INSTITUTIONAL CHALLENGES

Europe's future: more power to the Union, more autonomy for the member states

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The main problem facing the European Union is that it has achieved great private union, but little public union. The solution is to bolster the Union's public resources and stop controlling and interfering in Member State's public policies. To build a political union like the EU, there is a need to build shared institutions such as a private market, secure and defendable borders, and public finances. The EU has almost completed the merging of its private market by means of the adoption of a common currency and the banking union currently underway. It is still only halfway there in terms of the security of its common borders, as shown by the recent immigration crisis, and is only just beginning to consider the need for collective defense. Additionally, it is still very weak in terms of public finances, with regard to both income and expenditure.

Without a strong public financial sector in the EU, Europe's political union will never happen. The current paradox is precisely the fact that European public finances are so scant that the EU has to intervene, control and, eventually, bail out the public finances of its Member States, a process that many regard as undemocratic. The EU is too interventionist because it is too weak. The alternative is to bolster the resources of the EU's institutions and return more fiscal autonomy to its Member States. We need to let go of the idea of a 'tax union' between the Member States and, instead, provide the Commission with more resources. The fiscal autonomy of each of the levels of government, of both the Member States and the Union, as well as of local and regional governments, is the only viable basis for political union.

With multiple levels of government, each dedicated to different issues, possessing their own resources and decision-making rules suited to their particular level, 'sovereignty' disappears. We have already witnessed the disappearance of the sovereignty of states, defined as the power to make final decisions on all issues within their own borders. Within such a context, the goal of a new nationalist 'sovereignty' could not be more out of focus. When Jean-Claude Juncker or Emmanuel Macron spoke of 'European sovereignty', his words rightly pointed to the Union having more powers, but the message was verbally confusing, as it clearly does not mean that it should take over all of them.

Learning from the process of building the United States

A lesson can be learned from the process of building the first modern union of states in a great continental area and inspired by democratic principles: that of the United States of America. The lengthy process of building the American Union, one that was gradual, conflictive and asymmetric, might be reminiscent of the process currently under way in the EU. It took close to 125 years from the initial undertaking to form the Union, with the ratification of the US Constitution towards the end of the eighteenth century, to the point that the US achieved solid federal institutions. From this standpoint, the European Union, which has lasted to date around half this time, has made greater progress in many fields than the United States had halfway through its construction process. However, the EU's principal hurdle in completing its political union is its public finance sector.

At the very start of its existence, around the turn of the eighteenth and nineteenth centuries, the US Federal Government was extremely weak, as weak as the European is now in terms of financial resources. The majority of its expenditure, including that on the wars against the British, came from the individual states, which had proclaimed their sovereignty before accepting the US Constitution.

'Scene at the Signing of the Constitution of the United States', Howard Chandler Christy (1940). Font: Capitoli dels EUA

After those wars, the US Treasury, headed initially by Alexander Hamilton, decided to

'mutualize' the states' huge debt: in other words, to create a federal debt able to absorb those of the individual states. The Federal Government began to bolster its strength at the states' expense, exchanging debt payments for power. Later on, Washington's institutions also made important investments in infrastructure throughout the country's process of westward expansion. The greatest degree of interference by the Federal Government in the internal policies of some states took place around the Civil War in the 1860s, and entailed the abolishment of slavery in the South and the elimination of states' sovereignty. The Federal Government was also bolstered with the creation of a permanent federal income tax to fund the war effort.

Nevertheless, it was only in the 1910s that all the states achieved self-government by democratic means and participated on an equal legal footing in the Federal Congress. The main federal institutions responsible for the security and public money, the FBI and the Federal Reserve, were also created around this time. The Federal Government secured control over more than half of total public expenditure as late as 1940, i.e. some 150 years after its creation, as a consequence of the fresh expansion of the public sector in response to the Great Depression. It has been only since then that the US Government has had enough financial clout to develop wide-ranging federal programs in the fields of defense, infrastructures, social security, healthcare, research, and development. Unlike the EU, the US Federal Government has been implementing broad-based stimuli against recessions, most recently since 2009.

The other side of the coin of this particular history has been that, during the course of this process of bolstering the Federal Government's resources, the US ceased providing financial aid to insolvent states or cities as early as 1840. Thousands of local governments have gone bankrupt, especially during the Civil War, the Great Depression and, most recently, the Great Recession: California, Illinois, and Detroit, to name but a few. State or local government debt is never mutualized, and states and cities can go bankrupt without federal bailouts or rescues. Against this backdrop of federal handwashing with regard to state finances, almost every individual state has adopted financial responsibility criteria. More particularly, they have adopted balanced budget amendments in their constitutions.

The present fiscal relations in the United States are the opposite of those between the European Union and its Member States. In America, the Federal Government is financially stronger than its states, in contrast with the weakness of the EU compared with its Member States. At the same time, and despite appearances to the contrary, Washington regulates the states much less than Brussels does the EU Member States. As the US Federal Government has far more resources than the institutions in Brussels, it is much more capable of developing its own large-scale policies and does not need to get involved in the shaping of individual states' public policies.

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The low degree of federal interference and the individual states' autonomy allows for a significant legislative disparity between the states of the American Union, especially with regard to contract, property, family and criminal law, as well as in terms of issues such as taxation, abortion, gun ownership and the death penalty. The key to this is that Washington is more powerful than Brussels and, because of this, does not need to monitor, oversee and protect the states as much as Brussels does in Europe. As a result, America's states are also more responsible for some of their own decisions —particularly with regard to their financial viability— than the Member States of the EU.

