

# Courts as political actors: Resistance to the EU's new economic governance mechanisms at the domestic level

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# EMU CHOICES

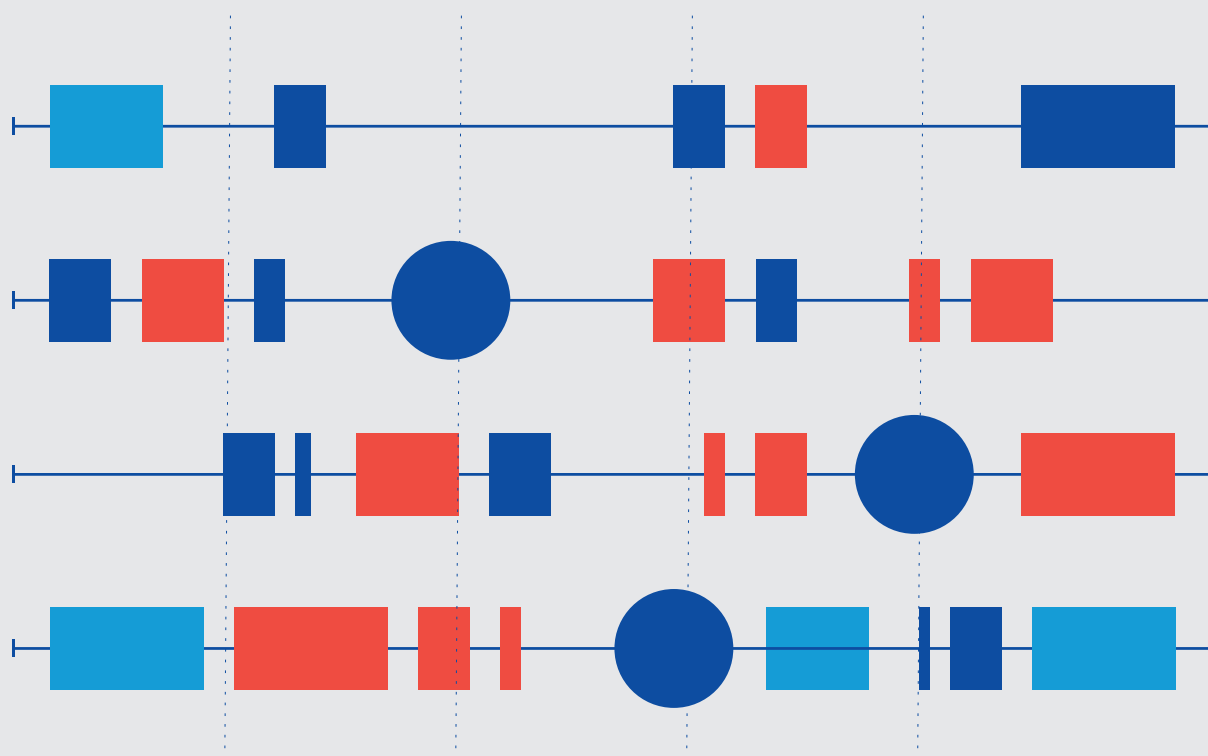
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## Courts as political actors: Resistance to the EU's new economic governance mechanisms at the domestic level

Sabine Saurugger and Clément Fontan

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## **Courts as political actors: resistance to the EU’s new economic governance mechanisms at the domestic level<sup>1</sup>.**

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### **Abstract**

Courts are increasingly considered to be political actors in liberal democracies as they deal with fundamental disagreements within a given polity. Because of its political salience and the extent of its consequences, the crisis of the Economic and Monetary Union (EMU) has exposed such fundamental disagreements between and within its member-states, which numerous plaintiffs have brought before domestic courts and the Court of Justice of the European Union (CJEU).

The aim of this paper is to analyze this judicialization of the EMU crisis. Using a database on lawsuits introduced in all 28 member states with regard to crisis measures and the new EMU governance mechanisms introduced since 2010, we study which actors use the courts and under which circumstances. This article is embedded in the politics of law literature, developed in EU studies since the 1980s. Based on this literature we developed five central hypotheses on actors and legal timing in order to understand the process and the reasons for the judicialization of the EMU crisis.

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## **Introduction**

Economic systems do not exist in a vacuum: they are embedded in a complex structure of social relations, political governance and law (Polanyi, 1944). In the Economic and Monetary Union (EMU) law plays a central, yet ambiguous role because of the lack of a unified economic government. On the one hand, EMU is a rule-based system in which law plays a central role in the coordination of national economies. On the other hand, the EMU is characterized by a logic of intergovernmental bargaining between its member states for its economic policies. Because of these two characteristics, the numerous political struggles over the EMU governance often result in struggles over the definition of the EMU legal system.

The legal system governing the EMU has been questioned since the start of the Eurozone crisis in 2009 for three reasons. First, the political answer to the crisis has weakened the responsiveness of the political system to citizens' demands (Schaeffer and Streeck, 2013, Hall, 2012, Scharpf, 2015). Second, the answer to the crisis has aggravated the tensions between creditor and debtor countries within the EMU (Dyson, 2014). Third, in order to overcome the crisis, EMU policymakers have created new EMU institutions and strengthened existing rules, reinforced the Court of Justice of the EU's (CJEU) and the Commission's competencies, while the ECB has largely expanded its role within the EMU governance. Logically, this extension of EMU governance has opened new venues for legal challenges. Because of these three elements, courts increasingly participate to the build-up of the EMU institutional settings and the settlement of disputes about the rules governing EMU.

In other words, the Eurozone crisis opened the opportunity for the judicialization of EMU politics, that is "the reliance on courts and judicial means for addressing core moral predicaments, public policy questions, and political controversies" (Hirschl, 2008: 1). Beyond human and societal rights' issues, the judicialization process indeed increasingly encompasses "mega-politics", which are matters of the utmost importance that often divide or define the boundaries of the whole polity. The political answer of the Eurozone crisis is doubtless part of mega-politics as it tackles fundamental issues such as the degree of solidarity among EMU countries or the relationship between Europe's economic and social constitutions, which affect basic core normative values such as democracy, transparency and social rights (Tuori and Tuori, 2014). Since the crisis, European courts at the national and supranational levels have been asked to deal with core normative issues that were left unspecified or unsolved during the EMU creation.

The judicialization of the political answer to the Eurozone crisis has been mainly tackled by law scholars. They have analyzed the decisions taken by national high courts on Eurocrisis measures by developing a comparative constitutional analysis (Contiades, 2013; Adams, Fabbrini and Larouche, 2014; Fabbrini, 2014; Amtenbrick, 2014; Beukers, De Witte and Kilpatrick, 2017) or by focusing on specific countries such as Hungary (Mohay, 2013), Portugal (Martins, 2015) and Italy (Martinico and Pierdominici, 2014). In addition, scholars have paid attention to CJEU rulings on EMU crisis resolution's measures such as the ECB monetary instruments (German Law Journal special issue 15 (2)) and the European Stability mechanism (German law journal, special issue 14 (1)). This stream of research focuses on the content of courts' rulings and on their impact on the European constitutional order and the process of European integration.

The goal of this article differs from the existing legal literature on the topic. Rather than analyzing the judicial decision from a legal point of view, we adopt a politics angle by focusing on the reasons that bring actors to choose the court venue. From that point of view, our analytical angle focuses on the factors driving judicialization (Hirschl, 2014). The present article contributes to this debate in adopting an actor-centered approach. We focus on the reasons that push plaintiffs to go before domestic courts when challenging specific EMU crisis resolutions in 28 member states from 2011 to 2016. We adopt an agnostic stance about these motives and consider the whole range of approaches for our systematic study of the cases brought in front of courts during the EMU crisis. By doing so, we aim to contribute

to both the politics of law literature as well as the vast body of research focusing on the Eurozone crisis. On the one hand, comparative constitutional analyses take into account plaintiffs' motives but do not compare them (Adams, Fabbri and Larouche, 2014; Beukers, De Witte and Kilpatrick, 2017). On the other hand, the role played by national courts in the negotiations and implementation of EMU reforms have not yet been systematically analysed by political scientists. Through the study of the plaintiff's motives and actions<sup>2</sup>, we aim at contributing to our understanding of political divisions and power struggles taking place during the EMU crisis at the domestic level.

The data set consists of over 50 cases, which were brought before the courts in the period 2010 to 2016. These cases were analyzed based on court data, secondary literature and a data set of national newspaper articles. Our data selection is based on all cases brought before domestic constitutional courts that directly stem from the decisions and the rules adopted at the EMU level to answer to the crisis. For example, the 2008 member-states' budgetary and bailout decisions are not included in our corpus because, at that time, these policies were not decided at the EU level (Quaglia, 2012). On the contrary, the 2011 Italian budgetary reforms are included because they were taken under the ECB pressure, as revealed by the leaked letters of Mario Draghi and Jean-Claude Trichet to the Italian government. Moreover, we do not consider the cases brought in front of supervisory systems which are not judicial systems such as the Greek complains to the International Labor Organisation about the 2<sup>nd</sup> MoU. Finally, we are aware that different national judicial systems offer different opportunities for political players. However, as we seek to shed light on the judicialization process of the EMU crisis by analyzing the motives of the plaintiffs and not the variance of the number of appeals, our strategy to compile every existing law case in relation with EMU crisis does not create a significant bias.

The first section of this article exposes a set of hypotheses on variables that push plaintiff's to go to court. Section II sets out the context of legal action by outlining the main reasons, reforms and tensions of the EMU crisis. Section III exposes our empirical results for the 28 EMU member states and analyses the plaintiff's motives in light of the hypotheses presented in part I. Our conclusion spells out the contribution of our research to the literature on the EMU crisis and the field of law and politics.

### **1. Why do actors mobilize Courts?**

The new economic and financial rules adopted by the Member states at the EU level to manage the euro area sovereign debt crisis combine a scope and swiftness, which is unprecedented in the 60-year history of European integration. At the same time, these rules were contested at the domestic level, both politically, through debates in national parliaments, the media, and through protest movements, and judicially by calling upon national constitutional courts.

In the traditional model of parliamentary democracy for much of the 19<sup>th</sup> and 20<sup>th</sup> century, citizens had limited options to contest decisions from political actors. Political appeals were possible through petitions sent to members of parliament or through creating protest movements. Judicial review of legislation and executive acts through the capacity to take social conflicts to courts, however, emerged only slowly over the 20<sup>th</sup> century. The judicialization of conflicts in public policies has fundamentally transformed the European political landscape and thus reshaped the way citizens interact with the judiciary (Bricker 2015, 2; Stone Sweet 2000).

Judicialization, as defined in the introduction, refers "to the process through which a third party dispute resolver (e.g., a judge) emerges in a social system, and then develops authority over the institutions (e.g., the norms, rules and principles) meant to govern that system." More precisely it "concerns how judicial lawmaking – defined as the law produced by the judge through normative interpretation, reason-giving, and the application of legal norms to facts in the course of resolving disputes – influences the strategic behaviour of non-judicial agents of governance" (Stone-Sweet,

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<sup>2</sup> As political scientists, we will not systematically study the judicial reasoning behind each court's decision. We rely on the research conducted by law scholars quoted above when referring to the courts' decisions.

2010, 7). In more general terms, judicialization is to be understood as the transfer to courts of contentious issues of an outright political nature and significance. Beyond questions of social rights, which have been important in court decisions since the 1950s, such as *Brown vs Board of Education*, these contemporary contentious issues include electoral processes and outcomes, restorative justice, regime legitimacy, executive prerogatives, collective identity, and nation building (Hirschl 2004).

It is important to note, however that three conditions are necessary for judicialization to proceed (Stone Sweet 2010, 8): First, public or private actors must appeal to the court: without a case load, courts will have no influence in policy making. Second, once activated, courts must resolve these disputes and provide reasons for their decision. Third, those who are governed must accept that legal meaning is partly constructed through judicial interpretation.

A number of recent publications have dealt with the second and third conditions necessary for judicialization in the context of how courts have responded to the legal measures adopted by the political branches to tackle the EU economic and financial crisis (Höpner & Schäfer 2012; Amtenbrink 2014; Fabbrini 2014; Tuori & Tuori 2014; Saurugger 2016).

