



AN COMHCHOISTE UM GHNÓTHAÍ AN AONTAIS EORPAIGH

ÉIRE: AAE, LÁNPHÁIRTÍOCHT AGUS CUNTASACHT

Samhain 2014

JOINT COMMITTEE ON EUROPEAN UNION AFFAIRS

IRELAND: EMU, INTEGRATION AND ACCOUNTABILITY

NOVEMBER 2014

31ENUA0017

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1. Introduction

A core function of the Joint Committee on European Union Affairs is to consider issues arising from Ireland's membership of the European Union and Ireland's adherence to the EU Treaties.

Central to Ireland's membership of the European Union is our participation in Economic and Monetary Union (EMU), and the single currency, the euro. Ireland has a clear strategic interest in ensuring that the right policies are put in place underpinning EMU, particularly in view of the negative impact on Ireland, of the economic and financial crisis.

The crisis in Europe prompted debate at European level and in Member States (MS) regarding the role and response of the European Union to that crisis.

A number of steps resulting in greater economic coordination and integration in the EU have been taken in response to the crisis, and further significant integration is envisaged in the medium-term.

For this reason, the Joint Committee agreed that, in line with its orders of reference, it should contribute to that debate. This report is the result of those deliberations, and addresses under two headings, the main themes that emerged, which are:

- 1.** Genuine Economic and Monetary Union – Ireland's strategic interest as a Eurozone member; and
- 2.** Democratic legitimacy and accountability in EMU itself, and the EU more generally.

Two major papers published in late 2012 – the European Commission's ambitious *Blueprint for a Deep and Genuine Economic and Monetary Union*, and European Council President Herman Van Rompuy's report *Towards a Genuine Economic and Monetary Union* – provided an outline for the future design of EMU and set the scene for the Joint Committee's deliberations. Ideas were put forward and considered under four

essential strands of a genuine EMU: financial integration, economic policy integration, budgetary integration, and stronger democratic legitimacy and accountability.

1.1 Methodology of this report

This report deals with material collated during 2013, including verbatim transcripts from thirteen Joint Committee hearings as well as evidence presented in six written submissions.

In this report the entire body of evidence is organised thematically. Each section sets out the main opinions and evidence of witnesses and Committee members on given topics, to gauge which issues generated most debate and to set out clearly the range of ideas and suggestions for future action.

Over the course of the Committee deliberations, in some instances, events have since overtaken some contributions made in the 2013 sessions: the intervening year has seen a number of issues advanced or resolved: agreement has already been reached on the banking union package and the 2014-2020 Multiannual Financial Framework is in place.

2. Summary Recommendations

Recommendations:

The following recommendations are made by the Joint Committee. The rationale for these recommendations is set out in the report.

Democratic Accountability and Policy Development

Under this heading, the Joint Committee recommends that:

1. Ireland has an open debate on its own strategic objectives within the EMU and EU;
2. to achieve its strategic objectives, Ireland must have a clear and well defined and co-ordinated policy objectives;
3. Ireland must be a leader, not a follower, in policy debate and be heavily involved at every 'design' stage of future EU policy development;
4. Ireland position itself to exert as much influence as possible in shaping the future of EMU and Europe, bearing in mind French and German preferences for a 'core' or 'two-tier Europe';
5. a re-calibration of the 'European Social model' be undertaken in the context of overall EU policy development;
6. the role of the House of the Oireachtas in EU affairs be expanded, particularly in setting Ireland's overall strategic direction and policy objectives in the EU in order to address the democratic deficit;
7. the role of the Houses of the Oireachtas be agreed and formalised in the context of the EU Semester procedure, to counter-balance greater EU involvement in traditionally sovereign competencies;
8. additional resources and time be allocated to enable greater engagement by the Houses of the Oireachtas in a wider EU remit and to ensure efficient scrutiny of proposed EU legislation;
9. more enhanced and formalised engagement between the Houses of the Oireachtas and with Irish MEPs, representatives of the Committee of the Regions and the European Economic and Social Committee be developed;

10. national parliaments, in general must be further empowered in terms of input into EU policy development;
11. steps be taken to improve public awareness and understanding of EU policy. National and EU communication strategies should be developed and implemented, in order to improve public awareness and understanding of EU policy and in particular in the context of EMU policy;
12. the principle of subsidiarity must be respected in all EU policy decisions and emerging legislative proposals in view of the diversity of 28 member states;
13. inter-parliamentary co-operation must be strengthened and enhanced in the context of EU policy development;
14. further development of the 'political dialogue' or the 'Barosso initiative' be undertaken, as this procedure is currently under-used by national parliaments generally;
15. the question of representation in the European Parliament should be re-examined to allay the fears of smaller Member States.

Genuine Economic and Monetary Union: Ireland's Strategic Interests

Under this heading, the Joint Committee recommends that:

16. the role of the Houses of the Oireachtas be strengthened in order to counter-balance the implications of closer fiscal integration, that is, a move towards centralised (EU) control of national budgets, taxation and public spending, functions which are at the heart of sovereignty and independence;
17. all systems introduced on the progression to greater EU fiscal integration must be democratically accountable;
18. the Houses of the Oireachtas make full use of the provisions provided to it in the Single Supervisory Mechanism (SSM) including regular engagement with Ireland's representative to the SSM.

19. the Houses of the Oireachtas should debate any changes to Ireland's policy directions in relation to tax harmonisation measures, as further integration in EMU may require difficult policy trade-offs;
20. at EU level a co-ordinated move away from the policy of austerity towards sustainable growth and job creation be instigated, in order to address this aspect of the Eurozone crisis;
21. Ireland should continue to seek retrospective re-capitalisation for its banks from the EU as a 'special case', as acknowledged in the June 2012 European Council Conclusions;
22. the issue of Eurobonds be considered and debated at EU level and should be debated in the Houses of the Oireachtas to achieve a Irish Parliamentary position on the issue;
23. a single Europe-wide deposit guarantee system will be a necessary component of complete Banking Union;
24. the introduction of a central fiscal fund to deal with future asymmetric shocks should be strategic objective of the Irish government.

