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EU Constitutional Governance: Failure as Opportunity!?

The French and Dutch rejection of the proposed EU Constitution in May 2005 threw the European Union into what many observers regard as its deepest crisis to date. This crisis can also be seen as a unique opportunity for political, economic and institutional renewal, however. The following article outlines the problems presently facing Europe and discusses what changes would have to be made in the EU system of governance in order to overcome them.

On 17 June 2005, the European Union summit broke up in a bitter dispute over the EU's budget and the future of its constitution. Arguments about the Union's financial plans, even sullen accusations of national egoism, have been a usual element of European politics for years. But the popular rejection – just prior to the meeting – of the proposed EU constitution by France and the Netherlands, two major advocates of European unity, had raised deep questions about the union's legitimacy and purpose. Hopes by some that successful ratification in the remaining EU countries would change the French and Dutch stance were soon dispelled. Already at the summit, the Dutch Prime Minister announced that his country would not vote again on the same, unamended document; Denmark, Portugal, Ireland, the UK and the Czech Republic put their referendum schedule on hold. Nearly fifty-five years since the beginning of the European voyage, attempts to reach the EU's "final and natural constitutional destiny"[1] appeared to have thrown the Union off course and into "a deep crisis".[2] Or is Europe facing a unique opportunity for political, economic and institutional renewal?

By way of introduction, this article briefly sketches some elements of the EU's current economic status, its institutional aspirations and *realpolitik*, and the range of challenges that a European constitution was envisioned to meet. It then outlines key considerations for assessing the origin and performance of constitutional governance and the political economy of federalism and applies these to a critical review of EU constitutional efforts resulting in the Draft Treaty, which was published by the Convention for the Future of Europe in July 2003, accepted in its final version by the leaders of the EU25 in June 2004,[3] and eventually rejected by the French and Dutch referenda in May 2005. The final part of the article invites readers to speculate about alternative strategies for "re-engineering" EU governance based on a review of European regional economic activity and a growing interest in the devolution of political control.

Robert Schuman and Jean Monnet, the founding fathers of the EU, tried to lay the institutional foundation for economic prosperity in order to stabilise a war-ridden, disunited continent. Current constitutional initiatives also respond to pressing needs. But this time they arise from growing popular discontent with the EU's economic and institutional achievements, perceived democratic deficits and calls for political reforms.[4] Clearly, whether one deems the EU's record of attainment and future priorities satisfactory or legitimate largely reflects one's own historical perspectives, economic interests and political biases. But there can be little doubt that, as Europe's overall economy is waning and stakeholders grow in numbers and diversity, the union in its current set-up will be hard pressed to sustain cohesion.

Europe's Economic Performance

Consider the region's ailing macroeconomic record. While the world economy is projected to expand by 4.4% in 2005, the EU25 and euro area are likely to grow by a mere 1.9% and 1.2% respectively. While in 2004 world merchandise trade expanded at twice

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[1] In the words of Germany's foreign minister Joschka Fischer, quoted in: A. J. Menéndez: Between Laeken and the Deep Blue Sea, in: European Public Law, Vol. 11, 2005, No.1, pp.105-144.

[2] Jean-Claude Juncker, Prime Minister of Luxembourg, chairman of the Brussels summit, quoted in: The Economist: Europe's identity crisis deepens, 18 June 2005.

[3] European Convention for the Future of Europe: Draft Treaty establishing a Constitution for Europe, 2003, http://www.european-convention.eu.int.

[4] Cf. EU Commission: White Paper on Governance, COM 2001, p. 428; A. J. Menéndez, op. cit.; C. Skach: We, the Peoples? Constitutionalizing the European Union, in: Journal of Common Market Studies, Vol. 43, No. 1, March 2005, pp. 149-171.

Table 1

Indicator	Maximum Score		Minimum Score	
GDP growth, percentage change. based on national currency at constant prices, 2003/4	Romania	8.59	Portugal	0.04
Industry % GDP	Romania	41.90	Ile-de-France	16.70
Service % GDP	Ile-de-France	83.10	Romania	44.60
Productivity, GDP (PPP) per person employed, US$	Luxembourg	96,456.77	Romania	18,232.89
Labour productivity: GDP (PPP) per person employed per hour, US$	Ile-de-France	56.44	Romania	9.15
Total hourly compensation for manufacturing workers (wages + supplementary benefits), US$	Denmark	35.37	Romania	0.53
Unemployment rate (% of labour force)	Iceland	3.10	Poland	18.80
Long-term unemployment	Norway	0.28	Slovenia	11.00
Exports of goods - real growth, % change based on US$ values, 2004	Poland	38.41	Ile-de-France	-15.89
Balance of trade, US$ billions, 2004	Germany	197.30	UK	-116.40
Terms of trade index, unit value of exports over unit value of imports (2000 = 100), 2004	France	111.62	Scotland	64.43
Government final consumption expenditure, % of GDP	Hungary	10.51	Sweden	28.20
Government budget surplus/deficit, % of GDP	Norway	9.63	Greece	-6.85
Dependency ratio: (population under 15 and over 64 years old, divided by active population (15 to 64 years))	Rhone-Alps	63.20	Slovak Republic	40.42
Social cohesion is a priority for the government, 0-10	Poland	2.65	Denmark	8.06
Income distribution - percentage of household incomes going to lowest 20% of households	Portugal	5.80	Czech Republic	10.30
Income distribution - percentage of household incomes going to highest 20% of households	Portugal	45.90	Slovak Republic	34.80

the rate of world output, Europe, accounting for about 46% of global trade, recorded the lowest real merchandise import growth of all regions and saw its exports increase by less than global trade. Whilst the US unemployment rate fell to 5.1% in May 2005 and Japan's unemployment rate appears stabilised at around 4.4%, the euro area unemployment rate grew to 9%. Yet the concern for aggregates blocks our view of vital differences. Europe is but a label. It covers nations with GDP growth rates ranging from 8.6% to –1.2%, export expansions varying from 38.4% to –15.9%, and national unemployment rates stretching from 3.1% to 18.1%. Europe houses economies with an industry/agriculture share of more than 65% of GDP and others whose economic activities are more than 80% service-related. In terms of labour productivity, in 2004 a European employee generated as much as US $56.44 or as little as US $9.11 worth of output per hour; hourly manufacturing wages ranged from $35.37 to $0.53. In addition, while disparities among European nations are pronounced, regional differences within them are becoming economically and politically even important.[5] In 2004, productivity per capita in Bavaria ranked $10,100 above the German average and a Catalan added $5,200 more to the Spanish GDP than his average countryman. Among the Union's 250 regions, GDP per capita was almost three times higher in the ten wealthiest locations than in the ten at the bottom of the scale.[6] Differences in skills and infrastructures explain patterns of economic activity and rising income polarisation – the coexistence of regional growth magnets and poverty traps. Enlargement adds to this.

