

Europe in search of a new settlement

EU-UK relations and the politics of integration



Published in 2013 by Policy Network

Copyright © 2013 Policy Network

Policy Network

11 Tufton Street, London, SW1P 3QB

Tel: +44 20 7 340 2200

Email: info@policy-network.net

Website: www.policy-network.net

All rights reserved. Except for the quotation of short passages for the purpose of criticism and review, no part of this publication may be reproduced, stored in a retrieval system or transmitted, in any form or by any means, electronic, mechanical, photocopying, recording or otherwise, without the prior permission of the publisher.

Editors: Seamus Nevin and Renaud Thillaye

Design and layout: Alan Hunt, alanhunt1@mac.com

Policy Network is a leading thinktank and international political network based in London. We seek to promote strategic thinking on progressive solutions to the challenges of the 21st century, impacting upon policy debates in the UK, the rest of Europe and the wider world.

Through a distinctly collaborative and cross-national approach to research, events and publications, Policy Network has acquired a reputation as a highly valued platform for perceptive and challenging political analysis, debate and exchange.

www.policy-network.net

Contents

Introduction

Political choices in a polarised Europe	4
Olaf Cramme & Renaud Thillaye	

A Europe of competing visions

The EU five years from now? Integration, like it or not	5
Sylvie Goulard	

Beyond Europe's zero-sum game	7
Paweł Świeboda	

Two Europes?	9
Thierry Chopin	

An ever closer eurozone?

EU quo vadis redux	11
André Sapir	

Towards a (more) political union	13
Jakob von Weizsäcker	

A social compact for European cohesion	15
Paolo Reboani	

The British question

On the outside looking in: the fate of Britain in Europe?	17
Anthony Teasdale	

Cameron's European gambit	20
Kathleen R. McNamara	

Adapt and overcome: The institutional strength of the EU	22
Stephen Wall	

Political choices in a polarised Europe

Olaf Cramme & Renaud Thillaye

“The EU must be able to act with the speed and flexibility of a network, not the cumbersome rigidity of a bloc” – this was the essence of David Cameron’s critique in his long-awaited speech on Britain’s relationship with Europe in January 2013. If in the last few years profound reforms to the EU’s architecture have been driven by economic necessity rather than political choice, then now is the time to reverse this dynamic. The intervention was nothing less than a thinly disguised challenge to those fellow EU leaders who believe there is only one direction: that of a Union dominated, if not entirely absorbed, by a deeply integrated eurozone in which ever closer coordination of multiple policy areas is becoming all but indispensable.

To be sure, this challenge is real, dividing europhiles and eurosceptics alike. In both camps, many seem to believe that the benefits of the single market are somewhat exaggerated, not least because further liberalisation stalled some time ago and new trade barriers within Europe are hardly conceivable. What is basically left is membership of the common currency. According to this view, any country which does not aspire to join has little to gain from belonging to an outer and gradually marginalised tier.

At the same time, there is still no consensus about how much more integration is desirable in the euro area itself. EU citizens are wary of any further moves and ready to rebel against unwanted or unsolicited decisions. Populist forces are on the rise in much of Europe. But if the eurozone crisis has already caused a lot of damage and suffering, it has produced at least one valuable result: the issue of EU integration has entered the electoral arena and is finally being politicised. Maybe not everyone has been inspired by the questions that David Cameron has asked, but the responses to them are far from preordained. The EU is again up for debate – and this is positive news.

In this debate, questions of political economy and institutional change are intimately connected: can the single market be sheltered from the eurozone’s regulatory steamroller? Is there a life for non-euro members and for other cooperation circles in a more flexible EU? How can the euro work better for all, export and import countries, north and south, without giving in too much to centralisation against popular will? How can EU policymakers reconcile conflicting demands for a more effective EU with greater ownership by states and citizens?

This collection of short articles seeks to provide guidance and clarity on some of these questions. Nine leading thinkers on EU affairs highlight the range of strategic options and preferences which ultimately have to be reconciled. The nature of this debate will be highly political. EU leaders and political parties must now come out fighting.

Olaf Cramme is director of Policy Network

Renaud Thillaye is a researcher at Policy Network

The EU five years from now? Integration, like it or not

Sylvie Goulard

In order to consider where the EU will be in five years time, it is essential to reflect upon the commitments that have been taken by member states in the past. The current and future environment calls for more collective action, not less

Many people, including David Cameron, present the question of the future of Europe in the wrong way. It was not just the common market which Britain signed up to in the 1970s and British governments have negotiated at every treaty modification since accession. From the outset in 1950, Europeans were aiming at achieving more than simply a market. Every change has been submitted to the British Parliament to authorise the ratification. It is time for British politicians to stop telling half truths about Europe and their role in it, exactly as it is time for politicians on the continent to realise what belonging to the eurozone really means. Seemingly these realisations are only just beginning, as highlighted by the European Council's working documents entitled *Toward a genuine [sic] Economic and Monetary Union*.

Previous commitments: no hidden agenda

It is not simply a question of 17 member states in the eurozone and 10 outside, but rather 25 (including Sweden) who are already committed to joining the single currency, aiming at creating a political entity, and only 2 (the UK and Denmark) who have established derogations. Latvia has already begun its accession procedures. Within the next 5 years, many others may also join this path, including Poland. In a democratic framework like the EU, a small minority of member states can not impose its view on the huge majority of EU citizens.

Of course, the single market is an important corner stone of the EU, and it is desirable to complete it in order to ensure growth and jobs. However, for this to be possible, it is also essential to reconcile Europeans with the single market, as proposed by Mario Monti in his report to the Commission¹, and developed in the authors' recent book². A dose of tax harmonisation and the establishment of certain safeguards to ensure a reduction in inequalities could go a long way to helping this. The UK is pleading for the single market in general, but does not hesitate to dismantle it on the details, such as in the field of financial services. When it asks for a veto on the European Banking Authority or national rules on the capital requirements for banks, London contradicts its own pleas for a fair, EU-wide level playing field.