While all three conditions are crucial, the aim of this article is different. It concentrates on the first aspect: who are the actors that appeal to the court and why do they do so? Adopting a law and politics approach, we analyse which actors went to court at the domestic level to challenge the decisions taken by the member states and why. The article thus engages in a debate on the reasons for mobilizing judicial tools in order to resist aspects of European integration (Saurugger and Terpan, 2016) and, more specifically analyses why actors use national constitutional courts to challenge new economic governance instruments. Answering this question will help us to better understand the role of constitutional courts in a political system, as well as the motivations of actors going to court. It contributes to our understanding of legality in political systems not only as foundation of power but also as an exercise of power.

Hence, the study of the role of constitutional courts in politics (Tate and Vallinder 1995; Shapiro and Stone Sweet, 1994, 2002; Ferejohn 2002; Commaille & Dumoulin 2009; Stone Sweet 2010; Hirschl 2014 for a typology of different approaches) has taken various forms and presented us with a variety of hypotheses. While purely functionalist approaches have lost ground in political science approaches, criticised for neglecting power struggles amongst actors (Alter 1996), *institutionalist approaches* constitute one of the most widely shared approaches, arguing that judicial politics reinforce democratic decisions (Dahl 1959; Bricker 2016; Caporaso and Tarrow 2009; Jupille and Caporaso 2009). According to *institutionalist approaches*, when confronted with a powerful opposition, a government can call upon the court to seek for legitimation. Here decisions taken by constitutional courts confirm the legitimacy of parliamentary and executive decisions, while at the same time allow for decreasing a joint decision trap (Scharpf 1988; 2004). Hence, in order to gain in the acceptability of a decision, decision makers themselves call upon the Court in order to validate the decision judicially. (H1)

The strategy of actors searching to bind the hands of their successors refers to the *judicialisation from above* approach. Judicial review can in fact enhance the current political majority, in creating a precedent, which is symbolically and legally difficult to question by a future government. This is also linked to the fact that in absence of the power of a purse or the sword, courts need the executive to enforce its decisions (Bricker 2015). This makes it highly plausible that actors searching for codification of their decisions go to constitutional courts in order to assure the posterity of their political decisions (H2).

A variant of the *judicialisation from above* approach can be found in the decision of the political opposition to go to court. Opposed to this argument of reinforcing the legitimacy of a decision is the idea that opposition parties appeal to courts in order to challenge the government. Where debates in parliament or in the public sphere is not considered to be sufficient to create a context of change, intra-

parliamentary opposition might search to make their case heard before constitutional courts. Although they might lose, the salience of this process allows them to increase the publicity about their claims (Tate and Vallinder 1995; Dotan & Hofnung 2005) (H3).

Appealing to the court can offer minority groups protection of decisions taken by a majority. This idea is at the heart of *rights-centred approaches* to judicialization. A recent strand of literature argues that the rise of constitutional courts creates a system of post-democracy (Bicker 2016), in which citizens, NGOs, or ombudsmen gain policy-making or policy-changing power through the courts to circumvent both the parliament and the executive. This understanding is linked to the argument that courts are no longer only perceived as the “mouth of the law”, as positivistic legal research would have it, but are indeed policy-making actors. While the idea that courts should sit in judgement of legislation was for many years an anathema in Europe, where Courts were considered a subservient branch of government (Stone Sweet 2000), research has shown that parliamentary as well as executive actions must conform to the constitution as interpreted by constitutional courts. Nearly all European countries now allow individuals the right to petition the constitutional court directly or indirectly. As Bricker (2016) underlines, with the growing importance of judicial review to policy outcomes (Stone Sweet 2000, Martinsen 2015) and the near universality of judicial review today, it is all the more important to understand to what extent judicial review contributes to the normative goals of democracy and democratic performance. The increased judicialization is thus not only an element to protect the minority in democracy, but to create the possibility for all actors to circumvent domestic parliamentary democracy or to question the democratic character of supranational decision-making as in the case of EMU (H4).

Finally, and taking a more sociological approach (*court-centred approaches*), a part of the literature argues that activist judges call upon citizens and lawyers to bring cases to the court (Vauchez 2012). Here, the judges aim at contributing to increase the authority of European law, and hence their professional prestige as well as the influence of the court on which they sit through nudging citizens into bringing cases to the court (H5).

## **2. The political answer to the EMU crisis**

After having exposed factors explaining why political players mobilize courts, we explore in this section the substance of political conflicts that were activated during the EMU crisis. Despite the fact that the EMU crisis was caused by complex financial imbalances between creditor and debtor countries, the political answer to the crisis mainly consisted in a financial rescue of the creditor states attached to tough conditionality measures. These elements are crucial to contextualize the factors that pushed actors to go to court, which will be analyzed in section 3.

The EMU’s asymmetry between the supranational integration of the monetary policy and the intergovernmental logic of economic governance has been considered as a major factor in the build-up of economic imbalances. Indeed, currency areas need risk-sharing systems such as automatic fiscal transfers and financial stabilization mechanisms to function smoothly (Feldstein, 1998). However, the EMU was deprived of such mechanisms because of joint-decision traps and the reluctance of creditor countries, worried about moral hazard concerns and the undermining of the principles of central bank independence and sound money<sup>3</sup> (Scharpf, 1997). In order to circumvent these resistances, the European authorities relied on financial mechanisms to foster the convergence of European economies (Gabor and Ban, 2015). However, as we know, EMU financial integration did not lead to economic convergence. Rather, uncontrolled capital flows from the core to the periphery of the Eurozone led to an excessive level of public and/or private debt, indeed against the rules of the Stability and Growth

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<sup>3</sup> Hence, the German resistances against economic integration caused the failure of the first proposal of an economic and monetary union in 1970.

pact, inflationary pressures and ultimately loss of competitiveness in the borrowing countries (Blyth, 2013). During the ten first years of the Eurozone, these financial mechanisms were conducive to the creation of two distinct groups of countries (Dyson, 2014): creditor countries (Germany, Netherlands, Finland, Austria, Estonia, Luxembourg, Malta, Slovakia, Slovenia) and debtor countries (France, Greece, Portugal, Italy, Spain, Ireland, Belgium, Cyprus). The unwinding of the economic imbalances between these two groups of countries led to the Eurozone financial crisis (Nedergaard and Snaith, 2015).

Yet, despite its complex financial roots, the EMU crisis has been mainly framed as a sovereign debt crisis caused by unsustainable fiscal policies and the lack of structural reforms (Matthijs and McNamara, 2015). This framing reflects the asymmetrical power game between creditor and debtor countries in the political answer to the crisis (Dyson, 2014). As debtor countries cannot regain financial market's confidence without the financial guarantees of creditor countries, the latter group of countries can impose their narrative about the causes of the crisis and, therefore, their policy solutions. Creditor countries are also constrained in their answer to the crisis. Indeed, they have to provide some financial support to the countries which lost market access in order to mitigate systemic risks that could threaten the very existence of the common currency and weaken their banking sector. At the same time, creditor countries still wary about an excessive sharing of their fiscal resources and risks of moral hazard. The framing of the crisis as a fiscal crisis allowed creditor countries to follow the thin line of "constructive ambiguity" between these two sets of constraints.

The unwinding of Eurozone imbalances started in December 2009 when Greece could not refinance its debt at sustainable interest rates while large European banks, holding Greek debt, were experiencing severe financial difficulties. The option of Greek debt restructuring was side-lined, against the advice of the International Monetary Fund, because it would have weakened the banks from core Eurozone countries which were holding it. In May 2010, the heads of States and governments of the Euro area issued a €110 billion emergency loan to Greece to stabilize the market valuation of its debt.

As this loan was not enough to address systemic risks threatening public finances and banks' balance-sheets, both fiscal and monetary authorities had to tackle the problematic lack of financial stabilization mechanisms within the Eurozone. On the one hand, member-states set up and capitalized a temporary financial vehicle in order to lend to distressed Eurozone countries (the European Financial Stability Fund, EFSF<sup>4</sup>). The EFSF has subsequently provided financial assistance to Ireland in November 2010, Portugal in May 2011 and the second Greek bail-out in March 2012. On the other hand, the European Central Bank (ECB) lowered its interest rate near to zero, extended its liquidity offers to the banks and it finally crossed its Rubicon when it started to purchase the sovereign bonds of distressed countries on the secondary markets with its Security Market Program (SMP).

In order to avoid moral hazard, the financial programs were conditional to the implementation of fiscal retrenchment policies. The bailout processes involve bargaining between the bailed-out countries and their creditors and possible revisions following the deal. The conditions for granting the loans have to be agreed between the bailed-out countries and the Commission, in consultation with the ECB and the IMF (European Council 2010) and are laid down in a Memorandum of Understanding (MoU). On-field representatives from the Commission, the ECB and the IMF (the troika) monitor and verify that the implementation of the economic policies conditions is fulfilled.

EMU authorities have prolonged their initial crisis measures with three sets of instruments (Braun, 2013). First, the EFSF has been substituted by the European Stability Mechanism (ESM) in 2012. The ESM sells bonds on behalf of the Eurozone in order to finance the assistance programmes for the financially distressed countries. Like the EFSF, the ESM loans are conditional to the implementation of economic reforms monitored by the troika and ESM representatives. As the EU treaties offered no

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<sup>4</sup> From a legal standpoint, the EFSF is a public company operating under state law.



grounds for financial rescue mechanisms<sup>5</sup>, the Eurozone states set up the ESM outside the EU treaties by signing a treaty in September 2012 under public international law<sup>6</sup>. The ESM continued the EFSF programmes in Ireland and Portugal and it provided new loans for Spain, Cyprus and the third Greek programme in 2012, 2013 and 2015. From a legal point of view, the loans granted by the EFSF/ESM and the MoUs that are attached are situated outside EU law.

Second, the ECB pursued its liquidity offers to the banking sector with the implementation of its Long-Term Refinancing Operations (LTRO) and its purchases of financial assets on the secondary markets. More precisely, the ECB stabilized the sovereign bond markets with the announcement of the Outright Monetary Transactions (OMT) programme in August 2012 and the implementation of its expanded asset purchase programme in March 2015. In contrast with the SMP, the potential purchases under these two programmes are unlimited. The ECB relied on its monetary tools to force economic reforms in countries under financial difficulty such as in Italy, Spain and Greece (Fontan, 2013).

Third, EMU governance was reformed in order to strengthen the fiscal rules and the monitoring of the implementation of structural reforms to avoid to build-up of macroeconomic imbalances. Since 2011, the budget proposals of member-states must follow the European Commission's recommendations in the context of the European Semester. If they fail to do so, the two-pack and six-pack agreements provide enhanced coercive tools to the EMU authorities that can lead to financial sanctions. 25 out of 28 EU member-states enshrined these fiscal dispositions within national legal orders when they signed the Treaty on Stability, Coordination and Governance (TSCG), an intergovernmental treaty often dubbed "fiscal compact". In addition, Eurozone member-states agreed on a banking union in order to rebuild market confidence in banks and sovereign and enhance banking supervision and resolution (Howarth and Quaglia 2016). However, EMU reforms are still incomplete because they lack fiscal transfer mechanisms to correct the economic imbalances in crisis times and a common deposit guarantee scheme to protect Eurozone bank depositors. In fact, creditor states remain reluctant to set up these crucial components for the smooth functioning of a currency area, mainly because of moral hazard risks and the fear of electoral backlash. Non-Eurozone countries were less directly impacted by the EMU crisis-solving measures because they didn't have to commit to financial assistance schemes, nor to the TSCG<sup>7</sup>. Only Hungary, Latvia and Romania had to strictly comply with adjustment programmes as they asked financial assistance from the EU and the IMF in 2008-2009.

In sum, EMU governance deepened and became more integrated according to the prevailing ideas and preferences of dominant players enshrined in the EU legal order (Hall, 2012, Verdun, 2015, Ryner, 2015). In fact, the first emergency measures combined financial support with strong conditionality measures and the more permanent reforms enhanced the monitoring of budgetary deficits and the implementation of structural reforms. The lack of fiscal redistribution mechanisms also mirrors the political cleavages prevailing during the EMU creation.