Table 1 presents an array of European socio-economic indicators. Some of the underlying data is often aggregated to suggest patterns of economic performance and common political interests. But delineation, such as "euro bloc", "old" and "new" Europe, "Anglo-Saxon pragmatists" and "Continental welfare idealists", even if useful to incite an argument, often prove too crude to predict any consistent political behaviour. Indeed, the growing diversity of economic capacity and policy preference at the national and regional levels presents the single most important challenge to the pursuit of the EU's core objectives of market creation, policy coordination and cohesion. Past efforts to speed up decision-making and enhance the Union's management role have largely failed. France's threat of withdrawing from the Council had maintained national veto powers on all matters of "vital national interest" until the adoption of the Single European Act (SEA) in 1986. Since then, consultation and coopera-

[5] A. Maza, J. Villaverde: Regional disparities in the EU, in: Applied Economic Letters, Vol. 11, No. 8, 2004, pp. 517-523.

[6] EC Commission: 2nd Report on Economic and Social Cohesion, Brussels 2001.

tion procedures were to centralise the policy-making power in the Commission, and qualified majorities were to replace unanimity in taking substantive policy decisions. But many of the resulting policies were simply not executed. Today, twenty years later, the most crucial SEA directives have still not been implemented in the former 15 member states; distortions in markets and political representation continue and unmet policy challenges frustrate the public and necessitate fundamental reforms.[7] We shall now consider a few of these.

Demography and Productivity

In its Green Paper "Confronting Demographic Change",[8] the EU succinctly outlined the challenge ahead: with an average EU fertility rate of 1.48 and a mean increase in life-expectancy of around 4.5 years since the 1960s, Europe's working population will have shrunk by almost 20.6m in 2030 but it will have to shoulder an increased dependency ratio (currently 49%, then 66%). In addition, ageing will not only halve Europe's GNP growth potential from currently 2-2.25% to 1.25% in 2040, but the demographic profile of their electorate may make it impossible for a range of EU states to reform their unfunded pay-as-you-go pension systems. Three policy responses could, in principal, be combined:

- increase labour supply (by means of immigration, family policies, increase in employment rate, hours worked per day and over life)
- increase productivity (through improved education, R&D, technology and infrastructure investments)
- cut claims.

The pros, cons and respective feasibility of these strategies have been widely discussed.[9] What is of interest here is how the EU approached the issue.

In March 2000, heads of EU states and governments adopted the so-called Lisbon strategy. They intended to end the EU's high level of structural unemployment and widening skill and technology gaps, principally by committing their countries to a 70% employment rate and national R&D expenditure of at least 3% of GDP. The strategy involved an "open method of coordination" (OMC) – an informal, non-binding approach to building consensus among peers – as well as regular checks of targets and half-yearly reviews by the EU Council. Regrettably, the novel soft-law approach gave rise to a proliferation of non-operational objectives, process fatigue and cynicism. Within a year, the scope of the Lisbon strategy had been extended to capture the attainment of competitiveness, social cohesion and environmental sustainability; 16 action plans had formulated 28 main objectives, 120 sub-objectives and 117 indicators. In the words of one observer "(w)ith the enlargement of the Union no less than 300 annual reports are to be produced in order to check progress. (…) There is an obvious technocratic attempt to replace (…) trial and error processes inherent in the functioning of markets in general and in the fostering of innovation in particular."[10] Disappointingly also, by 2004 only two member states had spent 3% of their GDP on R&D, and the EU had lost even more ground in international benchmarking exercises, particularly in the area of productivity and technology adoption.[11]

Based on this, the reaction of the Barroso Commission in March 2005 is noteworthy for two reasons. First, it re-launched "the Lisbon Strategy (as) – a key priority of the Commission".[12] Second, it renewed the OMC process without however addressing its lack of operational clarity, incentives and sanctions. Why prescribe a general 70% employment rate irrespective of productivity differences? Why does the EU's most important policy to date receive a mere 0.1% of the EU's GNI as financial backing? Why are there no effective controls on member state implementation? No wonder therefore that, at the level of practical politics, the "Lisbon strategy" – the EU's key strategy to ensure competitiveness – is increasingly sidelined relative to more salient issues such as budget rebates, the common agricultural policy or the management of enlargement. No wonder also, that recent reviews of this policy – discussing the appropriate allocation of tasks between the Commission and member states as well as process concerns[13] – compare it unfavourably with the EU's more structured working in areas such as the Stability and Growth Pact. But particularly with regard

[7] H. Kassim: Internal Policy Developments, in: Journal of Common Market Studies, Vol. 40, Annual Review, 2002.

[8] EU Commission: Green Paper: Confronting Demographic Change, Brussels, March 2005.

[9] See e.g. S. Ederveen et al.: Growth and Jobs, in: INTERECONOMICS, Vol. 40, No. 2, March/April 2005, pp. 66-69.

[10] L. Csaba: Poetry and Reality about the Future of the Union: Reflections on the Dimensions and Nature of the Re-launch of the Lisbon Strategy, in: INTERECONOMICS, Vol. 40, No. 2, March/April 2005, pp. 61-65.

[11] C. Denis et al.: The Lisbon Strategy and the EU's structural productivity problem, in EU Commission: European Economy, in: Economic Papers, No. 221, Brussels, February 2005.

[12] J. M. Barroso: The Lisbon Strategy – a key priority of the EU Commission, talk delivered to the ETUC conference, Brussels, reprinted in: EurActiv, 1 March 2005.

[13] L. Csaba, op. cit.; C. Denis, op. cit.; and S. Ederveen et. al., op. cit.

to the latter, these reviewers may give more credit than is due.