At the peak of the sovereign debt crisis, the euro member states and the ECB made a clear choice, even if unfortunately it has passed almost unnoticed: the single currency is here to stay. However, it can only stay if all participant member states have growth perspectives, if European heterogeneity does not increase and if the governance of the eurozone makes the tough yet necessary reforms.

Democratic reform

Reform is needed in the economic, social and tax fields. In order to ensure an optimal currency area labour mobility and some financial transfers are also unavoidable. These steps require more transparency in the decision making process and greater accountability, which means more democracy at the level of the eurozone (or of the eurozone and countries committed to joining),

¹ 'A New Strategy for the Single Market, At the Service of Europe's Economy and Society', Report to the President of the European Commission José Manuel Baroso by Mario Monti, 9 May 2010 *De la démocratie en Europe, voir plus loin, Sylvie Goulard and Mario Monti, Flammarion, 2012*

² *De la démocratie en Europe, voir plus loin, Sylvie Goulard and Mario Monti, Flammarion, 2012*

through a reformed European Parliament. National parliaments alone cannot provide legitimacy for European decisions. The European Council must be controlled collectively and, one day, made accountable at that level.

One final important point concerning democratic accountability: a real EU budget is desperately needed instead of the national contributions we currently call the EU budget. If we continue bargaining in order to defend national rebates, the CAP, structural funds and other politics of the past, we will never give the EU the means it requires.

Another field where – whether we like it or not – we might be obliged to integrate further is that of defence. We need a strategy in response to the fact that the US will sooner or later look towards the Pacific not Europe – despite David Cameron’s doubtful claim that the UK can “make (its) own way in the world (outside of the EU)”. As hopes of freedom and democracy in the countries of the Maghreb and the Sahel born during the “Arab Spring” are transforming into a nightmare where dictators rule and impose Sharia law, the EU is facing new threats right on its doorstep. Europeans should pool their resources in order to ensure their continued security and bear their share of the responsibilities. The war in Mali is not just the French interfering in Africa, but a concrete example of where a dedicated European action would make sense to defend together our shared values such as freedom and democracy.

Whether national politicians admit it or not, a closer union is on the agenda. Even if, at this stage, many in the UK may reject it, just as the majority of the French believe they can still refute the institutional changes, or many in Germany, the “*Transferunion*”. We will probably muddle through, lose a lot of precious time, miss the pedagogy but ultimately we are already on the way to a federal type of union, which will soon require a commonly accountable government and a common budget. There is of course an alternative: chaos, disintegration and populism. It could happen but we should think twice about it being the preferred option.

Not all member states are going to participate in all policies. Differentiation already exists and will continue to in the future. But the dynamics concerning the common currency and defence could evolve much more quickly than we currently foresee. Sooner or later it needs to be made clear that no one will have full membership without being fully committed.

Sylvie Goulard is a Member of the European Parliament and group coordinator for the Alliance of Liberals and Democrats for Europe (ALDE/ADLE). She is co-author, with Mario Monti, of *De la démocratie en Europe, voir plus loin* (Flammarion, 2012)

Beyond Europe's zero-sum game

Paweł Świeboda

The eurocrisis has created a sense of dislocation between the EU and its citizens. The immediate concern is stability, but in the long-run Europe needs a new settlement between the citizens, nation-states and EU institutions

Europe's existential struggle is not only about the survival of the common currency but also about a renewed sense of purpose. The crisis has created a massive sense of dislocation between elites and citizens. For now, the all-absorbing objective is stability. Efforts are made to restore the basic functionality of the eurozone and correct the flaws of the past. The next step will be to achieve long-term fiscal and financial safety while avoiding the incompleteness which has troubled the common currency since the beginning.

Social contracts under renegotiation

Against this background, the EU's organising principle is mutating fast. In the past, it was solidarity. Its vestiges remain, including in the form of the EU budget. But solidarity will not recover its role of a mobilising force of European integration. In the crisis, it has been replaced by the logic of mutual surveillance and discipline. The risk of moral hazard, exposed by the eurozone crisis, has led everyone to believe the EU should avoid cutting corners at all costs. Looking over the shoulder and checking up on the others has therefore become part of the EU's operating manual.

In parallel, there is a major effort at renegotiating the social contract, both within and between member states. Part of this is fought on the streets and in bitter negotiations between social groups as the welfare state is cut in size. At the European level, the different national capitals strive to tilt the bargain in their direction. The process is dynamic with no final blueprint at hand.

The main battle, however, is about the new balance between individualism and collectivity. Europe has glorified its "community spirit" and "community method" which have been part of the Union's genetic code from the early days. It has overlooked, however, that the collectivity assumed growingly disabling characteristics. Member states have often become dormant as competences were transferred out of their realm and into the political no-man's land. The EU cannot be blamed for what was in reality a delegation of responsibility by the member states without a parallel delegation of power.

The UK's relevant question

If the UK is revolting against something at the moment, it is what it sees as the stifling character of supposedly enforced collectivity, coupled with a growing inability to define its own agenda. If played well, the process it is launching will become much bigger than it seems. It may not be entirely backward-looking, as the UK's opponents tend to believe, precisely because Europe needs to empower the member states to better look after themselves just as it needs a strengthened sense of community. The two are not contradictory. It may be difficult to come to terms with but attempts to reconcile the movement of the eurozone towards a quasi-federation and the UK-driven process of the review of competences can help the EU reinvent itself.

Empowering the member states and the citizens while modernising the community are necessary to lead the EU out of the zero-sum logic in which it increasingly finds itself. The former can be achieved not only through additional flexibility but also a system of incentives which would reinstate the power of initiative and a sense of responsibility to the capitals. The EU will need to work out a better mechanism to zoom in and out, with a clearly defined path for agreeing on the binding rules of the game at the macro level, but also with room for manoeuvre left to implement decisions at the national level. This will need to materialise both in political practice, with the European Council being responsible for key decisions rather than micro-management; and through adoption of the legal code, perhaps with a fast-track judicial procedure ensuring implementation of the principle of subsidiarity.

