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**CONSULTATION ON**

**The Green Paper on the feasibility of introducing Stability Bonds**

By:

**The Class  
of  
'European Governance'  
2011/12  
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## 1. Introduction

The current Euro-crisis is the most severe crisis the European Union (EU) has faced since its inception. It has threatened to bankrupt member-states, jeopardises the livelihood of citizens and puts a bomb under the European Economic and Monetary Union. European leaders and institutions have struggled to find an answer to the problems.

As a transnational group of young students, we are very concerned about the developments of the past two years, the consequences of which will be felt throughout Europe for years. We are therefore happy that the Commission Green Paper on Stability Bonds has given us the opportunity to use our combined expertise and creativity to advise the Commission on the way forwards. We certainly hope our ideas contribute to finding a solid and sustainable solution to the Euro-crisis.

This advice was written by a group of 25 students of Utrecht School of Governance (USG), Utrecht University in the Netherlands. In the course we follow, we focus on European governance which makes the European Euro-crisis an interesting subject to us. The students in our class come from different European and non-European countries, and have different disciplinary backgrounds. However, we were able to overcome our different views on the crisis and possible solutions, and managed to agree on a coherent set of recommendations to the European Commission on their Green Paper on Stability Bonds.

To come up with a common response to the Green Paper on the feasibility of introducing Stability Bonds, we divided our consultation in several themes:

- Economic pros and cons of the three alternative plans.
- Political pros and cons of the three alternative plans.
- Implications for democratic deficit and accountability.
- New, bigger and better: Alternative solutions for the crisis.

Every theme was worked out by a part of our group. The Green Paper aims to provide and structure the political debate in the EU. We hope that with our recommendations we will contribute to this debate and ultimately to the solution of the crisis.

'European Governance' – Class of 2011/12  
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## **2. The Economic Dimension**

### **Introduction**

In this chapter, we examine the economic effects of the Stability Bonds proposal (European Commission, 2011). The proposal lists three different options, which could be named full, partial, and minimum integration of debt. We start by reviewing the effects the different options may have on the financial markets and to what extent they would be effective. Secondly, we evaluate the moral hazard involved in the three options. The third paragraph will argue that the Commissions stability-bond proposals as such are an insufficient answer to the complex problems Europe faces, and should be embedded in a range of other measures. We conclude with recommendations.

### **Financial markets**

The response of the financial markets has proven to be essential in finding an answer to the Euro-crisis. For the Stability Bond proposal to be successful, it needs to convince the markets and rating agencies of the credibility of European sovereign bonds. If the stability bonds succeed in doing so, this will result in low interest rates on the bonds and lower the borrowing-costs to those states that are currently perceived as risky. On the other hand, introducing Euro-bonds increases the volume of bonds. This makes it harder for individual market-players to affect the interest-rates on sovereign bonds, and dampen speculation.

The pooling of guarantees may, however, also result in a rise in the borrowing costs of the countries that are currently deemed highly reliable. This risk may be limited, since the overall risk will be decreased as all debts and guarantees are pooled together. However these effects may turn out to be larger than expected if the crisis is allowed to spur out of control even further. Even the countries that are perceived as the most financially healthy are currently under scrutiny of rating agencies (Thesing, 2011). Adding the responsibility of the debt of other European countries to their burden may worsen the situation.

In conclusion, we find it hard to see how the minimum option identified by the Commission could be economically effective. The effects of pooling the guarantees as well as increasing the volume of sovereign bonds to counter speculation are simply too small to have the desired effect. In addition, we feel that it is essential that the EU comes up with a timely decision on this and other measures to calm down the markets, for the full and partial options to be successful.

### **Moral hazard**

Historically, harmonising economic and fiscal policies has proven a difficult nut to crack for the EU member-states. The past decade has shown that even the institutionalisation of debt and deficit norms in the Treaty and Stability and Growth Pact has not been enough to convince political leaders to make sustainable changes in economic and fiscal policy-making. And even the outbreak of the crisis has not yet induced leaders to prevent unhealthy fiscal behaviour. The upside of the continuous unrest on the financial markets is that governments

throughout Europe feel additional pressure to improve their credibility and solvency.