Stability and Growth

There is still no free lunch! The benefits of a European Monetary System – deeper capital markets, better risk allocation, enhanced contestability and trade creation – come at a price: the recognition that Europe is not an optimum currency area and for that reason has an even stronger need for fiscal constraints. Unsynchronised business cycles, inflexible product and factor markets and little practice of fiscal solidarity make Europe susceptible to asymmetric shocks.[14] Fiscal rules, like those enshrined in the Maastricht Treaty's Stability and Growth Pact (SGP) should lessen pressures for more expansive monetary policies and the risk of crowding out private-sector or, in a common financial market, smaller-country borrowers. In addition, fiscal restraints limit national discretion and may be sought as a form of self-restraint to curb domestic rent-seeking behaviour. But this theory has two problems. First, painful fiscal consolidation may attain the targets in the short term but may be difficult to sustain thereafter. Second, simple rules, such as a budget deficit limit of 3% and a debt ratio of a maximum of 60% of GDP, can be gamed. Hence, the question is how to monitor and enforce the arrangement?

None of the market and non-market mechanisms currently available seem sufficient. Interest rate differentials for government bonds within the EU are negligible,[15] suggesting that financial markets may not be able to distinguish the offers of various EMU members. On the other hand, national ministers drafting national budgets possibly should not be relied upon in deciding whether they are in breach of the Treaty. Recent discussions therefore focus on how to involve national central banks, the European Court of Auditors or some central refinancing mechanism in monitoring a country's fiscal performance and on how to sanction non-compliance. But that discussion seems academic in view of the fact that the EU finds it difficult to punish big offenders, and recently suggested reforms dilute standards to the point that they turn the SGP on its head and disregard basic principles of fairness.

The Commission's recent proposal to accept a breach of the 3% deficit limit given "exceptional circumstance",[16] has come just after the Union's decision to sanction Portugal's but not France's and Germany's violation of fiscal commitments. This has led to debates about the likely economic rationale for treating different stakeholders differently – depending on size, timing of entry or generational membership. Is special treatment for larger countries justified based on their presumably larger adjustment costs and slower turnaround time or simply because of the fear that their hardship may spill over into smaller neighbours? Is the two-year waiting period prior to EMU membership, the Exchange Rate Mechanism II, truly necessary to facilitate macroeconomic convergence and structural change in accession countries, even if some – like Estonia, Lithuania and Slovenia – have a long-term record of fulfilling the very SGP criteria, which several EU15 members fail to meet? Finally, and in view of the demographic challenge discussed above, should both the debt and deficit limits not be much tighter, rather than looser, to ensure inter-generational justice and prevent current generations living at the cost of future ones? Clearly, as in the previous case, it is difficult not be grow concerned about the EU's methods of stakeholder representation.

Stakeholder Representation and Policy Games

EU decision-making processes are highly intricate and, with expanding membership, will grow in complexity. But will legitimacy improve? Concerns about national representation and policy adoption serve as an illustration here. On several occasions following the enlargement of the EU, larger member countries demanded a re-weighting of EU Council votes to avoid minorities blocking decisions that require a qualified majority (i.e. in nearly 80% of all cases). But such adjustments often came at high political cost and the price of operational efficiency. For instance, in 2000 the European Council meeting in Nice established the provision that a qualified majority must include a majority of states and represent at least 62% of the EC's population. Yet, the formula not only reduced the passage probability in an enlarged EU27 to 2.1%, thereby effectively deadlocking decision-making,[17] it also required concession in operating another EU institution. The Nice Council meeting sought to establish fair methods for redistributing seats in the EU Parliament to facilitate the ultimate enlargement to EU27 without (greatly) increasing the number of seats. However, in the final hours of negotiations "complications arose"

[14] Cf. R. Mundell: A Theory of Optimum Currency Areas, in: American Economic Review, Vol. 51, 1961, pp. 657-665; R. McKinnion: Optimum Currency Areas, in: American Economic Review, Vol. 53, 1963, pp. 207-222.

[15] W. Boonstra: Proposal for a Better Stability Pact, in: INTERECONOMICS, Vol. 40, No. 1, January/February 2005, pp. 4-9.

[16] For a discussion see C. Hefeker: Will a Revised Stability Pact Improve Fiscal Policy in Europe, in: INTERECONOMICS, Vol. 40, No. 1, January/February 2005, pp. 17-21.

[17] R. Baldwin, E. Berglöf, F. Giavazzi, M. Widgrén: Nice Try: Should the Treaty of Nice be Ratified?, CEPR Paper MEI 11, London 2001, Centre for European Policy Research.

and so "seats were thrown around 'like loose change' in order to make Belgium (and later Greece and Portugal) accept the new voting weights. (As a result) "the Czech Republic and Hungary, with the same population as Belgium, were given fewer seats".[18] Clearly, political representation within the EU is a major cause for concern; but so are member states' strategies for setting policy agendas, shaping legislation or obstructing implementation.

All member states have a principle interest in "uploading" their policies to the European level, but they differ in their willingness and capacity to drive standards.[19] In drafting EU environmental rules, for example, Austria, Denmark, Finland, Germany, the Netherlands and Sweden tend to "set the pace," using their combined voting powers and national expertise in dealing with the Commission. Operating from a less developed regulatory base, Greece, Portugal and Spain typically "drag their feet" and accept more stringent measures only if compensation can be obtained. Belgium, France, Ireland and the UK pursue a "fence-sitting" strategy – playing the "environmental card" in negotiating unrelated issues or scape-goating Brussels for inconvenient policy decisions. Clearly, preferred strategies change with topics. The level of regulation that is finally obtained reflects the composition of the winning coalition and the voting method applied. However, with stakeholders growing in numbers and diversity, how likely is it that centralised institutional bargaining within the EU will result in adequate, economically efficient and legitimate policy?

In sum, recent EU policy experiences illustrate three points. *First*, soft-law methods, as in the case of the Lisbon Strategy, tend to end up in a proliferation of objectives and monitoring mechanisms, cause process fatigue and cynicism and drag on even after their failure has long been established. *Second*, structured approaches to European market regulation, as in the case of the Single European Act or the Stability and Growth Pact, often suffer from a mix of non-compliance and under-enforcement, ultimately leading to the discriminatory application of ever more diluted standards and the acceptance of effective defiance by some. *Third*, both outcomes reflect the EU's mode of operation, its set of responsibilities and type of stakeholder representation. The public expresses its frustration in voter turnouts and opinion polls.[20]

More broadly, however, these three issues represent the fundamental challenges faced by any union, political or otherwise. Alliances are viable only to the extent that they create and maintain procedural and substantive consensus and deference to it. They tend to expand to some point of saturation and disintegrate once membership grows further in numbers and diversity, its leadership is closed to participation or does not deliver benefits, and necessary reforms are delayed or not pursued by all.[21] The EU faces a typical alliance problem and is forced to review the scope of policy-making at, and in between, different levels of government and to establish efficient rules of engagement and adjudication. It is a matter of institutional and constitutional reform.

