitutional Studies of Spain, Ortega y Gasset Institute in Madrid, and Institute of European Studies of Macau. In 2010 he was awarded the prestigious Gulbenkian Prize for Science. Previously he was made Commander of the Order of Santiago da Espada by the President of the Portuguese Republic for literary, scientific and artistic merit (2006). He was the first person to be awarded the Rowe and Maw Prize at the European University Institute. His extensive published works include: "We the Court - The European Court of Justice and the European Economic Constitution", "The past and Future of EU Law" and "The Plural Constitution - Constitutionalism and the European Union". He was Law consultant in several cases of international significance and joined the High Level Group of the European Commission on Media Pluralism and Freedom of Information. He was a member of the Political Committee of Aníbal Cavaco Silva's candidacy in the 2011 presidential elections. He was appointed to his new post in the Government of Portugal on 11 April 2013.

Pierre KROLL

He is 'The unavoidable caricaturist in Belgium'. Every Belgian newspaper and magazine has published his work. Today, he is the regular cartoonist of the daily Le Soir and the weekly Cinétélérevue, and is also featured in many other publications.

Pierre Kroll also has a busy career in television, particularly at the French speaking national channel in Belgium, where he has been a fixture since 1985. His speciality is the creation of relevant illustrations during live debates of delicate political and social issues. He has also been a commentary writer, illustrator and even co-presenter of many other programmes.

Since 1995, he has published at least one album of his best drawings per year, which are bestsellers in all categories in Belgium.

Pierre Kroll is a member of « Cartooning for Peace », the project created by Jean Plantu of the French newspaper Le Monde and sponsored by the United Nations.

European Commission

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Par Margaritis Schinas

2013 : le temps des architectes

Depuis le déclenchement de la crise économique et financière de 2008, les autorités européennes – nationales et communautaires – ont dû donner la priorité à leur rôle de pompier, en vue de combattre les ravages occasionnés par le déclenchement puis la propagation de cette crise. Parce que tous les moyens y ont été consacrés, l'objectif d'éteindre l'incendie est aujourd'hui atteint, ou peu s'en faut, et tant l'euro que l'Europe sortent renforcés de cette épreuve.

Surtout, les leçons de l'Histoire ont été tirées, ainsi qu'en attestent pour l'immédiat l'entrée en vigueur du pacte budgétaire européen et du mécanisme européen de stabilité, et pour le moyen terme le rapport « Pour une véritable union économique et monétaire », présenté en juin 2012 par les présidents du Conseil, de la Commission, de l'Eurogroupe et de la Banque centrale européenne.

En ce début d'année 2013, les conditions semblent réunies pour que le temps des pompiers étant presque achevé, s'ouvre maintenant le temps des architectes et que la priorité des dirigeants européens soit désormais de concevoir – puis de bâtir – une véritable union économique et monétaire, qui aille encore au-delà de ce qui a déjà été obtenu et mis en œuvre au cours des quatre dernières années.

C'est à cet objectif que répond le Blueprint élaboré par la Commission, première contribution écrite à proposer une approche intégrée et exhaustive de ce que pourrait – et devrait – être une véritable union économique et monétaire, dans toutes ses composantes – économique, législative et politique.

C'est à ce sujet, majeur pour l'avenir de l'Union européenne, qu'est consacré le premier numéro de l'année du *BEPA Monthly*.

L'avenir de l'Europe n'est pas pour autant dans la seule préoccupation de soi. Du fait de son histoire et du rôle spécifique qu'elle entend jouer dans le concert des nations, l'UE continuera à s'impliquer dans les affaires du monde; 2013 lui donnera de nombreuses occasions de se rappeler cette nécessité, qu'il s'agisse des questions de sécurité sur le continent africain ou des perspectives d'un accord transatlantique de commerce.

L'année 2013 se promet pleine d'opportunités et de défis européens à relever. La Commission sera au rendez-vous.

