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Banking and Fiscal Union in Europe: a Solution or a Trap?*

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This paper addresses the insoluable conflict between the letter and spirit of the Lisbon Treaty/TEU 2009 on the one hand and the not so creeping supranationalism, that has emerged from a series of crisis-manging measures at the Community level in 2008-2015, on the other. While the TEU is firmly grounded in intergovernmentalism, the series of ad-hoc innovations translate into an ever growing supranationalism. The latter is expressed in a programatic fashion inthe Juncker Note of February, 2015[2]. The latter implies a qualitative change in the nature of the EU as we had known before, which was known to be a community of nation-states.

The global financial crisis of 2007-2009 and the still looming debt and confidence crises of the EU have triggered a series of measures aimed at pre-empting the worse case scenarios and creating an up until now non-existent fire fighting mechanisms at the Community level. At the end of the day, federalist arrangements, that have seemed to stand no chance of implementation even a decade ago, have become reality by now. *Banking and Fiscal Union/BFU is a done deal* – agreed upon at the December 13-14 2012 Council. The only open question is the precise mechanisms of their implementation on the ground.

I. Banking Union is no longer just a Dream

Le tus confine ourselves to listing just the most significant amongst the changes, which are new and *have become constitutive features for the new structure of EMU.* First and foremost: the ECB has developed into a fully-fledged central bank for the Euro-zone, including the function of *a lender of last resort.* The unlimited liquidity provision since September, 2012, reinforced by the outright monetary

* Contribution to the volume: FEHRMANN,Th.ed: *Nationalstaat un Europaeische Integration: eine Bestandaufnahme.* Baden-Baden: Nomos Verlag, 2015.

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2 *Juncker, J.-C./2015/:* 'Preparing for the Next Steps on Better Economic Governance int he Euro Area- *Analytical Note.* Brussels: Informal European Councul, 12 February, via: ec.europa.eu/priorities/docs/economic-governance-note_en.pdf/- retrieved: 14 February, 2015.

transactions, and more recently by the big stimulus package of January, 2015 are the milestones. These are complemented with targeted purchases of government bonds of ailing states. The above listed steps have fundamentally re-tailored the workings of an originally entirely de-politicized monetary authority. If the original ECB mandate was strictly confined to securing price stability in the euro-zone, and was supposed to be indifferent to what is happening at the „regional" level[3], meaning the economies of individual member-states, this has been broadly re-interpreted in practice/though not inthe statutes or inthe EU/. Currently concerns about the level and intensity of economic activity, employment concerns, state of public finances in large member-states all count among the real, openly declared priority concerns. All in all, both the self-interpretation of the mission of ECB, and even more the actual conduct of affairs, has become increasingly akin to the FED. The latter is a central bank of a federal state, which the European Union is certainly not.

Let us note: as long as the ECB is indeed willing to provide 'unlimited liquidity' to the system, whose actual size is known only retro-actively[4], its macro-economic role far exceeds that of the European Stability Mechanism, the permanent rescue mechanism of the Euro-zone. The way how the pre-fixed sum of 500 bn Euros/out of the subscribed capital of 705 bn Euros/ can and should be spent has beeen a subject of vivid – legal, economic, and political – controversies. However the latter sum – equalling to about three years of Community budget, or half of the Pluriannual Financial Framework for 2014-2020 – is dwarfed against the involvement of the ECB, whose size we may only guess.

Recall: at the time of setting up the ECB it was made explicite[5]: the Bank has been insulated institutionally from the usual checks and balances exactly in order to keep it at bay from any concievable fiscal functions. The latter is known to be at the heart of any democratic deliberation process.[6] Therefore if and when the ECB enters in the slippery slope of re-distributing costs and benefits across member-states, be that via bailouts of governments or commercal banks, or through targeted liquidity provision to stimulate growth in certain members/but not in others/, the need for political accountability and also of ex ante transparency of its operations

3 Le tus note: central banks of large countries, as of Brazil or India, also do not conduct monetary policies along the cyyclical or political needs of their federal states. Thus this should not come as an overly rigid or abstract proposition, if we consider currency union seriously, as was the case in say Austria-Hungary.