In fact, the current debate on the EU's constitution emanates from institutional reform initiatives intended to improve performance and re-establish operational consensus. These were inspired by member states calling, at the Nice Summit, for a debate on the delineation of competence between the EU and the member states, the principle of subsidiarity and the role of the national parliaments in the EU's institutional architecture. They were furthered by the Prodi Commission's White Paper on Good Governance proposing opening up the EU Commission to national, regional and local consultation and accountability while giving it more direct powers to speed up the implementation of legislation. Finally, they were channelled by a Committee of "wise men," conveyed ad hoc by the Belgian government, in the Laeken Declaration in December 2001. Yet, relative to previous initiatives which concentrated on improving the functioning of EU decision processes, the focus of the Laeken Declaration was on *democracy* and *legitimacy* – it resulted in an explicit process of constitution making. But was the process and outcome of trying to constitutionalise the EU democratic and legitimate? Does the proposed constitution fix the alliance problem? Which conceivable alternatives ought to be considered and which standards apply?

[18] A. Moberg: The Nice Treaty and Voting Rules in the Council, in: Journal of Common Market Studies, Vol. 40, No. 2, 2002, pp. 259-82.

[19] For a detailed assessment see T. A. Börzel: Pace-Setting, Foot-Dragging, and Fence-Sitting: Member State Responses to Europeanization, in: Journal of Common Market Studies, Vol. 40, No.2, 2002, pp. 193-214; and D. Liefferink, M. S. Andersen: Strategies of the "Green" Member States in EU Environmental Policy-making, in: Journal of European Public Policy, Vol. 5, No. 2, 1998, pp. 254-70.

[20] The voter turn-out in the elections for the European Parliament in June 2004 reached an all-time low of 45.7%. In a spring 2004 Eurobarometer opinion poll, taken in the 15 countries that made up the EU before enlargement, 21% of the respondents said that they had a negative image of the EU and 26% that considered it "a waste of money."

[21] For a review of classical perspectives see R. Dougherty, J. Pfalzgraph: Theories of International Relations, New York, 1984, Harcourt.

Some Perspectives on Constitutional Governance

Before assessing the EU's recent constitutional efforts a number of questions ought to be clarified. What is the role of a constitution and what makes it legitimate? Who should set norms and implement policies for the purpose of efficiency? What are the costs and benefits of alternative methods for allocating responsibilities across different levels of government?

Political systems differ not only in terms of who articulates and aggregates interests and who makes, implements and adjudicates policy decisions, but also in terms of the focus and extent of regulatory output, the level and distribution of income and the forms and expressions of political culture. The predictability of a given system relies on its underlying rules being understood and stable in guiding cases of unavoidable discretion. To this end, constitutions provide the highest-ranked, legally justifiable definition of powers and duties among governmental organisations, societal actors and citizens.[22] The fact that they can only be amended by special procedures not applicable to ordinary legislation provides a stable basis for assessing issues of accountability. But it also poses questions about a constitution's own legitimacy – a priori and over time.

Some recent reviews of EU constitutional efforts apply some notion of "output-oriented" authority.[23] Accordingly, a constitution may be considered legitimate if it is believed that "for that particular country at that particular historical juncture no other type of regime could assure a more successful pursuit of collective goals".[24] But without counterfactual evidence and any clarification of process and performance objectives how is one to judge? Clearly, output-oriented authority is a pragmatic shortcut into a blind alley. A deontological discussion of legitimacy is required and necessarily broader.

Normative theories of constitutionalism – from classical natural law foundations to current perspectives on "deliberative democracy"[25] and constitutional economics[26] – link legitimacy to voluntarism, participation and efficiency. Reasonable people escape the brutish state of nature by handing over certain individual liberties to a state that monopolises the power of coercion and from thereon guarantees their private autonomy. Put differently, bottom-up delegation "constitutes" the original state. What legitimises its evolution thereafter, hinges on citizens' right to limit state activity and participate in deliberating and monitoring laws and policy.

In Continental European and common law tradition, with their respective emphasis on legislative and judicial norm development, public rules are, for all practical purposes, legitimised through either direct or representative democracy or the election of constitutional courts.[27] Requirements for "deliberatively democratic" legitimacy are stronger, calling on citizens to have the principle opportunity to participate in identifying problems, selecting alternative responses for analysis and deliberation, formulating and reviewing norms, and screening reviewers and judges. Direct political participation not only protects individual rights but it is also seen to educate citizens and make them aware of and respect the positions of others; it is the source of civic virtues. In the words of the classical theory of democracy, the "deliberatively democratic" ideal is a *polyarchic* constitution, which results from full "popular inclusion" in providing legislative inputs and complete "popular contestation" of legislative results.[28] Real-world rule-making, however, often falls into three other categories, which limit citizen involvement to either providing inputs or ratifying outputs, or exclude the public entirely from any legislative participation.[29] In the latter case, *hegemonic* constitutions result that attempt to impose a central design on decentral circumstances. As such, this mode not only conflicts with any "deliberatively democratic" ideal but also falls short of central efficiency concerns espoused by the economic analysis of law.

Efficient Governance and Inter-governmental Coordination

Constitutional economists and public choice theorists argue for the devolution of legislative and regulatory powers and the need to constrain political

[22] For a detailed discussion see J. Raz: On the Authority and Interpretation of Constitutions: Some Preliminaries, in: L. Alexander (ed.): Constitutionalism, 1998, Cambridge University Press, pp. 152-153.

[23] C. Skach, op. cit.

[24] J. J. Linz: Crisis, Breakdown and Re-equilibration, in J. J. Linz, A. Stephan (eds.): Breakdown of Democratic Regimes, Baltimore 1978, Johns Hopkins University Press, p. 18.