### **3. The judicialization of the EMU crisis.**

The deepening of EMU integration since 2010 has fuelled political contestations within EMU creditor and debtor states. On the one hand, the political leaders of creditor states faced domestic pressures from a large portion of their electorate who believe that debtor countries' financial difficulties stem from their fiscal profligacy and their inclination to spend more than they earn (Scharpf, 2013: 129). On the other hand, debtor countries' governments were confronted with stronger resistances from their citizens denouncing the austerity plans and the infringement of their sovereignty (Della Porta and Parks, 2016). Overall, the framing of the crisis as a fiscal crisis in creditor countries reinforced the perceptions that the crisis was a moral issue rather than a fast unfolding of the economic imbalances caused by past political choices. According to Dyson (2014), the politics of creditor/debtor relations

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<sup>5</sup> Article 125 of the TFEU

<sup>6</sup> At the same time, EU member states amended the article 136 of the TFEU in order to pass the ESM more easily.

<sup>7</sup> Bulgaria, Denmark and Romania voluntarily opted-in

are aggravated by a moralizing language of “saints” and “sinners” in which debt is perceived as a negative outcome of wrong moral choices from the State. The political elites and the media in both creditor and debtor countries conveyed the moralization of debt issues (Mylonas, 2012, 2014).

In both cases, however, governments did not follow their citizens’ demands. The centrality of markets’ imperatives in the EMU political answer to the crisis seems to be the main reason for this lack of policy feedback (see section 2). On the one hand, the withdrawal of creditor countries’ financial support would have amplified the systemic crisis of the Eurozone, maybe until the collapse of the single currency. On the other hand, debtor countries could not avoid the implementation of austerity plans and stricter fiscal rules as it was a necessary condition for creditor countries’ participation to their financial rescue and, thus, the alleviation of market pressures. This lack of political responsiveness from EMU governments gave more opportunities for political parties located at the fringes of the partisan spectrum to contest crisis measures. In sum, as decision-makers were mostly taking into account market imperatives, the crisis amplified the isolation of the EMU policymaking sphere from other societal demands (Streeck and Schaeffer, 2013, Della Porta and Parks, 2016). In this context, courts were seen as an alternative to the traditional circuits of representative democracy to express these demands.

In order to identify the plaintiffs who challenged EMU crisis measures before the courts and to explore their motives in light of the hypotheses presented in section 1, we have compiled in a comprehensive manner every relevant case-law in the 28 member-states. In this section, we explore the judicialization of the EMU crisis by analyzing the motives of the plaintiffs in (1) creditor countries, (2) debtor countries (3), countries under financial assistance and (4) non-eurozone countries. This is done by systematically mobilizing the hypotheses developed in section 1 to explain why structural conflicts about the EMU governance were brought in front of courts.

### *Creditor countries*

In creditor countries, large portions of the electorate were not willing to engage their domestic financial resources to stabilize periphery countries. For example, during the early stages of the crisis solving process, the German negotiators were already constrained by the reluctance of their electorate, wary about fiscal transfer risks between Germany and the peripheral countries under financial assistance<sup>8</sup>. This popular backlash was most acute in Germany for three reasons. First, deep-seated ordo-liberal ideas promoting fiscal rectitude are widespread among the German electorate (Schmidt and Crespy, 2014). Second, the popularity of ordo-liberal ideas was fuelled by the perceived success of the Agenda 2010 reforms of the Red-Green government (Young and Semmler, 2011). Third, partisan power-games reinforced ordo-liberal ideas: some political actors adopt a hardliner role within the government (such as Wolfgang Schäuble, the German Finance minister since 2009) while opposition parties (such as the SPD and the Greens) did not challenge ordo-liberal ideas (Zimmermann, 2014).

Table 1. Judicialisation in creditor countries

| National judicial system            | Cases                 | Political context of the cases                           | Plaintiffs                                         | Outcome                         |
|-------------------------------------|-----------------------|----------------------------------------------------------|----------------------------------------------------|---------------------------------|
| Austria (Constitutional Court (CC)) | ESM TSCG <sup>9</sup> | March 2013 Regional Elections in Carinthia <sup>10</sup> | ESM Province of Carinthia (FPK <b>government</b> ) | ESM: Rejected<br>TSCG: rejected |

<sup>8</sup> In particular, the set-up of the EFSF was constrained by the North Rhine-Westphalian regional elections, which were taking place at the same time.

<sup>9</sup> ESM : (VfSlg 19.750/2013) (filed in september 2012) TSCG : (VfSlg 19.809/2013) (filed in October 2013)

<sup>10</sup> The FPK government is a coalition of two far right wing parties: the Freedom Party of Austria (FPÖ) and the Alliance for the Future of Austria (BZÖ).

|                                    |                                                             |                                                                                                   |                                                                                                                                                                                                                                                                                   |                                                                       |
|------------------------------------|-------------------------------------------------------------|---------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------|
|                                    |                                                             | October 2013 : federal elections                                                                  | TSCG: <b>1/3 of the Parliament</b> including FPÖ, BZÖ and Greens                                                                                                                                                                                                                  |                                                                       |
| Estonia (CC)                       | ESM <sup>11</sup>                                           | EFSF contested 2011: elections                                                                    | <b>Ombudsman</b> <sup>12</sup> .                                                                                                                                                                                                                                                  | ESM: rejected                                                         |
| Finland (Parliament) <sup>13</sup> | Every EMU reform was debated <sup>14</sup> :                | 2011: elections<br>Rise of the far right wing party (True Finns).                                 | <b>Parliament</b> uses its reviewing power to ensure its participation to EMU negotiations                                                                                                                                                                                        | Measures are compatible with the Constitution                         |
| Germany (CC)                       | Bilateral loans<br>EFSF<br>ESM<br>TSCG<br>OMT <sup>15</sup> | Continuous regional elections<br>2013: federal elections<br>Rise of a far right wing party (AfD). | Bilateral loans: <b>5 individual complaints</b> <sup>16</sup><br>EFSF: same composition<br>ESM + TSCG: <b>37000 citizens, including Die Linke + Peter Gauweiler (CSU) + Herta Daubler Gmelin</b> <sup>17</sup> .<br>OMT: <b>12000 citizens including Gauweiler, and Die Linke</b> | All rejected, but sets limits for further integration <sup>18</sup> . |
| Luxembourg (Parliament)            | None                                                        | 2013: change of government.                                                                       |                                                                                                                                                                                                                                                                                   |                                                                       |
| Malta (CC)                         | None                                                        |                                                                                                   |                                                                                                                                                                                                                                                                                   |                                                                       |
| Slovakia (CC)                      | No.                                                         | 2011 Fall of the government (EFSF issue)                                                          |                                                                                                                                                                                                                                                                                   |                                                                       |
| Slovenia (CC)                      | EFSF <sup>19</sup> .<br>National laws stemming from TSCG    | 2012 elections                                                                                    | EFSF: challenged by <b>37 deputies from PdS</b> <sup>20</sup><br>TSCG : challenged <b>28 times by the Ombudsman for human rights</b>                                                                                                                                              | EFSF : rejected<br>TSCG: many dispositions amended                    |

<sup>11</sup> (Decision 3-4-1-6-12) filed in July 2012

<sup>12</sup> The Ombudsman already informally complained about EFSF and filed a formal complaint for ESM (Sikk, 2013)

<sup>13</sup> Constitutional law committee : ex ante review on request of the Parliament according to Art 94 of Constitution: duty to consult on proposals for EU measures

<sup>14</sup> Opinions 27 of 2011 and 1 of 2012 (TESM); Opinions 37/2012, 34/2011 (TSCG); Opinion 49/2010, Opinion 6 of 2011 (136(3) TFEU); Opinion of 4/2012 by the Grand Committee on the Banking Union and the Future of the EMU

<sup>15</sup> Bundesverfassungsgericht judgement of 18 March 2014, 2 BvR 1390, 1421, 1438, 1439, 1440/12, 2 BvE 6/12

<sup>16</sup> The individuals are one former economic teacher, one former SPD member, two EU law professors and a former MEP belonging to the AfD.

<sup>17</sup> Peter Gauweiler, a Bavarian CSU politician, resigned at 65 from his parliamentary seat in 2015. In Nov. 2013 he became deputy chairman of the CSU (considered a move towards the eurosceptics of his party). His attempts to have the German CC block measures that enhance the EU's powers at the cost of national sovereignty (2003, 2005, 2010, 2012) tended to win support amongst the conservative voters including backers of the Eurosceptic AfD party. Both, Herta Daubler-Gmelin, the former SPD Minister for Justice, and Christoph Degenhart, a former German Law professor (University of Leipzig) are Kuratoren (Board members) of the Association 'Mehr Demokratie', which mobilizes for more direct democracy in Germany. Die Linke is a radical left wing political party.

<sup>18</sup> The German Court notified that Germany should retain blocking rights within the ESM and draw limitations to the OMT.

<sup>19</sup> UL 59/10, 79/11

<sup>20</sup> Opponent center right wing party

In the first stages of the crisis, a small group of academics and former politicians contested bailout politics before the *Bundesverfassungsgericht*. Then, the contestation widened as the legal complaints against the ESM, the TSCG and the ECB's OMT were filed by more than 37000 and 12000 citizens from the whole political spectrum (from the CSU politician P.Gauweiler to Die Linke). How can we explain this rise of legal complaints? The lack of responsiveness of the political system would be a first answer. As the first legal complaints and popular backlash against financial assistance schemes did not stop the creation of new EMU institutions, the contestation amplified. Access to the judiciary created the possibility for all actors to circumvent domestic parliamentary democracy or to question the democratic character of supranational decision-making as in the case of EMU (H4). Moreover, since the build-up of the informal grand coalition in 2011 between the CDU and the SPD, the voices of the hardliners who refused any financial assistance scheme had less impact as their support was not crucial anymore for the government (H3). In short, the judicialization process of the EMU crisis in Germany is unique in the sense that both citizens and the political personnel from the whole political spectrum brought action in front of the *Bundesverfassungsgericht*.

The judicialization of the EMU crisis in other creditor countries was more limited. In Slovenia, Netherlands and Austria, the legal complaints were filed by political opponents, often for electoral motives (H3). In fact, the far-right wing's Austrian FPÖ regional government and the Dutch political Geert Wilders filed their complaints against the ESM, even though they had no chance to succeed, because they were also campaigning for elections at that time. Moreover, the legal actions against the TSCG forged alliances between "strange bedfellows" such as the Greens and the FPÖ in Austria and Die Linke and representatives from the CSU in Germany. Again, the lack of responsiveness of the political system pushes political outsiders to voice their dissent before the courts. Finally, some judicial activism has been displayed in Slovenia, Finland and Estonia to the extent that the Ombudsman are linked to the judicial system (H5).

