

Fabian Amtenbrink*, René Repasi and Jakob De Haan

Is there Life in the Old Dog Yet? Observations on the Political Economy and Constitutional Viability of Common Debt Issuing in the Euro Area

DOI 10.1515/rle-2016-0045

Published online October 25, 2016

Abstract: Departing from a political economy analysis of the benefits of common debt issuance by the Eurozone member states, we examine to what extent the various proposals for Eurobonds may be considered admissible under EU law and exemplary national (constitutional) laws, including those of Germany, Estonia, France, Ireland and Poland, from which one can deduce general national constitutional requirements applicable in all Eurozone member states. The medium and long-term potential gains from increased Eurozone stability and improved fiscal discipline must be traded off against the considerable legal and political obstacles of implementing any of these proposals. Yet key to the success of any common debt issuance is the effective dealing with the legacy debt of the Eurozone member states.

Keywords: Eurobonds, Euro crisis, sovereign debt, TFEU, constitutional law

JEL Classification: G01, G15, H63, K33, F34

1 Introduction

In seeking long-term solutions to the sovereign debt crisis that has dominated European Union policies and debates, common debt issuing in the euro area has been debated by academics and policy makers alike, primarily as a means to provide for a structural instrument to cope with Member States being in financial distress. These debates on what has been coined “Eurobonds” have resulted in a number of notable proposals from academia, namely by economists (De Grauwe and Moesen, 2009; Delpla and von Weizsäcker, 2010; Juncker and Tremonti, 2010; Brunnermeier et al., 2011; De la Dehesa, 2011;

*Corresponding author: Fabian Amtenbrink, Erasmus Universiteit Rotterdam, Netherlands,
E-mail: amtenbrink@law.eur.nl

René Repasi, Erasmus Universiteit Rotterdam, Netherlands

Jakob De Haan, De Nederlandsche Bank NV, Amsterdam, Netherlands

Suarez, 2011; Favero and Missale, 2012), and cumulated in the 2011 European Commission Green Book on the feasibility of introducing Stability Bonds (European Commission, 2011), as well as a European Parliament Resolution on this topic (European Parliament, 2011). While some euro area Member States have signalled support for a system of common debt issuing, namely France and Italy, others were openly opposed to such an idea. The German government explicitly rejected such plans; the German chancellor Merkel went on record as dismissing the European Commission's plans as "extraordinarily distressing" and "inappropriate".¹ While these plans did not materialize into concrete legislative proposals, they remained on the European policy agenda for some time. In the European Commission's 2012 blueprint for a deep and genuine economic and monetary union, which aimed at proposing "steps towards a full banking, economic, fiscal and political union", the common issuance of debt was considered as a way to create "new means through which governments finance their debt and offer safe and liquid investment opportunities for savers and financial institutions, as well as a euro area-wide integrated bond market that matches its US dollar counterpart in terms of size and liquidity" (European Commission, 2012:3/13). Also the 2012 Four-Presidents Report proposed the establishment of a "well-defined and limited fiscal capacity" at the Union level, which should then "offer an appropriate basis for common debt issuance without resorting to the mutualisation of sovereign debt" (van Rompuy, 2012:5/12). Yet, interestingly, while promoting the idea of a fiscal union, the 2015 Five-Presidents Report does not refer to common debt issuance at all. Instead, the Report proposes other strategies to increase the sustainability of public debt and the working of fiscal automatic stabilisers at the Union level (Juncker et al., 2015). For the time being, the project of Euro- or Stability Bonds seems to have been shelved at the European level due to a lack of sufficient political support.

In the following, it will be argued that common debt issuing should, from a political economy point of view, not be dismissed as an instrument to build a more sustainable Economic and Monetary Union (EMU). Under certain conditions, common debt issuance appears to be even a more promising way to impose fiscal discipline than the traditional way of economic policy coordination, namely the Stability and Growth Pact,²

¹ As reported by the German weekly journal *Der Spiegel*. www.spiegel.de/international/business/euro-bonds-debate-german-resistance-to-pooling-debt-may-be-shrinking-a-799692.html

² European Council, Resolution on the Stability and Growth Pact, 17 June 1997, OJ 1997 C 236/1; Council Regulation (EC) No 1466/97 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies, OJ 1997 L 209/1 amended by Council Regulation (EC) No 1055/2005, OJ 2005 L 174/1 and by Regulation (EU) No 1175/2011,

Six Pack,³ Two Pack⁴ and the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (TSCG).⁵ Yet, whilst there are political economy arguments for certain models of “Eurobonds”, common debt issuance comes with significant legal challenges at European and national constitutional level. Following the elaboration of the political economy considerations (Section 3), the broader constitutional implications (Section 4) of the several models of “Eurobonds” as proposed by academics (Section 2) will be examined.

2 The various models of “Eurobonds”

Academia developed several models of “Eurobonds”, which differ significantly. The proposals can be distinguished according to the guarantee structure, to the extent to which bonds issued at the European level would substitute national sovereign bonds, to the way they address the “moral hazard” problem, and to the nature of mutualised debt.

Firstly, as regards the guarantee structure, there are proposals that refer to joint and several guarantees by the participating Member States (Delpla and von Weizsäcker, 2010; Jones, 2010; Favero and Missale, 2012) and those that prefer

OJ 2011 L 306/12; Council Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure, OJ 1997 L 209/6 amended by Council Regulation (EC) No 1056/2005, OJ 2005 L 174/5 and by Council Regulation (EU) No 1177/2011, OJ 2011 L 306/33.

3 The “Six Pack” consists of five regulations and one directive: Regulation (EU) No 1173/2011 on the effective enforcement of budgetary surveillance in the euro area, OJ 2011 L 306/1; Regulation (EU) No 1174/2011 on enforcement measures to correct excessive macroeconomic imbalances in the euro area, OJ 2011 L 306/8; Regulation (EU) No 1175/2011 amending Council Regulation (EU) No 1466/97 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies, OJ 2011 L 306/12; Regulation (EU) No 1176/2011 on the prevention and correction of macroeconomic imbalances, OJ 2011 L 306/25; Council Regulation (EU) No 1177/2011 amending Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure, OJ 2011 L 306/33; Council Directive 2011/85/EU on requirements for budgetary frameworks of the Member States, OJ 2011 L 306/41.

4 The “Two Pack” consists of two regulations: Regulation (EU) No 472/2013 on the strengthening of economic and budgetary surveillance of Member States in the euro area experiencing or threatened with serious difficulties with respect to their financial stability, OJ 2013, L 140/1, and Regulation (EU) No 473/2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area, OJ 2013, L 140/11.

5 Available at: www.consilium.europa.eu/european-council/pdf/Treaty-on-Stability-Coordination-and-Governance-TSCG.

pro-rata Eurobonds, where participating Member States would only be liable for their predefined share of the overall “Eurobond” liabilities (Juncker and Tremonti, 2010; De Grauwe and Moesen, 2009). Secondly, some proposals entail that Eurobonds would replace all national bonds, whereas others plead for a substitution of only a part of national bonds. The most prominent one amongst the partial substitution proposals intends to replace all national debt below 60 % of GDP by Eurobonds with senior status superior to the remaining national bonds that refinance all national debt above 60 % of GDP (Delpla and von Weizsäcker, 2010). Thirdly, “moral hazard” is addressed by all proposals advocating joint and several liability, as “moral hazard” arises from the reduced incentives for Member States for fiscal discipline under such a liability regime. Proposals referring to partial substitution of national bonds consider “moral hazard” to be sufficiently addressed by the costs of refinancing the remaining national debt with national junior bonds (Delpla and von Weizsäcker, 2010). Another proposal seeks to overcome the “moral hazard” issue with short-term maturity of mutualised debt of less than one year (Hellwig and Philippon, 2011). According to this proposal, participation in the common issuance of short-term debt is conditional on fiscal discipline so that each year when new short-term debt is to be issued, European authorities decide on whether a Member State remains part of the common issuance. Other proposals suggest to set reinforced fiscal surveillance as a precondition for introducing joint and several liability (European Commission, 2011:8). Costs and benefits should be equalised according to a third group of proposals, which suggest the introduction of a scheme that compensates stronger participating states for gaining some liquidity but assuming the higher credit risks of weaker participating Member States (Favero and Missale, 2012:263; De Grauwe and Moesen, 2009; Mayordomo et al., 2009; Boonstra, 2010; Muellbauer, 2011). Such a compensation scheme indexes the interest to be paid by the participating Member States. Since markets are no longer in a position to indicate the costs for the “national share” in Eurobonds, the interest would have to be calculated based on the default risk priced in national bonds issued before the introduction of Eurobonds (De Grauwe and Moesen, 2009), based on Credit Default Swaps (CDS) (Mayordomo et al., 2009), or based on fiscal parameters, e.g. referring to deficits and debt levels, set administratively by a European authority (Muellbauer, 2011; Favero and Missale, 2012:264). Moreover, some proposals include penalties in case of free-riding or violations of fiscal discipline, such as losing access to European funds (Boonstra, 2010:5).

