

Delegation and the Commission role in fiscal policy coordination in Economic and Monetary Union

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7911 words + table of 796 words

Abstract

Delegation theory can be usefully applied to explore the Commission's role in macroeconomic – and specifically fiscal – policy coordination in terms of the monitoring powers and responsibilities delegated to the Commission under the TEU and the Stability and Growth Pact (Stability Pact, Pact, SGP) and to downplay its entrepreneurial leadership, political strategic and ideological roles. It will be argued that the Commission's potential to perform these other roles is maintained yet constrained by the terms of delegation. These terms provided some scope for Commission action in fiscal policy coordination during Stage II of the EMU project (1994 to the start of 1999). However, since the start of EMU's Stage III on 1 January 1999, the Commission's margin of manoeuvre in fiscal policy coordination (and specifically the budgetary surveillance) element of EMU has become more constrained. This constraint reflects the problematic management and watch-dog functions delegated to the Commission that have hindered the previously less encumbered policy initiation and mediation functions which have been, arguably, so important to the Commission's role in the history of monetary integration and the development of fiscal policy coordination. The March 2005 reform of the Stability and Growth Pact creates new opportunities for the Commission to enhance its central role in fiscal policy coordination.

Introduction

The European Commission – its President, its Commissioner for Economic and Financial Affairs, Directorate-General ECFIN and the Commission agency Eurostat – has performed an important role in macro-economic (and specifically fiscal) policy coordination. Accusations abound that the Commission has been excessively rigorous in its insistence upon the application of Maastricht Treaty (Treaty on European Union, TEU) convergence criteria and macroeconomic policy coordination provisions, Stability and Growth Pact rules and several regulations on fiscal policy coordination. The on-going Commission reply to these accusations is that it is fulfilling its

responsibilities according to the powers delegated to it by the EU member state governments through the TEU and the Pact. The Commission's role in macroeconomic policy coordination in EMU – in the period leading to the start of Stage III of EMU (1 January 1999) but also since – can be interpreted in several ways. The Commission's role can be described in terms of policy initiation – even 'entrepreneurship'¹ – mediation, management and monitoring. The Commission's role has also been seen in terms of political strategy. It has been argued that in the lead up

¹ The concept of entrepreneurial leadership in the context of international bargaining and decision making has attracted increased academic attention in recent years (Frohlich et al., 1971; Malnes, 1995; Young, 1991). Bargaining in the international realm is distinct because of its decision rules, collective action problems, and degree of uncertainty. Given these characteristics, it is often hard to achieve success (principally due to collective action problems), even when there is considerable agreement among the international actors involved. For Young (1991), the difficulty of achieving position alignment creates a crucial role for leadership. There are a number of definitions of entrepreneurial leadership (see Malnes 1995 and Underdahl 1991) which differ mainly on scope. Most applications of this concept incorporate certain core features including the innovative bargaining ideas that the leader introduces to negotiations and the ability of the leader to achieve successful outcomes in a changing environment. In his study of Delors' entrepreneurial leadership role, Van Assche (2005: 281) applies Young's (1991) definition of an entrepreneurial leader 'as an individual who uses negotiating skills to frame issues in ways that foster integrative bargaining and put together deals that would otherwise elude participants. Such framing can be achieved through skilful agenda setting, popularization of issues, and the construction of inclusive packaging deals.'

to Stage III the Commission selectively marshalled the political and economic significance of Europe's emerging Single Market and induced key economic and political actors to re-articulate their preferences in terms of monetary union (Fligstein & Mara-Dritta 1996; Jabko 1999).² It has also been argued by academics and politicians alike that the Commission has played an ideological role, interpreting the rules of EMU in a manner consistent with neo-liberalism (Jabko 1999).³ The aim of this paper is to explore Commission's role in macroeconomic – and specifically fiscal – policy coordination in terms of the monitoring powers and responsibilities delegated

² The Commission certainly concurs with this interpretation. Yves Thibault de Silguy, Commissioner for Economic and Financial Affairs in the Santer Commission from 1995 to 1999, asserted that the Commission had a vital role to play in providing momentum to the EMU project and leading and encouraging reflection and preparation on EMU (de Silguy, 1995: 38).