3. Genuine Economic and Monetary Union: Ireland's Strategic Interest as a Eurozone member

3.1 Introduction

This section of the Report outlines the evidence and analysis heard by the Joint Committee on European Union Affairs on Economic and Monetary Union (EMU) and the related topics – banking and financial integration and economic policy and budgetary co-ordination/integration. From this evidence, the Joint Committee has drawn conclusions and recommendations in relation to Ireland's strategic interest in the future development of EMU as a member of the eurozone.

3.2 The Crisis

The background to the economic crisis which threatened the existence of the Euro currency was explained to the Joint Committee. The economic crisis exposed interrelated banking, fiscal and competitiveness weaknesses in many eurozone countries. The Joint Committee heard that this came about as overstretched financial institutions became vulnerable to market corrections that began with the sub-prime market collapse in the United States, leading to massive investor withdrawal and stock market crashes. The problems of distressed sovereign debt markets in countries such as Ireland, Portugal and Greece threatened the financial institutions of those countries and those of other eurozone member-states. The level of indebtedness on the periphery in particular was almost insupportable.

It was explained to the Joint Committee that a combination of these pressures, as well as fiscal imbalances and divergences in competitiveness, posed a serious challenge to the survival of the single currency. EMU was not fully equipped for the following reasons:

- Proper warning systems and resolution mechanisms did not exist: prior to the economic crisis, no real framework had been put in place for the management of financial crises within the eurozone;

- There was no centralised authority responsible for the regulation of financial institutions, no fiscal transfer or fiscal stabilising mechanisms at EU level for dealing with major problems;
- There was no lender of last resort at EU level for sovereigns;
- The crisis made it difficult or impossible for some countries in the eurozone to repay or refinance their government debt without the assistance of the European Central Bank (ECB) and/or the International Monetary Fund (IMF);
- Banks in the eurozone were under-capitalised and faced liquidity and debt problems.

In short, the eurozone was ill-equipped as a single currency union, which certainly curbed the ability of European leaders to respond effectively and may even have exacerbated the crisis and exposed serious flaws in the original design of the currency framework.

3.3 The Aftermath: Response and Reform

The Joint Committee heard in evidence that the initial response of European leaders was to try to contain, control and minimize the damage.

Rescue policies focused on restoring the liquidity and capital of banks, in an effort to get the financial system functioning again. The moves to restore stability included setting up provisions for granting emergency loans to member-states in distress in return for the enactment of economic reforms.

The European Central Bank intervened through the Securities Markets Programme (SMP) and, eventually, the Outright Money Transactions (OMT) indirectly buying government bonds.

The European Financial Stability Facility (EFSF) – an initial, temporary facility – and later the European Stability Mechanism (ESM) on a permanent basis, were set up to provide emergency funds to distressed

states in an effort to stabilise the euro. The €500 billion ESM is funded by member-state contributions as shareholders.

Subsequently steps have been taken to re-design the systems of financial regulation and supervision, but resolution of the Europe-wide problems was complicated by a lack of clear and cohesive policy, conflicting goals or mandates and limited powers at EU level.

Banking Union legislation, dealing with supervision and resolution, has subsequently been enacted and will be implemented incrementally from November 2014. It aims to sever links between banks and sovereigns, to deal with the recapitalisation of banks and to set up a harmonised guarantee scheme for depositors.

The Stability and Growth Pact (SGP) was strengthened - to provide for greater budgetary surveillance - initially by the introduction of the Sixpack¹, Fiscal Treaty provisions and later by the Twopack² mechanisms.

The structure of EMU is still in flux as financial, budgetary and economic frameworks evolve. The institutional architecture is being reformed. The two major 2012 blueprint papers from late 2012: one from the European Commission and another from the president of the European Council, set forth a number of short, medium and long term objectives. A number of these - including the European Semester and other budgetary oversight mechanisms: the 'Sixpack' and 'Twopack', as well as Banking Union - have been implemented.

The Joint Committee was also told that the long-term viability of Economic and Monetary Union (EMU) depended on the ending of the three

¹ The EU economic governance **Sixpack** is a set of European legislative measures designed to reform the Stability and Growth pact and introduce greater economic surveillance. A complete explanation of **Sixpack** can be found on the European Commission website:

http://ec.europa.eu/economy_finance/articles/governance/2012-03-14_six_pack_en.htm

² A further step towards increased fiscal discipline of member States of the European Union was taken on 23 November 2011, when the European Commission proposed two Regulations, also known as the **Twopack**, which introduced additional coordination and surveillance of budgetary processes for all eurozone members. A complete explanation of **Twopack** can be found on the European Commission website:

http://ec.europa.eu/economy_finance/articles/governance/2012-03-14_six_pack_en.htm

interlocking crises – the sovereign debt crisis, the banking crisis and the problems of low growth, high unemployment and high private indebtedness. Since then, the threat from the first two elements may have receded somewhat, although – as Banking Union will only go into effect in late 2014 – there is still a lot to do and of course the major legacy debt issues persist with a significant debt overhang on the periphery which continues to be a drag on growth.

The crisis has spurred the eurozone to initiate closer integration of its financial systems and generally closer economic policy co-ordination across all Member States of the EU to ensure consistency and coherence and common purpose.

3.4 EMU - Unfinished Business

The Joint Committee heard that the present structure of EMU constitutes a half-built house. There is monetary union but a very incomplete economic co-ordination.

It heard that the eurozone's initial responses to the crisis had been somewhat insufficient in dealing with the sovereign debt crisis: the ECB's OMT initiative had essentially saved the euro in 2012, but now needed to be re-examined, especially in terms of its implementation, and it needed to be more accessible.

It is in Ireland's interests to consider new measures of fiscal integration, to strengthen EMU, shore up its resources and place it in a state of readiness for possible future crises.

3.5 Economic Policy: Co-ordination and Cohesion

The Joint Committee heard that the main thrust of overall EU economic policy has been the effort to establish stable prices, robust public finances and a steady sustainable balance of payments. The Joint Committee also heard that there is a view that the balance of payments element is not as important a tool as it used to be: once a country is in the eurozone,

balance of payments is less important as a mechanism for influencing the exchange rate of the euro.