If all the market pressure were to be released from individual countries – as would be the case if the full option of stability bonds was implemented – this additional push towards sustainable economic and fiscal policies would be lost (Economist, 2011). The full option of stability bonds may in fact support unhealthy fiscal behaviour since it lowers the cost of taking on more debt while shifting part of the burden to other countries. This problem of moral hazard creates the need for measures that limit the possibilities of taking on too much debt. Rather than rules, this is most likely to succeed if an arrangement can be made so that the interest of individual countries is aligned with the interests of the countries that share the burden. This way, interest in healthy economic policies are internalised instead of enforced externally, which would result in genuine commitment from states (Stone, 2003).

We feel these positive effects and internalisation of healthy policies would best be ensured by the partial option identified by the Commission. Limiting the use of Stability Bonds to the EMU limits would have the much-needed inbuilt incentive for governments to adopt healthy economic and financial policies.

### **Healthy Economic Policy**

In our view, other measures are required to raise the credibility of the Stability Bonds. In the end, financial discipline can never be the only or most salient (economic) value. What matters most is the health of the economy on which the financial state of the government depends (European Commission, 2011). Opponents of austerity-measures are right in saying that stringent fiscal policy does not solve the crisis. Moreover, financial sanctions on breaching the SGP-rules may actually worsen the economic downfall of states in trouble. This is not to say that there should be no rules on fiscal discipline, but they are only secondary to necessary reform measures.

The credibility of European debt eventually depends on the willingness of governments to commit to economic reform in general – including measures to improve labour-markets, pension-systems, housing-market and private debt- and detach from their commitments to the old and failing ways of the past. We are convinced that a healthy economy with only mild fiscal discipline is better than an unhealthy economy constrained by impossible fiscal demands. This means reform should be embraced during crisis situations, and the pain of the required fiscal discipline should be felt during good times. This is a politically difficult position and requires courage from our political leaders.

### **Conclusion and recommendation**

We have examined the economic aspects of the Stability Bonds proposal and concluded that effectiveness of this plan rests on how it effects the faith in European states in the eyes of the financial markets and rating agencies. The minimum option does not have this effect and is therefore not considered to be an improvement over the current situation. The risk of moral hazard tells us that full integration of debt and guarantees can only exist if all countries involved commit to reform and fiscal discipline. Given the wide divergence of views on this issue, it is not very likely that it will be the case in the near future. The Stability Bonds should therefore be only partial and leave a substantial fraction of the governmental

financing needs to be regulated by the pressure of the financial markets and the opinion of independent rating agencies.

### **3. The Political Dimension**

#### **Introduction**

In this chapter, we examine the political effects of the Stability Bonds proposal. In order to gain insight in the political feasibility of the Commission plans, we start with assessing the differences in the political procedures which implementing the three different options of the Stability Bonds would involve. Secondly, we rate the proposals in terms of the effects they have on the supranational versus intergovernmental nature of the EU. In the third paragraph, we evaluate the consequences of implementing the Stability Bond plans for the process of European integration. We conclude with recommendations on how to proceed in the upcoming political battle surrounding the Stability Bonds proposals.

#### **Political Procedure**

The full substitution of national issuance by Stability Bond issuance is the most far-reaching. It entails the largest transfer of sovereignty to the EU-level. At the same time, this is also the option that has the largest stabilizing effect on the markets, as well as the biggest positive effect regarding stability and integration of the European Union.

For this version of the Stability Bonds, it is very likely that treaties have to be changed. This has an effect on the actors involved as well as the time consumed in the process. A new treaty has to be drawn up that is acceptable to every member-state (or at least the EMU-17). Every country can potentially block the process, ratification may prove difficult thus adding to the difficulties and lengthiness of the process. To implement the new policies, the commission may act as a debt management office.

Implementing the option would involve many of the same political benefits and drawbacks and actors. Most importantly, it would also entail a treaty change. The difference with the first option lies predominantly in its economic effects.

Implementing the minimum option would entail very different political process. This option would not require a treaty change, as Stability Bonds are still being issued as part of financial needs, but not with joint guarantees. The fact that there are no treaty changes needed means this option can be implemented within a much shorter time-frame. Implementing this version of the EU bonds can follow standard EU procedure. This means the main actors involved would be the Commission, the Council of Ministers and the European Parliament. The Commission draws the final design on the new policy, followed ultimately by the approval or disapproval of the Council of Ministers and the European Parliament. This circumvents ratification-difficulties and to a certain extent blocking veto by member-states.