³ Jabko (1999) explores the Commission's post-Maastricht leadership role in terms of its political strategy to build the support of a broad and stable political coalition in favour of the EMU project. He (*ibid.*: 486) sees the Commission as targeting those 'national politicians ... national central bank and finance ministry officials, members of the business community, especially in the financial sector, and, more generally, all actors or social groups who conceived a political, bureaucratic, or economic interest in the provision of fiscally conservative policies [and monetary orthodoxy].' In doing so, Jabko (*ibid.*) argues that the Commission deliberately 'framed EMU in terms of consolidating the liberal economic policy orientation embodied in the EMS and the Single Market'.³ Selling EMU in such practical terms was necessary because – as Frieden (1991) asserts – few social groups saw the project as economically necessary.

to the Commission under the TEU and the Stability and Growth Pact (Stability Pact, Pact, SGP) and to downplay its entrepreneurial leadership, political strategic and ideological roles. It will be argued that the Commission's potential to perform these other roles is maintained yet constrained by the terms of delegation. These terms provided some scope for Commission action in fiscal policy coordination during Stage II of the EMU project (1994 to the start of 1999). However, since the start of EMU's Stage III on 1 January 1999, the Commission's margin of manoeuvre in fiscal policy coordination (and specifically the budgetary surveillance) element of EMU has become more constrained. This constraint reflects the problematic management and watch-dog functions delegated to the Commission that have hindered the previously less encumbered policy initiation and mediation functions which have been, arguably, so important to the Commission's role in the history of monetary integration and the development of fiscal policy coordination.

Before continuing, the roles of the different Commission bodies involved in fiscal policy coordination should be clarified. Eurostat has been assigned the most important budgetary surveillance role, while Directorate-General ECFIN has been involved in economic forecasting element of the Stability and Growth Pacts Early Warning Procedure (EWP) and Excessive Deficit Procedure (EDP), the preparation (with Eurostat data) of the Broad Economic Policy Guidelines (BEPGs) and the monitoring of the Convergence and Stability reports submitted by member state governments. Only a handful of officials in both DG-ECFIN and Eurostat are directly involved with fiscal policy coordination. Of Eurostat's approximately 650 staff, only a few dozen professional and support personnel (including several statisticians seconded from member state national statistical agencies) (now in Directorate C,

previously Directorate B) focus on harmonizing data on money supply and monitoring the budgetary and public finance data of EU member states.

DG ECFIN's important role in the EWP and EDP has been due to in part to the failure to outline a forecasting model in the Stability Pact. Thus DG ECFIN is the sole arbiter of the forecasting model's economic and statistical assumptions. Savage (2005: 52) writes that, surprisingly, by 1995 Eurostat surpassed DG ECFIN as the central agency in the budgetary surveillance process.⁴ There are several reasons for Eurostat's important role: the entrepreneurial leadership of Yves Franchet, Eurostat director; Eurostat statistical expertise – the identification of ESA (European System of Integrated Economic Accounts) in the Maastricht Treaty for measuring national deficits and debt required Eurostat expertise to analyse national accounts data; and EU officials and member state governments considered Eurostat to be a more impartial organization than DG ECFIN.

1. Applying delegation theory

Delegation theory can be used to explain the Commission's leadership role in EMU in the preparations from 1994 for the 1999 start of Stage III – the irrevocable fixing of exchange rates and the transfer of monetary policy making powers to the European Central Bank – and the transition to the single currency, introduced from January

⁴ Savage (2005: 52) argues that Eurostat's role is more crucial: 'DG ECFIN's forecasting function may be viewed as only a precautionary device to warn of excessive deficits or to delay the imposition of sanctions, whereas the actual violation of the Pact turns on the MS exceeding the deficit and debt reference values, and it would be Eurostat certifying this had truly occurred.'

2002. (For applications of delegation theory to the Commission and European Union more broadly see, for example, Kassim & Menon 2002; Moravcsik 1998; Pollack 1997; 2002 & 2003.) The Commission's role in the EMU project generally and fiscal policy coordination more specifically has resulted from delegation that has taken place for two principal reasons. The first was the need for centralized experts to manage a complex policy making sector and to present expert proposals – technocratic 'focal points' – around which governments could coordinate their activities. The collective action problem facing governments is one of coordinating the production of information. Delegation took place because 'centralised authorities are best placed to exploit economies of scale and overcome coordination problems or national mistrust, thereby generating and disseminating sufficient information required for more efficient decision-making' (Moravcsik 1998, 71; see also Majone 1996, 41ff). Nugent (1995) argues that the Commission's role rests on its 'constitutional' powers and its knowledge and expertise. However, whether this capacity is put into effect depends on the member states' perceptions of the need for policy activity as well as the institutional context of decision-making.