It was also explained to the Joint Committee that economic management must embrace the wider issues of improving and completing the internal market, competition policy, employment policy, consumer protection and agriculture and fisheries policies. There needs to be a focus on economic and social outcomes, such as tackling unemployment.

Monetary stability is vitally important but should be accompanied by a more ambitious strategy for fuller employment and an increase in demand. To achieve this, the eurozone will require significant structural and institutional changes in the long term. Since the Joint Committee hearings, there has been wider acknowledgment of the need to address these issues. It was explained to the Joint Committee that a broad range of policies must hold across countries with completely different systems and approaches. For example, some countries might have higher levels of social protection or public provision, while member states such as Ireland might like to model theirs on a lower-tax and lower-spend basis. It seems realistic to suggest that economic policies in the EU be designed with all member states in mind and not involve the imposition of too many restrictions.

An interdependence has been built, which should continue to pay dividends and the Joint Committee agreed that, nevertheless, there is a 'contractionary bias'³ in policy, with insufficient attention paid to the overall aggregate stance: there is a view that there needs to be more focus on demand in the European economy in general.

The Joint Committee also heard more attention needs to be given to developing credible lender-of-last-resort supports, to reduce the fragility of individual countries. In addition on the supply side, reforms need to take place in labour and product markets.

³ Refers to the policy of austerity.

In conclusion, the eurozone is a monetary union but not a fiscal union. It has no income transfer system comparable to those which exist within member states.

3.6 Employment and Growth

In the discussions on employment and growth, the Joint Committee heard that little had been done to ease the problems.

Internal de-valuation policies had had an overall deflationary effect, causing economies to contract.

There may have been too much focus on austerity measures, but Ireland had to adhere to the terms of the bail-out programme and meet deficit targets to ensure continued funding of the country.

The Joint Committee heard that there was a growing consensus that the austerity programme is a significant component of low economic growth in Europe: that a fair balance had not been struck between the policies of austerity and stimulus. A policy change at European level may be necessary to bring in more growth stimulus, particularly in view of an acknowledgment by the IMF that every euro taken out of an economy has an effect far beyond that value, the 'multiplier effect'.

The Joint Committee heard that the eurozone should align monetary and fiscal policies to the goals of employment and growth. The broad framework required, involves intergovernmental co-ordination of policies to prevent competitiveness imbalances and domestic fiscal imbalances from growing too large. In order to help offset regional recessions and asymmetric shocks, such a framework will require a centralised fiscal fund.

With regard to high levels of unemployment in some Members States, it was suggested that such a centralised fund targeted towards growth and employment should be established.

There was consensus (among contributors) that a resolution of the problems in the banking sector is a prerequisite for growth in employment levels.

3.7 Banking Union

The crisis revealed deep flaws in national level regulation and supervision of banks and crucially, the potential for feedback loops between banks and sovereigns, where banks remain a national responsibility.

The Joint Committee was told that the main elements of Banking Union for the eurozone are already agreed, and the next few years will see their roll-out.

It was heard that a centralised Banking Union is a necessary component of any viable monetary union. In practice, this means independent centralised supervision by the ECB, regulation and resolution of financial institutions at the eurozone level and a deposit guarantee system.

It provides for the following instruments:

- the Single Supervisory Mechanism (SSM), making the ECB legally responsible for supervising eurozone banks,
- the Single Resolution Mechanism (SRM) to provide finance for distressed banks and to help co-ordinate 'bail-in' imperatives, and
- a bank deposit guarantee scheme has been agreed.

Each of the Banking Union elements contains provisions relating to accountability to the European Parliament and to national parliaments. Under the Single Supervisory Mechanism arrangements the Houses of the Oireachtas and other national parliaments are empowered to summon their respective representative on the ECB's Single Supervisory Mechanism to appear before it to explain and account for regulatory decisions. It is incumbent upon national parliaments, including the Houses of the Oireachtas, to fully utilise this provision on a regular basis.

The Joint Committee heard that the controversial mechanism considered for the resolution element of the package, which was subsequently agreed, will require bondholder bail-ins and large-depositor bail-ins, depending on the nature of the losses for the banks concerned, before the single resolution fund can be tapped. Such a bail-in provision will pose challenges and risks to investors and depositors – both household and corporate, which both should be made aware of, however, this will ultimately provide the required certainty in the marketplace.

The revamped banking system will be backed up by a European resolution fund, funded in a number of ways: by risk-based levies on banks, by a capacity to borrow possibly from the ESM, and by ex-post risk-based levies to repay such borrowings. The model aims to minimise public exposure. The resolution framework will need to be complemented by a stronger focus on ensuring banks are adequately capitalised and backed up by rigorous stress tests. It is also vital that investors are aware that if a bank is not failing but needs further capitalisation, it will not be coming from the sovereign.

Banking Union will have major implications for Member States. Protecting taxpayers and depositors in the future, while also dealing with issues of capital flight, particularly from the eurozone periphery, will require a centralised fund or a deposit guarantee scheme, perhaps along the lines of the Federal Deposit Insurance Corporation Scheme in the US.

In the interim, the deposit insurance element will remain a national responsibility, with deposits up to €100k guaranteed - although the design of national systems has been harmonised.

The Joint Committee heard that a single Europe-wide deposit guarantee system will need to be put in place eventually.

The Joint Committee was also told that, with parts of the European banking system still under significant capital and funding stress, care

must be taken in the phasing-in of the new system, not to impair further credit availability in the eurozone economy.

The Joint Committee heard that Ireland could justifiably ask for retrospective recapitalisation for its banks as acknowledged by the June 2012 European Council Conclusions. Efforts had been made by Ireland, during the crisis, to burden-share with senior bondholders but such a move was not possible at that time. There is a view, which is widely shared, that recompense in that respect may be due to Ireland, as that very same policy has been put in place subsequently at European level.

3.8 European Central Bank

As part of the roll-out of banking union, the ECB has been given additional powers of supervision over eurozone banks. But the accumulation of influence and power has not been matched by measures to provide for oversight and accountability. The European Parliament has no power over the ECB.