Fourthly and finally, as regards the kind of debt that is to be mutualised, one can distinguish proposals that seek only to mutualise national debt accumulated in the past (Sachverständigenrat, 2011) and those that aim at the common issuance of future debt.

In sum and for the sake of further assessment, questions revolving around the legal feasibility of “Eurobonds” have to address whether, first, a Member State can in principle be held liable for the debt of other Member States, whether, second, any joint and several liability must be limited to a certain amount of debt (defined by its size, its maturity or the date of issuance of the incurred debt) and, thirdly, whether a compensation scheme could overcome the legal obstacles relating to the common issuance of debt. Before addressing these legal questions, the political economy rationale underlying common debt issuing shall be highlighted in order to set the stage for the subsequent assessment of the constitutional implications of the several proposed models of Eurobonds.

3 The political-economy case for common debt issuing in the euro area⁶

3.1 Imposing fiscal discipline

The sovereign debt crisis in the euro area has shown that a system in which countries that share a common currency remain in charge of financing their own government debt is inherently unstable. Countries in a currency union do not have their own monetary policies or exchange rates. Consequently, a crisis cannot be (temporarily) alleviated by reducing interest rates or by devaluing the currency. Moreover, in times of crisis, national central banks are not in a position to provide their governments with infinite liquidity by buying sovereign bonds. These circumstances can trigger a situation in which financial market concerns about a country’s fiscal sustainability may become self-fulfilling prophecies. As pointed out by several authors, a solvent sovereign could be tripped into a fundamentally unwarranted payments default if the market were to adopt the “self-fulfilling fear equilibrium belief” that the government is not solvent (De Grauwe, 2011; Gros, 2012; Buiter and Rahbari, 2012). As long as market confidence is high, the government can afford the interest payments, as borrowing cost will be relatively low. However, if market confidence is low for reasons that need not be related to government policies, the government may face a problem, as the high risk premium requested will make debt service so expensive that the country’s fiscal policy becomes unsustainable. Doubts about the

⁶ The following part heavily draws on de Haan et al. (2012, 2016).

government's ability to service its debt could thus become self-fulfilling, as uncertainty about the ability to pay lead to higher rates of interest and thus ultimately to unsustainable fiscal policy.⁷ De Haan et al. (2014) have found periods of such misalignments for Greece, Portugal and Ireland.⁸ In fact, this problem may even occur if the government has a balanced budget, as a government that is highly indebted has to refinance a part of the debt that matures every year and thus requires refinancing. Because all countries in the euro area are vulnerable to these processes, financial turmoil in one Member State can easily spread to another. The implication of this analysis is, as Philippon (2015) has pointed out, that a "currency union needs a shared safe asset. That safe asset should not be the bonds of one particular member because this could trigger episodes of sudden stops and flight to safety. The price of a safe asset should increase in bad times, providing cheap funding to its issuers precisely when it is most needed."

Yet, in the case of the euro area Member States, a system of common debt issuing should not be limited to a crisis instrument to compensate for the absence of autonomous monetary policy instruments and exchange rates. In fact, it can also be perceived as a structural instrument to strengthen economic policy coordination in an EMU. Anno 2016 it has become abundantly clear that the legal framework on economic policy coordination introduced by the Maastricht Treaty in 1992 and thereafter operationalized by the Stability and Growth Pact in 1997 did not impose sufficient discipline on Member States before and, notably, after the introduction of the single currency. As has been argued elsewhere, the basic weakness of the framework has been its reliance on peer review and the lack of political will on the parts of the participating Member States to observe the basic fiscal rules laid down in Article 126(1) TFEU (Amtenbrink et al., 1997; de Haan et al., 2004; Amtenbrink and de Haan, 2006). These rules have been broken on numerous occasions by almost all Member States, in the context of which the limited enforcement system foreseen in Article 126(9)-(11) TFEU and Council Regulations 1466/97 and 1467/97, which form the core pillars of the Stability and Growth Pact, has moreover not been consistently applied. Undoubtedly the most referred to example involves the Council of the European Union's dealing in 2003 with persistently high

⁷ So there may be overshooting of bond yields. Yet, there is no consensus on the size and nature of this overshooting in the fast-growing literature on this topic. According to de Haan et al. (2014), who provide a summary of this literature, this in part reflects modelling uncertainty.

⁸ While these authors do not find support for consistent and massive mispricing for all countries in the periphery of the euro area, they do identify periods with misalignments for Greece, Portugal and Ireland.

government deficits in Germany and France that has resulted in an infringement procedure before the Court of Justice of the European Union (ECJ).⁹

What is more, the mechanisms foreseen in primary Union law, namely in the shape of the prohibition of monetary financing (Article 123(2) TFEU) and the prohibition for Member States or the Union to take on the commitments of another Member State (Article 125 TFEU), to let financial markets function as a disciplining force on Member States with high government debts, have not been particularly successful. Financial markets did not discipline euro area governments, as before the crisis they hardly differentiated between sovereign bonds, treating them all as (almost) risk-free.¹⁰ General risk aversion was very low before the crisis and financial markets apparently did not consider Article 125 TFEU as credible or – assuming a legal analysis on their part – as legally excluding all kinds of financial assistance, expecting instead that the Union would “renege” on a strict reading of this provision, “if needed, to avert a financial crisis” (Buti and Carnot, 2012:903). What is more, when market discipline eventually came by the end of the decade, financial markets were no longer willing to lend to certain countries (a so-called “sudden stop”).

Considering this experience, it is questionable whether the current system, which considerably relies on market discipline to keep Member States from overspending, can actually contribute to a sustainable system of economic policy coordination in the EMU. In fact, providing for such a sustainable system may require a shift in paradigm, which entails excluding Member States from entering the capital market on their own initiative.

Generally speaking, proposals for common debt issuing can be differentiated based on whether they suggest partial (Section 3.2) or complete (Section 3.3) substitution of national sovereign bonds. Both approaches have one problem in common, which concerns legacy debt (Section 3.4).

3.2 Introducing European next to national sovereign bonds

From the point of view of common debt issuing as an economic policy instrument, the introduction of a partial communitarisation of debt issuing is questionable. For proposals that suggest a partial substitution by Eurobonds (such as

⁹ ECJ, Case C-27/04, *Commission v Council*, ECLI:EU:C:2004:436.

¹⁰ De Grauwe and Ji (2012) argue that in the 2000–08 period, spreads were very close to zero even though the underlying fundamentals differed widely. According to these authors, the dramatic increase in spreads since 2008 significantly exceeded the changes in the underlying fundamentals.

the “red bonds” in the Delpla and von Weizsäcker proposal), given past experience, it is by no means evident that for the part of the debt that remains national, markets will indeed consider the new “no bail-out threat”, the main argument against “moral hazard”, for this part of the government debt to be more credible than past arrangements. By leaving part of the national debt to the Member States, no effective tools exist to actually force Member States to change their behaviour. Furthermore, as far as the junior national bonds are concerned, the proposed system does not rule out future market speculation against individual Member States.

3.3 Replacing national sovereign bonds by Eurobonds

A complete centralization of debt issuance in the euro area accompanied by joint and several liability for sovereign debt issued at the European Union level is the preferred option from a political economy perspective. Similarly to what can currently be observed for the ESM, loans would be granted against a common interest rate that covers the funding authority’s cost of funding and operations.¹¹ In this regard, de Haan et al. (2012, 2013) have argued that Eurobonds can be an effective instrument to enforce fiscal discipline if countries can no longer access capital and money markets on their own initiative at all.