The second reason for delegating powers and responsibilities to the Commission, which has structured the potential Commission leadership role in EMU, was the desire of member state governments to lock in policy coordination – here both soft and potentially hard, or binding, forms of macroeconomic policy coordination – and demonstrate the credibility of their commitment to the rules of the EMU project. By delegating to the Commission the right to interpret and implement (yet not enforce) EMU agreements national governments sought to restructure future domestic

incentives, encouraging future cooperation by raising the cost of non-decision or non-compliance.⁵

Delegation to the Commission in the EMU policy area – and pooling of powers over fiscal policy more generally – can be further viewed in two additional ways. First, delegation was a solution to the problem of ‘incomplete contracting’, which arose because national governments shared broad goals in favour of EMU yet found it too difficult to make technical agreements on the implementation of these goals. Governments therefore required efficient means of pre-committing to a series of smaller, uncertain decisions staggered at a series of times in the future, some of which were likely to be inconvenient but which taken as a whole benefited each of them (Moravcsik 1998). Member state governments delegated a great deal of scope over

⁵ Nugent (1995: 51-2) writes: ‘the articles of the [TEU] covering [EMU] were littered with references to the Commission: “The Council shall, acting on a recommendation from the Commission...”, “The Commission shall monitor the development of ...”, “The Commission shall prepare a report on ...” and “Where a Member State is in difficulties ... the Commission shall immediately investigate the position of the State in question ... and state what measures it recommends the State concerned to take”. See TEC articles 99(2-4), 100, 104(2, 3, 5, 13&14), 105(6), 107(5&6), 111(1-4), 114(1-3), 115, 116(2b), 117(6, 7), 119(1, 3), 120(2), 121(1, 2), 122(1, 2), 123(4, 5). Thus, even though the Commission had no final decision making role in the move to EMU there was considerable delegation of guiding, advisory and monitoring tasks which created sufficient scope for an important Commission role especially given the initial inertia of member state governments on EMU.

difficult and pressing technical policy formulation (albeit not final decision making) to the Commission. Second, delegation took place to increase the credibility of the EMU project in the perceptions of economic actors which were, in the post-Maastricht period, highly sceptical that Stage III would begin by the 1 January 1999 target date.

2. The Commission's role in fiscal policy coordination in the move to Stage III

Member state governments delegated implementation powers to the Commission thus allowing an important role for this supranational institution in the lead-up to the start of Stage III of EMU. As delegation theory would predict, member state governments needed to establish the credibility of the EMU project – and the credibility of their commitment to EMU – in the perceptions of financial market operators and other private economic actors (firms, workers, investors and consumers) (see Leblonde 2004). There are seven major ways in which the Commission (joined by the EMI in some areas) had a leadership role in Stage II of the EMU project, leading to the start of Stage III and then the introduction of the single currency from 1 January 2002:⁶

1. consulting relevant economic actors on their views concerning necessary developments in the transition to the single currency;
2. designing proposals for the transition for Ecofin and the European Council with the express aim of encouraging the action of member state governments;
3. mustering support from a broad political coalition;
4. preparing relevant economic actors for the transition;
5. preparing concerned national public administrations for the transition;

⁶ Howarth (2007) further elaborates on these ways.

6. monitoring economic convergence and budgetary discipline in the member states; and
7. designing proposals on budgetary surveillance from Stage III (in the context of the negotiations on the Stability and Growth Pact from November 1995 to December 1996).

The sixth and seventh ways are most relevant to this analysis yet several of the other ways had a fiscal policy dimension. The Commission lacked final say over the detailed content of the move to EMU's Stage III – including the application of fiscal policy rules in determining member state entry – which was left to national governments. In the terms of delegation theory, the Commission's lack of final decision making power is due to the nature of delegation which was not linked to reducing problems of the credible commitment of the governments (in the perceptions of other governments) *per se*. Rather delegation resulted from the inability of national governments to negotiate and include a complete contract in the TEU. When delegation is not about solving the credible commitment problem, member state principals are likely to keep tighter control over supranational agents (see Tallberg 2002). Here the delegation that took place, which allowed the Commission an important role in the implementation of EMU, was principally to reinforce the credibility of the EMU project – and fiscal policy coordination more specifically – in the perceptions of private economic actors. It was *not* – in most respects – to reinforce the credibility of the member state governments' commitment to the project in one another's perception – which, in the terms of delegation theory, would have involved granting the Commission considerably more powers. In the transition to EMU, private economic actors needed principles, rules, regulations and procedures to

focus their behaviour in the proper direction. Where Commission powers and responsibilities concerned the credibility of the commitment of governments – as in the area of budgetary surveillance – it can be argued that the Commission had more direct influence over final decision making in the Council of Ministers and the European Council, which nonetheless retained the formal final say given the politically sensitive nature of decisions in this area. This is explored below.