European citizens themselves have also become too passive in their reliance on the state. Faced with legal, financial and cultural barriers, Europeans have lost their entrepreneurial zeal to take risks. They need a liberating agenda which gives them more freedom but also a sense of obligation and commitment. Europe could be a greater “liberator” than the sum of the member states combined.

As the citizens are empowered, European politics will need to become better at micro-targeting and delivery across the granular reality of today’s political agendas. European societies are splintered on a growing number of issues as individual self-identities became like mosaics of views and positions. The European polity needs to adjust to that shift.

Finally, efforts will be needed to address the puzzling belief that collectivity has ceased to add value in Europe. The belief has to do more with a delivery deficit than with a misreading of a world in which the rise of new powers creates an obvious case for the EU to stay together. A “disfunctionality trap” is the real cause of the preference among some capitals to “go it alone”. This can only be addressed through a major focus on areas where the benefit of size is more than obvious – the single market, and trade as well as security and defence.

Paweł Świeboda is president of demosEUROPA – Centre for European Strategy in Warsaw. From 2001 to 2006 he served as director of the department of the European Union at the Polish Ministry of Foreign Affairs

Two Europes?

Thierry Chopin

The eurocrisis has made the rationalisation of the European Union necessary. A new category of membership to cater for states that choose neither to join nor to block a more united EU might offer a solution to the debate about a “multi-speed” or “variable-geometry” Europe

The repeated eurozone summits of the last few months have brought to light the widening gap that exists between the euro area and the rest of the Union. The crisis seems to have revived the debate about a “multi-speed Europe” and, in that context, the idea of a “variable-geometry Europe” has to be revisited.

Variable geometry on its way

To regain their sovereignty in front of the markets and their capacity to decide on their future, the euro area’s member states have understood that they need to form a more coherent whole. *De facto*, stricter common rules have been adopted in budgetary matters and the European Stability Mechanism (ESM) has entered into force; besides, in the past few months, the project of a banking union has made some progress. The crisis has led to a strengthening of the Economic and Monetary Union (EMU) through new rules that were also adopted by states outside the euro area, such as the Euro Plus Pact and the Fiscal Compact.

Furthermore, given the transfer of competencies implied by these common tools, the question of a political union can no longer be eluded. European decisions must enjoy sufficient legitimacy in the eyes of citizens; decision mechanisms must be simple and clear enough so as to be efficient and transparent. Without this, the economic union shall not meet the citizens’ expectations and the interrogations regarding the political vision that justifies European decisions - and thus regarding their legitimacy - shall remain.

In this perspective, the advancement of European integration, notably regarding budgetary issues, raises the question of a strengthening of EU differentiation from both a political and an institutional point of view. To give an example, the question of creating a specific assembly has been raised in order to strengthen the legitimacy and the democratic control of decisions taken on EMU. The European Parliament is obviously wary of not being put in the shade and thus has a preference for an internal sub-committee, just as the eurogroup is a sub-committee of the Ecofin Council and the eurozone summit a sub-committee of the European Council.

Yet, if the way towards a “variable-geometry Europe” is unavoidable, the latter is not a panacea because it leads to an increasingly complex European map. Different degrees of integration and multiple institutional arrangements make European integration increasingly hard to understand. They diminish legal security, make democratic debate more complex, reduce the efficiency of European governance and breed frustration among the member states.

The European Economic Area revisited

We propose to undertake clarification work that would enable the realignment of EMU with the European Union all the while satisfying the countries that wish to limit their participation to

the single market and a couple of other cooperation programmes. More specifically, it consists of revising the European Economic Area agreement in order to give equal voting power to those EEA member states that are not in the EU (such as Norway) over common policies to which they participate: most notably the single market, R&D programmes and cohesion policy.

This scenario offers numerous advantages: not only would this correct a democratic anomaly, but it would create the status the UK is looking for: continued participation and influence in the single market combined with exit from EU policies in areas such as agriculture, taxation and fiscal federalism.

Besides, the partners of the UK would be reassured since its influence within the single market would be preserved, while the Economic and Monetary Union would simultaneously be realigned with the European Union. Further integration of the euro area, which Mr Cameron has argued for in order to put an end to the euro crisis, would be made much easier.

Last but not least, this solution would provide an alternative to the risky “in or out” referendum promised by the British prime minister. It would consist of choosing between remaining in the European Union (a Union in which the United Kingdom could continue its promotion of a liberal agenda of reforms from inside by trying to rally a majority to support its positions) and finding a new type of association, which can neither be that of Norway (EEA with no voting rights) or that of Switzerland (ad-hoc bilateral treaties with the EU). Should the debate start in these terms, this would already represent progress compared to the crude “in or out” version, which would simply open the door to the vilest demagoguery.

Therefore, two levels of integration could be clearly identified. On the one hand, a politically and financially more integrated European Union associating the Euro area and the countries that have agreed to adopt the common currency upon their accession to the EU. Only two states, Denmark and the UK have opted out from the euro, but these are exceptions and not the rule. On the other hand, an enhanced European Economic Area providing non-EU members the opportunity to take part in decisions involving the single market. Obviously, several countries will hesitate between these two options, especially the United Kingdom, which could favour the second one. This option might also offer a solution in terms of extending the single market to new states, without bringing to the table any EU-accession.

Ever since the beginning of the crisis, we have gradually moved into a period of rationalisation and clarification of the Euro area and of the EU. This reorganisation must respect the imperative of overall coherence as much as it can. It is now time to open the debate in order to realign European institutions with the two main levels of integration: the single market and the Economic and Monetary Union.