As observed above, common debt issuing causes a moral hazard problem, as Member States may be tempted to free ride on other countries’ legal obligations to assume their debt in case of default. In fact, this is what Article 125 TFEU meant to rule out, that is that Member States can escape “the logic of the market when they enter into debt” (see further Section 4.1). What is more, the reduction of the borrowing costs at an aggregated level could disincentivise euro area Member States from conducting sound budgetary policies and undertake necessary structural reform measures, effects which would offset economic policy coordination. For this reason, a communitarisation of debt should be subject to the strict conditionality of any loans granted. In this context, the establishment of an independent Budgetary Authority has been proposed. The Authority should not only become the sole issuer of European sovereign bonds and thus have the exclusive right to grant loans to euro area Member States, but in such instances it should also be in charge of setting the conditions under which such loans are granted and, thereafter, of enforcing compliance with such conditions (de Haan et al., 2012, 2013). Member States would retain the autonomy to

¹¹ See the General Terms for the ESM Financial Facility Agreements, adopted by the ESM Board of Directors, 8 December 2014.

determine the size and composition of their national budgets, within the boundaries set by primary and secondary Union law and the TSCG, namely to have a balanced budget or a surplus in the medium term.

In a system where common debt issuing in the shape of Eurobonds would be the sole finance vehicle, the sanction regime would be arguably much more credible than anything that is currently imposed on non-compliant Member States because countries would have no access to finance except via the Budgetary Authority. This way, Member States will have every incentive to bring their public finances in line with the fiscal rules so as not to become subject to the strict conditionality regime, thereby addressing the moral hazard problem.

3.4 Dealing with legacy debt

The introduction of any partial or full communitarisation of debt issuing requires Member States and/or the EU to deal with any existing debt overhang in the participating euro area Member States first, making such a system a medium to long-term solution, rather than a quick fix in any ongoing crisis. Indeed, as Gros (2011) has rightly pointed out, “highly indebted countries would immediately be forced into a debt restructuring as they could no longer find buyers for the part only guaranteed nationally. This is why the system of blue/red bonds proposed by Delpla and Weizsäcker (2010) [...] cannot work if the countries concerned have a debt overhang”. This requires the installation of a separate debt redemption mechanism, such as proposed by the German Council of Economic Experts, which, in a nutshell, amounts to “a binding commitment of all participating countries to bring public debt ratios below the reference value of 60 % within the next 20 to 25 years”. The “participating countries can transfer their excessive debt exceeding the 60 % threshold at a certain date, into a redemption fund for which participating member countries are jointly and severally liable” (Doluca et al., 2012:1).

4 Constitutional implications

In a multidimensional legal system such as the European Union, the question of the broader constitutional implications of the introduction of common debt issuing arises both at the supranational, European (Section 4.1) and the national constitutional level (Section 4.2) (Athanassious, 2011:570–572).

4.1 Supranational perspective

From a Union law perspective, it is clear that the proposal to prohibit Member States from entering the capital and money markets on their own initiative for refinancing purposes is difficult to reconcile with today's Title VIII chapter 1 TFEU, both as regards the underlying principles and substantive prohibitions included therein.

Namely by means of Article 123 [prohibition of monetary financing], Article 124 [prohibition of privileged access to financial institutions] and the aforementioned Article 125 TFEU, the drafters of the EMU legal framework have introduced financial markets as a disciplining factor for Member States, as the latter are bound to refinance themselves at market conditions, thereby directly facing “the economic and budgetary consequences of a rising government debt” (Kämmerer, 2012:152)¹² in the shape of the default risk premium. By banning access to financial markets altogether, the implementation of the proposal introduced in Section 3.3 would turn one of the leading principles of the EMU on its head. As such, it is arguably hard to reconcile with the underlying rationale of today's Articles 123–125 TFEU.

Against this background, the question of whether a system of common debt issuing would also run counter to the substantive prohibition of Article 125 TFEU is somewhat secondary, as an amendment of primary Union law is inevitable in any event. Be that as it may, it has been argued that a system of common debt issuing that is secured by the joint and several liability of the participating Member States would violate the so-called “no bailout clause”. Arguably this does not already result from the granting of loans by a Union body to a Member State as such, as it has been rightly observed that a legal differentiation has to be made between the acceptance of existing commitments and the issuing of additional loans (Heun and Thiele, 2012:979). However, joint and several liability implies that each guaranteeing Member State can be approached for the payment of the total amount guaranteed (Expert Group on Debt Redemption Fund and Eurobills, 2014). Rather than to assume the existing commitments of the receiving Member State or only the creation of new commitments vis-à-vis a European or international body, in a system with not only joint but also several liability, Member States potentially take on each other's commitments deriving from the obligations under the common debt issuing scheme itself (Expert Group on Debt Redemption Fund and Eurobills, 2014:58–59).¹³

¹² Authors' translation.

¹³ These authors also reject the idea that Art. 125 TFEU does not stand in the way, as the joint and several liability actually arises vis-à-vis the debt-issuing body rather than the other

The ECJ has not as such ruled on the compatibility of common debt issuing with Union law, but the Court's interpretation of the relevant legal framework in its preliminary rulings in the cases *Pringle* and *Gauweiler* provide some important clues. In *Pringle* the ECJ emphasized in the context of the ESM that Article 125 TFEU does not prevent the Union or the Member States "from granting any form of financial assistance whatever to another Member State", in this context also referring to the stricter formulation of the prohibition of monetary financing of Article 123 TFEU.¹⁴ Reflecting on what kind of financial assistance is compatible with Article 125 TFEU, the European judges in *Pringle* refer to the origins of this provision and observe that it "ensures that the Member States remain subject to the logic of the market when they enter into debt, since that ought to prompt them to maintain budgetary discipline. Compliance with such discipline contributes at Union level to the attainment of a higher objective, namely maintaining the financial stability of the monetary union."¹⁵ Consequently, in the view of the ECJ, "financial assistance as a result of which the incentive of the recipient Member State to conduct a sound budgetary policy is diminished" is prohibited, as is "the activation of financial assistance by means of a stability mechanism such as the ESM [...] unless subject to strict conditions."¹⁶ This approach is confirmed in *Gauweiler*, where the ECJ in the context of the assessment of the ECB's announcement of outright monetary transactions in secondary sovereign bond markets has reiterated that the prohibition of monetary financing is to ensure that Member States adopt budgetary policies that take into account their refinancing needs on the markets and in doing so must bear the consequences "which a change in their macroeconomic or budgetary situation may have in that regard."¹⁷

As stated in *Pringle*, Member States may receive financial assistance if they remain responsible for their commitments and if the conditions attached thereto animate them "to implement a sound budgetary policy".¹⁸ With regard to the ESM, the ECJ considers the stability support and the credit line that can be granted to Member States to be in conformity with Article 125 TFEU, pointing out

participating Member States. Referring to the reasoned opinion of AG Kokott in *Pringle*, in their opinion Art. 125 TFEU also excludes "guaranteeing for any international organisation which is controlled by the Member States and thus an emanation of them". See also Smits (2011:2), who states that a reference to the argument that the Member States in effect assume liability for the debt issuing body "skirts the limits of the law".

¹⁴ Case C-370/12 *Pringle*, ECLI:EU:C:2012:756, para. 130, 132.

¹⁵ Case C-370/12 *Pringle*, ECLI:EU:C:2012:756, para. 135.

¹⁶ Case C-370/12 *Pringle*, ECLI:EU:C:2012:756, para. 136. Brackets added.

¹⁷ Case C-62/14 *Gauweiler et al.*, ECLI:EU:C:2015:400, para. 114.

¹⁸ Case C-62/14 *Gauweiler et al.*, ECLI:EU:C:2015:400, para. 137.

that the ESM does not effectively take on existing commitments or assume the debts of the recipient Member State. Instead, new debt is created that is owed to the ESM, and the loans are subject to strict policy conditionality. Yet, it should not be hastily concluded from this that the ECJ would therefore necessarily consider common debt issuing with joint and several liability also to be in conformity with primary Union law. Whilst the introduction of conditionality linked to a system of common debt issuing would accommodate the ECJ case law on this point, it is questionable whether a system of joint and several liability would be viewed in a similar vein. The reason for this is that according to the ESM Treaty, which formed the reference point for the ECJ's assessment of the scope of Article 125 TFEU, the liability of each participating Member State is limited, in all circumstances, to its portion of the authorised capital stock, and Member States are not liable, by reason of their membership, for obligations of the ESM (Art. 8(5) ESM-Treaty). What is more, changes in the authorized capital stock of the ESM are subject to national ratification procedures. As explained above, in a system of joint and several liability, Member States that are held liable for the total guarantee sum effectively take on other Member States' commitments in this regard.