Jabko (1999) argues that the Commission's role in mustering support for EMU was ideologically inspired. The Commission deliberately emphasised the liberalising dimension of EMU. Its take on macroeconomic policy coordination was as a mechanism to achieve liberalisation via significant structural reform. An application of delegation theory assigns the Commission a less ideologically-inspired role in mustering support for EMU, which can be seen as an implicit element of the preparation role delegated to the Commission. If the Commission tended to target certain actors over others in building support for EMU, this made strategic sense given the monetary orthodoxy and fiscal conservatism *embedded* in the terms of delegation (TEU), which inevitably made the project more or less appealing to some actors and social groups. Thus, if the political strategy of the Commission had an ideological flavour, this was due to the Maastricht Treaty's EMU provisions – which were however not explicitly liberal – not Commission manipulation *per se*. Jabko's assertion of the Commission's liberal economic orientation might at least be qualified: its support for partial liberalisation if necessary for member states to respect the convergence criteria – by which entry into EMU's Stage III was to be determined – is not the same as a liberal economic orientation. Building a political coalition around monetary orthodoxy is not the equivalent of building a political coalition around a liberal economic project. There is nothing inherently liberal about EMU and its

macroeconomic policy provisions. If the Commission saw creating a broad and stable political coalition in favour of EMU as one of its central roles in Stage II, this was because the incomplete contract of the Maastricht Treaty and the conditional terms imposed upon member state participation in Stage III made such a role almost inevitable.

Monitoring economic convergence and budgetary discipline in the member states

The management of the TEU's budgetary surveillance procedure provided the Commission with an additional role. As well as the broader delegation of monitoring responsibilities to the Commission since the Treaty of Rome (as 'guardian of the treaties'), the TEU included specific provisions on the Commission's monitoring role in EMU: namely, TEC articles...

- 99(2-4) on designing Broad Economic Policy Guidelines (BEPGs) for member states, monitoring member state progress in following their BEPGs and making recommendations to member states failing to respect their BEPGs;
- 100(1&2) on financial assistance to member states in exceptional circumstances;
- 104(2, 3, 5, 13&14) on monitoring the budgetary situation and the stock of public debt in the member states, reporting to the Council on the failure to respect specified deficit and debt reference values and recommending further action;
- 114(1-3) on requesting the Monetary Committee (the Economic and Financial Committee from the start of Stage III) for opinions on the monetary and financial situation in the member states and the Euro-zone more broadly;

- 115 on the Council and member states requesting the Commission to make a recommendation or a proposal on member states failing to respect their BEPGs and deficit and debt reference values;
- 116(2b) on reporting on the achievement of economic convergence in the member states prior to the start of Stage II;
- 119(1, 3) and 120(2) on investigating a member state suffering from a balance of payments crisis and recommending protective measures and potentially mutual assistance; and
- 121(1, 2) on reporting on the fulfilment of the convergence criteria to determine member state participation in Stage III.

Delegation on budgetary surveillance was to ensure the credibility of commitment of the member governments to meeting the criteria prior to entry into Stage III.⁷ Eurostat performed the necessary monitoring tasks that ensured the Commission an important say in determining whether member states had met the TEU debt and deficit criteria and the ‘gate-keeping’ role of excluding member states with excessive deficits (Savage 2005). The annual publication of the Commission’s convergence reports was an eagerly awaited event in Stage II as it was widely seen as the most objective and thorough indication of national preparedness for EMU entry. The Commission’s March 1998 reports identified which member states qualified for EMU membership. Given the greater credibility of these reports over national reports, it would have been very difficult for the European Council to have ignored them in determining EMU entry. Thus the immense political importance assigned to budgetary surveillance in

⁷ Jabko (1999) also explores the Commission’s monitoring role – and its increasingly vocal defence of the convergence criteria – in terms of its strategy of mustering a broad coalition of support for EMU and smoothing the transition to Stage III.

Stage II – and above all meeting the 3 per cent deficit criterion, with the goal of EMU a political priority in most member states – reinforced the central role of the Commission in the EMU process. Domestic German politics demanded that the 3 per cent rule be rigidly enforced, while many senior national politicians openly criticised this rigidity especially given the economic difficulties in many EU member states in the post-Maastricht period.