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BUREAU OF EUROPEAN POLICY ADVISERS
EUROPEAN COMMISSION

1 Moving forward on a deep and genuine EMU

*By Marco Buti**

The Commission's Blueprint presents a comprehensive vision for a deep and genuine EMU conducive to a strong and stable architecture in the financial, fiscal, economic, and political domains. It recalls the *raison d'être* and aspirations of the EMU, presents a diagnostic of the crisis of confidence in the euro area (EA), and identifies the rationale and objectives of a genuine EMU. It aims to rectify the shortcomings of EMU's original set up by proposing necessary short-, medium- and long-term actions for lasting stability and prosperity of EMU.

The Blueprint is the first document to provide a comprehensive, coherent, and concrete design for how EMU should develop. While focusing on economic necessities, it is fully aligned to the legal requirements and political context. Thus, it offers an ambitious, realistic and pragmatic basis for a serious debate and for tackling the crisis of confidence in the EA.

Why a Blueprint

The EU responded to the sovereign debt crisis with the five-point roadmap in autumn 2011. In parallel it tackled the challenges of vulnerable countries; strengthened the banking system; aimed to enhance the growth outlook through structural reforms; put financial firewalls on a permanent and more flexible footing; and set down a robust and integrated economic governance framework. Actions taken since the 2008 financial crisis amount to a significant EMU overhaul, including strengthening economic governance through the European Semester and six-pack legislation, and creating a flexible and permanent financial firewall.

For measures to have a positive impact on confidence, they will need to be seen working well for some time. That is why it has not been possible to prevent the sovereign debt crises from turning into a crisis of confidence that threatens the integrity of the euro area itself. A more important factor is the gap between the sharp acceleration of financial integration under EMU and the comparatively slow progress in the integration of EU-level financial regulation and supervision. The emergence of negative feedback loops between weaknesses in the financial sector, sovereign debt sustainability, and the growth outlook aggravated the sovereign debt crisis and led to a full-blown crisis of confidence, challenging the cohesion and very existence of the EA.

The June 2012 European Council decision to envisage directly recapitalising troubled banks through the ESM on condition that an effective single supervisory mechanism (SSM) is in place, and EU finance ministers' agreement on the SSM in December, were major steps towards breaking the negative feedback loop between banks and sovereigns. The ECB announcement to introduce Open Market Transactions to counter market speculation on re-denomination risk and to intervene in secondary sovereign bond markets of member states complying with ESM conditionality also contributed to stabilising the situation since the autumn. Yield spread developments clearly indicate that the strategy has started to work in terms of increased financial market stability.

A consensus existed already in June that the EU needed to move from temporary solutions to a stable overall architecture of integrated financial, budgetary, and economic frameworks and a commensurate evolution in democratic accountability and legitimacy.

Blueprint proposals

The crisis has clearly demonstrated the increased interdependence of our economies since the foundation of EMU and has shown that success or failure of EMU will impact on all. The threat of the crisis of confidence is however more fundamental and requires a more fundamental response to convince that achievements in the Single Market and currency will not be undone, and that unfulfilled achievements of citizens and business will be realised and be maintained. We also need to be better equipped for the future to avoid the mistakes of the past.

To be effective and credible, the response must chart a clear and realistic path towards that ultimate ambition based on the firm commitment of the EU institutions and its member states. The resulting vision must encompass a banking union that can end the disintegration of the EU's financial market and ensure reasonably equal financing conditions for households and business across the EU; sever the negative feedback loops between member states and banks; and ensure that divergences between the business cycles across the euro area are not artificially amplified. The economic and fiscal union will deal with macroeconomic imbalances in the EA and provide the cushion for future shocks. Due to the inevitable transfers of sovereignty, such measures would require underpinning sufficient democratic accountability.

The transformation of EMU cannot be completed overnight, particularly considering the significant additional transfer of political powers from national to European level. To arrive at an EMU that ensures its citizens' welfare, decisive steps must be launched in the short-term (in the next 6-18 months) that will be built on and followed up with steps in the medium- and long-term.

The way forward needs to be carefully balanced. Steps towards more responsibility and economic discipline should be combined with more solidarity and financial support. This balance must be struck in parallel and in each phase of EMU development. Commensurate political integration, ensuring democratic legitimacy and accountability must accompany deeper integration of financial regulation, fiscal and economic policy and corresponding instruments. The Blueprint's chosen gradual approach reflects the fact that actions requiring Treaty change will not be possible in the short term and that more ambitious objectives can only be reached once the foundations are laid down and tested. The Blueprint envisages Treaty change only where absolutely necessary but favours action that can be implemented *à traité constant*.