#### **Supranational versus sovereignty**

One of the biggest dilemmas the European Union has faced since its establishment is that between supranationality and sovereignty. On the one hand, EU member-states want to keep their sovereignty. On the other hand, in order for the EU to act effectively, it is necessary for

member-states to give up some of their sovereignty and hand over certain decision-making power to the European Union. The three stability bond options have a different effect on this dichotomy.

When it comes to the full substitution by Stability Bonds, the European Union would clearly choose the supranational approach. The creation of a single euro-area debt agency would mean the creation of a supranational organization that controls the joint bonds of the EMU members. This approach also entails a risk of freelancing. Member-states could benefit from other states' budgetary discipline. To prevent this there should also be a supranational organization that checks the budgetary discipline of the member-states. Inevitably, this leads to less budgetary sovereignty for the member-states.

The partial substitution is less rigorous in this respect. Its implementation would require EMU member-states to give up less of their sovereignty, as they still get to keep a part of their national issuance. Another aspect of this approach is that the amount of the joint bonds is to be negotiated by member-states and is not imposed by a supranational organization. Though this approach may have a less dramatic effect on the sovereignty of member-states, the joint risk this approach implies means that there must be budgetary discipline in order for this plan to work. Thus for the plan to be sustainable, member-states do have to transfer some of their budget sovereignty to the supranational level.

The minimum option identified in the Green Paper differs from the second approach in terms of the financial risks member-states face, since this approach does not include joint guarantees. This means that member-states have to give up less of their sovereignty, first of all because there is no supranational organization that controls the Stability Bonds, and second, because this approach implies less interdependence between member-states. Budgetary policy is left in the hands of the states and is not as stringently enforced by the supranational level as there is no need for a supranational organization that checks the budgets of the member-states.

### **Implications for the European integration process**

Implementing the Stability Bonds would also have consequences for the future of European integration. Would each of these options have a positive or a negative effect on integration and do we think it wise to further integrate Europe at this time?

The full substitution clearly promotes further economic European integration. It would increase feelings of responsibility and solidarity. Joint guarantee structures also enhance the political integration of the EU and act as an important symbol of the single European Currency and Union. This may help to rally political actors and citizens around the EMU and have a calming effect on the markets. The partial substitution may also entail these consequences, but to a lesser extent. It increases member-states responsibilities, but to a lesser extent and thus promotes less European integration in comparison to the first plan. The minimum option would not reap these benefits.

However, in the long-term risks could be involved in the pooling of guarantees and creation of a Euro-area debt agency. Euro-states do have to take their responsibility and the scenario may only play out if member-states' solidarity is genuine. In the full substitution (and to a lesser extent the partial) scenario higher rated countries will have to trust lower rated countries, as well as accept that those lower rated countries will gain more individual benefit from this plan. Only if all member states stick to the plan and make genuine efforts to prevent 'moral hazard' will occur, the first option for Stability Bonds can be a great enhancer



for European integration.

If problems do occur, the trustworthiness of countries that do not take their responsibilities will seriously jeopardize the willingness of others to take up pooled sovereignty in the future and decrease the market-credibility of the plans. Moreover, the legitimacy of the EU will decrease in the eyes of its citizens. All in all, this scenario may also turn out to be a real danger to the process of European integration.

We feel, that maybe the process of integration should be at a further stage before these bonds are introduced, and the legitimacy of the EU in the eyes of EU citizens should be increased ([www.spiegel.de](http://www.spiegel.de)). This may be accomplished by settling for the minimum and partial option. Maybe Angela Merkel is right and there is a need for further European integration before implementing these kinds of plans, maybe ‘taking it slow’ is the right thing to do. Maybe allowing member-states and EU citizens to get used to the idea of more ‘Europe’ could give them the confidence to be willing to integrate further in the future. While the partial and even the minimum option may thus have real political benefits for the future, these plans may not be far-reaching big enough to help resolve the financial problems Europe is dealing with.

### **Conclusion and Recommendation**

To sum up: While we think Stability Bonds could be an adequate solution for the current financial problems as well as a boost for European integration, there are some possible political drawbacks. Political actors are hesitant to give up their sovereignty and choose for a centralized decision making process. One of the main reasons for this is the many actors involved, each with different political agendas. Moreover, the two more rigorous versions of the stability bonds will involve a lengthy political process since they need treaty change. Again, this process is likely to prove difficult as all the member states have to approve the changes. Compromises have to be made to satisfy all member states thereby weakening the economic effects of the proposals. Overall, we think the option of partial substitution by stability bonds is the most politically feasible, it may not require treaty change and member states do not run the level of risk as they would with the full option. However, it remains the question if this option is enough to pull Europe out of its current crisis.