The awareness of the great temptation for member states to engage in creative accounting to meet the deficit criterion to qualify for entry into Stage III, placed further political importance upon a neutral monitoring mechanism, isolated from national influence. The Commission repeatedly reminded member state governments that Eurostat lacked the resources to perform this function as effectively as it should. (The subsequent revelations of the extent to which certain member states ‘cooked the books’ demonstrates the validity of Commission / Eurostat concerns.) Nonetheless, this did not fundamentally undermine the central role of the Eurostat in budgetary surveillance in Stage II. This was in large part because of Eurostat efforts to create harmonised and credible budgetary data – through the development of the European System of Integrated Economic Accounts (ESA) – and its attempts to control what it regarded as member state budgetary manipulation (Savage 2005). It is also important to recognise the importance of Eurostat’s ‘status as an independent, non-political, technical entity, combined with its entrepreneurial leadership, enabled it to play a critically important, if publicly unsung, role in the Maastricht Treaty’s convergence process’ (Savage 2005: 47). Prior to the annual publication of the Commission’s report, Eurostat issued its own top secret report, ‘Statistics on Convergence Criteria: Assessment by Eurostat’ (see, for example, Eurostat 1998) which was considered to

be the authoritative evaluation of member state budgetary data. As delegation theory would predict, even though the development of Eurostat's capacities might be considered politically problematic for governments seeking to bend the rules, the member state governments 'identifi[ed] with the integrity of the procedure, participate[d] in its development, and promote[d] the use of these rules in member state policy-making' (Savage 2005: 5). The member states did so because these procedures and rules reinforced the credibility of their commitment to the EMU project.⁸

Designing proposals on budgetary surveillance in Stage III.

The Commission played an important role facilitating the adoption of the precise provisions of the Stability and Growth Pact at the December 1996 Dublin European Council (see Heipertz and Verdun 2004). The German proposal for a 'Stability Pact for Europe' was presented to EU finance ministers at a November 1995 meeting of Ecofin (Waigel 1995a, b). The German government sought an intergovernmental

⁸ Jabko (1995: 487) interprets the significance of abiding by the convergence criteria and the rules of budget surveillance in terms of bargaining incentives. The TEU was the 'negotiating baseline as well as an instruction manual for the member states which aspired to EMU. Any deviation from its specific terms weakened not only a country's chances of reaching the promised Euroland, but also its bargaining position for deciding the details of EMU. The many aspects of EMU that were left relatively open for negotiation ... constituted a strong set of incentives for the member states to adhere to monetary orthodoxy. Since they too hoped to exert some influence on the specific terms of EMU, Commission officials faced bargaining incentives to appear as tough defenders of monetary orthodoxy.'

agreement in the form of an international treaty along the lines of Schengen which would have resulted in the marginalisation of Community institutions and procedures. The Germans also sought automatic fines to be imposed upon countries by a Stability Council which was unacceptable to many other countries (notably France). While debates on the design of the Pact raged over the next thirteen months, the Commission was asked to come up with a compromise solution.

The Commission (DG-ECFIN) had the difficult task of designing an EDP that avoided automatic fines yet retained the veneer of real deterrence. Its proposal was released in two draft regulations. The first called for the reinforcement of budgetary surveillance in the Stability Pact as a rudimentary device for economic policy coordination.⁹ The second draft regulation ‘on speeding up and clarifying the implementation of the Excessive Deficit Procedure’ (EDP) avoided automatic fines and reduced sanctions to a discretionary measure of Ecofin.¹⁰ It would be problematic to claim a significant role for the Commission in the negotiating process on the SGP. Indeed, the Commission’s initial preference was for less strict rules than those agreed at Dublin. However, the Commission was successful in achieving two of its main objectives: a solution within the Treaty framework – thus ensuring an ongoing central role for the Commission in budgetary surveillance and macroeconomic policy guidance – and the inclusion of the Commission’s surveillance recommendations in

⁹ Council Regulation (EC) 1466/97 on budgetary surveillance.

¹⁰ Council Regulation (EC) 1467/97, on speeding up and clarifying the implementation of the excessive deficit procedure, Official Journal L 209 of 02.08.1997.

the Pact, which further reinforced the Commission's central monitoring role (Heipertz and Verdun 2004).