In the short-term (in the next 6-18 months), the Blueprint suggests prioritising the full deployment of the new economic governance tools under the six-pack and two -pack regulations and the Single Supervisory Mechanism in the banking field. Proposals will also be made for a Single Resolution Mechanism (SRM) which will be in charge of the restructuring and resolution of banks of the member states participating in the Banking Union. The Blueprint also proposes the creation of a common financial instrument through which economic reform plans agreed in advance between member states and the Commission can be supported. Unifying the external representation of the euro area is also envisaged as part of the short-term dimension.

In the medium-term (18 months to five years), the Blueprint suggests closer economic and budgetary policy integration, including greater control over national budgetary policies – notably developing a dedicated fiscal capacity for the euro area, establishing a debt redemption fund, and commonly issuing eurobills.

In the longer term (beyond five years), a full Banking Union comprising supervision, resolution, and deposit guarantee insurance should be completed, and a common fiscal capacity could develop to help stabilise and smooth the adverse impact of asymmetric shocks in the EA. A deeply integrated economic and fiscal governance framework

* *Marco Buti is the Director-General of the DG for Economic and Financial Affairs.*

could ultimately allow the common issuance of public debt, which would enhance the functioning of debt markets and facilitate the conduct of monetary policy.

Looking ahead

With its Blueprint, the Commission sought to spark a European debate on a comprehensive, coherent, and concrete design for a deep and genuine EMU. This document is also a blueprint for concrete short-term action and should facilitate the adoption of the two-pack legislation. The Commission announced legislative proposals for 2013 on the creation of a Single Resolution Mechanism, a 'competitiveness and convergence instrument', and *ex-ante* coordination of major reforms. The European Commission will also work towards a single seat for the euro area on the IMF executive board.

The December 2012 European Council was not the occasion for agreement on specific proposals but provided a valuable opportunity to develop a common political vision and plan for short-, medium- and longer-term steps. The Conclusions refer to numerous Blueprint proposals for the immediate term, such as *ex ante* coordination of major national reforms; contractual arrangements between the member states and the EU institutions; and – linked to this – solidarity mechanisms at EU level to support the implementation of reforms.

The Blueprint's medium- and longer-term ideas remain on the table for the debate that will have to take place before significant changes to the Treaties can be envisaged. The Commission will identify – ahead of the next European Parliament electoral campaign – areas of possible Treaty change.

			A blueprint for a deep and genuine EMU Launching a European debate	Secondary law	Treaty change
ALL ALONG THE PROCESS	SHORT TERM	Within the next 18 months	1. Full implementation of **European Semester** and **six-pack** and quick agreement on and implementation of **two-pack**	✓	
			2. **Banking Union:** Financial regulation and supervision: quick agreement on proposals for a **Single Rulebook** and **Single Supervisory Mechanism**	✓	
			3. **Banking Union: Single Resolution Mechanism**	✓	
			4. Quick decision on the next **Multi-annual Financial Framework**	✓	
			5. **Ex-ante coordination of major reforms** and the creation of a **Convergence and Competitiveness Instrument (CCI)**	✓	
			6. Promoting **investment** in the **Euro Area** in line with the Stability and Growth Pact	✓	
			7. **External representation** of the **Euro Area**	✓	
	MEDIUM TERM	18 months to 5 years	1. **Further reinforcement of budgetary and economic integration**	✓	✓
			2. **Proper fiscal capacity** for the **Euro Area** building on the CCI	✓	✓
			3. **Redemption fund**		✓
			4. **Eurobills**		✓
	LONGER TERM	Beyond 5 years	1. **Full Banking Union**		✓
			2. **Full fiscal and economic union**		✓
			Political union: Commensurate progress on democratic legitimacy and accountability	✓	✓

Blueprint proposals for short-, medium-, and long-term actions for lasting stability and prosperity of EMU.