[25] For a review see C. Nino: The Constitution of Deliberative Democracy, New Haven and London 1996, Yale University Press; J. Habermas: Constitutional Democracy, A Paradoxical Union of Contradictory Principles, in: Political Theory, Vol. 29, (2001) pp. 766-781.

[26] For a review see D. C. Mueller: Public Choice III, 2003, Cambridge University Press.

[27] For reasons of the separation of powers, they are not seen to create new law but to interpret norms to execute legislative intent.

[28] R. A. Dahl: Polyarchy: Participation and Opposition, New Haven 1973, Yale University Press.

[29] C. Skach, op. cit., presents a positioning map along the dimensions of public inclusion and public contestation, with "polyarchic" and "hegemonic" presenting full and no score on each dimension respectively. "Full oligarchic" constitution-making has no public input but full public contestation, the reverse is labeled "inclusive hegemonic".

discretion through markets. Setting norms de-centrally is seen to better reflect local conditions and citizen preference, increase legal innovation and limit the negative impact of policy discretion or corruption. Issue-based voting best sanctions the process. From this perspective, aggregating issues into political platforms, harmonising rules, extending the reach of constitutional cover or centralising the making of a constitution amounts to colluding in the market for political control. Yet, it is also clear that for lower-level regulatory and legislative competition to work at all, some market-creating constitutional norms are nevertheless required. The challenge is to balance the benefits of decentralisation against potentially foregone efficiencies of central scale and coordination. How can the trade-off be managed?

Most of the literature on federalism, discussing the comparative efficiency of alternative mechanisms for inter-governmental coordination,[30] abstract from two classical models. On the one hand, there is Montesquieu's view of the *confederate republic*. It allows small city-states to pursue democratic rights and civic virtues while linking with others to further pursue common objectives based on unanimous decisions and the right to exit at any time. On the other hand, James Madison, appreciating the city-states' ability to efficiently produce in line with local demands, links them up in a *compound republic* under a central government that receives its legitimacy from the majority approval of all its citizens rather than from the unanimous consent of all city states. The executive implements the laws approved by the legislature. Juxtaposing both perspectives is sometimes meant to illustrate a presumed impasse between pursuing political and economic objectives, between civic virtues and efficiency. However, analyses on the political economy of federalism do not appear to support this.

Models of federalism typically explore the interaction of four sets of variables: levels of governmental hierarchy (local, state, central); levels of local representation in the centre (from town-meetings sending one representative to the central legislature to presidential formats in which all city states elect one representative in a single central election); assignments of policy responsibilities for supplying national or particularistic, local public goods; and decision-making by unanimity or some form of majority rule. Even at the risk of oversimplifying, some broad patterns emerge from these studies.

Under unanimity, increasing representation at the central level increases spending for both national and particularistic goods. Under majority rule, increases in spending on national public goods require increases in the representation of the coalition favouring that particular good, while spending on particularistic goods increases depending on who ultimately pays for building up the political demand for it. A strong central executive office may check on the potential risk of increased spending through increased representation but itself would need to be balanced by some representation of local interest. Alternatively, changing the assignment of responsibilities may lessen the need for adding layers of controls to deal with deep-seated distrust. In fact, modelling the impact of assigning policy responsibilities to local authorities for the above cases demonstrates that local provision of particularistic goods is most efficient as long as inter-state free-riding can be avoided. The rule of thumb is: national public goods are efficiently assigned to the centre; the provision of particularistic goods is better left to locals. Hence, there may not be a need to choose between civic virtue and efficiency as long as economies of scale and spillovers of governmental activities can be clearly identified, assignment principles are constitutionally pronounced and adequately applied. In practice, this is where the problem starts.

Altogether, constitutions present the highest-ranked, stable legal definition of societal organisation. They are legitimate as long as they reflect the principal of voluntarism and the public's participation in providing legislative input and contesting results. Hegemonic constitutions not only conflict with any deliberatively democratic ideal but, from an economic perspective, amount to monopolising the market for regulatory and political control. In general, devolving legislative and regulatory powers is best to capture local conditions and fuel regulatory innovation and efficiency, but finds its limits in potentially foregone efficiencies of central scale and coordination. Seeking to combine democratic benefits and civic virtue with the need for efficient public office, constitutional assignments of public responsibilities must reflect the economics of the given service. Where changes in underlying economic conditions blur decisions about assignments, political choice needs to be made contestable, principally by involving delegated, decentralised controls. These ideas will now be applied to assess the process and outcome of the EU's recent constitutional efforts.

Assessing the EU's Recent Constitutional Efforts

The *Draft Treaty establishing a Constitution for Europe*, as accepted in its final version by the leaders of

[30] For a review see R. P. Inman, D. L. Rubinfeld: The political economy of federalism, in: D. C. Mueller (ed.): Perspectives on Public Choice, 1997, Cambridge University Press, pp. 73-105; as well as D. C. Mueller: Public Choice III, op. cit.

the EU25 in June 2004,[31] is divided into four parts, all of equal rank. Following a *Preamble* recalling the history and heritage of Europe and its determination to transcend its divisions, *Part I* is devoted to the principles, objectives and institutional provisions governing the new EU. *Part II* comprises the European Chapter of Fundamental Rights. *Part III* includes the provisions governing the policies and functioning of the Union. *Part IV* groups together the general and final provisions of the Constitution, including entry into force, the procedure for revising the Constitution and the repeal of earlier Treaties. A number of protocols have been annexed to the Treaty establishing the Constitution, in particular the Protocol on the role of national parliaments in the European Union; the Protocol on the application of the principles of subsidiarity and proportionality, the Protocol of the Euro Group, the Protocol amending the Euratom Treaty, and the Protocol on the transitional provisions relating to the institutions and bodies of the Union.

In the words of the EU Commission, the Draft Treaty establishes the EU as a single legal personality and "provides a clearer presentation of competencies" and "a simplified set of legal instruments" to act. Moreover, it is seen "to confirm in one fundamental text a number of provisions aiming at more democratic, transparent and controllable EU institutions that are closer to the citizen".[32] The following assesses the *process* that led to the formulation of the Draft Treaty and its rejection by the French and Dutch referenda in May 2005, and the *outcome*, i.e. the relationship between the EU, member states and citizens that is being proposed.