4 From the theoretical perspective this is also questionable. As long the ECB does not give up formally its two pillar strategy, the ex ante calibration and management of money supply/M3 counts among its major indicators of evaluation. Thus it can not be calibrated at will, according to the needs of the day and their subjective assessment by top bankers. More ont hat in the book cited in the next footnote.

5 ISSING,O. – ANGELONI, A. – GASPAR,V./2004/: *Decision-making at the European Central Bank -2d, revised edition.*Cambridge/UK – New York: Cambridge University Press.

6 This is the famous 'no taxation without representation' principle ever since the American War of Liberation.

emerges in a qualitatively new way. The tricky question of 'who pays what and in exchange for what and when' can no longer circumvented.

A second, no less weighty change has been the investing the ECB with the role of *joint banking supervisory agency.* While the latter – unlike the former modifications – was not prohibited by its mandate, nor by the concrete stipulations of the Treaty on the European Union/TEU, the whole spirit and structure of the Lisbon Treaty was revolving around enhanced inter-governmentalism. Reacting to the French, Dutch and Irish referenda, all rejecting the draft Constitutional Treaty, the signatories agreed to 'de-constitutionalize' the Union, while maintaining the accomplishments of preceding decades.[7] Put it differently: dropping the symbolism and dropping the political was the crux of the matter.

Against this background vesting the ECB with prerogatives of of the sole joint regulator of systemically relevant major banks, with powers of pre-emptive intervention, was *anything but trivial.*For one, many a country operates a separate bank supervisory agency, not least including the United Kingdom, with deep capital markets and long-standing experiences in eminent banking. For the other, central banks may, and often do, get into *conflict of interest situations* vis-a-vis major players on the money markets in general and big commercial banks in particular. Furthermore: intervention and bail-out operations frequently may, and indeed do, involve fiscal costs, often of macroeconomic significance, to be born by taxpayers.[8] Thus there is nothing compelling to locate this function to an organ having no impact on taxes and no embeddedness in the political structure of checks and balances, including transparency and accountability. It is hardly a secret that the final arrangement, excluding most European banks from the joint supervision, is an outcome of tough political bargain, rather than any broader theoretical consideration.[9] This is, among others, the best guarantee against large-scale cross-border redistribution of bailout costs. Furthermore it ensures that no subsidy shopping takes place at the level of large financial institutions.

Third, the banking union is further strengthened by the *Single Resolution Mechanism/SRM,* addressing the issues of cross-border failures of banks, which is a truly hot potato. It is effective from January, 2015. The organization is to be set up in full until January, 2016, with a crew of 250. They are to manage 55 bn Euros, or about a half of an annual budget for the Union. The SRM has particularly strong prerogatives, including the right to pre-empt and supersede national regulators,

7 *Reh,C./2009/: '* The Lisbon Treaty:de-constitutionalizing the European Union?' in: Journal of Common Market Studies, vol.47.no.4.pp 625-650.

8 Inthe case of Ireland bank bail-outs translated into a tripling of public debt/GDP ratio in 2007, around 37 pc of GDP to no less than 91.2 pc by 2010 and further increasing to 123.7 pc by 2013. This is putting Ireland in the same league with Italy, Portugal and Cyprus, according to ECB: Statistics Pocket Book, September, 2014,p.46..

9 *Kudrna,Z./2012/:* Cross-border resolution of failed bank sin the EU after the crisis: business as usual? In: Journal of Common Market Studies, vol.50.no.2., pp283 – 299.

should the latter act belatedly or 'without the necessary resolve'.[10] Even though the SRM is being funded by the banks themselves, its supra-national prerogatives are crystal clear. It is hardly by chance that the UK government, representing the interests of the City of London, has not joined in, although this option was open to all non-Euro-zone members. Making use of this option Hungary did join both legs of the BFU. In terms of banking it was not really a matter of deliberation: once banks in neighboring Austria and Slovakia are being protected by the umbrella of the BU/SRM/ESM, while in case of abstention Hungarian commercial banls would not have been. Under these circumstances it would not take even a rumor to trigger major capital flight from Hungary. This is certainly not the case in the United Kingdom.