2 A genuine monetary union?

By Guntram Wolff *

At the December Summit, significant progress was made on completing the European architecture. But many urgent issues remain on the table.

First, on the positive side, the finance ministers agreed on the first important step towards a banking union: the establishment of a single supervisory mechanism (SSM). The compromise they have reached seems to be a good one.

The European Central Bank will be in a strong position and responsible for the overall functioning of the single supervisory mechanism. It will have direct oversight of euro area banks in a differentiated way, depending on the size of banks. But ultimately, all critical cases will be under the direct oversight of the European Central Bank which will also have the right to scrutinise banks below the size threshold. This is important to avoid competitive distortions but also to prevent major problems arising from small banks, which taken together still represent a large share of the EU banking sector.

Also, when financial assistance is given, the European Central Bank will become the supervisor of the banks concerned, meaning coverage can be extended to a number of Spanish Cajas with balance sheets of less than 30 billion euros. The compromise also appropriately allows non-euro area countries to participate in the single supervisory mechanism.

The common supervisor will play an important role in overcoming the financial market segmentation that is currently observed in the euro area. Part of the segmentation is a direct result of the actions of national supervisors, which limit the liquidity operations within banking groups located in different countries. Anecdotal evidence indicates that this situation has been a constraint for a number of large banking groups in Europe. This constraint has *de facto* aggravated the segmentation of the interbank market, which the European Central Bank via its liquidity operations had to compensate for. The first task of the new European Central Bank supervisor will therefore be to end current supervisory practices that lead to a segmentation along national borders.

Second, the Council Conclusions stress the need to move ahead with a common bank resolution authority and acknowledge that a purely national system of resolution would not be effective. This is a major and very important change in the European policy position: until very recently, many member states, and the European Commission, argued that national resolution would suffice. However, a banking union without a common resolution authority would not be a genuine banking union. Without a common form of resolution, there can be no form of risk-sharing because the moral hazard issues could not be contained otherwise. Also, without risk-sharing, one of the main aims of the banking union – to break out of the vicious circle linking bank debt and sovereign debt – cannot be fully achieved. The single financial market would remain fragmented.

Centralising resolution powers entails a major transfer of sovereignty, which in turn requires very deep reforms and clear thinking about democratic accountability. The European Commission's *Blueprint for a deep and genuine economic and monetary union* claims that such a resolution mechanism can be created without changes to the

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European Union Treaty. At first sight, it is difficult to see how this could be possible. It is certainly of major importance to explore in the coming weeks what would be feasible in the current framework and what other options exist besides Treaty change. One option may be to agree on a new intergovernmental Treaty.

So on the banking front, the December European Council made quite a bit of progress even though much remains still to be settled. Regarding fiscal union, the summit was a disappointment. The founding fathers of the euro were aware of the need to complement monetary with fiscal union, but left difficult choices for future decision-makers.

The time has come to address a series of unanswered questions. Should there be a proper euro area budget? Should a new system be conceived as an intergovernmental transfer scheme? Or should the ability of sovereigns to borrow be restored through some form of mutual guarantee? What should be the degree and type of conditionality? What kind of sharing of sovereignty is needed? What institutional changes need to be put in place before more fiscal integration can be achieved? What does a euro area fiscal union mean for the European Union as a whole?

Europe needs to think more deeply about how to organise the deleveraging of its debt. It is unlikely that prolonged high levels of savings would alone be enough to do the trick. However, the proposals that have been floated, such as for eurobills and the redemption fund, all insufficiently reflect on the institutional foundations that such solutions require. The European Commission could make a greater effort to consider on the institutional basis that more risk-sharing would involve.

It was evidently too early to take any decision at the summit given the limited technical and political consensus on the issues. However, a reflection process should have been initiated. European Council President Herman Van Rompuy was willing to oversee it. The European Commission was right in its pre-summit Communication on the Blueprint to highlight the important issue of how to deal with the debt overhang in the euro area. Had Europe's leaders agreed to work further on these issues, they would have demonstrated that they are able to think strategically.

A further criticism can be made about the Council's and Commission's analysis of the macroeconomic situation. While a relatively detailed timetable for a banking union exists, no specific steps to restore growth in Europe quickly are currently on the table.