Process

Before discussing the democratic credentials of the process that led to the formulation of the Draft Treaty it is necessary to pin-point its beginning. This is important since it has been argued that the Draft Treaty requires neither any broad-based "public inclusion" nor "contestation" as it merely elaborates an already existing constitutional order based on the Treaties, the European Court of Justice doctrine and the language used in it.[33] Already in 1963 the European Court of Justice's position on *Van Gend* spoke in terms of the Communities creating a "new legal order of international law for the benefit of which the states have limited their sovereign rights".[34] And in *Les Verts*, 1986, the Court described the Treaty as the basic constitutional charter of the Community.[35] However, judicial norm-setting is typically limited to expressing legislative intent. Yet, since the Treaties are merely diplomatically negotiated international contracts they do not provide any direct democratic foundation for constituting the Union. EU constitutional efforts are clearly more recent and their democratic legitimacy ought to be discussed.

The initial thrust – emanating from the announcements of member states during the Nice summit, the Prodi Commission's White Paper of Good Governance, the ad hoc meeting of "wise men" and finally the "selection" of the Convention's chairman and vice-chairmen – reflected political entrepreneurship and secretive, bureaucratic manoeuvring rather than any direct democratic involvement. However, during the Convention representation, at least formally, improved. All but two members of the Convention on the Future of Europe were elected representatives appointed by national and European parliaments. In addition, the Economic and Social Committee and the Committee of the Regions, the social partners and the European Ombudsman were allowed to send observers.[36] Still, the agenda had been broadly set upfront, and most effort was spent on process deliberation, with little time left for the concrete discussion of final proposals. In addition, voting had been excluded to drive consensus on key issues. Given that the Convention often failed to document why certain decisions had been taken, a voting record would have lent outcomes at least some modicum of normative authority.[37]

The Convention concluded its work at the end of July 2003, which drastically shrunk any opportunity for in-depth public debate prior to the intergovernmental negotiations that began in the autumn. The Intergovernmental Conference, shrouded in secrecy and hampered by drafting complexities, gave no chance to the general public to bring divisive issues, like those surrounding "Social Europe," to the fore. During the European Council meeting in December 2003, Poland and Spain vetoed the principle of double majority, thereby blocking an agreement, and gave rise to at least six

[31] See Treaty establishing a Constitution for Europe, 29 October 2004, http://ue.eu.int/igcpdf/en/04/cg00/cg00087-re02.en04.pdf.

[32] See htpp://europa.eu.int/constitution.

[33] For a detailed discussion of this point see P. Craig: Constitutions, Constitutionalism and the European Union, in: European Law Journal, Vol. 7, No. 2, June 2001, pp. 125-150.

[34] Case 26/62 N.V. Algemene Transporten Expeditie Onderneming van Gend en Loos v. Nederlands Administratie de Belastingen (1963) ECR 1, 12.

[35] Case 294/83 Parti Ecologiste 'Les Verts' v. Parliament (1986) ECR 1339, 1365.

[36] Still, it has been argued that already the composition of the Convention might have tilted the balance towards a centralised outcome. Cf. The European Constitutional Group: The Constitutional Proposal of the European Convention: An Appraisal and Explanation, in: IEA Economic Affairs, March 2004, pp. 22-27.

[37] A. J. Menédez, op. cit.

major modifications of the original Draft. It was only due to the dismissal of both countries' incumbent governments in the spring of 2004 that the final agreement was reached in June 2004. In the eyes of an observer "(t)he failure of the Brussels Summit in December 2003 and (…) the dilution of the Draft put forward by the Convention (…) entrenched the perception that the process of writing primary Union law was a matter of cruel bargaining and pork-barrel politics".[38]

Arguably efforts to initiate and develop an EU constitution did not include the general public in any direct way. In fact, one may question whether it was at all possible for elected politicians, national and European parliaments and the Convention to capture the mind of the EU public, let alone its common constitutional will. In an opinion poll, taken in the 15 countries that made up the EU before enlargement, only 43% of the respondents said they had a positive image of the Union, against 21% that had a negative image and 26% that considered it "a waste of money".[39] The voter turn-out in the elections for the European Parliament in June 2004 had reached an all time low of 45.7%; in the Netherlands, for instance, it had dropped to less than 30% compared to almost 80% in 1979. With very little "public inclusion" in the origination of the Draft, maintaining some democratic legitimacy required involving the general public in "contesting" the outcome.

In September 2004, eleven of the 25 EU countries – Belgium, the UK, the Czech Republic, Denmark, France, Ireland, Luxembourg, the Netherlands, Poland, Portugal and Spain – had promised or all but promised to hold a referendum on the constitution. To be clear, citizens were not asked to vote, let alone comment, on parts of the text but to either endorse or reject it *en bloc*. Yet, following the French and Dutch rejection of the Draft Constitution in May 2005, Denmark, Portugal, Ireland, the UK and the Czech Republic put their referendum schedule on hold. This reaction was not unexpected. A year earlier, the Intergovernmental Conference had adopted a "Declaration on the ratification of the treaty establishing the Constitution" providing for a "political solution" to be found if a member state failed to ratify the Treaty. This sheds a sobering light on a process that had been started by interpreting the public's discontent with the EU as "an unarticulated will to enact a constitution for the Union"[40] and was to celebrate democracy and legitimacy. Did the French and the Dutch reject the constitution or the method used to attain it? With the process lacking democratic credentials, is the result more in line with the outlined normative reference?

Outcome

The following comments on the Draft Treaty relate to

- its constitutional character
- aspects of institutional representation
- the Commission's roles and the concepts of subsidiarity and proportionality
- the Council voting rules
- concerns for regulatory competition viz. harmonisation
- the logic of task assignment.

First, for constitutions to provide the highest-ranked, stable, legally justifiable definition of powers, duties and rights in society, they are necessarily meta rules, at the top of any other legislation, requiring lower level laws to spell out specifics. They need to cover vital principles to avoid under-constitutionalisation but must refrain from over-specifying lest they stifle the discretion necessary to deal with specific circumstances. The Draft Treaty comprises of four, in various ways highly interrelated, parts of different level of detail but equal constitutional standing. To avoid the evident danger of over-constitutionalisation, inevitable reforms require simplified procedures. But this drastically diminishes the constitutional role that the Draft Treaty can play.