True, a series of countervailing measures have also been earmarked. First, the principle of national funding of bank bail-outs was adopted. Second, the SRM is not funded by the taxpayers either. Third, the European Supervisory Board is separated from the daily, routine activities of the ECB, thus trying to minimize conflict of interest situations. Fourth, the Board of the SRM is to be approved by the European Parliament, thus ensuring formal political accountability in operations on par with the rest of ECB.

These measures notwithstanding it is hard to overlook the very resolute move towards a more uniform and more centralized decision-making, the growing cross-border burden-sharing, and even the *increasing intertwining* among fiscal and monetary, banking and regulatory *functions*. Such intermingling, especially if unplanned and not clearly intended, are customarily treated with great suspicion in the broader literature in economics, public administration and finance alike.

Given that the new arrangements are yet to take their final shape at the time of writing, further that practical implementation on the ground may also bring major modifications in its *modus operandi,* it is perhaps pre-mature to offer an overall assessment of its outcomes. However, it is hard to overlook, that the ever closer possibility of a Grexit[11] and the fragile situation of the French, Spanish, Portuguese and Italian economies and banks may sooner create an actual stress test for this arrangement than its evolution would eventually warrant. Contested issues, currently swept under the carpet – primarily the basic question of who pays what and when – are likely to show up and burden the new mechanisms of decision-making. The relatively upbeat results, coming from the largely speculative stress test, conducted in the European banking Authority in october, 2014, showed 25 of those biggest of

10 The flow of relevant official documents are made available through the website: www.ec.europa.eu/finance/general-policy/banking-union/single-resolution-mechanism/index-en.htm/ retrieved on 14 February, 2015.

11 *Visvizi,A./2016/:* Greece and the troika inthe context of the Eurozone crisis. Forthcoming in: Magone,J. – Laffan,B. – Schweiger,A.eds: Core-periphery Relations inthe European Union: the Politics of Differentiated Integration inthe European Political Economy. London: Routledge, forthcoming

the banks failing, out of the tested 123, spread across 11 countries. They registered an overall shortfall of 24.6 bn Euros, all preceding the eruption of the newest Greek crisis trigered by the Syriza government's rejection of negotiating with the troika and accept a third bailout package. The stress test, conducted earlier, included among the failed financial institutions all major Hellenic banks.[12]

II. Is Fiscal Union Looming?

The term 'fiscal union' is a polite way explaining how and why a much more centralized and uniform management of public finances, policed by the European Commission and the Eurogroup of finance ministers could and should bring about structural reforms and overdue adjustment in highly indebted, still rule-non-abiding markets, primarily though by no means exclusively, in the Mediterranean.

Conventional wisdom, built into the mandate, procedures as well as in techniques operating the European Monetary Union[13] would find the *unification of fiscal policies*, and especially of procedures of adopting those not only superfluous, but *positively harmful.* If for no other reason, because of the need to adjust to regionally and nationally different challenges. This is the straightforward answer to the traditional objection to a monetary union inthe lack of a political union: different business cycles are being managed by different national fiscal policies. They are capable of reacting to asymmetric external and internal shocks, whikle structural measures address macroeconomic imbalances, also within each country. Meanwhile price stability is being guarded by the de-politicized single monetary authority, with the sole mission of safeguarding and protecting this common accomplishment at the all-Union/Eurozone level.

It is bordering with the platitude to observe that the global financial crisis of 2007-2009 has shaken the credibilityof EMU as a waterproof financial architecture, able to withstand any external shock. While some countries, like Luxembourg, Estonia, Finland were faring quite well, others, especially in the South, but also Ireland and France, could deliver much less well. As the troika of Commission, IMF and ECB, in theory a least politicized group of crisis managers, have gained prominence in micro-managing the slump in several EU states, doubts about the wisdom and efficiency of their conduct of affairs multiplied in the academe and the broader public/including the streets/ alike. While a detailed analysis of the causes, consequences and outcomes, as well as review of the contentious literature re-

12 In: *Wall Street Journal,* 26 October, 2014.
13 *De Haan, J. – Osterloo,S. – Schoenmaker,D./2010/:* European Finacial Markets and Institutions. Cambridge/UK – New York: Cambridge University Press.

quires a separate analysis[14], currently we confine ourselves to major aspects of fiscal policy co-ordination only.