What is more, the ECJ has stressed in rather general terms that the activation of financial assistance by means of a stability mechanism such as the ESM is not compatible with Article 125 TFEU unless it is “indispensable for the safeguarding of the financial stability of the euro area as a whole”,¹⁹ which is also reflected by paragraph 3 of Article 136 TFEU, stating the conditions for the establishment of a stability mechanism.²⁰ In analysing the ESM Treaty, the Court observes approvingly that financial assistance is only foreseen for countries “which are experiencing or are threatened by severe financing problems only when such support is indispensable to safeguard the financial stability of the euro area as a whole and of its Member States” and thus not “as soon as a Member State whose currency is the euro is experiencing difficulties in obtaining financing on the market.”²¹ This broad interpretation of Article 125 TFEU could be interpreted to rule out a system in which loans would be granted to Member States based on their individual budgetary needs, rather than with the overarching objective of the financial stability of the euro area as a whole.

¹⁹ Case C-370/12 *Pringle*, ECLI:EU:C:2012:756, para. 136.

²⁰ See European Council decision of 25 March 2011 amending Article 136 of the Treaty on the Functioning of the European Union with regard to a stability mechanism for Member States whose currency is the euro (2011/199/EU), OJ 2011 L91/1.

²¹ Case C-370/12 *Pringle*, ECLI:EU:C:2012:756, para. 142.

In sum, against the background of these findings, a revision of Article 125 TFEU alone, for example along the lines of what Smits (2011:4) has suggested in the past,²² would not suffice to introduce the proposed system of common debt issuing, given the shift in paradigm that comes with the introduction of an obligation at least for euro area Member States to turn to the EU level for all their refinancing needs. The need for a more substantive Treaty amendment would arise even more if proposals for the establishment of a new European body charged with common debt issuing (e.g. a European budgetary authority) with an independence similar to that of today's ECB would materialize. It must be borne in mind that the ECB's independence is actually safeguarded by primary Union law (Articles 127(1) and 282(3) TFEU, as well as Article 7 of the Statute of the European System of Central Banks and of the ECB).²³

A substantive amendment of primary Union law seems the only viable option, as the introduction of secondary Union law, namely based on Article 136(1) TFEU or Article 352 TFEU, would arguably not suffice. Article 136(1) TFEU does allow euro area Member States to adopt specific measures to strengthen the coordination and surveillance of their budgetary discipline in order to ensure the proper functioning of the economic and monetary union. It can be noted in this context that this provision constitutes a separate legal basis for the adoption of measures that complement the objectives of the two provisions that are explicitly referred to in Article 136(1) TFEU, namely Articles 121 TFEU (multilateral surveillance procedure) and Article 126 TFEU (excessive deficit procedure) (Potacs, 2012:1581). Yet, while a system of common debt issuing would also be aimed at achieving budgetary discipline in line with what Articles 121 and 126 TFEU state, this does not remove the aforementioned conflict with Articles 123–125 TFEU. The same applies for the so-called flexibility clause of Article 352 TFEU, which, according to the established ECJ case law, forms “an integral part of the institutional system based on the principle of conferred power” and as such “cannot serve as a basis for widening the scope of [Union] powers beyond the general framework created by the provisions of the [TFEU] as a whole and, in particular, by those defining the tasks and the activities of the [Union]”.²⁴ Whilst the establishment of a system ensuring sound budgetary policies can be considered a Union objective in the sense of Article 3 TEU, no secondary legal act could

²² Smits has proposed adding a new paragraph 3 to Article 125 TFEU, which states that this provision does not prevent euro area Member States from “jointly issuing debt instruments and, in this context, guaranteeing such issuance, provided the Member States participating in this issuance ensure an equitable distribution of the proceeds and respect Article 126”.

²³ Protocol No. 4 annexed to the TEU and TFEU, OJ 2012 C 326/230.

²⁴ Brackets added. Joined Cases C-402/05 P and C-415/05 P, *Kadi*, ECLI:EU:C:2008:461, para. 203.

overcome the substance of Articles 123 to 125 TFEU. This would require a Treaty change, which cannot be achieved on the basis of Article 352 TFEU.²⁵

Avoiding Treaty amendment through the use of a purely intergovernmental solution similar to the ESM Treaty would, furthermore, not be an option for the proposed system of common debt issuing either, as the ECJ has made clear in *Pringle* that Member States “may not disregard their duty to comply with Union law when exercising their competences” and that commitments that are created by an intergovernmental agreement such as the ESM Treaty have to be “consistent with European Union law”.²⁶

The introduction of common debt issuing would thus have to take place via the stony path of an ordinary Treaty amendment procedure as laid down in Article 48 TEU with all the associated political pitfalls and risks of failure. A simplified Treaty revision procedure as foreseen in Article 48(6) TEU by unanimity decision by the European Council is not an option, since this path is only open if the proposed amendment does not increase the competences conferred on the Union in the Treaties. Yet, the introduction of an exclusive right for the Union to issue loans to Member States and the prohibition for Member States to refinance themselves in the markets constitutes such an additional transfer of competences.

What is more, the impact of the introduction of such a system would not be limited to Title III TFEU on Union policies and internal actions, but also touch upon the institutional provisions in primary Union law, namely if a new Union body would be created for that purpose. In fact, it has been rightly observed that the establishment of common debt issuing requires an adequate mechanism ensuring democratic legitimacy and accountability. In its final report, the Expert Group on Debt Redemption Fund and Eurobills observes in this regard: “Parliamentary accountability is key. Models should be found to ensure it at both levels: accountability provided by the European Parliament for decisions taken at European level, but also a key role for national parliaments given their continued power of the purse” (Expert Group on Debt Redemption Fund and Eurobills, 2014:86). The case for solid legitimacy and accountability mechanisms is further supported by the fact that for the reasons stated above, common debt issuing would have to be accompanied by strict conditionality. Past experience with the monitoring of the economic adjustment programmes by the so-called Troika, consisting of (representatives of) the European Commission, the ECB and the IMF, highlight how problematic such arrangements can be.²⁷ It is somewhat

²⁶ Case C-370/12 *Pringle*, ECLI:EU:C:2012:756, para. 68 and 109.

²⁷ See e.g. European Parliament, Report on the enquiry on the role and operations of the Troika (ECB, Commission and IMF) with regard to the euro area programme countries (2013/2277(INI)).

of a missed opportunity that the ECJ in *Pringle* did not reflect on the consequences of the application of the ESM and specifically of policy conditionality on the Union's own structural principle of representative democracy stated in Article 10 TEU (Amttenbrink, 2014:233).

It is exactly on this last point that national (constitutional) law may restrict the options of the Union legislator and Member States in designing a system of common debt issuing.

4.2 National perspective²⁸

For the reasons stated in the previous section, from a supranational perspective, the introduction of a system of common debt issuing would arguably be subject to the very high hurdle of an ordinary Treaty amendment procedure. Part of this hurdle is created by the necessary ratification process in all Member States in accordance with their respective constitutional requirements. Leaving aside the question of whether the required majorities could be achieved in the national parliaments, an essentially political issue, the question arises, to what extent a European system of common debt issuing under the control of a newly created independent European body, paired with the prohibition to seek financing in the financial market, would face fundamental constitutional objections in the national domain.

4.2.1 Deducing national constitutional requirements for common debt issuance from national constitutional identities

A comprehensive overview over the several national constitutional requirements would go beyond the scope of the present contribution as it would have to involve the study of the legal situation in at least all 19 euro area Member States. However, recent decisions by national highest (constitutional) courts on the relationship between national (constitutional) law and EU law, both before and after the break-out of the sovereign debt crisis, arguably provide important clues to the type of national constitutional hurdles that the introduction of such a system could face. Indeed, it should be recalled that national (written and unwritten) constitutions, as well as highest (constitutional) courts, continue to fulfil a vital role in today's Union, as "the European legal order defines and limits the exercise of public power beyond the state, it only provides for the organisational framework required to

²⁸ The following draws in parts on Amttenbrink (2012) and Amttenbrink (2014).

legitimise the exercise of public power to a limited extent,” as courts take on the role as a guardian of broader constitutional identity (Amtenbrink, 2012:47/62).

It is this admittedly rather vague concept that connects rulings of highest (constitutional) courts in different Member States, which in different ways and concerning a variety of Union acts identify what may be referred to as a constitutional core, the alteration of which by the Union legislator may be conditional on the consent of the constituting power or even excluded altogether. What makes some rulings by national highest (constitutional) courts interesting in the present context is the direct link that is made between the principle of democracy and the role of national parliaments with what national courts consider to constitute the constitutional core.