Thierry Chopin is head of research at the Robert Schuman Foundation (Paris) and visiting professor at the College of Europe (Bruges)

EU quo vadis redux

André Sapir

For most member states, the euro represents what President Van Rompuy calls “the material and symbolic heart of the European Union.” However, a dynamic single market is and will remain Europe’s main competitive asset in a rapidly changing world

The euro debt crisis and subsequent policy responses are transforming not only the euro area itself but also the relationship inside the European Union between euro and non-euro members.

All the policy responses designed to strengthen the governance of the euro area have been adopted by all euro countries. Some, like the European Stability Mechanism treaty, are restricted to euro countries only. Others, however, are open to all EU countries and have been (or will be) adopted by most non-euro countries. Thus the Fiscal Compact treaty was signed by 25 EU countries and the banking union (or more exactly the Single Supervisory Mechanism) may be adopted by 23 countries or more.

As a result the EU today is squarely divided into three groups of countries. The first comprises all euro-area members, which belong to all the new economic mechanisms. The second comprises of most other EU countries, which belong to at least some of the new mechanisms. The last group comprises of only one (or perhaps two) members: the United Kingdom and the Czech Republic, if the latter decides to stay outside the banking union as it did with the Fiscal Compact.

How will this situation evolve during the next 5 to 10 years?

Two main scenarios seem plausible. The first would be the creation of a two-and-a-half speed EU. The first speed would comprise of an enlarged euro area (with perhaps 22 or 23 of the current EU27 members) with the kind of shared economic, financial and fiscal mechanisms that are necessary for the smooth functioning of the monetary union. The second speed would mainly or perhaps solely comprise of the United Kingdom still outside the euro area and of its enhanced policy environment. In-between these two speeds would be a small group of perhaps two or three EU countries having adopted some of the enhanced euro-area mechanisms which would make them fit and ready to adopt the euro relatively rapidly. Hence the situation would be not very different from a two-speed EU with almost all of the current EU27 countries on one side and the UK on the other.

The second plausible scenario would be a situation of increasing variable geometry, whereby different sub-groups of euro and/or non-euro countries would join forces to experiment with different policies of common interest, like for instance the Financial Transaction Tax set up last year by 11 euro-area countries using the EU instrument of “enhanced cooperation”. This situation would preclude, for the time being, the kind of coherence that would prevail among the euro countries under scenario one. However the absence of coherence in the short term might be compensated by the benefits of learning through experimentation which might eventually lead to a more robust system, at least for the euro-area countries and their close followers.

The UK perspective

From the viewpoint of the UK the second scenario obviously sounds much better than the first one since there would be less clear distinction between countries and therefore less distance between the UK and the others, even though Britain would still be in a small minority of EU countries outside the euro area. Yet the second scenario is unlikely to be permanent. Eventually scenario one has more chance to prevail since it brings with it policy coherence for the countries in the monetary union. Hence the UK's increasing loneliness inside the EU, which results from its refusal to adopt the euro and to participate in policy initiatives designed to ensure its sustainability, is bound to remain or even grow further.

The increasingly uneasy relationship between the UK and its EU partners is rooted in a different vision about the "European project" that goes back more than 50 years when the countries of Western Europe divided in two groupings with different objectives: the six founding members of the European Economic Community (EEC) "determined to lay the foundations of an ever closer union among the peoples of Europe" (Treaty of Rome, 1957); and the seven original members of the European Free Trade Association (EFTA) simply "determined to facilitate...the removal of trade barriers and the promotion of closer economic cooperation between [the countries of Europe]" (Stockholm Convention, 1960). The EEC's political objective and EFTA's purely economic objective translated into different choices of integration: "establishing a common market and progressively approximating the economic policies" for the EEC members; and the creation of a free-trade area for EFTA members.

It is probably fair to say that although the UK embraced the common market project when it joined the EU in 1973, and was actually the main proponent of the single market programme launched in the mid-1980s, it never quite signed up to the notion of "progressively approximating the economic policies". Certainly, the UK always intended to retain as much sovereignty as possible, only ceding grounds in policy areas which it viewed as absolutely necessary for the functioning of the common/single market. It never considered that the single monetary policy belongs to this category. Paradoxically, the UK probably understood better and certainly sooner than most euro area countries that the single currency is a political project, which is why it refused to adopt it.

Today, most EU countries accept that the euro represents what President Van Rompuy calls "the material and symbolic heart of the European Union". For the UK, however, the single market is the core of the EU. Can these two visions continue to coexist within the EU, now that the euro area is attempting to surmount its "existential crisis" with new policy initiatives like the banking union which the UK itself regards as essential for the euro but refuses to join? My sense is that it will not be easy but it is possible. After all the single market may not be regarded as "the material and symbolic heart" of the EU by most euro countries, but it is just as vital to their economic well-being as it is to other EU countries. A dynamic single market is and will remain Europe's main asset to improve its competitiveness and attractiveness as a location for innovative production in a rapidly changing world.

André Sapir is senior fellow at Bruegel and professor of economics at the Université Libre de Bruxelles

Towards a (more) political union

Jakob von Weizsäcker

In response to the crisis, Europe needs a number of substantial institutional improvements to the architecture of the euro, but arguably a more important achievement would be a more political union, one with an ambitious policy agenda

As the past 3 years have demonstrated, the initial architecture of the euro area was ill suited to weather a serious crisis. To some of the founding fathers of the euro, this did not come as a surprise. They saw the creation of the single currency as a stepping stone towards substantially closer political integration and quite possibly a “United States of Europe”, as made explicit by Helmut Kohl in his Maastricht speech.

Theoretically, the euro might have worked as a “currency without a state”: in the presence of proper institutional safeguards, of reliable arrangements for countries within the euro area to dampen divergences through national policies, and in the presence of firmly rooted convictions that any remaining shocks should be absorbed the hard way.

In practice, those with sufficient grasp of politics and history already suspected early on that such conditions might be difficult to sustain, especially as the euro area expanded rapidly. They saw, in the words of the late Tommaso Padoa-Schioppa, that “a strong currency requires a strong economy and a strong polity, not only a competent central bank.”