### ***Debtor countries***

In debtor countries, social protests were fuelled by the weakening of social protection caused by the economic crisis and the closeness of political institutions towards citizens' demands (Della Porta, 2015). Indeed, the framing of the crisis as a fiscal crisis and the resulting strengthening of fiscal rules neglected its financial and banking causes. Fiscal tightening often took the form of austerity plans, which are characterized by a disproportionate share of the fiscal adjustment burden carried by the least well-off segments of the population (Stuckler and Basu, 2013). Moreover, citizens claimed that they should not be held responsible for the past governance mistakes of political elites. Therefore, citizens, civil society and political players, which are affected by austerity plans asked for more social justice in the answer of political authorities to the crisis. Finally, interest groups and lobbies had less access to EU negotiations and citizens struggled harder to influence government policies through elections than in normal times (Streeck and Schaeffer, 2013). Countries following a MoU were obviously the most affected by these dynamics. Moreover, even though Spain and Italy did not sign a MoU under the supervision of the troika, they had to comply with similar adjustment programmes under the pressure of the ECB and the European Council. France and Belgium were less constrained but they also had to accept more fiscal consolidation when they signed the TSCG

Table 2. Judicialisation in debtor countries

| National judicial system   | Cases                                                                                                                                        | Political context of the cases                                                                                                | Plaintiffs                                                                                                                                                                                                                                                             | Outcome                                                                             |
|----------------------------|----------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------|
| Belgium (CC) <sup>21</sup> | EFSF <sup>22</sup><br>ESM <sup>23</sup><br>TSCG <sup>24</sup>                                                                                | April 2010 – October 2011: no government.<br>General elections in May 2014, NvA in the government                             | EFSF: 4 citizens (members of <b>minor radical left-wing political parties</b> <sup>25</sup> )<br>MES: cf. EFSF<br>TSCG: <b>class action</b> (Human Rights' lobbies, Employee's trade union, citizens' association former Green MP, far-right wing MPs (Vlaams Belang)) | EFSF and MES rejected<br><br>TSCG rejected                                          |
| France (CC)                | TSCG <sup>26</sup><br>Derivative national law <sup>27</sup>                                                                                  | Presidential Elections in 2012                                                                                                | TSCG <b>President of the Republic</b><br>National law: <b>Prime Minister</b>                                                                                                                                                                                           | Conformity between TSCG and the Constitution                                        |
| Italy (CC)                 | National application laws for fiscal consolidation measures <sup>28</sup> .<br>Decree laws <sup>29</sup><br>Constitutional Law <sup>30</sup> | Summer 2011: Intervention of the ECB<br>Nov. 2011, resignation of Berlusconi<br>2013: elections, strong political instability | National application laws, decree laws and constitutional laws.<br><b>Italian Regions</b> <sup>31</sup> , <b>magistrates, diplomats and professors</b> <sup>32</sup> .                                                                                                 | Only magistrates won.<br>Regions: only 220/2013 won                                 |
| Spain (CC)                 | Decree-Law <sup>33</sup><br>2011 Golden rule<br>National dispositions stemming from TSCG <sup>34</sup>                                       | 2011: elections<br>2012: intensification of regional tensions<br>2013 Rise of Podemos                                         | Decree law 2010: 85/2011: <b>trade unions</b> .<br>Article 135: Challenge by <b>parliamentary coalition United Left</b> <sup>35</sup><br>TSCG: <b>Regional Governments</b> <sup>36</sup> more than <b>3000 municipalities</b> (mostly from Catalonia) + <b>50 MPs</b>  | Decree law 2010: rejected<br>Art 135: rejected<br>TSCG: some dispositions suspended |

<sup>21</sup> In Belgium, the powers of the Constitutional Court are limited to a posteriori review on the provisions which govern the division of competences between federal and regional levels.

<sup>22</sup> Two complaints filed in February 2011 (11/2011) and in January 2012 (33/2012)

<sup>23</sup> (156/2012) filed October 2012

<sup>24</sup> (62/2016) filed November 2014

<sup>25</sup> Including the Greens, Vivant and Comité pour une Autre Politique (CAP).

<sup>26</sup> (No. 2012-653 DC of August 9, 2012)

<sup>27</sup> (Decision No. 2012-658 DC of December 13, 2012)

<sup>28</sup> Decree-Law 31 May 2010, no. 78 (after SMP agreement)

<sup>29</sup> 2011 (nos. 98, 138 and 201) (under ECB pressure)

<sup>30</sup> 20 April 2012, no. 1 (anticipating Fiscal Compact). Law 24 December 2012, no. 243

<sup>31</sup> Decisions 70/2012, 115/2012 148/2012, 151/2012, 192/2012 and 236/2012 : Regions Abruzzo Campagna, Puglia Valle d'Aosta, Liguria, Emilia-Romagna Friuli-Venezia. Decisions 26/2013, 60/2013, 104/2013 220/2013, 250/2013, 266/2013: Regions Abruzzo Molise, Lazio, Veneto, Campania, Lombardia, Trentino-Alto dalle Regioni autonome Friuli-Venezia Sardegna Giulia e Sardegna e dalle Regioni Piemonte e Calabria). Decisions 70/2015: Reggio Emilia

<sup>32</sup> Decision 223/2012, Decision 304/2013, Decision 310/2013

<sup>33</sup> 8/2010 (on wages and pensions' cuts), anticipating the SMP.

<sup>34</sup> Translated in the Organic Law 2/2012 of 27 April and Regional decree law of 29 April (16/2012) State Law 27/2013

<sup>35</sup> (Esquerra Republicana – Izquierda Unida – Iniciativa per Catalunya Verts) (9/2012)

<sup>36</sup> Andalusia, Asturias, Canarias, Catalonia, Navarre and the Basque Country (decisions 239/2012, 122/2013 and 142/2013)

In Spain and Italy, legal venues became a significant mean of action for the opponents of the adjustment programmes such as regions, municipalities, professional associations and trade unions (H4). Before the crisis, these players used to enjoy a certain level of autonomy in the definition of their own policies or to influence the definition of governmental policies. They also have the resources to conduct successful legal actions. In Spain, political opponents from the radical left also challenged national budget laws before the courts (H3). In Belgium, a rare class action, a type of lawsuits where one of the parties is a group of people who are represented collectively by a member of that group, which included civil society as well as political actors located at the two ends of the political spectrum as well as stemming from two linguistic communities challenged the signing of the TSCG (H3 and H4).

In the French case, former President Hollande's left wing government asked for the opinion of the *Conseil Constitutionnel* on the constitutionality of the TSCG. This decision was strategic insofar as Hollande had promised to reopen the negotiations on the TSCG during his presidential campaign. Once elected, he did not realise his pledge, which triggered a profound divide within his own political party (*Parti Socialiste*). In the words of a French Treasury official: "The Treasury reminded the President the French engagements with its EMU partners. One could say that the Treasury matters much more for the definition of French positions in the EMU governance than the ruling political party<sup>37</sup>". In this context, it was likely that members of his own political party could challenge the TSCG in front of the court. Therefore, his referral can be understood as a strategy to reinforce his political legitimacy (H1).

Table 3. Countries under financial assistance programmes.

| National judicial system                                                          | Cases                                                                                                                          | Political context of the cases                                                                                    | Plaintiffs                                                                                                                    | Outcome                                  |
|-----------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------|------------------------------------------|
| Cyprus (CC)                                                                       | National laws derived from MoU                                                                                                 | Loss of market access in 2011 coalition government in Feb. 2013                                                   | Eight <b>public sector employees</b> <sup>38</sup> and <b>one advertising company and 13 private plaintiffs</b> <sup>39</sup> | Rejected                                 |
| Greece (Diffuse control of constitutionality among all the courts <sup>40</sup> ) | National laws derived from 1 <sup>st</sup> MoU : Council of State <sup>41</sup><br>Appeal to the ECHR (May 2013) <sup>42</sup> | 2010: 1 <sup>st</sup> MoU<br>2011: PM resignation<br>2012: 2d referendum and coalition government<br>2015: Syriza | Council of State: <b>trade unions and professional associations</b> <sup>43</sup>                                             | MoU: Rejected by Council of State + ECHR |

<sup>37</sup> Interview French Treasury official, Paris, October 2016

<sup>38</sup> Case no. 1480/2011

<sup>39</sup> Ledra's case (Joined Cases C-8/15 P to C-10/15 P)

<sup>40</sup> When courts find a law unconstitutional, they cannot annul it and cannot refer to the CJEU but they have the possibility not to apply the law. Council of State's role (the Supreme Administrative Court) is similar

<sup>41</sup> Council of State, Cases no. Decision 668/2012 1285/2012, 2 April 2012; and 1286/2012, 2 April 2012. See also Council of State, Case no. 1283/2012, 2 April 2012; and 1284/2012, 2 April 2012.

<sup>42</sup> Cases no. 57665/12 and 57657/12

<sup>43</sup> Athens Bar Association, the Technical Chamber of Greece, the Trade Union Confederation of Civil Servants, the journalists' union ESIEA, the Technical Chamber of Greece, the academic personnel of the Faculty of Social Sciences of the

|                                                |                                                    |                                                                                           |                                                                                                                                                                                   |                                                                                                                                             |
|------------------------------------------------|----------------------------------------------------|-------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------|
|                                                |                                                    | gouvernement<br>and 3d<br>referendum                                                      |                                                                                                                                                                                   |                                                                                                                                             |
| Ireland<br>(Superior<br>Courts <sup>44</sup> ) | ESM <sup>45</sup><br>TSCG <sup>46</sup>            | 2010: MoU<br>2011:<br>Coalition<br>gouvernement<br>Tensions over<br>MoU<br>renegotiation. | ESM: Thomas<br>Pringle ( <b>Irish<br/>left-wing<br/>independent<br/>politician</b> )<br>TSCG: Pearse<br>Doherty ( <b>Sinn<br/>Fein<br/>spokesperson</b> )                         | ESM: rejected+ referral to<br>the CJEU.<br>TSCG: rejected.                                                                                  |
| Portugal<br>(CC)                               | Budget laws<br>derived from<br>MoU <sup>47</sup> . | May 2011:<br>MoU.<br>June 2011:<br>Coalition<br>gouvernement                              | <b>Group of<br/>socialists</b> (plus<br>left Bloc MPs <sup>48</sup> )<br><b>President and<br/>Ombudsman</b> <sup>49</sup><br><b>President of the<br/>Republic</b> <sup>50</sup> . | In 2012, the court gave a<br>one off free pass by<br>suspending its decisions but<br>ruled in favour of the<br>plaintiffs rest of the time. |

Under programmes of financial assistance, political systems seem no longer responsive at all to citizens' demands. The International Monetary Fund (IMF) learned after the contested bailout of the 1980's that adjustment programmes are more efficient when there is a country ownership of the programs (Khan and Sharma, 2001). Country ownership is part of the IMF guidelines since the 1990's: every political party participating in government on a regular basis must sign the MoU when loans are granted. Therefore, mainstream parties form coalitions or succeed one another in power without changing the terms of the bailout and the course of the adjustment programmes. In other words, elections give little leeway for citizens to contest the terms of the MoU and outsider parties are less likely to influence public policies.

In this context, courts represent a strategic venue for contestation even when their power is limited, such as in the case of Greece. More precisely, in Greece and Cyprus, trade unions, professional associations and citizens who were directly affected by the austerity measures went to the courts (H4). In Ireland and Portugal, on the contrary, political actors were those who challenged the decisions before the courts, albeit for different motives. The Irish case is an example of legal action by those political actors who did not participate in government (H3). The Portuguese case is more peculiar to the extent that it is the only case in our corpus in which austerity measures were taken before court not only by the opposition (socialists) (H3) but also by a preeminent political actor belonging to the political party implementing the measures (in this case, the President of the Republic Aníbal Cavaco Silva, an historic figure of the center right wing Social Democratic Party). It was also the only successful legal challenge leading to the suspension of the austerity measures, up to the point that the

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University of Crete, together with other associations and individual complainants including Ms Koufaki, senior investigator at the Greek Ombudsman.

<sup>44</sup> High Court, which has full original jurisdiction, the Court of Appeal and the Supreme Court.

<sup>45</sup> (filed in July and October 2012) IEHC 296 and IESC 47

<sup>46</sup> (IEHC 296)

<sup>47</sup> Decision 396/2011 (State Budget 2011), 353/2012 (State Budget 2012), 187/2013 (State Budget 2013), 474/2013 (Public Workers Requalification), 602/2013 (Labour Code), 794/2013 (40-Hour Work Week), 862/2013 (Pensions Convergence), 413/2014 (State Budget 2014), 572/2014 (Special Solidarity Contribution 2014), 574/2014 (Pay cuts 2014-2018), 575/2014 (Special Sustainability Contribution)

<sup>48</sup> RULING No. 353/12, 396/11

<sup>49</sup> RULING No. 187/13, 413/2014, 572/14

<sup>50</sup> RULING No. 474/13, 862/13, 574/14, 575/14

Troika started to complain about these legal challenges<sup>51</sup>. In this case, the President of the Republic acts beyond partisan politics, in the name of the best interests of the nation. The legal actions of the President are therefore close to some form of defence of citizens' rights (H4).