Already prior to the crisis, the French Constitutional Council (*Conseil Constitutionnel*) in its decision on the French Act pertaining to copyright and related rights in the information society²⁹ referred to rules and principles that are “inherent to the constitutional identity of France” that cannot be disregarded “except when the constituting power consents thereto”.³⁰ As has been argued elsewhere, “the reference to a constitutional identity of France suggests that the primacy of the European legal order would not be considered acceptable in a situation in which this would run contrary to the basic constitutional structure as laid down in Article 1 of the French Constitution. This provision refers *inter alia* to France being a secular, democratic and social Republic, organised on a decentralised basis” (Amtenbrink, 2012:48).

In its decision on the constitutionality of the Treaty of Accession to the EU, the Polish Constitutional Tribunal (*Trybunał Konstytucyjny*) noted: “The principle of interpreting domestic law in a manner ‘sympathetic to European law’, as formulated within the Constitutional Tribunal’s jurisprudence, has its limits. In no event may it lead to results contradicting the explicit wording of constitutional norms or being irreconcilable with the minimum guarantee functions realised by the Constitution. In particular, the norms of the Constitution within the field of individual rights and freedoms indicate a minimum and unsurpassable threshold which may not be lowered or questioned as a result of the introduction of Community provisions.”³¹ The Polish judges also stated that in case of *irreconcilable inconsistency between national and European norms* it is up to the Polish constitutional legislator to take an “autonomous decision as

²⁹ Thereby transforming Directive 2001/29/EC of the European Parliament and of the Council of 22 May 2001 on the harmonisation of certain aspects of copyright and related rights in the information society (OJ 2001 L167/10).

³⁰ 2006-540 DC. para. 19.

³¹ Judgment of 11th May 2005, K18/04, para. 14.

regards the appropriate manner of resolving that inconsistency, including the expediency of a revision of the Constitution”.³²

Already in its much-cited decision on the constitutionality of the ratification of the Treaty on European Union (Maastricht Treaty), the German Federal Constitutional Court (*Bundesverfassungsgericht*) noted that the development of the German state is bound “to the essential content of the constitutional order specified therein, and seeks thus to fortify the constitution in force against a development aimed at a new order, without being able itself to lay down rules binding on the constitution-making power”.³³ In its ruling on the constitutionality of the German act ratifying the Treaty of Lisbon, the German Court has emphasized the importance of the observance of democratic principles and the obligation of the German constitutional bodies to ensure that “as regards the transfer of sovereign powers and the elaboration of the European decision-making procedures [...] in an overall view, the political system of the Federal Republic of Germany as well as that of the European Union comply with democratic principles within the meaning of Article 20.1 and 20.2 in conjunction with Article 79.3 of the Basic Law.”³⁴ In fact, Germany’s highest judges reserve to themselves the right to an “identity review”, which is considered to have its roots in Article 23(1) in conjunction with Article 79(3) of the German Basic Law and which basically protects from amending Article 1 on the inviolability of human dignity and binding force of human rights, as well as Article 20, which defines the basic constitutional principles, specifically the principle of (parliamentary) democracy.

The relevance of the position of national constitutions, and specifically the principle of democracy embedded therein, in considering any supranational or international legal regime introducing common debt issuing is highlighted by recent decisions more directly related to the regulatory response to the sovereign debt crisis in the euro area, *inter alia* on the adoption of the EFSM Regulation, the amendment of Article 136 TFEU, and the conclusion of the ESM Treaty and the Fiscal Compact.

In their decision on the Polish act of ratification of the European Council Decision amending Article 136 TFEU, the Polish judges seem to be critical on the reach of the ESM Treaty, which for the time being actually does not even apply to Poland as a non-euro area Member State. In their view, this Treaty “changed the architecture of the Economic and Monetary Union”, which has serious

³² *Ibid*, para. 1.

³³ BVerfGE 89, 155. English translation available in [1994] 1 CMLR. 57, section B, para.32

³⁴ Brackets added. BVerfG, Judgment of 30 June 2009 – 2 BvE 2/08, para. 245. The English language version is available at www.bundesverfassungsgericht.de/SharedDocs/Entscheidungen/EN/2009/06/es20090630_2bve000208en.html

implications for the signatory Member States that “accept an obligation [...] to cover their share of capital in that institution, as well as to provide – upon fulfilment of further premises – funds to cover the subscribed capital, or even to cover the shares of any insolvent signatories to the Treaty [, which] implies a substantial burden for the budgets of the Member States involved.”³⁵ Given this view, it is not surprising that the Polish judges have suggested that a future ratification of the ESM Treaty may become subject to constitutional review.³⁶

The Irish Supreme Court has taken a rather European-friendly approach to the constitutional review of the ESM Treaty, concluding that said Treaty does not encroach upon the economic or monetary sovereignty of Ireland and as such does not infringe Irish constitutional law.³⁷ Even the emergency voting procedure of Article 4(4) ESM Treaty, which allows for the decision on financial assistance to be taken by a qualified majority of 85% of the votes cast, thereby making it arithmetically possible to overrule Member States with a small capital share in the ESM, was considered “a specific policy of the ESM Treaty, through a specified mechanism, within the limits of the specified maximum financial contribution”, rather than a major restriction of parliamentary sovereignty.³⁸

By contrast, the Estonian Supreme Court (*Riigikohus*) came to the preliminary conclusion that the granting of financial assistance as a result of the application of the emergency voting procedure foreseen in Article 4(4) ESM Treaty may in fact “affect the revenue and expenditure of the Estonian state budget and thereby restrict the budgetary-political choices of the Estonian Parliament (*Riigikogu*)” and considered this “an interference with the financial competence of the *Riigikogu* [which] brings about also an interference with the principle of a democratic state subject to the rule of law and of the state’s financial sovereignty since indirectly the people’s right of discretion is restricted.”³⁹ For the majority of presiding judges, the way out of the looming clash of Estonian constitutional law with the ESM Treaty was the construction of a constitutional justification based on the given (economic) circumstances at the time. Yet, as has been observed elsewhere, the extent to which the Estonian

³⁵ As already noted in Amtenbrink (2014:229–230). Polish Constitutional Tribunal, decision of 26 June 2013, Ref. No. K 33/12, section 7.6.1. Brackets added. The English language version used here is available at <http://trybunal.gov.pl/en/news/judgments/art/4607-europejski-mechanizm-stabilnosci-zarzadzanie-warunkami-uczestnictwa-polski-w-unii-walutowej-okre>.

³⁶ Polish Constitutional Tribunal, decision of 26 June 2013, Ref. No. K 33/12, section 7.6.1.

³⁷ The Supreme Court, Appeal No. 339/2012, judgment of 19 October 2012, sections 17 iv and vi.

³⁸ Supreme Court, Appeal No. 339/2012, judgment of 19 October 2012, section 17 xi of the judgment. See already Amtenbrink (2014:230).

³⁹ Brackets added. Estonian Supreme Court, constitutional judgment 3-4-1-6-12 of 12 July 2012, para. 153, 159. An English translation can be found at www.riigikohus.ee/?id=1347.

Court was split on this issue becomes clear from the number and tone of descending opinions (Amttenbrink, 2014:229).

The approach of the German Federal Constitutional Court to the constitutionality of the crisis measures completes the picture. Already in its decision on the constitutionality of the ratification of the Treaty on European Union, the German Court stressed that Article 38 of the German Basic Law on parliamentary elections and the general right to vote excludes a transfer of tasks and competences to the supranational level that would result in the draining of the legitimation of and influence on the exercise of state power that derives from general parliamentary elections on such a scale that the principle of democracy, which is protected from amendment by the eternity clause of Article 73(3) of the German Basic Law, is violated.⁴⁰

Yet it is the German ruling on the constitutionality of the German (bilateral) financial aid to Greece and the German guarantee in the context of the EFSM that may offer the clearest view of the kind of national constitutional issues arising from the introduction of a system of common debt issuance in the euro area that comes paired with a system of joint and several liability and some type of independent European budgetary authority. In the view of the German Court, “[t]he decision on public revenue and public expenditure is a fundamental part of the ability of a constitutional state to democratically shape itself [...]. The German Bundestag must make decisions on revenue and expenditure with responsibility to the people. In this connection, the right to decide on the budget is a central element of the democratic development of informed opinion”.⁴¹ In this context, the German federal constitutional judges have stressed that this right to decide on the budget not only constitutes “an instrument of comprehensive parliamentary monitoring of the government”, but also “brings the fundamental principle of equality of the citizens up to date in the imposition of public charges as an essential manifestation of constitutional democracy [...]”. In relation to the other constitutional bodies involved in establishing the budget, the elected parliament has a paramount constitutional position.⁴² Consequently, the Court has emphasized that “[a]s representatives of the people, the elected Members of the German Bundestag must retain control of fundamental budgetary decisions even in a system of intergovernmental administration”.⁴³

⁴⁰ BVerfGE 55, 189, Headnote No. 1.