The freedom to function without political interference is accepted, but there are concerns that the ECB is accountable to no-one for the way it makes decisions or the rationale for them.

3.9 Economic Policy Integration

It was outlined to the Joint Committee, that the vision for economic co-ordination in Europe is for a framework for systemic ex-ante co-ordination of economic policy, involving arrangements of a contractual nature between member-states and the EU, as well as a financial instrument to incentivise reforms.

This would most likely take the form of bi-lateral agreements with each state, detailing a specific reform programme for that particular state, on the basis of recommendations by the EU Commission, and the conditions for drawing down such funding.

The Joint Committee heard concerns about the nature of such contracts: that they must be monitored and approved by national parliaments, otherwise they constitute a subversion of democracy, binding governments but not states.

The suggestion was made to the Joint Committee that the development of inter-parliamentary co-operation together with scrutiny by national parliaments, might counter-balance the pit-falls.

3.10 Monetary Policy

Up to now EMU has combined a centralised monetary policy, with the ECB heading up the European System of Central Banks and a mandate to maintain price stability and to protect itself from political considerations. Whereas fiscal policies are decentralised and are the responsibility of national governments.

3.11 A Lender-of-Last-Resort

A lender-of-last-resort is an institution, usually a central bank, that offers loans to banks or financial institutions in distress or near collapse that have no other recourse to borrowing and whose failure to obtain credit would dramatically affect the economy. The goal is to prevent financial panics and bank runs spreading from one bank to the next due to a lack of liquidity. It is assumed that the lender-of-last-resort would not have to be activated as the 'promise' is enough to boost confidence and therefore prevent panic in the markets.

The view was expressed to the Joint Committee that a lender-of-last-resort is needed, if economic crises are not to recur in the EU. A permanent mechanism to prevent sovereign borrowing debts becoming unsustainable should be made available but only to member states who are willing to pursue a sustainable fiscal path.

Formally the ECB is prohibited from acting as a lender of last resort. The Joint Committee heard that a 'special-purpose-vehicle' such as the ESM

could fulfil this role on a formal basis. The establishment of a lender-of-last-resort is key to resolving long term issues and making EMU sustainable.

Lender-of-last-resort is associated with concerns about moral hazard: that the safety net it provides can encourage excessive risk taking by both bankers and investors. Furthermore, the lender-of-last-resort mechanism is considered in some cases to exacerbate the situation by delaying the ultimate resolution of a problem.

Proponents of such a facility insist it would not lend to failed banks, but it is noted that it is difficult to distinguish lack of liquidity from insolvency, in a time of crisis.

3.12 Fiscal Policy

The Joint Committee was told that on the fiscal side, the fundamental obstacle to cohesion and a proper functioning of the eurozone, has been the fact that each government determined its own fiscal policy with limited regard to its impact on the eurozone as a whole. This issue was considered to be at the heart of the eurozone's problems.

A framework to address this is now in place, with the introduction of the European Semester for economic policy co-ordination and the Sixpack and Twopack mechanisms controlling debt and budgetary deficits.

The new measures came into effect in Ireland in 2013, altering the timing of the budgetary cycle and raising questions as to how Ireland should interact with the EU Commission. Should the Commission liaise only with Department of Finance officials or should it present to the Houses of the Oireachtas? The Twopack mechanism provides for the EU Commission to be answerable to national parliaments. It is important that Ireland makes use of this provision.

It was pointed out to the Joint Committee that although oversight of draft national budgets is highly intrusive, the European Semester model may

make the budgetary system in Ireland more open and transparent in ways that can give advantage to parliamentarians. The budget will no longer be a secret contained in the briefcase of the Finance Minister. National parliaments will be able to engage with the Commission on its recommendations, as well as with their own governments. In this context the involvement of the Houses of the Oireachtas will need to be formalised. The Oireachtas should use the powers available to it.

The Joint Committee was advised that the European Semester model was built on a consensus that macroeconomic stability, rooted in sound public finances, is a prerequisite for sustainable economic growth. Under the Stability and Growth Pact (SGP) member states have agreed to avoid excessive deficits and to fix them quickly if they do occur. The SGP strengthened the fiscal rules of Maastricht governing the procedures for mutual surveillance and peer pressure among member-states. But a key element of the SGP, the limit on government deficits of 3% of GDP had historically been ignored by member states. So, in 2011, the Sixpack and Twopack mechanisms, were introduced to further strengthen the regulations governing deficits.

The Joint Committee heard that closer fiscal integration will mean, to a greater or lesser extent, a move towards centralised control of national budgets, taxation and public spending, functions which are at the heart of sovereignty and independence.

After having taken the steps to contain the damage from the economic crisis, the eurozone now seeks to re-design and re-structure its fiscal architecture. The Joint Committee was told that initially this will involve fiscal capacity – a certain degree of fiscal integration – then, in the longer term, the possible introduction of a central EU/eurozone budget with a stabilisation function. The longer-term model is similar to a federal system involving the centralisation of some areas of taxation.

The Joint Committee also heard that part of this vision entails a greater degree of common decision-making and therefore, common responsibility and perhaps common mutualisation of indebtedness. All of this will provide fiscal solidarity against shocks. It also assumes a level of fiscal integration, which – depending on the degree – may in turn require a review of treaties to ensure parliamentary oversight and democratic legitimacy.

3.13 Tax Harmonisation

Fiscal integration would be likely to involve some element of tax harmonisation across the EU. The ad-hoc Financial Transaction Tax (FTT) was cited as a good example of enhanced co-operation, but only 11 countries have signed up to it. Ireland is not among them: as a peripheral small country it is striving to maintain control in order to present certainty for foreign direct investment in Ireland. In this respect, it was noted that the problem with FTT is that the costs and benefits vary for individual states and that as Ireland will never have the leverage of a large country it needs to use whatever leverage it has.

It was heard that Ireland needs to consider its strategic priorities in relation to any tax harmonisation proposals in the wider context of the development of EMU.