The need for institutional improvement

In response to the eurocrisis, we clearly need a number of substantial institutional improvements to the architecture of the euro. Key challenges include the design of the banking union, eurobonds, macro-insurance, contingent fiscal capacity and so on. However, the sum of these technical fixes will be no substitute for some form of political union.

There are two fundamental reasons for this: first, even the new architecture of the euro, while likely to be much improved, won't be able to put both monetary policy and fiscal policy on autopilot. To think otherwise would be technocratic hubris. At the same time, the limits of democratic legitimacy of intergovernmental decision making at the EU level became painfully clear during the crisis. Therefore, it would be problematic to try and organise a banking union or macro-insurance scheme without proper democratic and executive oversight and control at the EU level.

Second, a minimal political union just covering the conflicts that can arise within the context of the common currency might well be unstable because of the potentially divisive nature of some of the underlying distributional choices to be made. By adding more dimensions to the EU level decision space, the scope for mutually beneficial logrolling across political dimensions is increased. Multidimensional decision making in a deeper union can help us move from the politics of head-on conflicts of interest (where some countries are even considering their outside options) to the politics of mutually beneficial trades.

Package deals

While package deals across policy dimensions are already frequently used at EU level¹, the lack of obvious cross-fertilisation between the intergovernmental Euro rescue activities and the intergovernmental budget deal of this month is striking. It is hard to imagine that a proper European government would not have brought the two much more in line as part of a package deal. The extent to which the European Parliament with its present powers might still move decisions in that direction will have to be seen.

An unlikely yet instructive example of the kind of mutually beneficial package deals that a closer political union would enable concerns the area of defence. The location of army garrisons is traditionally co-determined by military and regional policy considerations. The case for regional policy considerations is further reinforced as most countries in the EU phased out conscription and now need to competitively recruit in the labour market. With that in mind, the move towards a European army as part of a package deal could easily have significant military, regional policy and fiscal benefits.

The point is not that we need a European army in order to save the Euro or the other way around. We don't. But it is reassuring to think that deeper political integration could help to make the EU's internal and external agenda mutually reinforcing by virtue of non-obvious package deals.

In principle, such package deals can be negotiated within the present intergovernmental set-up or even with countries outside the EU. But in practice, transaction costs quickly become prohibitive. That's the basic rationale for political union. But arguably even more important would be to achieve a more political union, one with an ambitious policy agenda, one that seeks to strike historic deals. As Jean Monnet observed: *"L'Europe se fera dans les crises et elle sera la somme des solutions apportées à ces crises"* ("Europe will be forged in crises, and it will be the sum of the solutions to those crises"). Unfortunately, the short term and somewhat domestic approach currently pursued by key European leaders might not add up to much in the end.

Jakob von Weizsäcker heads the economic policy department at the Economics Ministry of Thuringia and is a non-resident fellow at Bruegel. He writes here in a personal capacity

¹ Kardasheva, R., *Package Deals in EU Decision-Making*, (London, 2008).

A social compact for European cohesion

Paolo Reboani

Europe is facing increasing inequalities, soaring unemployment, rising social exclusion. It is time to restore the fundamentals of the European project around a clear political and economic agenda

The 2008-2009 recession has brought the eurozone and the European Union to an unprecedented crisis. This situation is now difficult to overcome without a clear departure from the choices adopted in recent years. Even the final agreement on the 2014-2020 EU budget – highly unsatisfactory – have shown how complicated it is for the European Union to identify a solid strategy for growth and social cohesion. Just like its predecessor the Lisbon Agenda, Europe 2020 – the EU's long term economic and social strategy – is on the brink of failure, because national governments are largely unable to coordinate their policies and to strengthen economic integration. At the same time there is an increasing disillusionment about the European project among the people of Europe, and particularly the young.

The risk of disintegration

This crisis is not only economic. It is not simply due to the recession and divergent economic conditions and policies among the member states. It is, in fact, mainly a political one due to the lack of democratic accountability in EU decision making; to the absence of a long term vision about the European Union; and to the resurgence of national interests. This increase of nationalism is feeding the growing populism throughout Europe and is a severe challenge for the European project.

There is a growing risk of political and economic disgregation. It is time to restore the fundamentals of the European project around a clear political and economic agenda. The 2014 European election can be a solid rock upon which to build a new phase of this political agenda, paving the way to a new Convention and a revision of the Treaty. The next steps on Economic and Monetary Union (such as the Banking Union) should open the way to more integrated economic policies. Moreover, it is also time for strengthening the fiscal union and for defining an industrial compact and, also, a social compact. These achievements are possible in the medium term if national governments, the European Commission and the European Parliament are able to work together.

The twin challenges of stability and growth

Only with these reforms can the eurozone become a solid and wealthy economic area, able to restore trust and to promote growth. Surely, financial stability and solid public accounts should be confirmed as a prerequisite but a different package of policies should be enforced, aimed at stimulating growth and producing wealth. The so called "Fiscal Compact" has to be completed by more symmetric correction mechanisms in order to make the adjustments more compatible between countries in different budgetary positions. In this framework, even a stronger common control of member states' budgets would be possible. The idea of "convergence and competitiveness contracts" between the Commission and member states would incentivise structural reforms by making use of the European budget.

However, such developments should be accompanied by a more equilibrating economic policy that could develop actions for infrastructure, research, human capital, territorial and social cohesion. Finally, more coordinated economic policies also means a stronger single market. It is necessary to complete the liberalisation processes, as it is important to make progress in other fields such as a common space for research and innovation or common investment in strategic areas (defence).

Revisiting social Europe

Europe 2020 objectives focus on the social dimension of the European Union. Three of the five targets are connected to labour market and social policies: increasing the employment rate, reducing poverty and social exclusion, and improving human capital. However, Europe is now facing increasing inequalities, soaring unemployment, and rising social exclusion. The coordination of labour market and social policies developed in the last decade has been insufficient to tackle these problems. The idea of a Social Compact for Europe should be taken into account.