3. A disabled Commission role with a muddled rule-book

If the credentials of the Commission were boosted by its role in Stage II – and the entry of eleven member states into Stage III and the launch of the single currency in 2002 – the terms of delegation have also worked to undermine the Commission's role in EU fiscal economic policy coordination since 1999. As outlined above, the Commission was delegated important budgetary surveillance powers and responsibilities. Added to these are specific provisions in the SGP.¹¹ Thus the

¹¹ The Stability and Growth Pact stipulates that 'the Commission:

1. will exercise its right of initiative under the Treaty in a manner that facilitates the strict, timely and effective functioning of the Stability and Growth pact;
2. will present, without delay, the necessary reports, opinions and recommendations to enable the adoption of Council decisions under Article 99 and Article 104; this will facilitate the effective functioning of the early warning system and the rapid launch and strict application of the excessive deficit procedure;
3. commits itself to prepare a report under Article 104(3) whenever there is the risk of an excessive deficit or whenever the planned or actual government deficit exceeds the 3 per cent of GDP reference value, thereby triggering the procedure under Article 104(3).
4. commits itself, in the event that the Commission considers that a deficit exceeding 3 per cent of GDP is not excessive and this opinion differs from that of the Economic and Financial Committee, to present in writing to the Council the reasons for its position' (European Council 1997).

Commission monitors and privately and publicly criticises the convergence / stability plans of member state governments; helps draw up the Broad Economic Policy Guidelines to which member state governments publicly commit themselves to following; criticises governments for failing to meet their plans and respect the guidelines; recommends that Ecofin launch the Early Warning Procedure (EWP) in the event that a participating member state government risks exceeding the 3 per cent deficit threshold; and then recommends the Excessive Deficit Procedure (EDP) when a member state government has exceeded the 3 per cent figure.

In terms of delegation theory, the Commission was assigned these budgetary surveillance and macroeconomic policy guidance powers and responsibilities in Stage III in order to render the commitment of the governments to the TEU and SGP fiscal policy rules more credible, reducing the risk of free-riding with certain Euro-zone member states running higher deficits and higher inflation whilst profiting from the low Euro-zone interest rates made possible through the low inflationary policies of the other participating member states. In turn, this delegation was expected to contribute to the on-going credibility of the EMU project and of the European Central Bank's (ECB's) monetary policy in the perception of economic actors. However, the member states were cautious with regard to the powers they delegated to the Commission, which was granted the power neither to develop the rules of macroeconomic policy coordination nor to launch the EWP and the EDP, let alone the power apply the full rules of the EDP which, following a member state's excessive deficit over a period of three years, can lead to the imposition of fines. Ecofin (the member state governments collectively) retained these powers. The argument can be made that the Commission's watch-dog function operates in the case of EU law because the final

arbiter is the European Court of Justice (ECJ) and its judgements are expected to be implemented. However, delegation in terms of the watch-dog function in the case of SGP rules is problematic because the immediate judge is the Council and the fact that Ecofin ministers have to judge one another poses an obvious incentive problem.¹²

In retrospect, had the Commission been given the power to launch the EWP and the EDP, it is likely that this more complete delegation would have further undermined the Commission's role in EMU. It is difficult to imagine certain member governments – notably French and German – allowing the Commission to apply the EDP and in particular the fines that it can result in. The great potential for conflict would have transformed the Commission into even more of a scapegoat than it already has been in this policy area and would have certainly undermined the Commission's position in this area. As it is, in a period of sluggish economic growth in which some member state governments would face major political difficulties in making sufficient cuts to national budgets, the Commission was bound to be placed in a situation whereby the performance of its watch-dog function of calling for the implementation of European law would attract considerable antagonism from struggling governments. More so than in any other policy area, the temptation for governments to scapegoat the Commission is great. While scapegoating the Commission is problematic (in that the Commission has no final authority with regard to EU fiscal policy making) several governments have nonetheless done so. To take but one example, on 18 September 2003, in their joint EU growth initiative, the

¹² The Commission is partly responsible for this problematic delegation which itself reflects the limited leadership role it played in the Monetary Committee discussions over the Stability Pact (see above).

French and German governments energetically attacked the Commission which, in its commitment to low deficits, was accused of being bent on de-industrialising Western Europe (*Le Monde*, 19 September 2003).

Beyond the Commission's monitoring function – which creates potential for member state antagonism and scapegoating – the principal difficulty facing the potential strengthening of the Commission's role in EMU is the problematic nature of the terms of delegation in the SGP fiscal policy rules, which have been widely contested by both governments and academic economists. Notably, the asymmetrical nature of the deficit cutting requirement has attracted criticism as it encourages such action at the bottom of the economic cycle when governments should be increasing spending. Furthermore, the need to cut deficits when national inflation might already be well below the ECB's inflation target (and thus deficit spending cannot be considered to be excessively inflationary) is perceived as problematic.¹³ Other considerations of a particular national fiscal situation (debt load) were also ignored by the Pact's rules.