In the related analytical literature we find two fundamentally different trends of thought, which seem to agree only in one aspect. Namely that the EU level supranational set of rules, including sanctions, governance mechanisms, and incentives/disincentives have proven largely ineffectual all across the past 10-15 years, both in pre-empting and punishing misdeeds.[15] That is: it was not the crisis which provoked inefficiency, it has only uncovered pre-existent and demonstrable feebleness.

However, professional consensus seems to end at accepting this point. The interpretation goes in two, diametrically opposed direction. Adherents of the 'old school' blame national reactions in case of failures. They point to the unquestionable fact that EMU membership has not universally generated depression and instability, as in Greece. It is those who have dodged overdue structural reforms who primarily pay a price for their omissions. In this line of thought, to use economic jargon, it is not asymmetric shocks but asymmetric behavior of national fiscal policies/against the spirit and letter of the jointly adopted stability pact/ which is at the root cause of troubles. Those policies tended to dodge promised reforms for over a decade at good times/especially between 2000 and 2007/, and also regularly circumvented the stipulations of the common fiscal framework, both in good times and bad.[16]

The alternative view, originating with the Keynesians, but shared by a much broader public opinion, and gaining ever more professional acceptance as well, blames the misconceived common financial architecture in general, and particularly its open disregard for activity and employment considerations as well as its indifference to national diversity in terms of economic structure, level of development and of the business cycle.[17]

It has been ironic to observe in the past years that the second view, aiming at a fundamental re-arrangement of the constitutive elements of EMU's architecture has been gradually, but definitely gaining ground at the initiatives of precisely those agents, who – abstractly seen – could have been expected to be the major guardians of status quo. In the preceding section mention has already been made of the highly innovative actions by the ECB President *Mario Draghi*, largely re-interpreting the original mandate of the Ban. This happened through outright actions, like entering

14 *Csaba,L./2015/:* On thecrisis of the Euro-zone: Failed conception, failed implementation or failed crisis management? In. McGowen, J. – Dallago,B,.eds: A Global Perspective on the European Crisis. London: Routledge.

15 *Ioannou, D. – Stracca,L./2014/:* Have the euro area and EU governance worked? Just the facts. In: European Journal of Political Economy, vol.34.no.3.pp 1-17.

16 *Boltho,A. – Carlin,W./2013/:* EMU's problems: asymmetric shocks or asymmetric behavior? In: Comparative Economic Studies, vol.55.no.3.,pp387 – 403.

17 *Blankenburg,S. – King,L. – Konzelman,S. – Wilkinson,F./2013/:* Prospects for the eurozone. In: Cambridge Journal of Economics, vol.37.no.3., pp463-477.

the government bond market, prohibited by the original ECB mandate as a form of monetization of debt. But it also happened by passive acceptance:, not least by volunteering for some non-trivial assignments and responsibilities with considerable fiscal implications. The parallely ongoing continuous blaming of the German government for all ills across the European Union has also beein instrumental in bringing about a series of innovations, which translate in official parlance to a 'fiscal Union'. In reality, this is a customary overstatement, reflecting ambitions rather than realities.

Let us note: most of the innovations were born out of ad-hoc deliberations, dictated primarily, if not exclusively, by the need to act swiftly and to do so in a politically respectable fashion.The latter implies the need to sell the bargain to different domestic audiences with opposing expectations. Therefore it would be hard to look for – and even harder to find –a secret master plan that would follow the once dominant logic of German *Ordnungspolitik und Ordnungsdenken* in action on the ground. In reality, by and large the opposite seems to have been the case.[18]

As discussed inthe preceding section, the Lisbon Treaty/TEU 2009, reacting on three compelling national referenda defying symbolic supra-nationalism of the Constitutional Treaty, has been targeted to re-inforce the role of national governments in managing their public finances. Therefore it only formalized, but obviously nottextended, pre-existing forms of *non-binding fiscal co-operation and surveillance*, such as the Broad Economic Policy Guidelines, the Stability and Growth pact, as re-interpreted in its 2005 edition, and the Stability and Convergence Programs.