## 4. The Democratic Dimension

### Introduction

The democratic deficit of the European Union has been one of the most intensely discussed and analysed topics not only at national and European levels, but also at the international one. It constitutes a subject upon which the institutions of the European Union have keenly concentrated their attention, and in this way becoming a major focus of strategies such as the one outlined by the White Paper on European Governance (2001).

Enforcing the new Stability Bonds plan would entail the transfer of an even larger amount of sovereignty from individual member states to the European Union institutions, especially when it comes to the issue of fiscal regulations, a matter considered one of the cornerstone attributes of national sovereignty. The image of an Economic and Monetary Union driven by economists and finance ministers who are not directly elected by the citizens of member states, in other words a European Union led by technocrats, bureaucrats, and the newly vehicled term “eurocrats”<sup>1</sup> will deepen even more, precisely within the framework of a not so well consolidated integration of economic and budgetary policies. Therefore, the issuance of Stability Bonds is conceivable only in an economic environment with appropriate regulatory supervision as well as effective enforcement mechanisms.

Given a sovereign state and its own currency, citizens are willing to accept directing their tax money towards the poorest areas of the country. A sign of mature democracy is that mostly in times of crisis, citizens are prone to show economic solidarity that manifests by an ability to sacrifice their own interest for the collective good. Turning now to the European Union, its financial crisis is fundamentally political. There is no single European currency of all the 27 member states, and even where it exists (the Euro zone), there is no “European people”, there are no solidary citizens with a sense of belonging to it. The reaction of the “European demos” to the Stability Bonds plan as a solution to the financial crisis should be a lesson for each of us. But the dissolution of the European Union is not an answer to the current economic problems; instead, the alternative is to strengthen the EU, be it by pooling the debt and by increasing the supervision of economic rules’ enforcement or other means. Even though such mechanisms are not easy to create and even though popular support for them is not easy to gather, the democratic deficit is possible to be reduced, if taken the necessary and appropriate measures. “Democracy may seem like a mad dream in a community of 27 nation-states, and perhaps it is. But unless one is prepared to give up on building a more united Europe, it is surely worth considering.”<sup>2</sup>.

### Legitimacy

One of the most important questions in determining the level of democracy of EU policy is the question of accountability: who is responsible for the decision taken and who is going to render account for those decisions; in other words, how to make sure that EU-decisions are legitimate and therefore accepted by European civilians. The transfer of a large amount of

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1<http://www.businessandfinance.ie/bf/2011/12/commanalyde2011/politicsofdemocracyanddeficits>

2<http://www.mmegi.bw/index.php?sid=2&aid=557&dir=2011/December/Friday9>

national sovereignty that we mentioned before creates a challenge in terms of legitimacy and accountability. After all, the question is: if national governments and parliaments are not the ones responsible for the decisions made, then who is? And how does the answer to this question impact the democratic deficit as a whole?

It is thus quite clear that the introduction of Stability Bonds really accelerates European fiscal, economic and monetary integration. Since European integration is subject to many debates and discussions throughout Europe, we find it striking that words such as accountability, legitimacy and democratic deficit were not mentioned once in the whole Green Paper. To us, it is impossible to implement the stability bonds plan without presenting some proposals on the legitimacy of decisions, a possible new debt management office (DMO) or another possible new supranational institution that might be needed in the future.

For now, we consider all three alternatives of the stability bonds for the theme of legitimacy and accountability. It turns out that each version entails in one way or another the form of some coordinative agency for the whole euro-zone. This new single euro-zone debt agency needs to have a very solid democratic basis. It might be possible to make members of this agency directly elected by the European citizens. To us, there is a strong need for this agency at least to be linked to the European Parliament. It could be that in some way the parliament has a certain amount of control over the decisions made by this agency. We consider it is never appropriate that a new agency takes decisions without at least the possibility for control by a directly elected institution, like the European Parliament. Since fiscal policy is one of the most important policy instruments for national governments, it is still very important that European citizens have a certain degree of influence over this issue. In general, we think it is impossible to implement the stability bonds plan without this.

Since this represents a big change in European financial and fiscal politics and it really makes the euro-zone far more integrated than it was before, European civilians must have the possibility to define their positions on this theme. The change the new plan entails is far too big for the decision to be made too fast, especially because this is a decision that cannot be undone afterwards.