### Non-Eurozone countries

Table 4. Judicial action in non-eurozone countries

| National judicial system        | Cases                                                                        | Political context of the cases                                                                                          | Plaintiffs                                                                                           | Outcome                                                                                  |
|---------------------------------|------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------|
| Bulgaria (Constitutional Court) |                                                                              | 2009 : austerity<br>2013: government resignation                                                                        |                                                                                                      |                                                                                          |
| Croatia (CC)                    | Two national laws following 2014 Excessive Deficit Procedure <sup>52</sup>   | Elections in November 2015.                                                                                             | Nine <b>Trade Unions</b> and affected <b>citizens</b> <sup>53</sup>                                  | Rejected                                                                                 |
| Czech republic (CC)             | No challenges                                                                | 2011, fiscal austerity June 2013: government collapse and political instability. January 2014: anti austerity measures. |                                                                                                      | .                                                                                        |
| Hungary (CC)                    | Fiscal compact <sup>54</sup>                                                 | 2010: Super majority for Orban government                                                                               | <b>Hungarian Minister of Public Administration and Justice</b> <sup>55</sup>                         | Require a 2/3 parliamentary majority to sign the international treaty                    |
| Poland (CC)                     | Article 136 (3) <sup>56</sup>                                                | Surprise change of government in 2014.                                                                                  | Art 136 (3) : <b>PiS MP</b> <sup>57</sup>                                                            | Ratification act is not unconstitutional, no higher threshold for ratification required. |
| Romania (CC)                    | Constitutional reform <sup>58</sup><br>Labour's market reforms <sup>59</sup> | 2010 : MoU<br>2012: Strong political instability                                                                        | Constitution: <b>the Court itself.</b><br>On labour: the <b>police's trade union</b> <sup>60</sup> . | Constitution change rejected<br>Reforms invalidated                                      |

<sup>51</sup> European Commission, The Economic Adjustment Programme for Portugal 2011-2014 Occasional Papers 202 | October 2014; p. 21-22.

<sup>52</sup> Law on the denial of payment of certain material rights to employees in the public service in force as of 31 March 2015. Law on the denial of the right to increase salaries based on seniority, in force as of 1 April 2014

<sup>53</sup> Judgment U -I-1625/2014 and others, U -I-241/2015, U -I-383/2015, U -II- 1343/2015 as of 30 March 2015

<sup>54</sup> CC 22/2012.

<sup>55</sup> <https://www.degruyter.com/view/j/icl.2013.7.issue-2/icl-2013-0213/icl-2013-0213.xml>

<sup>56</sup> filed in May 2012 (k 33/12)

<sup>57</sup> [http://trybunal.gov.pl/fileadmin/content/omowienia/K\\_33\\_12\\_en.pdf](http://trybunal.gov.pl/fileadmin/content/omowienia/K_33_12_en.pdf)

<sup>58</sup> Including aspects of 2 pack et 6 pack in 2011 and 2014

<sup>59</sup> linked to MoU assistance programme (C-434/11)

<sup>60</sup> <http://curia.europa.eu/juris/liste.jsf?language=fr&num=C-434/11>



|                              |                                               |                              |                                                             |                                                  |
|------------------------------|-----------------------------------------------|------------------------------|-------------------------------------------------------------|--------------------------------------------------|
| Sweden<br>(Parliament)       | Amendment<br>Act on 136(3)                    |                              |                                                             | Simple majority.                                 |
| England<br>(Parliament)      |                                               |                              |                                                             |                                                  |
| Latvia <sup>61</sup><br>(CC) | Disbursement<br>Law<br>(stemming<br>from MoU) | 2009 : MoU                   | Merging of<br><b>pensioners</b><br>complaints <sup>62</sup> | Success (based on<br>human rights<br>arguments). |
| Lithuania<br>(CC)            | None                                          | 2009 : austerity<br>measures |                                                             |                                                  |

Finally, even though non-Eurozone countries were less impacted by EMU crisis solving reforms, courts were still mobilized to a certain extent. The Hungarian case is similar to the French one to the extent that the government filed a complaint in order to legitimize its own position (in this case, the ratification threshold for the modification of the Constitution) (H1). In Croatia, Latvia and Romania, citizens and specific social groups (pensioners, trade unions, professional associations) contested austerity measures, which affected them (H4). In Poland, the far right wing opposition party went before the court to contest the constitutional change triggered by the TSCG (H3). At that time, the governing party was weakened by multiple scandals and the Polish government collapsed unexpectedly in 2014. Finally, in Romania, the Court took action by itself during the constitutional revision (H5).

Table 5. Summary of our hypotheses on the plaintiffs' motives.

| Hypotheses         | H1                              | H2                             | H3                                                                          | H4                                                                                | H5                                    |
|--------------------|---------------------------------|--------------------------------|-----------------------------------------------------------------------------|-----------------------------------------------------------------------------------|---------------------------------------|
| Summary            | Decision-makers seek legitimacy | Decision-makers seek posterity | Opposition challenge government                                             | Citizens seek to protect their rights                                             | Judges seek to extend their influence |
| Relevant countries | France, Hungary                 |                                | Germany, Slovenia, Netherlands, Austria, Belgium, Ireland, Portugal, Poland | Germany, Spain, Italy, Belgium, Greece, Cyprus, Portugal, Croatia, Latvia Romania | Slovenia, Estonia (Finland), Romania  |

## **Conclusion. The patterns of judicialization during the EMU crisis.**

Our comprehensive compilation of the legal cases taken against EMU crisis measures provided the empirical evidence that the judicialization process of the EMU crisis is indeed taking place.

In fact, in each group of countries we have identified (debtor and creditor countries, countries under financial assistance, non-eurozone countries), citizens, civil society groups and political opposition went to the courts to challenge EMU crisis-solving measures (H3 and H4). More marginally, in Hungary and France, the government itself took legal action in order to reinforce its political decisions (H1). The role played by the Ombudsman in Estonia, Slovenia and Portugal also questions the issue of judicial activism (H5). However, we did not find any occurrence of a government challenging

<sup>61</sup> Latvia and Lithuania are classified in non Eurozone countries because the legal challenges occurred previous their accession.

<sup>62</sup> No. 2009-43-01 :

decisions taken in the context of EMU before the courts, in order to constrain the future actions of their successors.

We propose three explanations for the specific judicialization patterns observed in the context of the politics of the Eurozone crisis. First, the reasons invoked by the plaintiffs in both debtor and creditor countries reflect to a certain extent the way how the crisis was framed. While legal actions in debtor countries were taken against national austerity measures stemming from the adjustment programs, the legal actions in creditor countries contested fiscal sharing mechanisms and expansionary monetary measures. Second, when EMU reforms involved clear losses of sovereignty and principles of fiscal rectitude, legal actions were taken by strange bedfellows. In Belgium, Austria and Germany, both far right and far left wing parties filed complaints before the courts against the TSCG. Third, political timing as well as political context matter, in this in the case of all five hypotheses. On the eve of elections, legal complaints by political opponents against EMU reforms are more likely, even if the complaint has little chance to be successful, as it was the case in Netherlands and Poland. Moreover, when grand coalitions uniting the center-left and the center-right wing political parties are formed, political opponents and citizens are more likely to go before the courts in both creditor (Germany) and debtor countries (Italy, countries under financial assistance). In other words, when the outputs of the political system lack responsiveness towards citizens' demands, the judicialization of political conflicts are more likely.

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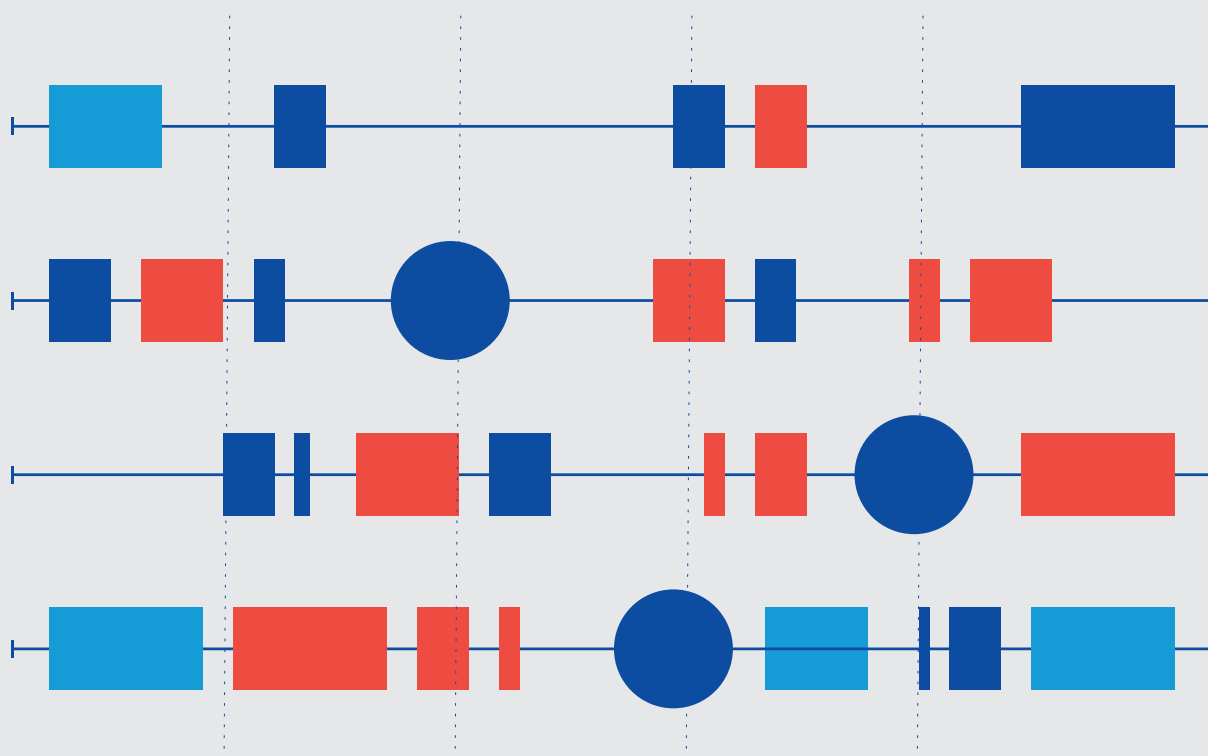
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## Circumventing constraints by internalizing Troika oversight? Italy and the Euro crisis negotiations Leonardo Morlino and Cecilia Sottilotta

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# **Circumventing constraints by internalizing Troika oversight? Italy and the Euro crisis negotiations**

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## **Abstract**

With the notable exception of Malta, South European countries were severely hit by the Euro crisis. In the extant literature, Southern Europe is often presented as a relatively homogeneous group of debt-ridden countries with converging preferences on the terms of future integration steps. Nonetheless, at a closer look, the ways in which South European countries adjusted to external constraints during the 2010-2013 negotiations diverged substantially. Greece, Portugal, Cyprus and (although in an attenuated form) Spain were all subject to direct oversight by the European Commission, the ECB and the IMF (the so-called ‘Troika’), while Italy, in spite of its gargantuan public debt, managed to avoid that. Starting from a discussion of the negotiated responses to the Euro crisis and of South European countries’ stances vis-à-vis a number of contested issues emerged during the negotiations, this paper engages with LI theory to suggest that at the height of the Euro crisis Italy managed to avoid external Troika oversight by internalizing it.

## **1. Introduction**

The economic and financial crisis started in 2008 is often described as a “critical juncture” in the history of European integration (Braun 2013; Heinrich and Kutter 2013; Morlino and Raniolo 2017), as relevant reforms to the architecture of the economic and monetary union bound to have long- term consequences were negotiated in a relatively short time span. Accounts of the Euro crisis negotiations based on Liberal intergovernmentalism (LI) seem to provide satisfactory explanations for the outcomes of the Euro crisis negotiations, highlighting their substantial congruence with the preferences of ‘core’ countries spearheaded

by Germany. Engaging with LI, this article aims to explore Italy's positions during the 2010-2013 negotiations, focusing in particular on the reform of the Stability and Growth Pact (SGP), that is the set of rules introduced in 1997 to underpin the stability of the European Economic and Monetary Union (EMU). The central argument of the paper is that rather than being motivated by pro-europeanism Italy's position can be chalked up to the primary objective of strategically avoiding structural adjustment under Troika oversight. Section 2 provides an overview of the reforms to EMU governance introduced in the wake of the financial-turned-sovereign debt crisis. Based on primary data, namely interviews with former decision makers and negotiators, Section 3 discusses the representation of Southern Europe as a relatively homogeneous bloc of debt-ridden countries whose domestic preferences mostly converged toward terms of integration based on mutualized adjustment costs (Hall 2012; Schild 2013; Schimmelfennig 2015). Section 4 seeks to single out and explain the peculiarities of the Italian case. Section 5 concludes.