Second, the Draft Treaty only slightly modifies the EU institutional framework. The European Council continues to operate as an advisory body to define general directions and priorities, largely based on consensus, with no legislative authority but now headed by a president elected for 2½ years. Art. 29 clarifies the judicial system as "the Court of Justice, the General Court and specialised courts". The High Representative for Common Foreign and Security Policy and the Commissioner for Foreign Relations are merged into a Union Minister of Foreign Affairs. The European Central Bank is identified as an EU institution. The Council of Ministers, together with the European Parliament, exercises legislative and budgetary functions by means of an extended co-decision procedure. The Commission continues its task of "inter-institutional programming", performs executive functions and (except for foreign and security policy) external representation.

[38] Ibid., pp. 119-120.

[39] Eurobarometer, op. cit.

[40] A. J. Menédez, op. cit., p. 122.

In this context, the role of the European Parliament, as the only directly elected representation of European citizens, is said to be enhanced by extending the co-decision procedure into the "ordinary legislative procedure," making it the "co-legislator in almost all cases, with the exception of a dozen acts, where it will only be consulted". But the Council's veto power qualifies the Parliament's position, and both institutions will continue merely to react to the Commission, which maintains its near monopoly of legislative initiative. Also, the EU Parliament is part of the EU institutional framework with no existence outside it and is therefore interested in maintaining the centre's role. European citizens have the right to submit legislative proposals to the legislator if they manage to submit 1 000 000 signatures from a "significant" number of member states. But the Draft Treaty does not commit the EU to any reaction. Finally, national parliaments are mere bystanders, entitled to receiving information and to guard national competencies based on the principle of subsidiarity. But here, too, the required process is far from clear-cut.

Third, Art.I-11 states that competencies not conferred upon the Union in the constitution remain with the member states; Art.I-13 specifies those areas in which the Union has exclusive competence. Art.I-14 contains a non-exhaustive list of shared competencies, in which both Union and member states may act in parallel. Art.I-17 specifies areas in which the Union will have competence to support, coordinate or supplement the actions of the member states. Art.I-18 provides a "flexibility clause" that allows the Union to expand its reach based on the Council's unanimous endorsement of a Commission proposal and with the consent of the European Parliament. The exercise of any of these competencies is governed by the principles of subsidiarity and proportionality.

Art.I-11(3) states that, "Under the principle of subsidiarity, in areas which do not fall within its exclusive competence, the Union shall act only if and insofar as the objectives of the proposed action cannot be sufficiently achieved by the member states, either at central level or at regional and local level, but can rather, by reason of the scale or effects of the proposed action, be better achieved at Union level." And Art.I-11(4) holds that, "Under the principle of proportionality, the content and form of Union action shall not exceed what is necessary to achieve the objectives of the Constitution."

What are the options for member states to resist? National Parliaments have six weeks to send a reasoned opinion to object but that period may – in urgent cases – collapse to ten days.[41] To respond in time, national parliaments need to continuously monitor EU activities and be able to change their legislative calendars to react. In any case, the Commission must review its proposal only if a third of national parliaments consider that a Commission proposal does not comply with the principle of subsidiarity. Hence, for any specific item affecting only a small number of member states, the coordination costs may be substantial and move competence to the EU centre. This raises the general issue of EU decision-making procedures, particularly voting rules, and thereby perhaps the most significant change proposed by the Convention.

Fourth, the scope of unanimous decision-making in the EU framework is broadly reduced. Laws on the Union's "own resources" and the "financial perspectives" must be adopted unanimously, as must any revision of the Constitution itself. Also, in addition to some specific provisions, unanimity is retained in the field of taxation and partially in the fields of social policy and common foreign and security policy. However, so-called *passarelles* allow a unanimous decision to be (partially) transformed into a qualified majority.

The new Council voting system repeals the weighting of votes and bases the qualified majority on only two criteria – majority of member states and of the population of the Union. Double majority is seen as an expression of double legitimacy. Different from the Convention's proposal, Art.I-25 of the Draft Treaty raises the threshold requiring

- a qualified majority to be supported by 55% of the members of the Council representing 65% (rather than 60%) of the population
- a blocking minority to comprise at least of four Council members.

Council members representing ¾ of the blocking minority – whether based on member states or population – can demand that a vote be postponed and the discussion continue for a reasonable time to reach broader consensus within the Council.

The changes will move the probability of acceptance above the level resulting from the Nice Treaty but lower than the calculated 22% in line with the original proposal by the Convent. This will limit the risk of blockage and speed up decision-making. But operational speed clearly is not the sole objective in deciding on constitutional standards. To quote an observer

[41] See both "Protocol on the Role of National Parliaments in the European Union" and "Protocol on the Application of the Principles of Subsidiarity and Proportionality", Annex I and II to the Draft Treaty, op. cit.

"(e)ven more than before, a majority of highly regulated member states could impose their regulations on the less regulated member states (…) As competition from the less regulated member states diminishes, the intensity of regulation will increase in the highly regulated member states".[42] Seen in this way, EU constitutional reform may speed operational efficiency but at the price of reduced regulatory competition and, ultimately, competitiveness. Other indicators point in the same direction.

Fifth, Art.I-2 lists a set of common values which are considered to be shared by member states and therefore are also reflected in the criteria for accession and suspending membership, Art.I-58 and Art.I-59. Art.I-3 covers the Union's internal and external objectives, including among other things the promotion of a "highly competitive social market economy" which, refined in Art.III-115 to Art.III-122, implies fulfilling "requirements relating to employment and social policy." Art I-15 states "1. The Member States shall coordinate their economic policies within the Union. To this end, the Council of Ministers shall adopt measures, in particular broad guidelines for these policies. ... 2. The Union shall take measures to ensure coordination of the employment policies of the Member States, in particular by defining guidelines for these policies. 3. The Union may take initiatives to ensure coordination of member states' social policies." The Member States shall facilitate the achievement of the Union's tasks and refrain from any measure which could jeopardize the attainment of the Union's objectives" (Art.I-5(2)3). Despite its frequent assertions to the contrary, the EU clearly aims at creating cohesion based on harmonising policies rather than benefiting from internal regulatory competition. What is the economic rationale for the EU's broad-scale involvement?