The Commission was placed in a position of having to defend the SGP rules even though the Commission President Romano Prodi publicly accepted that these rules were 'imperfect' and 'stupid' (*Le Monde* 17 October 2001) and excessive deficits in

¹³ Governments are required to pursue countercyclical deficit cutting during periods of slow economic growth in order to respect the 3 per cent target but have little incentive to cut deficits during periods of stronger economic growth – which would enable them to meet the medium term aims of the Pact of a budget in balance or surplus. Thus governments facing recession are required to lower their deficits even if the national inflation figure is well below the ECB's target rate.

certain member states coincided with national inflation rates that were well below the ECB's target. On 18 November 2003, the Commission found that France had not taken effective action and Germany had adopted inadequate measures to implement the Council's recommendations. The Commission therefore issued recommendations to the Council to advance with the proceedings and, in particular, to take action with respect to Art 104(8) or Art 104(9) EC respectively (Dutzler and Hable 2005). Furthermore, the Commission decided to make the politically risky and – in retrospect, legally unfounded – move of taking the Council of Ministers to the ECJ following Ecofin's 25 November 2003 decision to suspend the application of the EDP with regard to France and Germany.¹⁴ While supported by some of the smaller member state governments that insisted upon the application of Pact rules – who thus looked to the Commission as a potential leader in this policy area – the legal move succeeded in outraging the French and German governments. The ECJ's judgement –

¹⁴ The Commission made two claims to the ECJ. First, it sought to annul the decisions of the Council not to adopt the formal instruments contained in the Commission's recommendations pursuant to Article 104(8) and (9) EC. Second, the Commission sought to annul the Council's conclusions in so far as they involve the decision to hold the excessive deficit procedure in abeyance, the recourse to an instrument not envisaged by the Treaty, and the modification of the recommendations decided on by the Council under Article 104(7) EC. In the Council's opinion, the action of the Commission was inadmissible, or should, alternatively, be dismissed (para 22 and 23). The Court shared the Council's perception and declared the action inadmissible to the extent that it concerned the failure of the Council to adopt the recommendations. In turn, it followed the Commission's claim and annulled the Council's conclusions in its essential elements (Dutzler and Hable 2005).

which rejected the annulment of Ecofin's decisions on the EDP yet agreed with the Commission's request to annul the actual Ecofin recommendation of putting back the deadline for bringing the government deficit below the ceiling of 3 per cent – was far from a clear vindication of the Commission's position.

The Commission has also continued to perform its policy initiation function presenting itself as a centre of expert advice on EMU. Romano Prodi's criticism of the SGP preceded the political difficulties created by the infringement of Pact rules by Germany and France. This very public encouragement of Euro-zone governments to consider reform was the first for a serving high profile European statesman. Whilst defending the application of the existing Pact's rules and performing its monitoring function, in November 2002 the Commission issued a communication to the European Parliament and the Council which called for a strengthening of budgetary coordination in the European Union (Commission 2002b).¹ (See Table 1 in the appendix for a full outline of the Commission's reform proposals.) Presented in advance of the March 2003 European Council discussion of proposals to reinforce economic policy coordination, the Commission's communication was in effect the first full reform package of the SGP incorporating a more flexible interpretation of the Pact's rules, while recommending that the sanctions against non-compliant member states be strengthened. In 2003, Ecofin (Ecofin 2003b) agreed several modifications to the Pact in line with the Commission's package, although there was on-going debate on the need for additional reform following the Council's suspension of the EDP in November 2003. Ecofin, in line with the Commission, emphasised a more flexible interpretation of the SGP's medium-term rule to take into account the size of public debt, the economic cycle and the quality of public investment. The final

reform package agreed in March 2005 incorporated these concerns but also allowed the Euro-zone member states much greater ‘flexibility’ in the application of Pact rules. (See Table 1 in the appendix for a full comparison of the Commission’s reform proposals and the Ecofin reform package.)

The flexibility introduced with regard to both the short and medium term deficit goals of the SGP – and in particular the margin of manoeuvre of member state governments with regard to the determination of acceptable deficit levels – will likely eliminate much of the tension created between member state governments and the Commission in the application of the original Pact’s rules. The Commission retains its power of recommendation, yet the increased margin of manoeuvre promised to decrease the pressure on the Commission to engage in public conflict with Ecofin and individual member state governments. There could be a difference in interpretation of acceptable deficits for a particular country but the EDP trigger was qualified.