There is obviously a major structural component to Europe's weak growth that needs to be addressed urgently. Structural action however, would produce growth in perhaps three years' time; so the outlook for the next two years would remain bleak. This holds true particularly for the countries of southern Europe.

The European Commission and the Council need to use the European Semester procedure more sincerely to agree on the truly important macroeconomic policies that Europe should enact now to overcome its dramatic decline in growth. The European Commission as the initiator of the European Semester will have to take the lead and argue for a comprehensive position on how Europe's macroeconomic policy should be shaped in the next few years. Long-term reforms are no substitute for this need, because anaemic growth in Europe will undermine them. Pro-forma, across-the-board policy recommendations as currently set out in the European Semester do not constitute a strategy.

3 Completing the EMU governance jigsaw puzzle

*By Iain Begg **

The severity of the crisis and its progression from the banking sector to sovereign debt exposed numerous shortcomings in the design of EMU, so that a comprehensive recasting to achieve a 'deep and genuine economic and monetary union' was, arguably, unavoidable. The question now is whether the range of measures taken and the proposals for further reform summarised in the Commission's *Blueprint for a deep and genuine economic and monetary union* will suffice to put economic and monetary union back on track.

Blueprint steps for actions

As explained in section 2 of the Blueprint, the reforms enacted are far-reaching, encompassing various measures aimed at assuring fiscal discipline, better policy coordination and more effective crisis resolution, alongside a strengthening of financial regulation and supervision. The Blueprint is correct to emphasise the progress that has been achieved and the coherence of the further measures in the pipeline, but it is regrettable that financial markets and many commentators have been slow to appreciate their scope. A possible metaphor is a jigsaw puzzle in which all the pieces were scattered over the table early in 2010. These pieces have progressively been assembled into a picture which, while still having some gaps, looks coherent.

The Blueprint contains a number of more contentious elements, such as macroeconomic conditionality and the notion of a 'contract' between the member states and Commission, both of which reinforce the controlling role of EU governance. While the rationale for such measures is well explained, it is acknowledged that the corollary must be strengthened accountability. The Commission, in particular, will have to be very sensitive in how it approaches the use of sticks and carrots in performing this role. To take one example, the suggestion (page 23) that 'under certain conditions, consideration of relevant factors may lead to not placing a member state in EDP', could be provocative where a member state simply reaches a different conclusion based on credible alternative analysis. So far so good, but will it be enough? There are three areas in which what is proposed risks falling short, all of which exemplify the messy political economy of transforming EMU.

Gaps and challenges

The first is that the proposals in the Blueprint for an EU level stabilisation capacity seem rather too tentative. The discussion of fiscal capacity is couched in terms of supporting economic coordination in the short- and medium-term, and refers for the long-term, to supporting 'member states in the absorption of shocks'. The focus on asymmetric shocks suggests that the trickier question of EU level stabilisation policy is not being countenanced and that monetary policy will remain the primary instrument to deal with a future symmetric shock. Will this be enough? While the collective fiscal stimulus agreed in 2009 in the wake of the steep recession was a timely – and necessary – response, it was *ad hoc* and the absence of a genuine EU level stabilisation capability could be construed a gap in a genuine EMU.

Although even a limited instrument to support member states in difficulty would, nevertheless, be valuable and revives a debate held in the early 1990s about buffer funds or similar approaches, how it is constructed will matter. The Blueprint explicitly distinguishes such a capacity from the existing EU budget, but in the public mind, the distinction is likely to be problematic. Consequently, efforts will be needed to explain and justify an increased call on taxpayers. Equally, this could be an opportunity to rethink what might – somewhat pompously – be called the fiscal constitution of the EU, revisiting the power to tax in the

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multilevel governance system as well as the scale of EU budgetary policy.

The Blueprint argues that a new fiscal mechanism should be funded by 'own resources' and should eventually have the right to borrow, but suggests that its size should be determined by being able to 'provide sufficient resources to support important structural reforms in a large economy under distress'. This line leaves it unclear whether the motivation would be about stabilisation or purely allocative, and therefore risks being a source of confusion. Compounding the problem is the continuing reluctance by member states to accept the idea of EU taxes other than the very limited financial transactions tax agreed on 21st January 2013. It is therefore useful to consider what other own resources (but let's call them what they are: EU taxes) could be adopted and how they would be set.