Sixth, we have above pointed to the need to clearly identify economies of scale and spillovers of governmental activities as the basis for task assignment. Research on fiscal federalism offers a host of considerations on how to determine at which level of government to allocate the responsibility for various tasks.[43] But there is no evidence that the EU's constitutional effort is inspired by any attempt to assess the economics of public service provision. The Draft Treaty, through the notion of subsidiarity and proportionality, merely establishes a process that member states may follow to contest any further encroachment by the EU. The relevant protocols define the need to consider quantitative and qualitative evidence only at that review stage. In addition, contrary to the principles outlined in the Prodi White Paper on Good Governance, there has been no attempt to market-test the need for the public provision of specific services or the allocation of tasks to local or regional levels of government. Any argument for or against specific task allocations is therefore bound to reflect the observer's (de-)centralisation biases rather than economic evidence.

In sum, contrary to the Commission's intention to bring more democratic EU institutions closer to citizens, efforts to initiate and develop an EU constitution did not allow for public inputs and resulted in a document that the general public was to either endorse or reject *en bloc*. However, it is not only for process reasons that the rejection by the Dutch and the French referenda should be welcomed. Rather, the outcome of the process is simply unacceptable. Formally, the Draft Treaty's comprehensiveness requires simplified adjustment mechanisms that cancel out the constitutional role that it could play. Institutionally, the relationship between the Commission, the Councils, and citizen representation are largely maintained. The value of co-decision procedures has not been upgraded; citizens may provide input but its impact is unclear; national parliaments are largely in a reactive role. Finally, utilising the principles of subsidiarity and proportionality requires an economic assessment of public service provision that should have taken place at the outset of the constitutional effort. This might not have resulted in a completely different allocation of tasks and responsibilities, but it would have at least helped to address the EU's need for attaining deference and procedural and substantive consensus. But this would have required dispassionate constitutional initiative able to side-step Europe's conventional patterns of political organisation.

Re-engineering Europe

Devising a constitution for Europe is also about finding the right scale at which to coordinate a competitive European economy. The current discussion almost entirely focuses on the interaction between the EU and nation states and thereby neglects important regional or even urban dimensions. In fact many commentators now see city regions as motors of the European economy and as useful political vehicles for managing EU enlargement. Others advocate devolving power from national to regional and local governments simply because traditional state benefits – such as free trade among regions, the efficient provision of public goods, or access to national infrastructures and standards

[42] European Constitutional Group: A Proposal for a European Constitution, in: European Policy Forum 2004.

[43] Cf. W. E. Oates: An Essay on Fiscal Federalism, in: Journal of Economic Literature, Vol. XXXVII, 1999, pp. 1120-49.

– could be made available within a broader and possibly more efficient, supranational framework.[44]

At present, European regions and metropolitan areas differ in their constitutional set-up, degree of autonomy and fiscal and plan-making powers. But they share an ambition that inadvertently challenges formal regional and national boundaries and the competencies of adjacent levels of political hierarchy. A cursory view suffices to show that issues surrounding the need for inter- and intra-regional coordination mirror those involved in constitutionalising Europe. The ultimate response in either case must be the same.

At the regional level, a location's economic base and performance drives its choice between cooperative and competitive coordination. While cooperation within and among the EU's waning objective II regions appears motivated by the need to co-opt competition,[45] urban growth areas are often observed to be single-mindedly pursuing their individual growth objective and to look outside their "home" base for economic leverage and political clout. The Region Urbaine de Lyon, for example, accounts for 80% of the GDP of the Rhone-Alp region but is reported to see its economic interests more closely linked to its vibrant cross-regional partnership with Montpellier and Marseilles and its own interaction with the European Commission. A host of issues may arise from this. But whether one debates the extent to which regional cooperation delays adjustments, or the need for strong regional centres to support ailing peripheries, in the final analysis the question is who should decide and which process coordinates best?

National responses to growing regional demands reflect different views on policy aims and means. Italy and Spain granted more fiscal autonomy to regions, which allowed those with a strong tax base to compete with equally powerful European centres, while it kept others more closely tied to state transfers. Conversely, German Länder, in spite of having large responsibilities and resources, have no autonomy over taxation and, for reasons of social cohesion, see their tax revenues largely equalised. Following reunification, an initiative by the federal government has led to the review of regional and urban structures in an attempt to promote metropolitan areas for global competition. French regions, which contrary to the common view of French centralism had enjoyed substantial freedom to fix tax rates, recently lost some of their fiscal autonomy. In addition, Paris controls budgets and EU funds to hold regions accountable for infrastructure investments and forge competitive linkages between them. Here one may challenge the merits of fiscal competition in a federal system or any government's ability to outsmart markets in determining growth centres. But the key concern should be, who should decide and which process coordinates best?

Finally, the EU Commission's view on regions is at best ambivalent. On the one hand, the EU's Committee of Regions, set up in 1994 under the Maastricht Treaty, is an advisory body composed of the EU's regional and local authorities to ensure that regional and local prerogatives are represented. On the other hand, the Commission avoids antagonising powerful member countries and therefore does not overtly encourage regionalist ambitions. For that reason, the Committee of Regions presents only a weak form of grassroots representation, and the constitutional convention rebuffed any effort by Catalonia, Scotland, Flanders or the German Länder to have a bigger role for regions written into the Draft Treaty. In addition, a European Parliament resolution of 1999 called on the EU to avoid uneven growth, which translated into initiatives by the EU's Structural Funds and the Cohesion Fund to achieve regional uniformity of factor incomes. Of course, one may question whether the EU should represent member states, regions or citizens or whether any EU policy should aim for equity or efficiency as a means to sustain cohesion. But also here the key concern should be, who should decide and which process coordinates best?

In each case the response must be the same. Devolving legislative and regulatory powers in line with economic efficiency and deliberatively democratic ideals calls for unanimous decisions on

- the centralisation of only a few key functions necessary for the provision of truly large-scale public goods
- the creation and enforcement of simple, market creating norms
- the delegation of authority on all other issues to the most decentralised level of governance.

This not only drastically limits the need for procedural and substantive consensus and deference to it, and so contributes to solving the EU's alliance problem. It also links civic virtues and efficiency and calls on citizens to self-select. What is the implication for the European constitutional efforts? Go back to the drawing board!

[44] P. Newman: Changing Patterns of Regional Governance in the EU, in: Urban Studies, Vol. 37, No. 5-6, May 2000.

[45] A. Amin: An Institutionalist Perspective on Regional Economic Development, in: International Journal of Urban and Regional Research, Vol. 23, No. 2, 1999, pp. 365-378.