### **Participation**

If the European Commission's plan to install stability bonds for the European financial market were to be accepted by the member states of the European Union, this would mean a big step in the history of the European Union. Of course, it still depends on which of the three options is going to be chosen, but without a doubt it has an important impact on further European integration of the financial market. Not only does it have implications for the financial market in Europe, but it has an impact on all the European citizens as well. The problem here is that for most citizens within the European Union, EU decision making seems terribly far away. It is widely known that there is little sense of belonging to the European Union and most citizens within the EU don't feel connected to the European Union and their fellow Europeans from other member states. This seems to be conflicting for further social and financial integration. With this being said, it is mandatory to be look at options for possible civilian participation in the process.

Stability bonds seem to be a fairly complicated matter for the average citizen who isn't familiar with the ins and outs of the financial market. One major issue with the first approach to stability bonds is the moral hazard that member states could effectively free

ride on the discipline of other member states, without any implications for their financing costs. Especially for citizens of the 'stronger' countries it may feel like they are paying for the mistakes made in the 'weaker' countries. One way to cope with this might be to install a civilian panel that can advise, debate and consult on the matter. This panel can be a way to let the 'average citizen' participate in the process and lets them have a voice, which can also help to close the democratic deficit that is said to be present in the European Union. To set up a panel where all the citizens from the 27 countries interact with each other's own interests can be quite a challenge, but it is possible to find appropriate mechanisms in this respect (see section 5).

Another way for civilians to participate in the process is to enable civilians to invest in Stability Bonds. For instance, if every member state had an organization coordinated by the Commission that invests in Stability Bonds, through which civilians can directly buy them, it could increase the sense of belonging to Europe and other Europeans. Because when people from all member states invest in the European bonds, they will more and more have similar interests, which is a positive sign for greater and more solid connection (see section 5).

Undoubtedly, there are many other options for possible civilian participation in the process, and we feel that resources should be invested in finding a satisfactory solution related to this aspect

### **Conveying the story & public awareness**

The Green Paper on the feasibility of introducing Stability Bonds aims to structure the political debate in the EU on the rationale, pre-conditions and possible options of financing public debt through Stability Bonds. It is the objective to launch a broad public consultation on the concept of Stability Bonds. As this concept is a technical matter, containing different options of implementing an issuance of sovereign bonds, the political debate on this subject is not open for everyone. People are not always interested in the politics of the EU, especially when they do not understand the implications European policy has on their own situation. On top of that, people do not always have the capacity to understand detailed technical information on a certain subject. But many of the implications of Stability Bonds go well beyond the technical domain and involve issues related to national sovereignty and the process of economic and political integration, which have major implications for the accountability and legitimacy of the EU and national governments.

Before raising public awareness and inviting people to participate in the decision making process on Stability Bonds, the EU must first provide its citizens a proper insight to the essence of this new plan, and explain to its citizens what a common issuance of sovereign bonds would mean. What are the advantages and disadvantages of a further economic and political integration? And what does the EU want to achieve, except for stability?

As said before: given a sovereign state and its own currency, citizens are willing to accept directing their tax money towards the poorest areas of the country. This suggests citizens are willing to sacrifice their own interest for the collective good, as long as they know in what plan they are participating.

The European Commission should initiate a real political debate amongst the people of Europe on its plans. Explain their thoughts in every-day language that people can understand. We feel it is very well possible to explain complex, technical measures in common language (we recommend the Commission to look at the short films of Explainty

Explains on You Tube [http://youtu.be/ttuXQWV\\_dtQ](http://youtu.be/ttuXQWV_dtQ) for some excellent examples of this). We would like to make the next four suggestions for communicating with the people of Europe to the Commission:

- focus on the essence of a new plan, and not on the possible methods of implementation of it; When people do understand the essence of a plan, public awareness is likely to be achieved.
- mention national and individual advantages and disadvantages;
- tell a clear story in which the common European (not national) goals are described;
- accept that not everyone is interested nor wants to participate.

### **Conclusion and Recommendation**

Even though the so called “democratic deficit” of the European Union has been subject to numerous academic debates and discussions, the concept has been given various meanings, depending on the different definitions of democracy that exist. In general, the notion of democratic deficit is referred to as the lack of accountability of the institutions of the European Union, and the relatively weak position of the European Parliament as the only directly elected body (Bache, George & Bulmer, 2011). In order for the new stability bonds plan to work and have the desired effect, this chapter highlighted the necessity and the importance of finding the appropriate mechanisms of rendering account and of ensuring democratic control between not only the EU’s institutions, but also between the whole institutional system of the union.