Meanwhile the tremors of the 2008-2009 global financial crisis have brought the mostly known – but hidden – weakness of the architecture based on voluntary rules abiding behavior and ensuing compliance to the open. The mishaps included the doctoring of official statistics – not only in the case of Greece, but also in France, the Czech Republic, and Spain – but not less the wider than commonly presumed use of creative accounting – which items not to include in officially monitored general government statistics.[19] The root cause of all those mal-practices were obviously the delays, omissions and inaction on long overdue structural reforms, the minimalist approach to solid public finances, the disregard for sustainability con-

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18 Explained in great detail in: *Young,B./2014/:* German Ordoliberalism as an agenda-setter for the euro-crisis: myth triumps reality. In: Journal of Contemporary European Studies, vol. 22.no.3., pp276 -287.

19 It all started with the Frech excluding pension outlays, then was followed by the Hungarians excluding costs of large-scale highway building, the Poles excluding pension provisions from deficit, but not from debt, the Greek excluding military expenditures, to mention just the more appalling cases. Debates still go on if development assistance, research and development outlays and/or environmental protection costs should also be excluded. Soberly seen the basic accounting principle of full coverage has been damaged- for political and cosmetic reasons - more than once! By contrast, most small businesses would be heavily penalized in each member-state for attempting to replicate practices common in public finances.

siderations and the ensuing lastingly slow growth. *It is axiomatic that in a slow growth environment fiscal adjustment hurts,* and ongoing over-taxation and over-regulation perpetuates the slow growth scenario, which in turn makes balancing the budget next to impossible[20].

When structural imbalances have come to the open, often through co-incidental factors or out of domestic politickling, as in Greece, the ensuing panic has triggered capital flight and the financing of several countries has become questionable. The EMU architecture has proven insufficient to ward off the crisis, and the IMF had to be resorted to overcome liquidity and solvency problems, oftentimes in EMU members. This has called attention to the largely unfinished nature of EMU. The latter relates to economic *governance* – ability to act swiftly -, *size of the funds* to be mobilized in a crisis scenario, as well as the *enforcement mechanisms* that ensure that agreements are being served, *pacta sund servanda.* The latter has become particularly obvious in a series of non-compliance cases in the Southern member-states.

This is not the place to re-iterate the causes, sequence and complex – often competing – interpretations of the crisis proper[21], as we are concerned here with the ramifications of those for the joint European fiscal framework only.

The period since 2008 has witnessed a series of occasions where Community organs were lost in internal wrangling over competences, and whatever they did deliberate, it was deemed too little too late by the markets. Already the much smaller scale pre-emption of the liquidity crisis in Hungary in October 2008 foreshadowed the most important and disturbing insight. Namely that *the IMF could not be left out of the deal,* since they were the only ones able to mobilize large enough resources. Forming, on a temporary and ad-hoc base, what was later known as the troika thus re-organized the basics of economic governance in the EU. While Hungary could be bailed out by a 'mere' 20 bn Euros, Greece alone required, until February, 2015, 12 times as much. And yet another problem countries, like Latvia, Spain, Ireland, Portugal and Cyprus all were showing up with their respective problems and funding needs. Especially the 'Club Med' and Ireland required the swift mobilization of funds in degrees and forms unknown ever before.

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20 Long run statistics indicates that EU convergence to the US in per capita terms has come to a halt already four decades ago, in 1973, while inthe 1995-2007 period income levels decreased from 70 to 67.5 pc of the American level. In other words, Europes divergence is not attributable to mis-management of the finacial crisis, it has been structural. C fin more detail in: *Halmai,P./2014/:* Krízis és növekedés az Európai Unióban/Crisis and growth int he EU/. Budapest: Akadémiai Kiadó, chapter 3.