The Joint Committee heard that opinion is divided on the desirable extent of fiscal integration – Ireland itself did not sign up to the FTT, for example. Nevertheless, the Joint Committee also heard that such multi-lateral agreements are problematic for the EU and create tension in the unifying fabric. This is a classic example of the dilemma at the heart of integration issues: the conflict between national and EU interests.

3.14 A Central Fiscal Fund

The Joint Committee heard there is a need for a central fund for asymmetric shocks, even though there are two possible stabilisers in the EMU system: a lender of last resort, which stops sovereign borrowing

costs from going out of control, and government budgets. But there is a limited capacity with government budgets.

The issue is how to set up such a central fund without full fiscal union. A view was expressed that a form of taxation is needed. It could be a form of consumption tax, (possibly 1% of VAT revenue). Alternatively, it could be financed from national contributions, financing from own resources, or a combination of both. There are suggestions that it could be borrowed by the eurozone, with a common debt issuance. It might entail the setting up of a central treasury. The Joint Committee heard that it is in Ireland's interest that this is further explored.

The Joint Committee was advised that greater fiscal integration could also involve, for example, the harmonisation of social protection and social welfare systems, or of social insurance, which would yield a greater European budget and create Europe-wide stabilisation. Such a move would represent a significant transfer of power from national to European level and would involve trade-offs to compensate for the pooling of sovereignty. Currently the EU Treaties provide limited scope for the EU to become involved in such policy areas as these are national competencies.

3.15 Eurobonds/Debt Redemption

The Joint Committee was told that the idea of Eurobonds is not a new one, and had been considered by the EU Commission and although it is described as a medium-term goal in the EU Commission blueprint paper, it does not seem to be gaining traction. Proponents of the idea contrast Europe with the US - where the Federal Reserve issues federal bonds - while the countries of the EU issue their own debt.

Debt mutualisation means that richer Member States are guaranteeing part of the debt of other Members States and this is not always politically acceptable.

A joint bond issued by eurozone countries could help the indebted member-states, as investors might be more willing to buy bonds from the entire region, as such, rather than from one country. Those economies therefore benefit from association with stronger ones.

Notwithstanding, the Eurobond idea has not been progressed and there are mixed views about the possible benefits.

The Joint Committee heard divergent views: that Eurobonds will not work because the models being considered give rise to moral hazard issues (the mutualisation of debt issue).

The Joint Committee heard that because only the first 60% is safe (the SGP and Sixpack and Twopack threshold), the balance is regarded by traders as “toxic”, so this is where a debt redemption fund would come into play. An additional problem, highlighted to the Joint Committee, is that the mechanisms involved in preventing sovereign yields going over a certain value, can be abused.

Debt redemption mechanisms require a significant transfer of sovereignty for as long as they are active, because they require binding consolidation agreements and control powers, as well as the mutual commitment of participating member-states. For this reason they can be unpopular. It was argued before the Joint Committee that the commitment involved in debt redemption mechanisms could result in less need for financial assistance through the ESM and unconventional monetary policy measures.

The Joint Committee heard the suggestion that instead of Eurobonds, a better solution to the risk of rising state borrowing costs would be to assign a banking license to a special purpose vehicle such as the ESM and use this as a de facto conditional lender-of-last-resort for sovereigns.

3.16 Ireland's Strategic Interest in EMU

The Joint Committee heard arguments supporting greater fiscal integration, however, dissent was expressed on the degree of such integration, particularly on the issue of complete fiscal union. A differentiated approach across countries was posited, one which would take into account the pace of recovery, fiscal positions and debt levels.

The Joint Committee also heard that the social stress of recent years cannot be ignored in any assessment of or support for closer integration. The view was expressed that support for closer integration from member-states will only be achieved if the social fabric can hold together and it may be that this is only possible if there is a policy change at European level, to create more stimulus.

On integration generally, the Joint Committee heard that Ireland's stance appears ambivalent. Ireland is a member of the eurozone. It is also in favour of EMU and the ESM, but it has not agreed to participate in enhanced co-operation on taxation measures. On tax harmonisation issues, Ireland continues to provide certainty for foreign investors in relation to its tax regime. In respect of Ireland's position on tax harmonisation, Ireland will face a trade-off with the further development of EMU.

During evidence the Joint Committee heard various views on how Ireland should proceed strategically in the EMU and the wider EU context. The Joint Committee considers that Ireland should work out a longer-term strategy and consider the risk and the downside of not having an economic policy that is compatible with the direction of the core European economy. Ireland has recapitalised and stabilised its banks and implemented the requirements of the Troika. The view was expressed that Ireland is in a strong position to advocate for developments at eurozone level, which other countries, due to their economic difficulties, may not believe they can do with authority.

The Joint Committee heard that Ireland must be prepared to fully engage and show a willingness to put in place the type of integrated systems that a functioning EMU needs, to ensure it becomes more stable and sustainable in the longer term. It is unlikely that Ireland can resolve its economic difficulties within the eurozone, without deeper economic and political integration.

The Joint Committee also heard that being a small country can be limiting and that Ireland needs to accept a certain amount of constraint in its choices: that there is a difference between real and nominal sovereignty, in the sense that a small country may get more of what it wants and needs when part of an alliance, but that this involves trading a degree of “nominal sovereignty”.

Due to vulnerability with regard to access to borrowing, Ireland may have to consider that complete recovery probably requires greater connection and integration: potential investors must be able to believe that Ireland will have access to official funding, should it need it.

The Joint Committee was advised that Ireland should position itself to exert as much influence as possible in shaping the future of EMU and Europe, and bearing in mind French and German preferences for a core or two-tier Europe. Ireland must be heavily involved at every ‘design’ stage.

The view was also put forward, that if Ireland cannot be strong, it must be clever: Ireland must look closely at how it can exert influence and power within a system that gives significant control to the “big animal” of centralised power.

The Joint Committee heard that as things change at European level, so too must things change at national parliament level. Reform in governance of Irish EU affairs and in domestic Irish affairs is required and that these reforms should go well beyond the level of change required at European level.

Ireland should also take an 'offensive' approach to dealing with the evolution of the EU: refining its stance on issues and policies and advancing its views coherently and consistently. It needs to be defensive too, against the worst excesses of European policy as well as its own internal failures.