Such a step requires employment policies to be better connected to other macroeconomic policies, and that member states give more power to the European Union. It is important to restore the fundamentals of an integrated economic area coupling monetary integration with flexible labour markets and high labour mobility. Against this background, a Social Compact for Europe should consider: more harmonised active labour market policies (the Commission proposal of a 'youth guarantee' is a good point of departure); a common basic European unemployment benefit, funded by the EU budget; employment legislation friendly to firms and able to deliver security to workers; increased tools to develop labour mobility across the EU; a common age of retirement, and common fiscal treatment of complimentary pension regimes.

Moreover, the Social Compact should also include better coordination of collective bargaining and wage formation. The Euro Plus Pact, the 'Six Pack' and the Fiscal Compact all intervene on wage formation, recommending the decentralisation of collective bargaining and a closer link between wages and productivity. Pressures from the European level on wage formation are increasing. At the same time, decisions of firm localisation, investment and production are increasingly transnational. Therefore, a European framework regarding wages, working conditions and employment policies, should be developed in order to ensure a solid and employment rich recovery.

Prospects for revival in the eurozone and in the European Union do exist. They should be based on incremental moves towards more accountable political decision making and more integrated economic policies. The principle of subsidiarity and the flexibility allowing each country to pursue their national objectives has to be reorganised around these guidelines if the EU wants to maintain its position as a key global economic and political player.

Paolo Reboani, chairman and chief executive officer, Italia Lavoro SpA and former economic and international adviser to the Italian Minister of Employment and Social Policies

On the outside looking in: the fate of Britain in Europe?

Anthony Teasdale

The last few years have seen the biggest change of Britain's EU policy in the history of its membership. This situation reveals a striking failure by pro-Europeans in the UK to win acceptance for the key notions that most governing elites on the continent largely take for granted

For most of its forty-year membership of the European Union, Britain has fought to avoid being 'on the outside looking in', as Peter Jenkins characterised the prospect in a powerful article written during the June 1989 European elections. Reacting to Margaret Thatcher's 'Diet of Brussels' advertising campaign, Jenkins saw the United Kingdom drifting away from the European mainstream in the face of pressure for Economic and Monetary Union and a social Europe.

Almost a quarter of a century later, it is now clear that, from the June 1975 referendum until the end of the Cold War, successive British governments largely succeeded in riding the twin horses of European integration and domestic public scepticism towards continental entanglements. Although Britain failed to join the European Monetary System in January 1979, the notion of a 'variable geometry' or *à la carte* Europe was long frowned upon in both London and in Brussels - being seen as strategically disadvantageous in one capital and as anti-*communautaire* in the other.

Ironic as it now seems, the Conservatives in opposition even chastised the Callaghan government for its 'obstructive and malevolent attitude' in staying outside the EMS. Mrs Thatcher described Britain's non-participation as 'a sad day for Europe'. From 1985, the new European Commission President, Jacques Delors, resisted pressure to sanction a 'two-speed' Europe. The prevailing philosophy remained that all member states should, wherever possible, move forward together towards the same goal, even if it meant progressing at the speed of the slowest. Britain often exploited this situation, rather like car driving as slowly as possible down the fast lane of a motorway, refusing to move over, leaving others behind flashing their lights in irritation.

Maastricht moment

The Maastricht settlement in December 1991 marked the moment that the UK-EU relationship first shifted towards a serious form of differentiated integration. The Commission reluctantly accepted British opt-outs on EMU, social policy and justice and home affairs - which in turn were hailed in London as major negotiating successes. A pattern was set: even if Tony Blair closed the social chapter opt-out, Labour in power deepened the JHA one and secured a partial exemption from the Charter of Fundamental Rights. Nevertheless, throughout the long years from Maastricht to the 2010 general election, there was a solid determination in Downing Street to try to keep Britain at the top table of EU decision-making. Messrs Major and Blair both described a two-speed or two-tier Europe as unacceptable. At Ellesmere Port in May 1994, Mr Major flirted with the idea of a 'multi-speed' or 'multi-tier' Europe, but only so long as the UK was not excluded from any kind of settled inner core.

Overall, in the 1990s and 2000s, Britain wanted the opposite of the EEA states: to exercise political maximum power from within the club, whilst exempting itself from rules it found inconvenient.

Mr Brown managed to ensure that Britain participated in the first eurozone summits, and even influenced their conclusions, without making any commitment to join the single currency. He was determined not to repeat his own mistake as chancellor of casual indifference to the emergence of the eurogroup of eurozone finance ministers.

Strategic shift

The Conservatives' relationship with the EPP Group in the European Parliament represented, in microcosmic form, an apotheosis of this UK approach. The Tory MEPs served as EPP Group spokesmen on many key legislative committees - including environment, single market and employment - but equally enjoyed complete freedom to diverge from a group whip that they played a disproportionate role in shaping. The decision by David Cameron to force the Conservatives out of the EPP Group in July 2009 was thus more than just, as many assumed at the time, a marginal sop to eurosceptics: it was an important early indicator of what was to become a major strategic shift in Britain's European policy.

The last two and a half years have in fact seen the biggest single change of government policy on EU issues in the history of British membership. From almost his first day in office, the prime minister indicated he would not attend eurozone summits, much to the chagrin of Angela Merkel and the disappointment of many in the City. His government said that 'closer integration was for the eurozone only' and passed an Act of Parliament, the 2011 European Union Act, that requires referenda for any significant transfers of power to European level. Fear of the need for parliamentary approval to an EU treaty change applying only to the eurozone resulted in his vetoing this route in December 2011: the intergovernmental Fiscal Compact Treaty was the result. Mr Cameron assumed that he could lead a coalition of the 'outs', but in practice eight of the ten non-eurozone countries, nearly all seeing themselves as 'pre-ins', quickly signed up to the new treaty anyway.