21 *Farkas,B.ed./2013/:* The Aftermath of Crisi int he European Union. Northampton/UK: Cambridge Scholars Publishing ; *Daianu,D. – d'Addan,C. – Basevi,G. – Kumar,R.eds/2014/:* The Eurozone crisi and the future of Europe: the political economy of further integration and governance. Houndmills- New York: Palgrave Macmillan.

The change inthe purely inter-governmental nature of fiscal integration has been re-inforced by setting up the European Stability Mechanism/ESM. The latter acts as a permanent rescue fund and is in operation since October, 2012. It manages 705 bn Euros subscribed capital, against the Pluriannual Financial Framework of 980 bn Euros for 2014-2020. The ESM is managed by a technocratic board, offers precautionary credit lines and also adopted a direct recapitalization instrument. It has already issued 2 year bonds in November, 2014 and similar instruments of 8 and 30 years maturity were floated in early 2015. The overall lending capacity of the ESM is 500 bn Euros. It is authorized to buy government debt in both the primary and secondary markets, as well as engage in direct and indirect re-capitalization of commercial banks.[22]

Finally the series of reform measures strengthening the *surveillance of fiscal discipline* and related national practices should be mentioned. These include the revised and strengthened Stability Pact, now termed as the Treaty on Stability, Coordination and Governance/or six pack/, and particularly its Fiscal Compact, the public finance part of it. The complex monitoring arrangements[23] are built on procedural norms/ the European semester/, and quantitative targets/debt ceilings and mechanic debt reduction plans/. These were all aimed at enhancing controls over profligate national authorities in the euro-zone. However, reality turned out to be different, with Italy and France flagrantly disregarding those stipulations not only in 2012-13, when conditions of a double dip recession might have warranted this, but also for the 2015-16 period. The possibility of fining them, with one of the main culprit, former French finance minister Pierre Moscovici in charge, does not sound as a realistic option.

From the *systemic angle* it is crystal clear, that the arrangements do follow a certain logic of their own. This is 'money for discipline only'. However, this is not the logic of the market/that allowed EMU to succeed inthe post-1999 period/. Nor is it a central bank of a federal state, which would call either for stringent no-bailout rules modelled on the USA, or further fiscal unification coupled with lavish financial transfers/along the model of the German *Finanzausgleich/.* In both cases a common policing agency is needed, with broad competences, but under tight political control and professional accountability to the public and legislation alike. The existing mixture falls short of it, while making clear steps towards supra-nationalism, as long any of the stipulations is implemented on the ground.

Let us be clear: the implementation deficit, just as in the case of previous arrangements, has been coded in the situation itself. The government of *AlexisTsypras*, of *Matteo Renzi*, of *Francois Hollande* have all but replicated similar, non-law-abi-

22 www.esm.europa.eu/index/htm provides regular information on its activities.
23 DG EcFin: Six pack? Two pack? Fiscal compact? A short guide to the new EU fiscal governance. In: www.ec.europa.eu, 26 July, 2013.

ding practices of their predecessors, especially at times of real difficulty. They continue to act under the constraints of the pre-eminence of domestic politics over commonly adopted rules of the game.

III. Perspectives for More Rules-Based Behavior in the EU

Talking about the crisis of the Union and its financial architecture borders with the platitude nowadays. This is all the more so, if we adopt the customary journalistic-bureaucratic standard of measuring outcomes on the originally stated objectives, disregarding the often fundamentally changing conditions of achieving those. Our critical assessment of the state of banking and fiscal union does by no means imply complacence or a negativistic/Euro-skeptic attitude.

The clue to any solution is it the following. We need to acknowledge the historic specificity of the politico-economic-legal nature of the European Union, which is an outcome of decades of evolution. As such, it transcends all conventional concepts in each of the individual, compartmentalized disciplines. The EU is not a nation state, not a federation, not even a confederation. But it is definitely more than a free trade area coupled with a customs union and some external trade policies. It is a true currency union, inthe lack of political and a fully fledged transfer- and fiscal union. It is not an independent subject of international law, still the European Court of Justice/ECJ may issue rulings taking immediate effect in the member-states, without a clumsy transposing procedure. The ECJ can overrule actions taken by sovereign governments, as the British are no slow to complain about.