3.17 Conclusions

The Joint Committee concludes that:

1. the eurozone was ill-equipped as a single currency union, which certainly curbed the ability of European leaders to respond effectively and may even have exacerbated the crisis and exposed serious flaws in the original design of the currency framework;
2. the crisis has spurred the eurozone to initiate closer integration of its financial systems and generally closer economic policy co-ordination across all Member States of the EU to ensure consistency and coherence and common purpose;
3. the current 'half-built house' situation regarding fiscal integration continues to make EMU vulnerable;
4. for the EMU to function properly there needs to be greater fiscal, financial and economic integration within the eurozone to match the monetary integration already achieved;
5. greater integration would strengthen the governance of EMU and give greater protection to the currency, however, at a cost of the transfer of some sovereignty;
6. a move against further integration may leave the euro vulnerable and could perpetuate fragmentation of EMU and lead to future crisis for the Eurozone;
7. as currently constituted the eurozone is a monetary union but not an economic or fiscal union. It has no income transfer system comparable to those which exist within member states;
8. with greater fiscal co-ordination being implemented, a case can be made for the establishment of a European central fiscal authority with

- its own fund, the ability to issue debt, carry out fiscal transfers, and have the right to monitor and enforce the regulations;
9. a formal lender-of-last-resort within EMU is desirable;
 10. any proposed increase in integration and centralisation will give rise to a need for greater democratic legitimacy and accountability;
 11. accountability mechanisms are provided for in the Banking Union legislation, but member states need to make sure that these provisions are used effectively;
 12. Ireland should consider its strategic position carefully in the context of any further treaty change;
 13. recent experiences show, that the time to adopt and refine crisis management tools, is long before one arises, or in this case before another one arises.

3.18 Recommendations

The Joint Committee recommends that:-

1. the role of the Houses of the Oireachtas be strengthened in order to counter-balance the implications of closer fiscal integration, that is, a move towards centralised (EU) control of national budgets, taxation and public spending, functions which are at the heart of sovereignty and independence;
2. all systems introduced on the progression on the path of greater fiscal integration must be democratically accountable;
3. the Houses of the Oireachtas make full use of the provisions provided to it in the Single Supervisory Mechanism (SSM) including regular engagement with Ireland's representative to the SSM;
4. the Houses of the Oireachtas should debate any changes to Ireland's policy directions in relation to tax harmonisation measures, as further integration in EMU may require difficult policy trade-offs;
5. at EU level a co-ordinated move away from the policy of austerity towards sustainable growth and job creation be instigated, in order to address this aspect of the Eurozone crisis;

6. Ireland should continue to seek retrospective re-capitalisation for its banks from the EU as a 'special case', as acknowledged in the June 2012 European Council Conclusions;
7. the issue of Eurobonds be considered and debated at EU level and should be debated in the Houses of the Oireachtas to achieve a Irish Parliamentary position on the issue;
8. a single Europe-wide deposit guarantee system will be a necessary component of complete Banking Union;
9. the introduction of a central fiscal fund to deal with future asymmetric shocks should be strategic objective of the Irish government.

4: Democratic Legitimacy and Accountability: EMU and the EU

4.1 Introduction

This part of the Report examines the issue of Democratic Legitimacy and Accountability and the EU, as this theme emerged strongly during hearings with witnesses. The summary below sets out a narrative of the issues discussed under this heading; conclusions are drawn and recommendations made in that regard.

4.2 What is Democratic Legitimacy and Accountability?

Democratic legitimacy, in its simplest sense, describes the authorisation of a person or entity, by another person or entity, to represent them. It is a two-way commitment involving the participation and continuing engagement of the citizen on the one hand, and responsiveness to the citizen and the performance of the representative, on the other.

Accountability – the assumption of responsibility for actions and decisions – is a key component of democratic legitimacy. It is the obligation to report, explain and be answerable for consequences.

The European Union, as an entity, has never scored high in any of these respects: there has been a historic scepticism and a reluctance to cede power. In recent times, its reputation is further weakened, on performance grounds, in light of the economic crisis. Now, in the aftermath of the crisis, the initiatives being prescribed, as well as decision-making procedures, are being questioned again as to whether they meet criteria for democratic legitimacy and accountability.

4.3 Background

Professor Brigid Laffan defines the EU as *"a group that is more than an international organisation but less than a state. It cannot mimic domestic political structures but it can improve the democratic fabric of its systems"*. She believes that that the EU will become more politicised, as the EU exercises greater authority.

In the 2012 report, "Towards a Genuine Economic and Monetary Union" the EU Council states that democratic legitimacy and accountability are particularly essential for the effective functioning of EMU within the broader EU context.

Against this backdrop and in the context of the challenges posed by tighter EU control of economic policy in the aftermath of the crisis, the Joint Committee considered Ireland's position in the European Union with regard to the issues of democracy and political union inherent in the closer economic integration envisaged for eurozone countries and for all member states in general.

4.4 Democratic Legitimacy: the Case for Reform

The Joint Committee heard from witnesses the view expressed that the coming years will be critical for the EMU project. The financial crisis and deep European recession that followed have highlighted and exacerbated a lack of democratic legitimacy which are inherent in the design of the design of the EU project.

There is now, a trend towards greater EU integration and a framework of economic governance in response to the economic crisis. The greater transfer of power from national level to European level, inherent in the new system of economic governance evolving in the EU and particularly in the eurozone, calls into question the role and effectiveness of current EU decision-making and legislative processes; and the ability of the EU to act quickly and decisively, while maintaining the core values of democratic legitimacy and accountability.

The Joint Committee also heard a view that the European Parliament is weak in holding various EU institutions to account. The move towards closer integration of fiscal and monetary policies is progressing without enough consideration of democratic principles.

As stated earlier, concerns regarding a lack of democratic legitimacy have been exacerbated in the aftermath of the economic crisis were expressed. There is a public perception of a democratic deficit across most European institutions and a lack of consent for the austerity measures imposed on some member states, including Ireland.