Outsider looking in

The Cameron policy on Europe combines the 'opt-out mentality of an opt-out government', as Tony Blair famously described his predecessor's approach to policy exemptions in the 1990s, with a new and unprecedented willingness to tolerate the UK's non-involvement in key decision-making structures. Critically, the idea of a two-speed or two-tier Europe, with the UK located in an outer grouping, however small, is no longer anathema. Indeed, the 'inexorable logic' of eurozone integration is accepted as likely to transform Britain's relationship into that of an outsider looking in on the real politics and power of a deepening and widening eurozone core. The main preoccupation is to try to ring-fence that process and contain any spillover from the core to the (political) periphery of the Union.

Perhaps to make the reality of marginalisation less painful for Britain, the prime minister would prefer the EU as a whole to evolve towards a complex variable-geometry system, in which the central obligations of membership are minimised for everyone. If this change cannot be achieved, the UK alone should be given a wide range of new, additional, country-specific opt-outs. Back in May 1999, William Hague as opposition leader already foreshadowed this concept in his now largely-forgotten Budapest speech - interestingly written by George Osborne - when he proposed that common EU policies, backed by supranational law binding on all, should essentially be limited to three areas: the single market, competition policy and external trade. Everywhere else, there could be a 'mix and match' Europe. Today, it is argued, this formula should be allowed to apply to Britain on its own, even if everyone else were to shun it.

For the first time since Harold Wilson in October 1974, Britain has a prime minister who no longer defends the terms on which the country belongs to the European Union. The fact that a significant majority of the current House of Commons almost certainly *can* support continued membership on these terms seems strangely immaterial. Whereas Mr Wilson planned to resolve this problem with a largely cosmetic renegotiation, followed by a referendum within nine months, Mr Cameron looks to a much more radical reformatting of the UK-EU relationship in four years' time.

Setting aside whether the prime minister can actually negotiate the outcome he wants - and what other countries might seek to extract in return - this situation reveals a striking failure by pro-Europeans in Britain to win acceptance for the key notions that most governing elites on the continent largely take for granted - notably, the idea of a European 'destiny shared in common', as Robert Schuman put it in May 1950, based on sovereignty-sharing in many areas of policy.

Eurosis

Whether because of the Westminster-centric nature of Britain's national institutions, the media's indifference to political life outside SW1, or the triumph of the English language and of Anglo-Saxon thinking in global discourse, a basic neurosis about Europe still exists at the heart of British politics and culture, and it shows no sign of abating. The consequences of this 'eurosis' are now becoming much more acute, exacerbated by the seeming impossibility of the Conservative party ever reconciling itself to the true nature of European integration.

One is reminded of what John Connally, President Nixon's treasury secretary, is alleged to have said when the United States broke the link between the dollar and gold in 1971: 'the President has a problem and he wants to share it with his friends'. After being held in check, but left resolved, during the Blair-Brown years, Britain's European problem is now back with a vengeance. It has recently been shared by the prime minister with our friends on the continent and has now become Europe's British problem too.

Anthony Teasdale, who works as a senior official in the European Parliament, is a former special adviser at the FCO and HM Treasury, a visiting fellow at the LSE, and co-author of *The Penguin Companion to European Union* (2012). He writes here in a personal capacity

Cameron's European gambit

Kathleen R. McNamara

It is not just domestic political issues which are forcing the UK to make key decisions about its future role in Europe. The real impetus lies in how the eurocrisis is fundamentally changing the shape of the EU

Last month, UK Prime Minister David Cameron outlined his plan for renegotiating Britain's relationship with the European Union (EU), promising to bring the result to the British people in an "in-out" referendum within the next five years. Speaking at the London Bloomberg offices, Cameron's announcement comes at a pivotal time, when relative tranquillity in financial markets has shifted attention from a possible Greek exit from the eurozone to a "Brexit," a British exit from the EU itself. Cameron presented a forceful vision of how British interests might be met while also forging a broader collective good for Europe and the world, but made clear that the EU's current course was straying far from that vision.

Highlighting developments within the eurocrisis, declining European competitiveness, and a lack of democratic accountability, the Prime Minister hammered home the idea that Britain should opt out of most of the EU's activities — but continue to participate as a full member of the EU's single market. This is an understandable position — the single market accounts for roughly half of all British exports and investment — but Cameron's desire to have his cake and eat it too is a nonstarter. While calling for an unwinding of Britain in the broader EU is a crafty political stance for domestic reasons, it ignores the reality that deep market integration is always and everywhere unsustainable without a broader panoply of laws, institutions, and political community to support such integration. No matter how Cameron tries to finesse it, we may be seeing the end of British membership in the EU before the end of this decade.

Diversionsary politics

Whatever else, the speech was a genuinely impressive piece of diversionary politics. Cameron is facing unrest in his Conservative Party, including a vocal minority in the UK Independence Party (UKIP) led by the ever entertaining euro-basher (and Member of European Parliament himself) Nigel Farage. But most damaging to Cameron's party's chances in the 2015 elections is an economy mired in recession and ravaged by austerity policies. Playing the Brussels card allows for voters to rally round the hated eurocrat bureaucracy in support of the Conservative Party, and puts Labour in a very awkward position of potentially having to campaign against holding a referendum on the EU.

However the irrevocable problem is that the play to isolate the single market from the other aspects of the EU ignores both history and logic. Deep integration across all the various factors of production — goods, services, capital and labour — does not occur without extensive rules and institutions to regulate and stabilise market exchange and protect investors, contracts, consumers, and workers. As Karl Polanyi argued long ago in his work on the historical embeddedness of markets, and Neil Fligstein has shown, political bargains and the institutions to support them are part and parcel of modern market economies. There is a reason why the WTO falls far short of the liberalisation of trade

that occurs within nation-states or in the EU: it lacks the complex series of rules and agreements and institutions that uphold markets and allow for the political and social bargains to support them. Britain could follow Norway or Switzerland to a looser free trade arrangement with the EU, but Cameron explicitly argued against this in the speech. Despite his rhetoric, however, the reality is a starker choice — all in, or all out — than he is making it out to be.