Academics in all disciplines struggle with the interpretation of this creature escaping the established cages and categories of each of the fields. Both analytical-descriptive assessments[24] and more normatively concieved treatises[25] highlight: a non-state can not and should not be measured – or measure itself – to a federal state like the USA or Switzerland, or indeed any similar structure. The nature of legitimation, as well as the reality of diverse polities, diverse economic systems and cultures of the constituents render the - otherwise natural and understandable – inclination to standardization, unification and across-the-board harmonization futile, actually a non-starter now and inthe forseeable future alike.

Furthermore: it is anything but surprising to observe the primacy of domestic balance of forces in established democracies. Indeed, international experience from Hungary to Greece, and from Vietnam to Iraq, is indicative of the inherent limitati-

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24 *Bellamy,R./2013/:* An ever closer union across the peoples of Europe: republican inter-governmentalism and *demoicratic* representation within the EU. In: Journal of European Integration, vol 35.no.5., pp499 – 516.

25 *Abelshauser, W.*/2013/: E pluribus unum? In: Zeitschrift für Staats- und Europawissenschaften, vol.11.no.4., pp466 -484.

ons of intervnetions from abroad, even if those include military and not purely financial means.

Likewise it is an established insight in many disciplines, from psychology via public administration to economics, that only those rules work lastingly and effectively of the ground, which have been internalized by those who are to play along them. Else circumvention, dodging, reinterpretation even of the simplest and clearest concepts, in order to fit the needs of the situation, and many other customary forms of opportunistic behavior are to prevail.

The EMU has emerged, from the very outset, as a club of gentlemen. In other words, it has always been intended to be a Community of the like-minded, governed by shared values and common norms, joint objectives. If this holds, that per se produces a fair degree of concerted deeds, up to the very point of common action, even in the lack of formal, oppressive enforcement mechanisms and related deterrence. Indeed, it is not fear of sanctions, rather than the internal conviction and ensuing willingness to do the right thinks for their own sake, which becomes decisive. The latter is the triggerer of most actions, inthe positive and abstention from wrong-doing in the negative, alike. *This is the only avenue open* for and among mature persons, just as much *among mature democracies,* constituted of and managed by such individuals.

In order to arrive at sensible and practicable rules, open, straightforward discussions and the ensuing emergence of first professional then subsequently political consensus is required onthe fundamentals, while allowing for the disagreements on the detail. This is the once much appreciated practice in many countries, known as *Grundkonsens.* The latter seem to have been around at the time of launching the EMU and also in most of its phases of implementation, often through learning by doing. Buti t seems to have evaporated since then. Establishment of the BFU in 2012-13 thus may be interpreted as a heroic attempt to revert things, getting them back to track. But the cart is put in front of the donkey.

In short: it should be obvious even from our rudimentary account of major events and the ensuing changes that these have followed *a myopic politico-bureaucratic logic.* In this framework the top-down approach as well as thepre-occupation with sanctions, disciplining and enforcement are the formative features. This is not a fault, this is integral, crucial, inevitable. By contrast, the broader approach shared by the series of applied social science disciplines referred above is based on a bottom-up approach. It is the internalization of joint objectives by the players themselves which matters at the end of the day.

Lacking the will and/or ability to comply, whatever different reasons lay behind that inthe instances of France, Hungary, Greece or Italy, inevitably translate into dodging the broader objectives, i.e of major structural adjustments. And even in the cases when nominal, short term targets are temporarily met, usually owing to one-off measures and fiscal cosmetics, *the purpose of the entire exercise, i.e attainment* *of sustainable public finances, is regularly being missed.* The devil, exorcised by the short-term one-off measures, returns through the backdoor, when problems swept under the carpet prop up again, for instance by finally releasing, often under big international political pressure, the corrected and internationally audited numbers for public finance positions.