4.5 The Citizen and the EU Institutions

On a basic level, the Joint Committee heard that there continues to be a low level of public understanding of how the EU works, and the widespread loss of public trust in its institutions. Eurobarometer Surveys results from the six largest Member States from 2013 recorded a collapse in trust which may reflect the unpopularity of the measures taken to address the crisis and the weaknesses in economic governance in Europe that were, in part, to blame for the crisis in the first place. While there had been continuous fallout of voter turn-out at successive European elections, voter participation stabilised in 2014.

The Joint Committee also heard diverse opinion on the issue of closer EU integration. At one end of the spectrum, the view that the solution is a federal Europe: at the other end, the belief that further integration constitutes authoritarian new-liberalism: a regime where economic policy is no longer open to political debate along traditional left/right lines, and where power is transferred from elected governments to unelected bodies such as European Central Bank (ECB) and the European Commission.

The question therefore arises on the timing of and support for greater EU integration among EU citizens, if the perceived and real deficiencies in democratic legitimacy and accountability are not addressed, given the low levels of public trust in the EU Institutions and a general lack of understanding of the mechanics of the EU.

4.6 Effective Democratic Oversight of EU Institutions

As referred to earlier, the Joint Committee heard that the economic crisis has weakened support for Europe's institutions and policies. The

measures taken to tackle the crisis have had some success; but it is the perception that decisions were made and action taken on an ad-hoc basis without due democratic oversight and accountability, which had and continue to have significant impacts on member states.

The aftermath of the crisis is also leading to economic integration.

In this context, the current role and powers of both the European Parliament and national parliament to provide sufficient democratic oversight of the EU Institutions are questioned.

4.7 The European Parliament

The Joint Committee heard that notwithstanding, the additional powers of the European Parliament, resulting from the Lisbon Treaty particularly as co-legislators with the Council of Europe, it appeared to be by-passed by EU leaders when making decisions 'in crisis mode'. These decisions affected the lives of ordinary EU citizens, it is argued, without due democratic oversight by elected representatives.

The Joint Committee also heard that other developments have progressed along non-legislative lines, for which democratic accountability is difficult to achieve. For example, the implementation of the European Semester and ex-post monitoring to see if measures are being properly implemented. These are more again executive-driven and less accessible to democratic processes.

The Joint Committee heard that accountability will always be a challenge to the EU and in particular for eurozone countries because of the complexity of structures, the technical nature of many of the activities, the hierarchy of accountability and the different cultures of member states.

In terms of wider representation, the Joint Committee considered the concept of a bicameral parliamentary system, where the European Parliament would become the lower chamber, directly elected by citizens

and the upper chamber would represent member states and would be what the Council of Ministers is today. An alternative recommendation was that the upper house would comprise delegates from national parliaments.

The view was also put forward, that the EP and its Committees must have more focus on ensuring implementation of agreements, in addition to overseeing legislation.

4.8 National Parliaments

With regard to strengthening the role of national parliaments, the Joint Committee heard that there is scope to enhance cooperation between national parliaments of Member States, not just for formal, but also informal cooperation. It was felt that more work needed to be done at national level on the consideration and scrutiny of legislation and feedback into the work of EP committees, for instance.

The Joint Committee heard that 'the principle of subsidiarity' is a good example of democratic legitimacy, but that using it to advance a country's particular interests was complex. The Joint Committee heard that member states should act almost like lobbyists within the process: that it was more effective to meet in an informal way to progress specific issues. In this respect better informal contact was called for, as well as more formal ties between national parliaments and European Parliament committees. It was heard that national parliamentarians can attend some EP committees in an effort to advance domestic interests.

The issues of contact and communication are relevant to the EP too, because it does not have a simple majority-minority system. The balance varies from issue to issue which gives the opportunity for different coalitions. It was stated that member states need to work constantly on forming alliances to further their interests. They must ensure that adequate resources are available to finance the necessary expertise in this regard.

A recurring theme during the Joint Committee sessions was the under-use of, and lack of significant communication between national parliamentarians with MEPs, as well as a lack of dialogue between Houses of the Oireachtas staff and the staff of the Irish permanent representation in Brussels, perhaps reflecting the traditional executive/parliamentary divide.

The Lisbon Treaty attempts to address the democratic deficit by drawing national parliaments more closely into the European process. Politicians need more time to deal with EU issues in addition to their domestic workload. However, domestic issues including the contest of national elections are pre-eminent and as long as this is the case, European issues are sure to remain a secondary consideration.

4.9 Interparliamentary Co-operation

Formal and informal co-operation of national parliamentarians of the EU does take place among themselves, and collectively with the European Parliament. It was heard that democratic legitimacy and accountability could be improved by new forms of co-operation between national parliaments and the European Parliament. For example the Fiscal Treaty provided for the establishment of an inter-parliamentary conference on budgetary matters comprising representatives from national parliaments as well as from the European Parliament. This has now been established.

Currently the Conference of Parliamentary Committees for Union Affairs of Parliaments in the European Union, COSAC, exists as the primary forum for interparliamentary co-operation of EU matters. In view of the need for greater democratic legitimacy and accountability COSAC could further define its role and become a more effective forum for interparliamentary co-operation, in order to increase the value of its contribution to and engagement with the EU institutions.

National parliaments could further explore the possibility of greater co-operation to maximise the effective use of their powers under protocol 2, that is, as guardians of the 'principle of subsidiarity'.

The view was expressed that the 'political dialogue' mechanism, which provided for communication between the EU Commission and member states on the substance of legislative proposals is under-used and needs to be strengthened.

4.10 "The Politics of Constrained Choice"

The new systems of governance broadens the responsibilities of representatives to embrace the interests of all member states, as well as their own national interests. At national level, budgetary and economic autonomy has been reduced, as has the freedom of governments to respond to their electorates without consideration of the wider European picture. With greater integration, there can be no hiding from this. National parliaments will have to find a way to nurture a change of public attitude and perspective and engender an understanding of this new rationale.

It is crucial that EU issues are integrated with domestic issues in the agenda of national parliaments. Ireland has tended to scapegoat the EU for unpopular measures in the past particularly in the context of the transposition of EU Directives.