Since the EU budget was last substantially reformed in 1988, there have been repeated attempts to identify new revenue streams that could be used to fund the EU budget. Various credible instruments have been identified and their respective attributes carefully dissected, but these efforts have – so far – come to nothing, with the result that a quarter of a century later, the share of national contributions in funding the EU budget has grown. Moreover, the European Parliament has the dubious characteristic of exercising representation without taxation, in stark contrast to the slogan of the Boston tea party. As part of the EU governance reforms, the case for assigning certain tax streams to the EU, or at least to the euro area, is worth a fresh look.

In particular, corporate taxation at EU level, which would be consistent with a more closely integrated single market, should be a contender, especially if a macroeconomic stabilisation role is envisaged. The scale of resistance is easy to anticipate and the complications of agreeing a common tax base are considerable. Nevertheless, a crucial property of corporate taxation is that it would provide a degree of automatic stabilisation of asymmetric shocks, for the simple reason that tax yields tend to fall in areas hit by economic downturns and to rise in areas experiencing booms.

A second challenge, one that will not disappear soon, is the disjunction between EU and euro area membership, exacerbated by that fact that there are differing positions among the ten current 'outs'. While it is tempting to think that, in the long-term (that is beyond the five years used to delineate it in the Blueprint), the number of 'outs' will have dwindled to two or three, the accession over a similar time horizon of more new member states will inevitably prolong the dilemma. Even if only Sweden and the UK continue to stand outside the euro, there would remain a governance problem. It is understandable that a Commission Blueprint should want to soft-pedal the notion of variable geometry in future, but as the Cameron speech of 23rd January 2013 makes clear, it is a problem that cannot be overlooked.

Third, the crisis has been dogged by a number of episodes of flawed communication in which careless language has 'spooked' markets. Central bankers have learned over decades the importance of careful use of language and the same lessons have to be learned in other domains of economic policy where economic stability could be compromised by unfortunate language or public airing of differences. It is an aspect of governance that is not directly addressed in the Blueprint.

Overall the Blueprint offers a careful and comprehensive basis for debate. It is, perhaps, a bit too circumspect in relation to the longer-term, with too much use of terms like 'could' or 'might also be considered' which make it hard to discern which ideas are central to the proposed framework and which are more speculative. The challenge for the Commission may therefore be to follow it with a clear statement of 'here is what we want the outcome to be'.

4 Think Tank Twitter

Think Tank Twitter (TTT) aims to provide regular information and updates on what is produced by think tanks and research centres across Europe (and beyond) on EU policy issues. As an analogy to the original Twitter, each summary – or tweet – does not exceed 140 words, rather than characters. Those who wish to signal new publications for possible inclusion can send them to the email address bepa-think-tank-twitter@ec.europa.eu

What is Political Union?

European leaders must make three choices about the type of political union they want. The first choice is between a limited economic federation aimed at stabilising the euro and a full economic federation taking on traditional nation state tasks, such as taxation, social welfare and redistribution. The second choice is between a rules-based federation with a very small margin for policy innovation and one with discretionary powers and policy instruments. The third choice is between a political system that relies on indirect legitimacy and is governed mostly through intergovernmental mechanisms and one that draws on direct legitimacy instruments and confers executive authority to supranational institutions. The authors state that a balance must be struck between these three options that allows the EU to retain legitimacy and be flexible, while still based upon rules.

http://ecfr.eu/page/-/ECFR70_POLITICAL_UNION_BRIEF_AW.pdf

Democracy in Europe

The author contends that democracy in Europe is facing a multi-layered crisis affecting several, if not all, levels of government. He argues that politics is currently at the service of private or partial, rather than general, interests. The discrediting of the functioning of democratic institutions entails a devaluation of democratic values, such as anti-discrimination, equality, and fundamental rights. Values such as coexistence and solidarity, in short, have come to be associated with a system that does not perform and deliver to everyone's satisfaction, so that defenders of an open society end up being seen as representatives of only a few. This anti-democratic drift has many expressions: a sharp drop in confidence in institutions, voter radicalisation, social mobilisation, particularly in Southern Europe, and disengagement through sheer alienation.