Eurocrisis - driving fundamental change

Ultimately, Britain is facing this decision about its future in Europe not just because of Cameron's domestic political issues, or unhappiness with the eurocrats in Brussels. Instead, the real impetus lies ultimately in the eurocrisis, as Cameron obliquely put it, "driving fundamental change in Europe." The dynamics that push forward political development when markets deepen also apply to the single currency. Europe now faces the fact that the euro cannot continue without a more federalised union, including fiscal consolidation at the EU level and new forms of political accountability in Brussels. Unprecedented actions on the part of the European Central Bank, new financial stabilisation institutions, a banking union, and ongoing discussions about ramping up political union mean that the core eurozone countries will continue to pull away from the vision of British interests Cameron laid out at the start of his speech. The collective good of the EU is demanding change, and it is a change that is unlikely to suit either political party in Britain. A Brexit and membership in the European Free Trade Association may ultimately be the most likely outcome, despite Cameron's savvy political politics.

Kathleen R. McNamara is director of the Mortara Centre for International Studies and associate professor at the Department of Government, Georgetown University. She is the author of *The Currency of Ideas: Monetary Politics in the European Union*. This article was originally published on TheMonkeyCage.org

Adapt and overcome: The institutional strength of the EU

Stephen Wall

The EU's ability to manage diversity has been essential to achieving the degree of common policy that enables it to be a big actor in global affairs. This dynamism is a key strength which we must safeguard

Dunlop used to run a TV commercial which showed what the world would be like without their products: tennis players without rackets, cars without tyres, gymnasts without trainers. The point was to show that they were indispensable but, of course, while the products were, others could do the job of providing them just as well. Has the EU reached its Dunlop moment?

If political prediction was a science then the Soviet empire would have outlasted the twentieth century, Japan would be the world's dominant economy, New Labour would still be in power in Britain and we would still think that banking was an honest profession.

We cannot know whether the United Kingdom will still be part of the European Union in five years' time, or how destabilising her potential departure would – or would not- be. We cannot know whether the federalising mission first described in a treaty signed in Rome 55 years ago will finally come to fruition in the eurozone. As to the first, David Cameron has mapped out a high-risk course, accompanied by the most passionate and persuasive arguments made by any British prime minister in my lifetime for Britain to stay in the EU. As to the eurozone, one Belgian banker I know likened the risk to that of a patient with pneumonia who leaps out of bed as the medicine kicks in only to relapse when, feeling much better, he decides that he does not need to go on swallowing the nasty stuff.

Pull factors and flexibility: a success story

That the monetary and fiscal management of the eurozone will become, and has already become, much more centralised and stringent does not necessarily mean that central control will spread more pervasively to all areas of domestic economic management. Or that discipline can be enforced if recovery reawakens the European Union's predilection for political fudge. Fudging is an essential part of compromise and it was compromise that undermined the single currency from the outset. Unless the conditions of convergence had been loosely interpreted, one or two countries, at least, would not have made it into the club. These were not easy judgements, any more than were those which turned a blind eye to some of the necessary conditions for accession for countries that were not ready. The beneficial 'pull' factor of the EU - of Germany in the case of the single currency; of the dynamic impetus inherent in enlargement – is not to be underestimated. But at 27 it becomes self-evidently harder to achieve.

De Gaulle kept Britain out of the EEC for a decade not because, as Macmillan put it, Hitler had not danced in Whitehall as he had danced in Paris, but because he correctly predicted that Britain's accession would radically change the character of the protectionist club he had shaped in France's national interest. Nevertheless, the EU has changed Britain as much as Britain has changed the EU. Monnet was more on the mark than de Gaulle. The unique institutional model has proved more powerful than the capacity of any single member state, or group of member states, to undermine it.

The strength of EU institutions

The EU's USP, its institutional structure, is the part of it about which we British have always been most queasy. And there is the flaw in David Cameron's argument for it, that is, the bits he denigrates are essential to achieving all the things he likes. No purely inter-governmental structure, let alone one operating by consensus, could achieve the reconciliation of the different interests of its members, could control its members' quarrels as they argue fiercely for their national interest or could, as a result, achieve the degree of common policy that enables the EU to be a big actor in the world in trade and aid.

The most important ingredient of future survival and success is the affirmation of that institutional model. We need a strong central bank, certainly, but, equally, a European Commission with the recognised authority, as well as the power on paper, to exercise its functions. And we have to accept that in the world of nation states which seems likely to continue for the foreseeable future, even with bits semi-detached, there is no satisfactory answer to the vexed question of democratic accountability. It will remain messily split between national Parliaments and the European Parliament and will not be solved by electing the president of the European Council or other palliatives.

Prospects for dynamic change

From the moment of the Schengen agreement in the mid-1980s, the EU has been a Europe of different speeds and different areas of common action. The single currency is the most prominent example. Another is cooperation in foreign and security policy where there is an EU led by France and Britain in which some others participate but in which many are spectators. So called common actions are common as to consent, not as to commitment.

We may hope that all member states will be effective foreign policy players and with the convergence to enable all to be part of a successful single currency, but we should plan on the basis that that is a desirable objective, not a likely reality. Since I do not believe that the countries of the eurozone will lose their separate national interests, I doubt if their convergence threatens the single market or the future of common policy making in areas such as energy and the environment. We need to manage the EU's financial sector, of which the City of London is still king, so as to protect the interests of all member states, in or out of the euro. Banking Union shows it can be done.

We cannot wish away the rise of global competition. We cannot, regrettably, realistically aspire to the kind of federal union that could give the EU a new competitive edge. But the Treaty of Rome is the only international treaty I know of that has a built in mechanism of dynamic change. Those who call it competence creep use a derogatory term for the one characteristic of the EU which we have to safeguard.

Stephen Wall is a former UK permanent representative to the European Union and advisor on EU affairs to the UK prime minister

Recent Policy Network publications