## **2. Negotiated responses to the Euro crisis**

In September 2008, US financial behemoth Lehman Brothers collapsed, with the ensuing credit crunch marking the start of a financial crisis which soon reached Europe. By the end of 2010, what had started as a quintessentially financial crisis had turned into a full-fledged sovereign debt crisis. Fear of contagion started to spread in October 2009 after Greek socialist finance minister Papacostantinou disclosed that the country's deficit in that year would soar to 12.5% of GDP, a much higher figure compared to that originally estimated by the former conservative government (Barber 2009). In May 2010 Greece lost access to capital market. A Greek Loan Facility (GLF) was then initially created but it became soon clear that a broader approach to the problem was needed. Two lending facilities were then established to support Euro area countries experiencing fiscal difficulties: a European Financial Stabilisation Mechanism (EFSM) was created in May 2010 and placed under the control of the European Commission, with a relatively small lending capacity (60 billion euros), and the European Financial Stability Facility (EFSF) was set up in June 2010 as a temporary "special purpose vehicle" managed by the European Investment Bank, with a lending capacity of 440 billion euros supplemented with a 250 billion euros commitment by the International Monetary Fund (IMF). Nonetheless, as the spread between Germany's 10-year government bonds interest rate and those of Greece, Ireland, Italy, Portugal and Spain kept soaring, it became apparent that

the EFSF and EFSM also due to their temporary nature were far from being a panacea to financial turbulence in the Euro area (Sibert 2010:4). In July 2011, the need for a permanent financial assistance mechanism thus pushed the Euro area member states to sign an intergovernmental treaty establishing the European Stability Mechanism (ESM). The lending capacity of the ESM was set at 500 billion euros and its payments –crucially subject to conditionality – are meant to operate as a “liquidity bridge” (Kapp 2014) to support countries until they reacquire capital market access.

It should be noted that in order to address the shortcomings of the institutional framework underpinning the process of financial integration within the EU (Jones 2015), after the introduction of the ESM further steps were also taken toward the creation of a European banking union. More specifically, the second half of 2012 was characterized by intense discussion on how to complete the EMU by introducing a common system governing the regulation, supervision, and resolution of financial intermediaries (Howarth and Quaglia 2013).

Parallel to the negotiation of financial support schemes, important fiscal integration steps were taken by EU member states. As well known, in the framework of the SGP, member states wishing to join the monetary union committed to a path of convergence entailing a 3% of GDP limit for budget deficit and a 60% of GDP government debt. Failure to comply with these requirements triggered the excessive deficit procedure which could eventually lead to the imposition of sanctions. Since its inception, the SGP had lacked effective enforcement mechanisms, apart from “peer pressure”, “moral suasion” and a no bail out clause which was generally deemed an adequate disincentive to discourage fiscally irresponsible behaviors (Larch et al 2010). In fact, the enforceability of the SGP was further called into question when, after exceeding the 3% deficit threshold, Germany and France banded together to vote down a Commission recommendation aimed at imposing sanctions against them under the excessive deficit procedure (Ngai 2012, 18). In 2005, the Commission promoted a reform of the SGP aimed at directly involving countries in the definition of their own fiscal policy’s medium-term objectives, which ended up introducing further discretion and political leeway in the procedures (Schuknecht et al. 2011: 11). Reflecting a view to some extent inconsistently, yet widely held among ‘solvent’ countries which ascribed the onset of the crisis to lax fiscal discipline, emphasis was then placed on strengthening both the preemptive and the corrective arm of the SGP. The first set of measures entered into force on 13 December 2011 was the so-called Six Pack, consisting of five regulations and one directive

meant to address public deficits and macroeconomic imbalances by reinforcing economic and fiscal surveillance in the EU. One of the capstones of the renewed EMU institutional architecture is the introduction of reverse qualified majority voting (rQMV) for the imposition of fines to non-compliant member states. This represents indeed a U-turn vis-à-vis the 2005 reform of the SGP, as rQMV in fact substantially reduces the political leeway previously characterizing the enforcement of the excessive deficit procedure: once the Commission issues a recommendation to the Council in this sense, the imposition of sanctions against a member state falling short of its medium-term budgetary objectives is automatic unless a qualified majority of member states opposes it. The Six Pack also introduced a “European Semester”, a comprehensive framework for the coordination and monitoring of fiscal policies across member states with standardized deadlines throughout the year. On 9 December 2011, while taking stock of the new rules contained in the Six Pack, the European Council declared that not all the necessary measures could be introduced via secondary law. More specifically, some member states were reluctant to introduce further solidarity measures in absence of a parallel increase in common, credible constraints on national expenditure (Mortensen 2013:14). At the same time, as the UK had overtly rejected the hypothesis of incorporating them into the EU treaties (Spiegel et al 2011), the only viable solution left was the conclusion of an international agreement to be signed by March 2012 (European Council 2011). Hence the negotiation of the Treaty on Stability, Co-ordination and Governance in the Economic and Monetary Union (TSCG), also known as the “Fiscal Compact”, which was adopted on 2 March 2012 and entered into force on 1 January 2013. Among the other things, the signatories of the TSCG committed to enshrine a “debt-brake” rule into their own constitutions, following the analogous principle – the so- called *Schuldenbremse* – already introduced into the German constitution in 2009. The signatories also accepted to be subject to the jurisdiction of the EU Court of Justice which oversees the transposition of such rule at the national level. Moreover, as explicitly stated in the preamble to the TSCG, the granting of financial assistance under the umbrella of the ESM is conditional to the ratification of the TSCG itself. The provisions of the TSCG were complemented with the “Two Pack” regulations which entered into force on 30 March 2013. This reform package reinforced coordination and transparency in budgetary policies, and introduced stricter surveillance mechanisms for euro area members, especially those experiencing financial difficulties. In the new framework, the Commission examines and issues an opinion on the draft budget for the following year that each euro area country must submit every year by October 15. In case of patent misalignment of a member state’s budgetary plan vis-à-vis the obligations deriving from the SGP, the



Commission can ask the member state to revise the plan and resubmit it.

In light of the rapid unfolding of the crisis and of the limited amount of financial resources available to the EU, it is not surprising that in general the member states' governments played a central role even after the activation of EU mechanisms. In this sense, LI seems to provide a suitable explanatory framework for the outcome of the Euro crisis negotiations. The main theoretical tenets of LI can be summarized as follows. Major breakthroughs in European integration are explained in terms of three elements, that is the (domestic) formation of economic interests, international-level bargaining whose outcome is influenced by the relative power of the participants, and the subsequent institutionalization of "credible commitments" (Moravcsik 1998:4). Adopting this standpoint, the negotiations can be considered as a "two-level game" (Putnam 1988), in which a first phase of interest-formation at the domestic level is ideally followed by a second phase in which political leaders negotiate at the international level trying to accommodate the requests of domestic stakeholders while at the same time containing the negative consequences possibly deriving from the bargaining process. For a negotiation to find a successful outcome, it is essential that a negotiating party's "win-set" – that is a set of measures that can be accepted or backed by domestic constituency – overlaps with the measures agreed upon with other negotiating parties.

LI has been variously criticized e.g. for disregarding the relevance of supranational institutions (Lindberg 1994) and in particular for its inadequacy at accounting for day-to-day governance of the EU (Wincott 1995). However, at a superficial glance the unfolding of the Euro crisis negotiations appears to be congruent with LI's theoretical tenets. In terms of preferences, the perception of the governments of Euro area member states was that the costs of disintegration would be prohibitive and thus measures should be taken to avoid it. Disagreement however started over the distribution of adjustment costs, with national positions mainly aligned with the fiscal position of the member states: according to a LI account, solvent "northern" countries preferred national adjustment, while debt-ridden "southern" countries were inclined towards a mutualization of adjustment costs (Schimmelfennig 2015). The negotiation phase, which has been described as a "war of attrition" (Iversen and Soskice 2013) or a "chicken game" (Schimmelfennig 2015), was characterized by hard bargaining aimed at extorting concessions from reluctant partners, epitomized for instance by Germany's resort to strategic pre-negotiations with France (Héritier 2017) or the Greek government's threat in October 2011 to call a referendum on the second bailout package (Inman and Smith 2011): More specifically, the reformed EMU

institutional architecture was focused on enhanced fiscal discipline with a strengthening of the SGP rules, semi-automatic sanctions for Euro area members falling short of their obligations, and the commitment – contained in the Fiscal Compact—to enshrine a “balanced budget” rule in national constitutions; arguably, the negotiations produced a renewed institutional framework embodying Germany’s “ordoliberal” vision of the EMU (Bulmer 2014), whose ultimate aim is to consolidate competitive markets regulated by strong, credible governments (Dullien and Guérot 2012:2), with some of the correctives inspired by the solidarity principle strongly advocated by France, namely the introduction of temporary and permanent financial support schemes (Schild 2013:30). Even if at first sight, as explained above, LI provides a compelling explanatory framework for the crisis-induced EMU reforms, the research questions addressed in this paper call for a deeper analysis. Following the falsifiability principle embedded in the original formulation of liberal intergovernmentalism (Moravcsik 1998:77), the next sections will shed light on the actual preferences of the actors involved, going beyond journalistic accounts and public declarations of political leaders. First of all, is the liberal intergovernmentalist claim that the preferences of “southern” debt-ridden countries are aligned to their fiscal position underpinned by primary empirical data? If not, what explains divergence? The next sections will show that a) the picture of Southern Europe is more variegated than a superficial analysis would suggest; and b) in the case of Italy, and contrary to what one should expect, an in-depth investigation reveals an apparently puzzling misalignment of this country’s negotiating positions vis-à-vis its fiscal predicament.

### **3. Southern Europe: the unfolding of the crisis**

What were the positions taken by South European countries during the 2010-13 SGP reform negotiations? Are they compatible with the claim, put forward by many observers, that due to their similarly problematic fiscal predicament the preferences of these countries essentially converged? Before addressing these questions, it is first of all useful to quickly recall how the crisis unfolded in each of the countries considered.

As far as **Greece** is concerned, in extreme synthesis the problem was that since joining the monetary union, the Greek government had been in the position to borrow at very low interest rates. This circumstance of course cannot per se be considered as a direct cause for the crisis; however, coupled with a tradition of poor accounting practices, it created the conditions for the ‘perfect debt storm’ to happen in the second half of 2009, once the financial crisis started

in the US spread to European markets. In this sense, it has been argued that the case of Greece is actually the only crisis genuinely linked to budgetary policy (Stein 2011): it should be recalled that in 2004 Greece had already received a warning by the European Commission for under-reporting budget deficit data (Saragosa 2004). Facing a bankruptcy, the government led by George Papandreou sought and obtained a first bailout worth 110 billion euros in May 2010; a new short-lived cabinet led by Lucas Papademos took over in November 2011 and finalized the negotiation of a second bailout package in February 2012; political instability led to new elections in May and June 2012, resulting in a government led by Antonis Samara which in turn would be replaced by radical left Syriza party leader Alexis Tsipras after the January 2015 elections.