http://www.cidob.org/en/publications/questions_cidob/n_122/democracy_in_europe_the_expressions_of_a_european_disease

Governing Risky and Uncertain Financial Markets

Policymakers should take a 'macroprudential' approach to financial systems, the author maintains, because it takes uncertainty and risk seriously and thus is a route to a more robust financial system. This approach limits the systemic fallout from a crisis by obliging financial institutions to build large buffers during strong economic times. Therefore, when banks have to pull themselves out of a crisis, capital adequacy requirements can be loosened. The macroprudential agenda also gives a more active role to regulatory authorities as well as greater attention to new methods for simulating the performance of models in worst case scenarios. The infrastructure for implementing macroprudential policies is already in place. Ultimately however, the culture of risk management must be reengineered, so that participants recognise that markets are environments characterised by both risks and uncertainties.

http://www.swp-berlin.org/en/publications/swp-comments-en/swp-aktuelle-details/article/governing_financial_markets.html

Southern Europe in Trouble: Domestic and foreign policy challenges of the financial crisis

Each author examines the effects of the crisis on the policies of Italy, Spain, Greece and Portugal, analyses the impact of the financial predicament on relations with the US and advances proposals on how to respond to the crisis while avoiding negative transatlantic fallout. To respond to the crisis and retain influence on the global stage, the authors suggest that Southern European countries create a new regional cooperation framework and support stronger EU economic governance. In regards to transatlantic interests, they should support a FTA with the US, help forge a common transatlantic strategy to facilitate the process of democratic change in the Mediterranean, and finally, work towards increasing NATO's projection through the Mediterranean dialogue and individual partnerships.

http://www.iai.it/pdf/mediterraneo/GMF-IAI/Mediterranean-paper_18.pdf

The Arctic: A region of the future for the European Union and the world economy

The EU should continue its bid for permanent observer status within the Artic Council as well as strengthen its relationship with Greenland to ensure that it is able to take advantage of climate change in the Arctic region. Via Greenland, the Artic is a new frontier, offering new maritime routes, easier access to off-shore natural resources and expanded fishery resources. With Greenland moving towards independence, the annual block grant from Denmark will be withdrawn. Since the financial repercussions of this are unknown and there is growing competition with Asian economies for access to resources, the EU should offer Greenland an economic 'safety net' and follow up on a 2012 letter of cooperation signed with Greenland that would secure its supply of rare earth materials.

http://www.robert-schuman.eu/doc/questions_europe/qe-263-en.pdf

The Changed Geopolitics of Energy and Climate and the Challenge for European Commission

The world energy system is undergoing a transition in which three agendas collide: an economic agenda; a security agenda; and a sustainability agenda. While Europe has pursued enlightened energy objectives, it has ignored major inconsistencies, massive government intervention and disappointingly small gains. Putting the market back at the centre, eliminating subsidies and learning from strategies that work among other 'E7' players would bring Europe closer to its objectives of sustainability, security and competitiveness. A transatlantic initiative to promote deeper integration of the world's three major regional gas markets around a common price discovery system could be a key stepping stone in developing broader architecture. This initiative should also include a better managed pricing system for carbon emissions in Europe and globally.

http://www.clingendael.nl/publications/2012/20121217_ciep_bressand.pdf

When the Rising Dragon Sees Fading Stars: China's view of the European Union

Due to the growing negative perception of the EU in China, Europe should work to improve Chinese public opinion as well as foster a deeper relationship. The EU should engage the new Chinese leaders on how China can help solve the European debt crisis; know which PSC members are in which factions to enable cooperation in policy fields; work with the Chinese to improve their position in multilateral organisations; and launch negotiations for an EU-China Investment Agreement. Finally, although the crisis has discredited the European model in some aspects, the EU should work to remain a model in areas such as consumer protection standardisation, ecological and sustainable urbanisation, education and research systems, as well as peaceful integration and cooperation with neighbouring countries.

http://www.ceps.eu/book/when-rising-dragon-sees-fading-stars-china%E2%80%99s-view-european-union

EU Democracy Promotion in the Eastern Neighbourhood: A turn to civil society?