As illustrated above, the arrangements of the BFU are built on the premise of external disciplining being an efficient device of bringing about long overdue structural reforms in non-complying countries, by a straightforward combination of sticks and carrots, money for discipline. This, however, is unlikely to be a workable solution. As recent comparative evidence indicates[26], even in small open economies, if internal conditions are set right, success can/could in the past 25 years be forthcoming even in the lack of massive external funding. By contrast, no amount of external money injection may make up for weak institutions, lack of governmental commitment, or missing professional consensus across decision-makers. Such cases, not discussed in the above volume, as of Portugal and France may be taken as telling cases in point.

This finding is anything but path-breaking in the analytical social sciences. Failure of attempts to impose democracy from above and from abroad has made this insight a commonplace ever since the examples of the western invasions in Afghanistan, Iraq and more recently in Lybia, or the western Balkans for that matter.

But applying the insight to *BFU renders the usual division of labor between Europhiles and Euroskeptics paradoxical and evden untenable*. Those who believe in fiscal discipline and federal Europe – in terms of *finalité politique* – should be vary of the stipulations embedded in the improvized architecture of BFU as it stands today. While attempting the impossible, systems' designers have created a framework of *limited accountability, of uneven checks and balances.* BFU embodies many dangers discussed in the more abstract financial literature as '*moral hazard'* where bills left over by one are regularly being paid by someone else. The surveillance and control mechanisms overseeing new supranationalist organs hinge, to a large degree, upon the monitoring ability of the European Parliament and of the general press. Both of those players have proven over the past two decades ill-equipped to deal effectively with highly complex and technical issues, like the ones incorporated in the BFU.

Just to give a few examples. Is it realistic to expect, that if the Commission finds France guilty of trespassing stipulations and commitments taken upon itself under the Fiscal Compact, say during the reviews conducted under the European Semester, the legislation of *la grande nation* would quickly rectify the misdeed, which was usually an outcome of tough political bargains among the legislators? No sign

26 *Aslund,A. – Djankov,S.eds/2014/:* The Great Rebirth: The Triumph of Capitalism over Communism. Washington,D.C: peterson institute of International Economics, December.

of it in 2013-16. Is it realistic to expect, that say any of the 25 big banks that have failed the stress test of 2014 will voluntarily turn to the ECB for restructuring assistance? Or indeed, that the ECB as a main supervisory agency, would indeed make good of its very broad mandate, and launch unilaterally and pre-emptively a restructuring program against the will of a defying bank's shareholders, who are expected to take heavy hair-cuts? Or can we even imagine – following decades of experience to the contrary – any big member-state actually paying a fine of 0.1 pc of its GDP for non-complying with the Fiscal Compact? Or can we realistically expect the Commission suspending agricultural payments to Polish farmers under cross-conditionality procedures?

All in all, the BFU project is a child of crisis-management with many unintended side-effects. As such it carries a number of defects, owing to the conditions and improvizations that surrounded its coming into being. Therefore it is hardly a surprise if we observe: while it did solve some problems, it created no fewer new ones, that may indeed be characterized as a very real trap.

The nature of this trap is twofold. First: it appears that unresolved problems are already being addressed via imposing tougher and more rigorous controls over players, irrespective of the issue of incentives and of balance of power considerations. It seems naive. Second, centralization is known to trigger, willy-nilly, even more centralization, interventions breed interventions. This is quite contrary to all normative claims we cited approvingly above. Thus the future is likely to see the further proliferation of improvized, poorly thought out and even more poorly coordinated decisions taken at the top level, without, however proper and timely accounting for their consequences. Federalism without proper checks and balances is unlikely to offer any solution to the fundamental problem of divergent preferences and priorities. And in public finances it is even more of a trap, as the need to place the BFU outside the existing formal framework provided by the TEU/Lisbon Treaty has symbolically indicated. *There is no exit from the „no taxation without representation" dilemma, which is at the root of any reflection onthe interrelationship of nation states and European integration they constitute*.