These reforms, far from undermining the Commission’s role in fiscal policy coordination, may increase it by decreasing the potential for member government - Commission conflict. On the other hand, for those virtuous smaller member states – notably Austria and the Netherlands – which turned to the Commission to uphold the rules when Germany and France insisted upon breaking them, these reforms are probably seen as undermining the Commission monitoring role. Crucially, in the context of its delegated powers, the Commission can exercise leadership in its generation of ideas and initiation of policies but also through its role as a budgetary statistical authority (thanks to Eurostat). The reinforcement of this authority – through an increase in financial and human resources dedicated to collecting

budgetary data – was the final point in the Commission’s reform proposals. Although it was not included in Ecofin’s reform package, most member state governments appear to accept the need for reinforcement. The Greek example – disclosed in late 2004 – of publishing false data on the state of government finances in the period leading to its entry into Stage III has reinforced the perceived need for the Commission to maintain if not improve its monitoring role and for Eurostat to improve its capacity to monitor national statistical agencies. In the context of delegation theory, the reinforcement of the Commission’s statistical authority is now essential for building the credibility of the member state commitment to EMU rules (even if these rules have now been significantly watered down) and, in turn, contributes to credibility building in the perceptions of private economic actors. The Commission’s reinforced capacity to monitor, name and shame governments which ‘fix the books’ will certainly reinforce its role in fiscal policy coordination. The potential for scape-goating the Commission remains. However, criticising governments and calling for further budgetary consolidation in the context of a more symmetric Pact is very different to the Commission’s monitoring role under the Pact’s first incarnation which involved criticising governments for not respecting problematic fiscal policy rules and applying established procedures. By depoliticising the application of the Pact’s rules, the potential for Commission leadership in the realm of economic governance is reinforced.

Conclusion

Delegation theory is a useful tool to elucidate the scope and limits of the Commission’s role in fiscal policy coordination in EMU. When member state governments delegate the implementation of their ‘grand bargains’ to supranational

institutions, the results may differ considerably from what would have been achieved had decision-making been kept at the intergovernmental level (see Sandholtz and Stone Sweet, 1998). In the case of EMU, there is good reason to doubt that the progress to Stage III would have taken place at the start of 1999 if the member state governments had been the only actors in charge of the transition. Ensuring the support of private economic actors for EMU – and more specifically the confidence of financial markets in the project – was a major concern which encouraged governments to delegate to the Commission an important role in Stage II. Establishing a credible form of macroeconomic policy coordination to bolster the confidence of financial markets in the credibility of member state commitment to meeting the convergence criteria was central to this role. The decision to grant the Commission important monitoring powers with regard to the TEU and SGP fiscal policy rules can likewise be interpreted through the lens of delegation theory in that member states saw – and certain governments insisted upon – a role for the Commission in rendering credible their commitment to these rules.

Delegation theory can also demonstrate why the Commission has had difficulty asserting a leading role for itself in the context of fiscal policy coordination in EMU and more specifically with regard to the application of SGP rules post-1999. The rules themselves have been widely challenged as problematic – by the Commission itself – and thus the Commission's efforts to implement them attracted member state opprobrium and undermined the potential initiating and mediating role that the Commission should have had with regard to the development of economic governance in EMU. Important member state governments – notably France, Germany and Italy – came to consider the original Pact as no longer vital for either

retaining the credibility of the EMU project for private economic actors (financial markets) or as a clear indication of their credible commitment to the EMU project in the perceptions of other member governments.

Yet delegation theory can also be applied to explain why there is considerable potential for the Commission to play a central role in the operation of EMU in the future – notably through the development of the Commission's / Eurostat's budgetary surveillance capacity, arguably crucial in the context of maintaining the long-term credibility of the EMU project and the credible commitment of governments to the project. The precise rules of the original SGP were problematic which rendered the Commission's watchdog role problematic. The rules of the new Pact are subject to greater member state manipulation yet they also make the Commission's monitoring role less problematic because the definition of free-riding has been qualified. The Commission's role remains to draw attention to all national public deficits at risk of exceeding the 3 per cent threshold. However, the new Pact effectively releases the Commission from the obligation of prosecuting all infringements. Its new responsibility of analysing the acceptability of excessive deficits – in the terms of the new SGP rules and its six 'other relevant factors' – allows for considerably more Commission room to manoeuvre to perform its watch-dog function sensitively and strategically. The Commission retains the possibility of challenging the acceptability of member state deficits yet it can now focus on infringements that amount to serious cases of free-riding, where national deficit and debt are *both* in excess of the Pact thresholds and they contribute significantly to high inflation.

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