The authors argue that the EU needs to review the way it implements civil society support in the Eastern neighbourhood if its initiatives are to effectively contribute to demand driven, bottom up reform. The EU must improve the balance between aid going to state and non-state actors; continue reforming funding procedures; develop modes to support civil society initiatives; and increasingly involve civil society actors in designing and implementing its aid programmes to governments in the regions. It should build bridges between civil society, political society and state authorities, and use other international aid organisation's successes as examples to ensure better use of resources provided. Finally, the EU needs to devise its own evaluation tools to assess the state of civil society in those countries where its aid is destined.

http://www.fride.org/publication-newsletter/1088/eu-democracy-promotion-in-the-eastern-neighbourhood:-a-turn-to-civil-society

6 BEPA News

Arrivals and Departures

BEPA is pleased to welcome new additions to its team. Inês Sérvulo Correia joined the Outreach Team from the President's Cabinet on 1 January to work on the pilot project on a new narrative for Europe. Jim Dratwa also joined BEPA in January from DG RTD to lead the Ethics Team and the European Group on Ethics (EGE) Secretariat. Didier Schmitt, a Seconded National Expert, joined BEPA from the European Space Agency on 1 December to work part-time with the Chief Scientific Advisor. Finally, BEPA is pleased to welcome Lynn Scavée, assistant in the Analysis Team.

João Marques de Almeida left the BEPA Outreach Team in January to pursue new opportunities at the Holdingham Group in London. We wish him all the best in his new endeavours.

Events

On 3 December, the EGE had its final Rapporteurs meeting of the year to examine the adoption of *Opinion No. 27 – An ethical framework for assessing research, production and the use of energy*, followed by a plenary EGE meeting on 11-12 December which led to the adoption of the Opinion No. 27 on 16 January.

On 14 December, BEPA hosted a seminar on the European Social Market Economy in partnership with the Church and Society Commission of the Conference of European Churches (CEC) and the Commission of the Bishops' Conferences of the European Community (COMECE). Topics discussed included the social and competitive aspects of the European social market economy, its development in member states, and challenges of youth unemployment in the EU. The discussion concluded with presentations of best practices and a call for deeper solidarity across country borders.

The three ESPAS Working Groups on economy, society and governance and power met for the first time on 18 December to discuss the respective winning bids and convene a working programme. The interinstitutional ESPAS Task Force also met on the same day to reflect on the overall ESPAS work programme, discuss the organisation of the ESPAS conference and the development of the project website, as well as give the external contractors the opportunity to present and discuss their proposals.

On 22 January, BEPA organised a seminar on public investment banks to exchange views and learn lessons on best practice. Panellists deliberated on the rationale of public investment banks, the role of the European Investment Bank and lessons to be drawn from experience in Germany, the EBRD and Brazil. The event was opened by BEPA Director-General Jean-Claude Thébault and participants included Arnaud Oseredczuk, Economic Adviser to President Hollande. Jonathan Faull, Director General of DG MARKT, gave a keynote speech over lunch.

Upcoming events

The European Group on Ethics will hold its next meeting on 19-20 February and will start working on a new Opinion on the ethics of security and surveillance.

On 18 February, the three ESPAS Working Groups will meet again with the contractors to discuss the first results emerging from their research on economy, society and governance and power.

On 18-19 February, BEPA will host the annual ESPAS conference titled "Developing Strategic Thinking in the EU-Global Trends 2030". A distinguished line up of international speakers from policy, think tanks, government and the EU institutions will be present and/or discuss global trends and the ESPAS project. President Barroso will give the opening speech. Topics to be discussed include ambitions for Europe, global trends, the challenges of prosperity, the empowerment of the individual as well as governance and power.

On 28 February, BEPA in partnership with Carnegie Europe, will host the 4th EU-Russia Forum. Participants – including 50 experts from Russia, the EEAS, the Commission, member state representatives, and think thanks – will discuss the political situation in Russia, bilateral trade issues, energy and the neighbourhood.