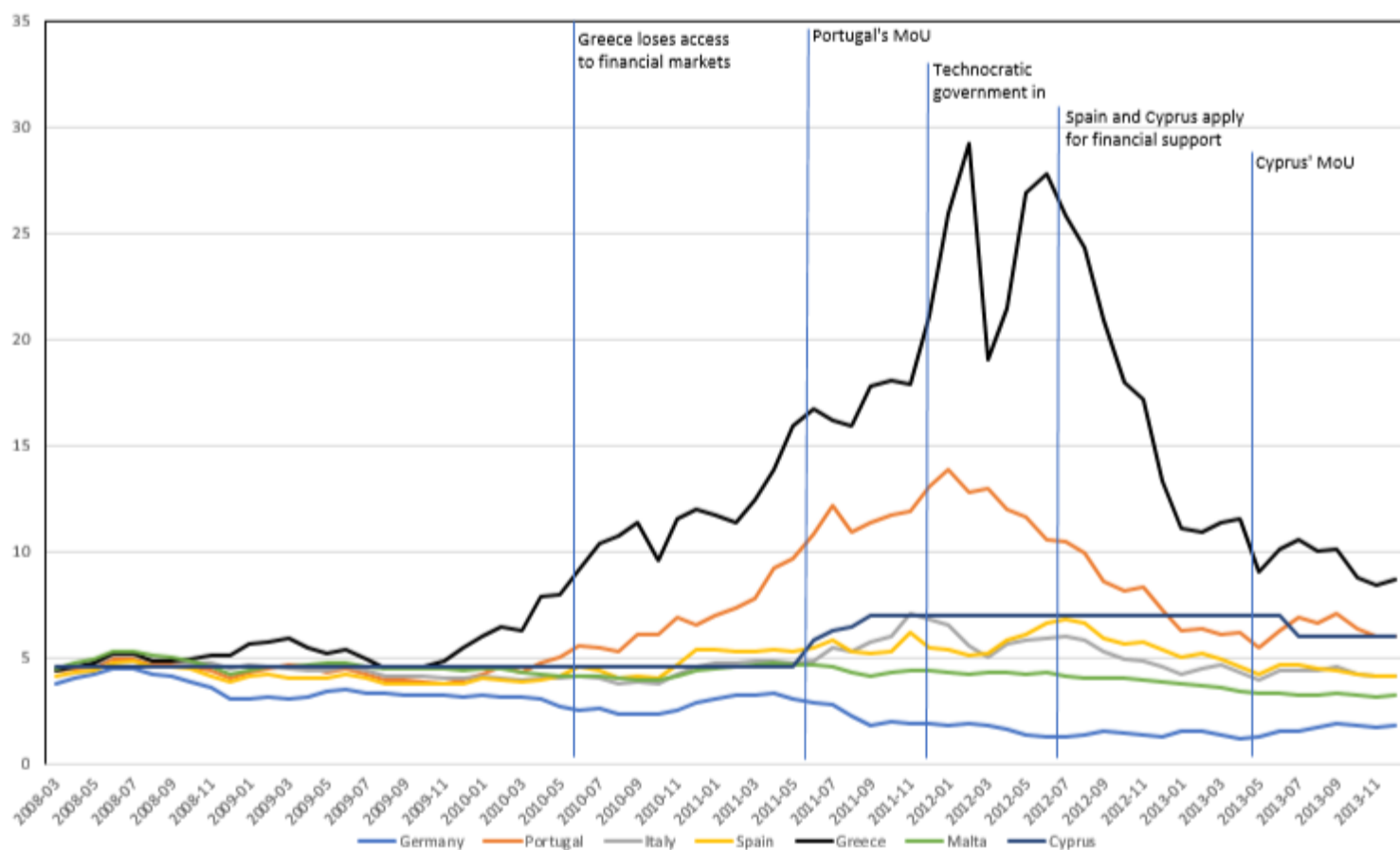
After Greece and Ireland, **Portugal** became the third euro zone country to apply for a bailout. It should be immediately stressed that rather than being ascribable to fiscal profligacy, Portugal's crisis was mostly due to economic stagnation and low productivity in the decade prior to the crisis (Reis 2015:434). In the face of increasing pressure from financial markets, in September 2010 the government led by socialist prime minister José Sócrates announced the introduction of austerity measures, including a freeze on state pensions, cuts in public sector wages and a rise in value added tax (Wise 2010). On March 23, 2011 the Portuguese parliament rejected a further government-sponsored austerity package, a move that triggered the resignation of Sócrates as prime minister and paved the way for a snap election the following June. Amidst political turbulence and after losing access to financial markets, in April 2011 Portugal applied for a bailout. In May a memorandum of understanding (MoU) listing the conditions for disbursement of financial support was signed by the Portuguese government and the European Commission, the European Central Bank and the International Monetary Fund.

Also for **Spain** the enabling conditions for the crisis are not to be directly found in the lack of fiscal discipline. Unlike Greece and Italy, in the years before 2008 Spain did not engage in excessive borrowing, its debt to GDP ratio was well under the Maastricht 60% threshold, and unlike Portugal its GDP growth rate in the five years before the crisis hit was comprised between 3 and 4%, thanks to which the public debt was indeed on a negative trend (World Bank 2015). The distinctive feature of the Spanish case is the construction bubble fed by easy credit, with investment in housing peaking at over 12% of the GDP in 2008 and being reduced to 7% by 2011 (Ortega and Peñalosa 2012), a shock which spread to the rest of the economy through virtually all existing channels: tightening financial conditions slowed down demand for housing, which pushed down house prices and had a negative impact on employment, not

to mention the serious strain faced by the banking sector (especially regional *cajas*) which had to absorb an increasing rate of insolvency of construction firms and found itself left with now almost worthless collateral – real estate property whose value had quickly fallen since the start of the crisis. These circumstances led to the June 2012 decision by the Spanish government led by Mariano Rajoy to accept (up to) 100 billion euros as a ‘loan’ by the ESM to recapitalize the country’s ailing banks.

The situation of **Italy** when the crisis erupted was yet different from that of the other South European countries. For most of its recent history, Italy has been characterized by high public debt; nonetheless, the country has also always had a good reputation in terms of debt management. Moreover – somewhat ironically – the relative isolation and ‘backwardness’ of the Italian banking sector coupled with effective supervision carried out by the Bank of Italy meant that when the crisis hit, Italy was better equipped than other southern European countries to cope with financial turmoil (Quaglia 2009).

Figure 1. 10 years interest rates (%) on government debt 2008-2013 and relevant events in South European countries



Italy's Achilles heel was (and to a large extent still is) to be found in the poor quality of regulation, a business climate that discourages foreign and domestic investment, low labor productivity, corruption, factors which, as the IMF recently put it (Miglierini 2016), account for 'two lost decades' in terms of economic growth in the country. Just as it happened in Greece, the crisis had a relevant political fallout in terms of governmental instability. As fear of contagion – epitomized by skyrocketing 10-years btp yields – soared at the end of 2011<sup>1</sup>, the government led by Silvio Berlusconi was replaced by a technocratic cabinet led by former EU commissioner Mario Monti. After the 2013 general elections, the Monti cabinet was in turn replaced by a short-lived 'grand coalition' government led by Enrico Letta, which resigned in February 2014 to be followed by a center-left cabinet led by Matteo Renzi. Among the troubled South European countries, Italy is the only one which managed to avoid any involvement of the Troika, in contrast with Greece, Portugal, Spain and Cyprus which all applied for more or less extensive financial support and therefore signed an official MoU.

While until 2007 the fiscal position of **Cyprus** was quite sound, with a 3.4% surplus and a 58.3% debt-to-GDP ratio bound to be further reduced by the end of 2008 (European Commission 2010a), by May 2011 the predicament of the country had dramatically changed. The roots of Cyprus' financial difficulties can be found in sluggish growth since the beginning of the financial crisis in 2008 and increases in government spending after the Cypriot Communist party took over in the same year, coupled with the overexposure of the Cypriot banking system to Greek financial institutions. On October 26, 2011 the European Council agreed to "...a significantly higher capital ratio of 9 % of the highest quality capital and after accounting for market valuation of sovereign debt exposures, both as of 30 September 2011, to create a temporary buffer... to be attained by 30 June 2012" (European Council 2011b). At that point, a feedback loop in Cyprus was inevitable: while it was extremely hard for Cypriot banks to raise the required capital, it would be equally difficult if not impossible for the government to bail in the banks. Unwilling to initiate a structural adjustment program under the aegis of the Troika, in the second half of 2011 the Cypriot government bought itself some time by securing a 2.5 billion emergency loan from Russia, but it should be noticed that such loan was meant to offer support for the country's budget deficit and excluded any recapitalization of the country's banking sector (Katsourides 2014:52). In June 2012, after a downgrade of the Cypriot sovereign by all of the "Big three"

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<sup>1</sup> As shown in Figure 1, in November 2011, the Italian 10-years government bond yields almost reached 7%, with a spread of over 5% vis-à-vis the German Bund.

credit rating agencies that made the government debt not eligible as collateral for borrowing from the euro system, the government finally asked for assistance for its banking system (The Economist 2013). In the run-up to the February 2013 election, the incumbent communist government claimed that the responsibility for the crisis in Cyprus lay with the banks (Orphanides 2014:22-23), and it was only in March 2013 that the newly elected conservative president agreed to a €10 billion bailout deal including a haircut to bank deposits under the threat that the ECB would stop providing liquidity to the Cypriot banking system (The Economist 2013). A MoU between Cyprus and the Troika was finally signed in April 2013.

Unlike the other five South European countries, **Malta** was virtually untouched by the sovereign debt crisis in the euro zone. In spite of the relevant role played by financial services in the Maltese economy, due to generally good levels of capitalization and relatively low level of external exposure of domestic banks (Azzopardi 2009: 105). Given such background of overall economic stability, it is not surprising that the 2013 Maltese general election, finally resulting in the success of the Labour Party led by Joseph Muscat, was dominated by issues of competence and credibility of the rival parties, in stark contrast with to the other five South European countries which were experiencing economic and financial difficulties (Fenech 2013).

#### **4. Southern Europe: Euro crisis negotiations and contested issues**

In order to provide a more nuanced picture of South European countries and their preferences against the backdrop of the Euro crisis this section will a) look at the contested issues emerged during the negotiations and b) actually map the positions of the six South European countries vis-à-vis those issues. This section is based on member states interviews conducted in the framework of the Horizon 2020 EMU choices project and focuses in particular on four contested issues which have spurred debate among the EU member states during the negotiation of the EMU reform packages. The first issue was whether or not to support Greece, and was discussed by the Euro group before the Greek government actually decided to ask for support in May 2010. The Euro group eventually decided to offer support on March 15, 2010 (European Commission 2010). The second issue hinged upon the possibility to endow the ESM with a firepower greater than € 500 billion, a figure that was considered adequate by some (e.g. Germany, Austria, Finland) whereas others would have preferred a

larger size. The third issue arose over the provision, eventually incorporated into the Six Pack, to introduce rQMV that is a semi-automatic mechanism triggering sanctions to punish member states violating the SGP. The fourth issue, emerged during the negotiation of the Fiscal Compact, was whether and how to institutionalize the commitment of member states to budget discipline by incorporating a debt brake into the domestic legal systems. In the first two drafts, reference was made to “national binding provisions of a constitutional or equivalent nature”, a vision that embodied the German preference, while the final text included a “softened” version of the original formula, referring to “provisions of binding force and permanent character, preferably constitutional, that are guaranteed to be respected throughout the national budgetary processes” (Kreilinger 2012: 4). As explained above, at first sight liberal intergovernmentalism can certainly be considered as a good theoretical framework to explain the outcome of the 2010-2013 negotiations. For one thing, it is undisputable that the final outcome largely mirrored the preferences of the countries with greater bargaining power – Germany in particular. However, some qualifications are in order when it comes to discussing and explaining the preferences of “South European countries” as generally presented even in authoritative accounts of the crisis (see e.g. Schimmelfennig 2015). First of all, equating “southern” and “debt-ridden” is inaccurate. As noted above, Malta is a clear exception in this sense. Moreover, although it is true that some countries, namely Italy and Greece, have historically been ‘debt-ridden’, it is equally true that other countries such as Spain and to some extent Cyprus had indeed been quite virtuous from the fiscal viewpoint prior to the crisis and that no matter how fiscally virtuous their governments were, piecemeal approaches to domestic banking crises (sometimes the only option on the table) turned out to be simply too expensive for taxpayers.<sup>2</sup> In this sense, it is plausible to infer that their primary interests – and thus, their future preferences – may not necessarily lie in debt mutualization. Second, as further explained below, the positions of South European countries were far from being completely aligned, especially as far as the third and fourth contested issues considered are concerned (see Table 1 below summarizing the issues and the positions). When it became clear that the situation of Greece was rapidly deteriorating and that the worsening of the crisis through contagion could threaten the very survival of the monetary union, virtually all EU member states, although with partially diverging motivations, agreed that some support had to be offered and that a permanent financial stability facility was needed.

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<sup>2</sup> On this point referred to the Spanish case, see Otero-Iglesias et al (2014 :53).