⁴¹ BVerfGE 129, 124, Headnotes No. 2 and 3. English language version available at www.bundesverfassungsgericht.de/SharedDocs/Entscheidungen/EN/2011/09/rs20110907_2bvr098710en.html

⁴² Brackets added. BVerfGE 129, 124, para. 122.

⁴³ BVerfGE 129, 124, para. 124–125.

The German judges have also delivered a stern warning to the German federal parliament, which “may not transfer its budgetary responsibility to other actors by means of imprecise budgetary authorisations. In particular it may not, even by statute, deliver itself up to any mechanisms with financial effect which – whether by reason of their overall conception or by reason of an overall evaluation of the individual measures – may result in incalculable burdens with budget relevance without prior mandatory consent, whether these are expenses or losses of revenue”.⁴⁴ In fact, parliament may not be limited to “merely re-enacting and [...] no longer exercise overall budgetary responsibility as part of its right to decide on the budget.”⁴⁵

Consequently, in the view of the Court, the German federal parliament cannot enter an intergovernmentally or supranationally agreed automatic guarantee or performance “which is not subject to strict requirements and whose effects are not limited, which – once it has been set in motion – is removed from the Bundestag’s control and influence.”⁴⁶ What is excluded is an “indiscriminate authorisation in a substantial degree to guarantees, fiscal disposals of other Member States” which “might lead to irreversible, possibly massive, restrictions on national political legislative discretions.”⁴⁷ The German judges go on to emphasise that “no permanent mechanisms may be created under international treaties which are tantamount to accepting liability for decisions by free will of other states, above all if they entail consequences which are hard to calculate” and, moreover, that the German parliament “must specifically approve every large-scale measure of aid of the Federal Government taken in a spirit of solidarity and involving public expenditure on the international or European Union level”.⁴⁸ Supranational agreements that may be “of structural significance for Parliament’s right to decide on the budget, for example by giving guarantees the honouring of which may endanger budget autonomy, or by participation in equivalent financial safeguarding systems” not only require parliamentary consent but must moreover ensure that “sufficient parliamentary influence will continue in existence on the manner in which the funds made available are dealt with”.⁴⁹

The German Federal Constitutional Court reiterated this view in its order on several applications for the issue of temporary injunctions to prevent the

⁴⁴ BVerfGE 129, 124, para. 124–125.

⁴⁵ BVerfGE 129, 124, para. 124–125. Brackets added.

⁴⁶ BVerfGE 129, 124, para. 127.

⁴⁷ BVerfGE 129, 124, para. 127.

⁴⁸ BVerfGE 129, 124, para. 128.

⁴⁹ BVerfGE 129, 124, para. 128.

ratification of the ESM Treaty and the Fiscal Compact.⁵⁰ Engaging the question under what circumstances a payment obligation or commitment entered into could be considered to encroach upon the protected core of budgetary autonomy of the parliament, the German judges refer to “a manifest overstepping of extreme limits”, whereby “the payment obligations and commitments to accept liability took effect in such a way that budget autonomy, at least for an appreciable period of time, was not merely restricted but effectively failed.”⁵¹ In this context, the Court has referred to a broad latitude of the legislator that has to be recognized also by the Court itself. With reference to the Treaty’s legal framework on economic and monetary policy, the Court notably stressed that in principle “it is not anti-democratic from the outset for the budget legislature to be bound by a particular budget and fiscal policy”, which also becomes clear from the constitutional debt break that the German Basic Law foresees itself, even when this restriction derives from an obligation under European Union law or international law.⁵² While concluding that the German constitution, specifically Article 38(1), as well as Article 20(1) and (2) in conjunction with Article 79 (3) of the German Basic Law, do not stand in the way of a ratification of the ESM Treaty, the German Court observed that its conclusion is reached based on a particular interpretation of the ESM provisions on the increased capital call, the provisions on the inviolability of the documents, as well as the professional secrecy of the legal representatives of the ESM.⁵³ With regard to the former, the German judges emphasised the importance of the binding limitation of Germany’s budget commitments resulting from the ESM Treaty and stressed that Germany “must ensure the required clarification in the ratification procedure” so that the liability is indeed limited to its share of the authorised capital stock that is foreseen in Article 8(5) ESM Treaty.⁵⁴

4.2.2 Core constitutional requirements across Member States’ constitutions

From the admittedly incomplete but nevertheless significant selection of judgments by highest national (constitutional) courts, several constitutional principles can arguably be deduced, which may be considered common among the

50 BVerfG, Order of 12 September 2012 – 2 BvR 1390/12. English translation available at www.bundesverfassungsgericht.de/SharedDocs/Entscheidungen/EN/2012/09/rs20120912_2bvr139012en.html

51 BVerfG, Order of 12 September 2012 – 2 BvR 1390/12, para. 216–217. Brackets added.

52 BVerfG, Order of 12 September 2012 – 2 BvR 1390/12, para. 224–225.

53 BVerfG, Order of 12 September 2012 – 2 BvR 1390/12, para. 240 et seq.

54 BVerfG, Order of 12 September 2012 – 2 BvR 1390/12, para. 242–243, 253.

constitutions of the Member States that would participate in a joint debt issuance scheme. They can be considered common because the principles applicable to a European debt issuance scheme derive from the principle of democracy, which can be found in all national constitutions. These core constitutional principles applicable to common debt issuance cover the right of the national parliament to decide autonomously on the revenue and the expenditure of the national budget and the protection of the national budgetary autonomy, which requires a predefined limitation of the possible commitments of national budgets for extranational purposes. The principled nature of the latter derives from the fact that the budgetary rights of a national parliament would be rendered meaningless if the extranational commitments of the national budget exceeded its overall revenue.

Against this background, it should be noted that the constitutional situation in Germany, as reflected in the judgments of the Federal Constitutional Court, while receiving much attention, may not be entirely unique in the euro area as this is unlikely to be the only euro area Member State for which this applies. This is arguably due to the fact that common debt issuance may in several regards touch upon what these courts could consider to form part of the core constitutional principles.

4.3 Assessing the various “Eurobonds” models against core constitutional requirements

Before assessing the several proposals for the introduction of a system of (partial) common debt issuing, as outlined in Section 2, against the core national constitutional principles just described, it is worth repeating the three distinctive elements of these models: the presence of joint and several liability, the provision for a limitation of the covered debt (based on either its size, maturity, or date of issuance), and the inclusion of a compensation scheme.

Common to all “Eurobonds” proposals is the banning of participating Member States from turning to the financial markets for those parts of the debt that are covered by a common issuance. Here the question arises whether already the exclusion of new borrowing could be considered a restriction of parliamentary budgetary autonomy in breach of the principle of democracy. While the answer to this question must obviously be reserved to a full constitutional evaluation for all Member States, it can be noted that currently already the Fiscal Compact obliges the signatory Member States to budgetary positions that are balanced or in surplus. In fact, Member States are even required to include a corresponding rule in national law that are “of binding force and permanent

character, preferably constitutional, or otherwise guaranteed to be fully respected and adhered to throughout the national budgetary processes” (Art. 3 (1)(a) and (2) TSCG). Moreover, national law must also foresee mechanisms that automatically apply to correct significant deviations from the medium-term budgetary objectives (Art. 3 (1)(e) and (2) TSCG). Against this background, it is questionable whether the exclusion of autonomous refinancing on private financial markets is necessarily problematic from a constitutional point of view.

As regards joint and several liability, it becomes clear from the above cited case-law of the German Federal Constitutional Court that a system of common debt issuing based on such joint and several liability may be difficult to reconcile with the budgetary autonomy of parliament, in particular if the actual decisions on the issuing of common debt and granting of loans would be in the hands of an independent European budgetary authority at the supranational level. In the first place, different to the ESM where at least in the case of Member States with large capital shares, no decisions can be taken without the consent of their governments, a democratic link to the national constitutional order would be absent in the case of a European budgetary authority that would be independent from government decision-making bodies at the European and national level, similarly to the ECB. It is rather doubtful whether possible national government or parliamentary involvement in the appointment of the decision-making body of such a European body would be considered sufficient to secure national budgetary autonomy of parliament. Yet, whereas a more direct involvement of national parliaments in the actual decision-making at the European level may provide a solution from the legal point of view, this would raise questions about the actual insulation of the decision to issue European debt from unwarranted (national) political influence.