4.11 The European Commission

The European Commission is appointed every five years after nominations from member states are considered by the European Council and the European Parliament. There were suggestions that democratic legitimacy would be better served if nominations were made by the European parties and that efficiency may be better served by having fewer Commissioners, as the voting mechanism complicates the decision-making process.

The Joint Committee considered the possibility of the direct election of the Commission President. Such reforms would require treaty change.

On the issue of EU Commissionerships, there is growing consensus that it is not appropriate for each country to have a Commissioner: there are not enough portfolios to go around. There is a view that Commissionerships were 'made up' to facilitate member-states.

The Joint Committee also heard the view that there needs to be greater politicisation of the European Commission, notwithstanding its independent role to act as guardians of the treaty and to act, in general, in the greater European interest.

4.12 Leadership in the EU

"Who do you speak to when you want to talk to Europe"?, a question once posed in relation to the perceived lack of leadership in the EU.

The Joint Committee considered the issue of leadership and the perception that nobody is really in charge of the EU. The concept of accountability goes hand-in-hand with that of leadership. This notion, which became rooted during the economic crisis, has fed into concerns about lack of accountability.

The Joint Committee heard that the close bi-lateral relationship between Germany and France was considered to have undermined the EU institutions and made decisions affecting all European citizens, and had driven the agenda at the EU Council and that the EU Parliament had effectively been ignored by the two member states.

The Joint Committee also heard that consideration should be given to the amalgamation of the roles of President of the European Commission and the European Council.

4.13 Problems of Meaning and Interpretation

Legitimacy depends on public understanding of what is happening and this becomes an issue of democratic accountability, as if you do not understand it is difficult to participate.

The Joint Committee heard about the workability of the complicated rules and regulations contained in, among others, the Twopack and Sixpack measures, as people cannot understand the complexities of complicated EU rules and regulations.

This lack of comprehension creates risk for the legitimacy of the process. The lack of clarity regarding meaning and interpretation of EU policy, may explain why there was little detailed analysis of elements of EU policy and a lack of specifics in recommendations about changing or improving the system.

The Joint Committee heard also that there may be a broader context: there can be no true analysis without clarity of interpretation and understanding. This affects the ability of politicians at national level to take effective action.

4.14 The Houses of the Oireachtas and the EU

The Joint Committee heard the need for more in depth Oireachtas scrutiny of EU legislation. In addition to the provisions of the Lisbon Treaty to review EU proposals under the principle of subsidiarity and proportionality, the Oireachtas can also contribute to the political dialogue on the substance of the proposals. Although it has been acknowledged that the standard of scrutiny of EU legislation has improved over recent years there is considerable scope for further improvement. The Joint Committee also heard there was criticism of the standard of scrutiny already being carried out: that directives and regulations come before Oireachtas Committees at the last minute and are passed with inadequate attention to detail. Moreover, there are delays in implementing

directives. There was consensus that Ireland is reluctant to use the leverage already granted to national parliaments.

Ireland should be more proactive in shaping EU legislative proposals at the earliest possible stage; at the Communication and Green paper stage.

4.15 Conclusions

The Joint Committee concludes that:

1. there is a degree of democratic deficit in the EU, which has been brought into focus by the response to the crisis;
2. public disquiet and some social unrest over austerity measures have highlighted the need for more public and political discourse on EU policy;
3. there has been a loss of trust and confidence in the functioning and democratic legitimacy of EU institutions;
4. the sheer complexity of the relationships in the EU model causes confusion in the general public;
5. national parliaments need to play a greater part in the development of the EU policy, the scrutiny of its legislation and the implementation of its policies;
6. in terms of representation in the European Parliament there are concerns that smaller member states do not enjoy the same representation as larger ones do, the Joint Committee notes the concern that Ireland is not represented on all European Parliamentary committees;
7. if there is a wider context for confusion about the meaning of policy and if politicians are unsure about the interpretation of a detail of policy, then they will be unable to engage effectively with it: whether to accept it or seek to change it;
8. a corollary of that may be the slight sense of inertia that characterised some of the contributions of Committee members: there was very

little consideration of finer detail and few concrete suggestions on possible action to change things for the better.

4.16 Recommendations

The Joint Committee recommends that:

1. Ireland has an open debate on its own strategic objectives within the EMU and EU;
2. to achieve its strategic objectives, Ireland must have a clear and well defined and co-ordinated policy objectives;
3. Ireland must be a leader, not a follower, in policy debate and be heavily involved at every 'design' stage of future EU policy development;
4. Ireland position itself to exert as much influence as possible in shaping the future of EMU and Europe, bearing in mind French and German preferences for a 'core' or 'two-tier Europe';
5. a re-calibration of the 'European Social model' be undertaken in the context of overall EU policy development;
6. the role of the Houses of the Oireachtas in EU affairs be expanded, particularly in setting Ireland's overall strategic direction and policy objectives in the EU in order to address the democratic deficit;
7. the role of the Houses of the Oireachtas be agreed and formalised in the context of the EU Semester procedure, to counter-balance greater EU involvement in traditionally sovereign competencies;
8. additional resources and time be allocated to enable greater engagement by the Houses of the Oireachtas in a wider EU remit and to ensure efficient scrutiny of proposed EU legislation;
9. more enhanced and formalised engagement between the Houses of the Oireachtas and with Irish MEPs, representatives of the Committee of the Regions and the European Economic and Social Committee be developed;

10. national parliaments must be further empowered in terms of input into EU policy development;
11. steps be taken to improve public awareness and understanding of EU policy. National and EU communication strategies should be developed and implemented, in order to improve public awareness and understanding of EU policy in particular in the context of EMU policy;
12. the policy of subsidiarity must be respected in all EU policy decisions and emerging legislative proposals in view of the diversity of 28 member states;
13. inter-parliamentary co-operation must be strengthened and enhanced in the context of EU policy development;
14. further development of the 'political dialogue' or the 'Barosso initiative' be undertaken, as this procedure is currently under-used by national parliaments generally;
15. the question of representation in the European Parliament should be re-examined to allay the fears of smaller Member States.