The process followed by the United States points to the steps that the European Union needs to take to progress towards political union. To sum up: initially, the US Federal Government bailed out the states' debts, more or less as the EU did during the years of the recent Great Recession. The states recovered their autonomy in exchange for fiscal responsibility, which entailed the obligation to assume their own debts. Nowadays, the states are much freer to develop their own public policies in a wide range of fields.

A pact with the devil

Some European states embarked upon irresponsible financial adventures because some of their leaders thought that, if they went bankrupt, they could always blame the European Union and demand a bailout using other Member States' money. However, the EU has not created its own debt capable of mutualising the public debts of its Member States. That is why the EU had to impose the supervision, regulation and control of Member States' finances.

From 2010 on, Euro Zone Member States have been energetically prodded to adopt a balanced budget mandate in their domestic legislation, preferably at a constitutional level. And, ever since 2013, The European Commission has been monitoring Member States' budgets. Initially, the focus was on the magnitudes of deficits and forecast debts, but more attention has gradually been paid to specific expenditure, taxes and other income, a decision that has proved highly controversial.

In the case of Greece, for example, a Memorandum of Understanding with the European Commission committed the government to implementing fixed policies on taxes, pensions, healthcare, bank regulation, the labor market, energy, administration, the fight against corruption and many other issues, 'for many years' In 2015, the result of a national consultative referendum was overturned by the government. Greece actually became a protectorate of the European Union; the country's new elections and institutions have been reduced to choosing which national governments will implement the decisions of the European Empire. In many countries, EU directives are the foundation for the majority of the Parliament's agenda on the annual budget and many economic and social policies. National institutions are limited to rubber-stamping important decisions taken by EU

institutions to a far greater extent than before the crisis.

The EU needs to confirm that it has learned from the way the Great Recession was handled and not perform any more large-scale bailouts of countries in crisis. The International Monetary Fund's reluctance to get involved in the bailouts of other European countries gave an indication of the turn events would take. Financial insolvency within the Union may be the only option for countries in crisis in the future. This would mean that the institutions in Brussels would have more confidence in themselves and also that the Member States would have gained more respect in terms of their real powers.

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Such a pact would entail the acceptance by the Member States of a significant transfer of resources to the Union. To increase the EU's political responsibility, an increase in its expenditure would have to be accompanied by an increase in its tax revenues, which would also have to be transferred from the States to the Union. The core doctrine of fiscal federalism is that taxes on localized activities, such as income, wealth or property, should be in the hands of local or state governments, whilst those leviable on moveable activities, such as trade and capital gains, should be collected on a broader scale. The EU, which is currently mainly financed by VAT on sales, is moving in the right direction (better, indeed, than the US, which collects income tax at a federal level and sales tax locally). However, the fact is that the EU will have to increase its tax collection powers.

The European Union will have to spend more than its current budget of 1% of the gross European product. These days, some two-thirds of the EU budget is allocated to agricultural subsidies and regional funds, and so little remains for other policies capable of directly stimulating growth and employment. Although the Union may resort to the Central Bank, the European Stability Mechanism and the European Investment Bank, the total amount of resources available to it is barely twice the strict EU budget.

Once again, in comparison, the US Federal Government spends more than 20% of the country's GDP. However, excluding defence and social security, it has discretional power over only around 3% of GDP. This figure could provide a provisional target for the EU. It would allow Brussels to broaden the scope of some Europe-wide public policies, especially with regard to infrastructure and research and development, which are crucial in promoting sustained growth. And it would then need to meddle less in other political arenas reserved for the Member States.

The EU's financial strength is the price to be paid by the Member States for cutting back on the EU's excessive regulation and restoring a good chunk of their lost autonomy. In fact, the EU's institutions have already started to undertake some of this work. At the start of his mandate, the outgoing EC President, Jean-Claude Juncker, stressed the EU's criteria of

subsidiarity which, he noted, is in French regarded as a synonym for 'deregulation'. He stated that he wanted a 'European Union that is bigger and more ambitious in the big things and smaller and more modest on small things'.

Over the course of the last five years, the European Commission has carried out more than 200 actions to simplify and reduce the regulatory burden and repeal legislation that is no longer necessary, mainly in the fields of agriculture, fishery and the environment, the internal market and SMEs, transport and migrations, visas and citizenship. What's more, it has withdrawn or amended dozens of existing proposals with little prospect of becoming law.

If the work is completed, a financially stronger and less regulatory EU would allow its Member States to develop their own policies on issues in which they decide to be different, including, particularly, civil law and social expenditure. The States would be autonomous to the point of being responsible for their own finances. They would have to be able to comply with their own laws and constitutions requiring balanced budgets, without having to be overseen by the EU. But they would also have to be free to go bankrupt and not expect to be bailed out by the EU at the expense of other Member States' taxpayers.

It may be that Europe's states may oppose such a deal and seek to keep the lion's share of both income and public expenditure in their own hands. However, then they would not be in a position to cast so much blame upon the EU for its interference and controls. Without financial muscle in Brussels, the EU's regulations and directives are the only way for the Union to attempt to keep the system in financial balance, provide some large-scale public resources and do something for Europe's citizens. But an underfinanced, heavily regulatory European Union will never be a strong one.

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