Table 1 Contested issues and South European countries positions

| Issues\ countries                                                                             | Cyprus             | Greece             | Italy              | Malta                                                          | Portugal                                                       | Spain     |
|-----------------------------------------------------------------------------------------------|--------------------|--------------------|--------------------|----------------------------------------------------------------|----------------------------------------------------------------|-----------|
| Support to Greece (final decision : 15 March 2010)                                            | In favour          | In favour          | In favour          | In favour                                                      | In favour                                                      | In favour |
| Increase the size of the ESM (final decision: 29 October 2010)                                | Strongly in favour | Strongly in favour | Strongly in favour | In favour                                                      | In favour                                                      | In favour |
| rQMV as decision making mechanism triggering SGP sanctions (final decision: 16 November 2011) | Contrary           | No position        | In favour          | Initially contrary, then came on board                         | Contrary                                                       | Contrary  |
| Introduction of Schuldenbremse in the constitution (final decision: 2 March 2012)             | Lukewarm support   | Lukewarm support   | In favour          | Contrary to constitutional level, accepting binding provisions | Contrary to constitutional level, accepting binding provisions | In favour |

This explains convergence with regard to the first two issues. However, moving to the third issue, it is safe to say that the positions of the countries considered were not completely aligned. The perspective to introduce a semi-automatic mechanism for the imposition of sanctions under the SGP, described by most interviewees as a “technical”, non-politicized issue, was not met with favor by the Cypriot negotiators. Although at the time Cyprus was not yet experiencing financial difficulties, the government would have preferred to maintain the status quo mainly because the introduction of rQMV would entail a significant loss of sovereignty for such a small country (Cyprus Interview 1, 2 and 3). The same applies to Malta, whose government leaned towards the status quo (Malta Interview 3 and 4). In both Spain and Portugal the issue was not discussed by the parliament and it was eventually decided upon by the respective governments. In Greece, the government reportedly had no position on this specific issue as it was focusing on more urgent problems and ended up by following the consensus that eventually emerged among the other member states (Greece Interview 3 and 5). As for Italy, its position was in favor of semi-automatic sanctions, thus running against the preferences expressed by the other South European countries. It is

possible to notice a discrepancy also with respect to the introduction of a constitutional-level debt brake rule debated during the negotiation of the TSCG. The Greek government, although it clearly found itself in a particularly weak position as it was in need of help (Greece Interview 1 and 2), found two orders of difficulties in supporting a text imposing an amendment of the constitution: while on the legal side there were objective impediments to incorporating the debt brake into the constitution, on the political side there was some resistance against the idea of losing control over fiscal policy-making and (Greece Interview 3 and 5). Ordinary legislation for the debt brake rule was also the preference of Cyprus, while Malta and Portugal shared concerns that it would be technically difficult to incorporate the rule into the constitution, although in principle they did not object to introducing binding provisions on fiscal discipline. When it comes to Italy and Spain, however, the situation is yet different. The governments of both countries speedily agreed to amend their constitution. While in the case of Spain this produced some domestic debate (Spain Interview 1 and 4), in Italy there was virtually no opposition, exception made for two small opposition parties, i.e. the Northern League and Italia dei Valori. The debt brake was incorporated in the constitution in an exceptionally short time,<sup>3</sup> with the last vote taking place on 17 April 2012. Moreover, constitutional law 1/2012 containing the provision was passed swiftly by both chambers of the Parliament with a two thirds majority, which avoided the possibility of a confirmative referendum.

From what said so far, it clearly emerges that the position of Italy seemed to be in stark contrast with its economic interests and to some extent also with the preferences of the other South European countries. How is it possible to explain this puzzle? In order to suggest a response to this question, the next section dwells upon Italy's "choice for Europe since Maastricht".

## **5. Explaining the Italian difference**

According to LI "the preferences of national governments regarding European integration have mainly reflected concrete economic interests rather than other general concerns like security or European ideals" (Moravcsik and Schimmelfennig 2009: 70). Following this line of reasoning, we should expect that a given government's negotiating stance be mainly aligned with domestic conditions, including (but not limited to) economic fundamentals. And

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<sup>3</sup> The first draft of the constitutional law had been approved on 30 November 2011 (Il Sole 24 Ore 2012).

yet, Italy's positions during the negotiation of the Six Pack and the TSCG as described above constitute a puzzle, as they clearly defy our reasonable expectations which would point to a preference for more flexibility rather than for stricter pro-austerity rules. How to account for them? A first possible hypothesis hinges on the concept of "vincolo esterno" (Moschella 2017). "Vincolo esterno" or "external constraint" can be defined as the strategic – and distinctive – use of external constraints made by Italian policy makers with the ultimate purpose of triggering domestic change (Vesan 2015: 499). The "vincolo esterno" principle was introduced by prominent policy-maker (and Treasury Minister at the time of the Maastricht Treaty) Guido Carli, who was convinced that only the external conditioning embodied by the European Union could "save Italy from itself" by fixing the country's dysfunctional economic and entrepreneurial system (Berta 2015: 484). A firm belief in the possibility and indeed desirability of "importing" macroeconomic discipline and credibility by joining the EMU – reinforced by the overwhelmingly pro-European attitude of the public opinion – indisputably influenced the orientations of Italian élites during the negotiation of the Maastricht Treaty (Quaglia 2004: 1107-1108). In fact, the articulated policy priorities set by Italy in the intergovernmental conference leading to the Maastricht treaty were on all counts consistent with this doctrine (Dyson & Featherstone 1996: 274). A further argument (borrowed from LI) that could be used to underpin the "vincolo esterno" explanation is that a key mechanism shaping institutional choice is that "...Governments transfer sovereignty to commit other governments to accept policies favored by key domestic constituencies and perhaps also to precommit the government to policies opposed by domestic groups unsupportive of the government" (Moravcsik 1998: 76). Thus, it would be reasonable to hypothesize that the technocratic government<sup>4</sup> led by Mario Monti – himself a pro-EMU economist – supported measures such as the introduction of the rQMV on the imposition of SGP sanctions, the accession to the TSCG and the "constitutionalization" of budget discipline out of the belief that they could facilitate domestic reform. A positive, recent example of how this principle can work in practice is the reform of the banking sector in Spain after the countries signed a MoU; in fact, it was only under the pressure of the Troika, an external actor whose legitimacy ultimately derived from its independence and expertise, that a full-fledged strategy for a truly impartial audit of the financial institutions, the acknowledgment of losses and a restructuration of the whole system eventually took place in a relatively short time (Otero-Iglesias et al 2016: 44).

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<sup>4</sup> The Monti cabinet almost perfectly embodied the ideal type of technocratic cabinet entirely made up of technocrats (Brunclík 2015: 59).

Compelling as the “vincolo esterno” explanation would be, however, the results of the interviews conducted lend little support to it. Coherently with the findings of Moschella (2017), who discusses the government’s commitment to external constraints as a possible explanation for Italy’s speedy accession to the TSCG, other factors seem to have been crucial in shaping Italy’s positions. In particular, it should be recalled that at the time of the negotiation of the Six Pack and of the TSCG, Italy was struggling to regain credibility in the eyes of international markets and the EU countries (Italy interviews 0 and 2). Thus, although it would have been plausible to expect Italy to oppose an excessive tightening of the rules, the top priority for the Italian government at the time was to restore credibility, hence the commitment to austerity measures as a way to send a clear message to other EU governments and calm down turbulent financial markets. In several occasions key members of the government, namely Italy’s prime minister Monti and minister for European Affairs Moavero Milanesi, overtly referred to more stringent fiscal discipline as necessary rather than desirable, and they stressed that strategies for growth should also be prioritized in the wake of the crisis (Moschella 2017). Thus, it can be said that fiscal discipline was conceived of as a “bitter pill” that nonetheless had to be swallowed in order to avoid the worst (Italy Interview 0). When updating the parliament on the fiscal compact negotiation, Monti stressed that the Italian government’s priority was to ensure a coherent framework for EU rules and to “avoid the introduction of constraints and stricter limits with respect to those already in force under the SGP and finally to balance the budget rules with mechanisms aiming to relaunch economic growth” (Monti 2011). In fact, “damage control”, that is extricating the country from a critical situation while at the same time containing the impact of external pressures, rather than using them strategically to induce domestic reform, was the primary objective of a government.<sup>5</sup> Mario Monti took office on 16 November 2011, only four days after the resignation of Berlusconi. A key role in his very appointment was played by the head of state Giorgio Napolitano, which took the initiative at a moment when Italy’s political parties were proving incapable of reaching any compromise on the formation of a new cabinet (Giannetti 2013) and after Greece and Portugal, Italy seemed to be the next in line for a default, with the aggravating circumstance that, with no financial support scheme in place yet, Italy appeared to be too big to fail and yet too big to bail (Elliott 2011). According to Marangoni (2012), 27 items classifiable as specific commitments can be singled out analyzing Monti’s inaugural

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<sup>5</sup> Significantly, one of the first measures taken by the Monti cabinet was the so-called “Save Italy” Decree, a structural adjustment package worth € 30 billion over three years (The Economist 2011).

speech. Of these, 7 referred to micro and macro economic policies aimed at boosting growth, while the remaining 20 commitments were distributed among the following policy areas: improvement in the public finances, reduction in the costs of maintaining elected bodies, rationalization of the public administration, reform of welfare, fight against tax evasion, taxation of property, selling off of publicly-owned real estate, intervention in the labor market (Marangoni 2012:141). Evidently, the measures envisaged by the new government's roadmap were tantamount to an ambitious program of structural adjustment whose contents and areas of intervention are similar to those included in the Greek and Portuguese MoUs. As Sacchi (2015) points out, in the case of Italy a mechanism of "implicit conditionality" was at play at the height of the sovereign debt crisis. In fact, Monti's government roadmap essentially reflected the contents of a confidential letter signed by Jean-Claude Trichet and Mario Draghi, ECB president and president-elect respectively, and addressed to Italy's then prime minister Silvio Berlusconi on 5 August 2011. In the letter, later leaked to the press (Corriere della Sera 2011), the ECB recommended urgent fiscal corrective measures including cuts in the cost of public employees and interventions in the pension system.<sup>6</sup> In sum, A *de facto* strict surveillance by European institutions coupled with Italy's vital need to maintain access to capital markets eventually put the Italian political establishment before the choice to either enter a formalized aid program or rather "internalize" oversight maintaining at least officially some autonomy in the implementation of the necessary measures.

## 6. Conclusion

The sovereign debt crisis constituted a critical juncture for the Eurozone, triggering a number of relevant institutional reforms in the architecture of the EMU. The Six Pack, the Two Pack, the Fiscal Compact, accompanied by the creation of the ESM, strengthened the surveillance and enforcement provisions of the SGP. In the extant literature, Southern Europe has often been presented as a relatively homogeneous group of debt-ridden countries with converging preferences on the terms of integration steps. Nonetheless, at a closer look, the paths leading to the crisis and the ways in which each of the South European countries adjusted to external constraints during the negotiations diverged substantially. If all South European countries were subject to direct oversight by the Troika, a notable exception was Malta, which was

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<sup>6</sup> It should be recalled that as of August 2011 the ECB extended its Securities Markets Programme – that is, purchases of sovereign bonds on the secondary market – to Italian and Spanish government bonds (Casiraghi et al 2013).

virtually unaffected by the crisis, and Italy, which experienced financial turmoil but managed to avoid entering a formal rescue scheme. When looking at some major contested issues emerged during the negotiations, it comes to light that the positions held by Italy on matters of fiscal discipline partly differ from those of the other South European countries and – somewhat surprisingly – seem to point to a preference for stricter discipline which is at odds with the country’s high level of public debt. The “vincolo esterno” principle, a plausible explanation for this puzzle, can however be dismissed in light of the evidence collected. Instead, the results of the interviews conducted in the framework of the EMU choices Horizon 2020 research project lend further support to the argument put forward by Sacchi (2015) and Moschella (2017), namely that the underlying logic governing Italy’s preference formation at the height of the crisis was a strong commitment by domestic decision-makers to avoid formal oversight by the Troika, although a mechanism of implicit conditionality vastly constrained the options available to them. In a nutshell, the Italy’s preferences are much more easily explained if they are correctly framed not in terms of a choice between stricter or more lax fiscal discipline but rather in terms of Euro area membership versus exit and possibly a financial Armageddon. From the theoretical point of view, it can also be concluded that LI still retains its explicative power but that the notion of “Southern Europe” needs to be problematized and a more nuanced study of the individual cases is necessary both to explain what happened and to make sounder forecasts about the future.

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