What is more, any incalculable risk-sharing under a permanent common debt issuing scheme would be very problematic. This would not only restrict the budgetary autonomy of parliament at the time of the initial agreement for the establishment of such a framework, but also future parliaments. At least from the perspective of German constitutional law it is very questionable whether this could be reconciled specifically with Article 20(1) and (2) in conjunction with Article 79(3) of the German Basic Law.⁵⁵ This consideration supports three conclusions. First, joint and several liability is not *per se* excluded by core constitutional requirements provided that, second, the amount for which a national budget can be held liable is defined in advance and limited in such a

⁵⁵ Another question is whether unrealized liabilities resulting from the participation in such a system would have to be considered as debt that is covered by the national constitutional debt ceiling.

way that national parliament is in a position to effectively appreciate the potential liability risk. Third, joint and several liability without any limitation is likely to conflict with national core constitutional requirements in a way that national constitutions would have to be amended in order to allow for such models of “Eurobonds”.

This may be different for those proposals (Juncker and Tremonti, 2010; De Grauwe and Moesen, 2009) that envisage the participating Member States’ liability to be founded on a *pro rata* basis combined with a system of paid-in and committed callable capital, as with the ESM. Such arrangements are less intrusive in a constitutional sense, as the *pro rata* principle makes the actual liability predictable. Yet, it is at least uncertain how common bonds that are not guaranteed jointly and severally by all participating Member States would be perceived by the financial markets. Perhaps in such a case the risk premium and thus also the conditions under which an independent European body could offer loans to euro area Member States could be much less favourable than would otherwise be the case.

This leads to the assessment of the second distinctive element of the “Eurobonds” proposals: the kind of limitation that would comply with core constitutional requirements beyond the *pro rata* principle. A limitation based on either the volume (Delpla and von Weizsäcker, 2010), the maturity (Hellwig and Philippon, 2011) or the date of issuance (Sachverständigenrat, 2011) certainly puts national parliaments in a position to better estimate the potential risk of entering into a joint and several liability arrangement. Yet, the fact that the financial risks for the national budgets can be quantified does not on its own result in a constitutionality of the Eurobond proposals containing a limitation. Besides the possibility to quantify the risk, the amount defined by the respective criteria for quantification may not undermine the budgetary autonomy. Given, for example, if the overall volume were limited by restricting common debt issuing to national debt amounting to 60 % of GDP (as proposed in the “blue bonds” proposal) for euro area Member States, that overall amount could still potentially equal around 6.000 billion Euro⁵⁶ in 2015. A comparison with the national budget of Germany, which amounted to 301.6 billion Euro in 2015, clearly shows that this limitation is unlikely to restrict the debt covered by joint and several liability in a way that would be considered not to harm the budgetary autonomy of the Member States.⁵⁷

⁵⁶ Based on the overall GDP of the euro area, which amounts to 10.4 trillion Euro in 2015, cf. Eurostat, GDP and main components.

⁵⁷ It is important to note that this comparison does not imply that a risk assessment has to be based on a “doom’s day” scenario where all participating Member States go bankrupt. The

Moreover, joint and several liability requires not only that a predefined share of national debt is included in the European scheme, but also that national parliaments are given the right to renew on a periodic basis the commitments of the national budgets. An example of such parliamentary involvement can be found in the “blue bond proposal”, according to which the annual decision on the allocation of the Eurobonds backed by a joint and several guarantee would be taken by the national parliaments of the participating Member States. According to this proposal, the refusal of a national parliament to adopt the necessary decision would result in the exclusion of the respective Member State from Eurobonds and hence, relieve it of all liability for the bonds. In this way, national parliaments would effectively decide annually on smaller portions of the guaranteed extranational debt. Yet, it may be argued that such a procedure may only delay the moment in time at which the threshold of harming the budgetary autonomy is reached by annually piling up extranational debt for which the national budget can be held liable. Moreover, from an economic point of view, the question is what the effects of the exit of a major euro area Member State from the liability regime would be on the marketability of European debt instruments and hence, on the conditions under which a European body could lend money to euro area Member States.

A different conclusion can, however, be reached with regard to the so-called “Eurobills” proposal, which only covers short-term mutualised debt of less than one year (Hellwig and Philippon, 2011). According to this scheme, Member States are only allowed to hold such short-term bonds to refinance debt up to 10 % of their GDP. This yields an overall risk of 1.000 billion Euro for the euro area. Since these short-term bonds have to be renewed at least once per year, the risk can be re-evaluated at regular intervals. The “Eurobills” proposal remains silent on the involvement of national parliaments, as it only mentions that the European body in charge (the so-called “joint debt management office”) would make quarterly issues of “Eurobills” covering the refinancing needs of the Member States. One could now imagine that, following the procedural requirements suggested in the “blue bond” proposal, national parliaments would approve the issuance of Eurobills either annually or even quarterly. Given the background of the core constitutional requirements for common debt issuance developed in Section 4.2.1, it may be concluded that the “Eurobills” proposal

assessment must rather be made on the basis of the likelihood of a payment in the event of a default of participating Member States and on the basis the ability of the guaranteeing Member State to refinance payments that are due in the event of such a default.

extended by a system of parliamentary approval can in principle be brought in line with national constitutional requirements.

Finally, as regards the introduction of a compensation scheme as a limiting factor, it has to be noted that such compensation is primarily required by EU law in order to meet the criteria set by Article 125(1) TFEU, rather than by core constitutional requirements. Compensation schemes aim at siphoning advantages for Member States that accrued on the basis of the better risk profile of commonly issued debt. These advantages could otherwise be considered as some sort of indirect financing of Member States whose national government bonds could only be sold at higher interest rates than commonly issued debt. From the perspective of national budgets, the “cost” linked to the interest rate advantage that is inherent to the idea of Eurobonds, is the differential between the interest rate paid by Member States to financial market operators when issuing Eurobonds as compared to the interest rate that they might have paid in case they had issued national bonds. In the event the differential amounts to an interest rate disadvantage, this cost is, however, presumably so little that it does not affect the budgetary autonomy and would therefore not conflict with core constitutional principles. Yet, such waiver of revenue for the national budget would most likely require approval by the national parliaments in order to pass the constitutionality check.

Finally, with regard to those models that require the fulfilment of certain economic policy goals in order to join and to remain in a system of common debt issuance, the role of the authority that negotiates and enforces strict conditionality in a recipient Member State could become the subject of constitutional challenges. The fact that – at least indirectly – the role of such an authority could become subject to constitutional review is highlighted specifically by the example of the several successful constitutional challenges in Portugal of budgetary laws *inter alia* aimed at implementing the economic adjustment programme agreed by the Portuguese government in the context of the financial assistance received under the EFSM/EFSSF.

In sum, mutualised debt secured by joint and several liability is difficult to align with core constitutional requirements. Only those schemes that limit the total amount of covered debt by predefined criteria could pass the constitutionality check, provided that the overall amount does not exceed the ability of a Member State’s national budget to assume the liabilities in the event of the most likely default scenario. As shown above, only the “Eurobills” proposal meets these criteria. Other than that, only schemes based on pro rata liability can be considered in line with core constitutional requirements. National parliaments must, in any event, retain the right to approve the common issuance of debt.

5 Concluding observations

To answer the somewhat rhetoric question included in the title of this contribution, it can be concluded from a political economy point of view that there is certainly still life in the idea of the introduction of a system of common debt issuing, even if this has to be perceived as a medium to long-term project, rather than a quick fix for current issues of the euro area. Indeed, common debt issuing can be more than a crisis instrument to compensate for the absence of autonomous monetary policy instruments and exchange rates. It could function as a structural instrument to strengthen economic policy coordination and sound budgetary policies in the euro area in a more sustainable way. Key to the success of any such system is the effective dealing with legacy debt.

Yet, the notable absence of any reference to Eurobonds or Stability Bonds in recent European policy documents signifies the current lack of political support, which may at least in the case of Germany also result from the clear language of the constitutional judges on the position of the budgetary autonomy of national parliaments at the core of what is effectively protected from constitutional amendment. In this regard, the German constitutional situation may somewhat distract from the fact that the introduction of such a system may not only face constitutional opposition in other Member States, but also requires a fundamental overhaul of primary Union law.

From the combined political economy and legal analysis, it becomes apparent that there are trade-offs between what is legally conceivable given the current state of European integration and what is desirable from a practical point of view to introduce an effective system of common debt issuing. Be that as it may, here it is argued that even with the reformed framework of economic policy coordination in place, the euro area is still in need of effective instruments to ensure budgetary discipline in the euro area in a credible way in the future. It remains questionable whether this can only be achieved by a large-scale transfer of fiscal policy competences to the supranational level.

References

- Antenbrink, F. 2012. "The European Court of Justice's Approach to Primacy and European Constitutionalism: Preserving the European Constitutional Order?," in H.-W. Micklitz and B. De Witte, eds. *The European Court of Justice and the Autonomy of the Member States*. Cambridge: Intersentia, 35–63.

- Amtenbrink, F. 2014. "New Economic Governance in the European Union: Another Constitutional Battleground?," in P. Purnhagen and P. Roth, eds. *Varieties of European Economic Law and Regulation*. Heidelberg: Springer, 207–234.
- Amtenbrink, F., and J. de Haan. 2006. "Reforming the Stability and Growth Pact," 31(3) *European Law Review* 402–413.
- Amtenbrink, F., J. de Haan, and O. Sleijpen. 1997. "Stability and Growth Pact: Placebo or Panacea?," 8(9/10) *European Business Law Review* 202–210, 233–238.
- Athanassiou, P. 2011. "Of Past Measures and Future Plans for Europe's Exit From the Sovereign Debt Crisis: What Is Legally Possible (and What Is Not)," 36 *European Law Review* 558–575.
- Boonstra, W.W. 2010. "The Creation of a Common European Bond Market," in Cahier Comte Boël, No. 14, ELEC, April 2010.
- Brunnermeier, M., L. Garicano, P. Lane, S. Nieuwerburgh, M. Pagano, R. Reis, T. Santos, and D. Vayanos. 2011. "European Safe Bonds: An Executive Summary," www.princeton.edu/~markus/misc/Europe/ESBies%20exec%20summary.pdf
- Buiter, W., and E. Rahbari. 2012. "The European Central Bank as Lender of Last Resort for Sovereigns in the Eurozone," 50(2) *Journal of Common Market Studies* 6–35.
- Buti, M., and N. Carnot. 2012. "The EMU Debt Crisis: Early Lessons and Reforms," 50(6) *Journal of Common Market Studies* 899–911.
- De Grauwe, P., and W. Moesen. 2009. "Gains for All: A Proposal for a Common Euro Bond," 44(3) *Intereconomics* 132–135.
- De Grauwe, P. 2011. "The Governance of a Fragile Eurozone," CEPS Working Document No. 346.
- De Grauwe, P., and Y. Ji. 2012. "Mispricing of Sovereign Risk and Macroeconomic Stability in the Eurozone," 50(2) *Journal of Common Market Studies* 866–880.
- de Haan, J., H. Berger, and D. Jansen. 2004. "Why Has the Stability and Growth Pact Failed?," 7(2) *International Finance* 235–260.
- de Haan, J., N.D. Gilbert, J.P.C. Hessel, and S.A.M. Verkaart. 2012. "Beyond the Fiscal Compact: How Well-Designed Eurobonds May Discipline Governments," 3 *Zeitschrift Für Staats- Und Europawissenschaften* 323–337.
- de Haan, J., N.D. Gilbert, J.P.C. Hessel, and S.A.M. Verkaart. 2013. "How to Enforce Fiscal Discipline in EMU: A Proposal," 149(2) *Swiss Journal of Economics and Statistics* 205–217.
- de Haan, J., J. Hessel, and N. Gilbert. 2016. "Reforming the Architecture of EMU: Ensuring Stability in Europe," in H. Badinger and V. Nitsch, eds. *Handbook of the Economics of European Integration*. New York: Routledge.
- de Haan, J., J. Hessel, and J.W. Van den End. 2014. "Are European Sovereign Bond Yields Fairly Priced? The Role of Modelling Uncertainty," 47 *Journal of International Money and Finance* 239–267.
- De la Dehesa, G. 2011. "Eurobonds: Concepts and Implications," European Parliament notes for the Monetary Dialogue of March 2011. www.europarl.europa.eu/RegData/etudes/note/join/2011/457357/IPOL-ECON_NT%282011%29457357_EN.pdf
- Delpla, J., and J. von Weizsäcker. 2010. "The Blue Bond Proposal," Bruegel Policy Brief 2010/03.
- Doluca, H., M. Hübner, D. Rumpf, and B. Weigert. 2012. "The European Redemption Pact: An Illustrative Guide," German Council of Economic Experts Working Paper 02/2012.
- European Commission. 2011. "Green Paper on the Feasibility of Introducing Stability Bonds," COM (2011) 818 final.
- European Commission. 2012. "A Blueprint for a Deep and Genuine Economic and Monetary Union," COM(2012) 777 final/2.

- European Parliament. 2011. "Resolution on the Feasibility of Introducing Stability Bonds," 2011/2959(RSP).
- Expert Group on Debt Redemption Fund and Eurobills. 2014. "Final Report," 31 March 2014.
- Favero, S., and A. Missale. 2012. "Sovereign Spreads in the Eurozone: Which Prospects for a Eurobond?," 70 *Economic Policy* 231–268.
- Geiss, M. 2012. "AEUV Artikel 352," in J. Schwarze, ed. *EU-Kommentar*. Baden-Baden: Nomos, 2585–2594.
- Gros, D. 2011. "Eurobonds: Wrong Solution for Legal, Political, and Economic Reasons," VOXEU, CEPR's Policy Portal, 24 August 2011.
- Gros, D. 2012. "On the Stability of Public Debt in a Monetary Union," 50(2) *Journal of Common Market Studies* 36–48.
- Hellwig, C., and T. Philippon. 2011. "Eurobills, not Eurobonds," VOXEU, CEPR's Policy Portal, December 2, 2011.
- Heun, W., and A. Thiele. 2012. "Verfassungs- Und Europarechtliche Zulässigkeit Von Eurobonds," 20(2012) *Juristenzeitung* 973–982.
- Jones, E. 2010. "A Eurobond Proposal to Promote Stability and Liquidity while Preventing Moral Hazard," ISPI Policy Brief, No 180, March 2010.
- Juncker, J.-C., and G. Tremonti. 2010. "Stability Bonds Would End the Crisis," *The Financial Times*, 5 December 2010.
- Juncker, J.-C., D. Tusk, J. Dijsselbloem, M. Draghi, and M. Schulz. 2015. "The Five President's Report: Completing Europe's Economic and Monetary Union," 22 June 2015, Brussels.
- Kämmerer, J.A. 2012. "Art. 123 AEUV," in H. Siekmann, ed. *EWU. Kommentar zur Europäischen Währungsunion*. Tübingen: Mohr Siebeck, 150–166.
- Mayordomo, S., J.I. Pena, and E.S. Schwartz. 2009. "Towards a Common European Monetary Union Risk Free Rate," NBER Working Paper Series No. 15353, Cambridge, MA, September 2009.
- Muellbauer J. 2011. "Resolving the Eurozone crisis: Time for Conditional Eurobonds." CEPR Policy Insight 59.
- Philippon, T. 2015. "The State of the Monetary Union," VOXEU, CEPR's Policy Portal, 31 August 2015.
- Potacs, M. 2012. "AEUV Artikel 136," in J. Schwarze, ed. *EU-Kommentar*. Baden-Baden: Nomos, 1580–1581.
- Sachverständigenrat (German Council of Economic Experts). 2011. "Assume Responsibility for Europe," Annual Report 2011/12.
- Smits, R. 2011. "Outline of the Legal Chapter on Eurobonds, Reply in the European Commission's Consultation on 'Stability Bonds'," http://renesmits.eu/files/8513/3097/8289/Outline_of_the_legal_chapter_on_Eurobonds_041111.pdf
- Suarez, J. 2011. "A Three-Pillar Solution to the Eurozone Crisis'," VOXEU, CEPR's Policy Portal, 15 August 2011.
- Van Rompuy, H. 2012. "Towards a Genuine Economic and Monetary Union," Brussels, 5 December 2012, www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/ec/134069.pdf