Moreover, special attention should be given to attempts of determining ways of getting European citizens involved in this new process, or at least of providing them the right information, so that their attitudes towards this plan are based on solid arguments and justifications. In addition, it should be taken into consideration the fact that explanations so complex as the ones encountered in the Green Paper will never reach the “average” European citizen, therefore clear and accurate facts, implications and effects have to be presented. After all, there is no perfect solution to the financial crisis the euro zone is dealing with; it is a matter of trade-off between advantages and disadvantages, it is a matter of how much we are willing to give in and how far we are inclined to go in order to accept or reject a proposed solution. We feel the European Commission should take up the challenge to really communicate with the European people.

## **5. Beyond stability bonds**

### **Introduction**

In the previous sections, we considered the consequences of introducing Stability Bonds as a possible solution to the Euro-crisis from an economic, political and democratic view. As the Green Paper aims to provide and structure the political debate in the EU, we would like to contribute to this debate by supplying the Commission with some innovative and creative alternatives measures that may help solve the Euro-crisis. It is this section in particular, in which we dare the European Commission and political and financial leaders of the EU member-states to think 'out-of-the-box', and go beyond the present plans for Stability Bonds.

Since what we feel is most striking in the Green Paper is the lack of concern for the effects of stability bonds on accountability, legitimacy and democratic deficit, many of our alternatives focus on this topic. We start carefully, by giving a little twist to the existing plans in Green Paper, and propose the introduction of stability bonds 2.0. A plan proven to be successful. In the second paragraph, we call on our leaders to think out of the box, take account of the latest scientific evidence on successful governance, and place citizens at the heart of EU decision-making. Finally, we want draw attention to common knowledge time and again supported in political and psychological studies: Even the fiercest punishment does not beat temptation when it comes to guiding people's behaviour. We therefore advise the institutions of the EU to go beyond posing sanction, and reward best practices. Again, we conclude this section with recommendations.

### **Stability bonds 2.0**

The first idea that we have coined is to invoke the European citizens in the Stability Bonds. In our eyes, the Belgium call of the former prime minister Yves Leterme for the Belgian citizens to buy Belgian bonds has set a good example. Leterme asked the Belgian population to support their country by buying Belgian bonds. The call from Leterme was a great success ('De Redactie', December 2, 2011), with the result that the Belgian government raised almost 5 billion Euro through this action. Now the Belgian inhabitants and investors are the proud owners of a piece of their country/government, and have a direct involvement and interest in sound budgetary policy-making.

Like Belgium, the European Union could all upon EU citizens to invest in Stability Bonds. In addition, to the financial benefits for the European states, this measure has great political and symbolic value. It shows public faith in, and support for the EU, contributes to building a European demos and increases the feeling that 'we, the people' are the European Union. This means that austerity-measures that used to have difficulty gaining public support, become directly and financially beneficial to citizens making them less difficult to implement. And finally, Stability bonds 2.0 will provide a good answer to the populist Eurosceptic politicians and restore the faith of the international markets in the European project.

### **The People in the heart of EU policy-making**

Another alternative to make the European Union stronger is by increasing the European awareness, and increase their sense of belonging to Europe. To add a feeling of European identity to peoples' national identity. citizenship. Given the rise of Euro-skepticism in these times of crisis, this is a much needed precondition to the Stability Bond plan. When you increase the feeling of being a European citizen, the European citizens will be committed to help (re-)build the European Union and will develop more interest and concern for the European Union.

A way to achieve increased public awareness fort, and identification with Europe is to have citizens attend meetings at various stages and levels of the decision making process. Recent scientific findings based on animal behavior shows that the quality of decision-output increases when citizens without political experience are present during meetings (Couzin et al, 2011, see also: <http://icouzin.princeton.edu/media-attention-around-our-last-science-article>). This idea could be implemented by using the organizational example of the system of calling upon citizens to take on jury-duty in Anglo-Saxon countries. Citizens could be invited to attend meetings by the European Commission, Parliament, Expert and even Working Groups on subjects that they have an interest in and contribute to the discussion.

This has the benefit of involving European citizens more in the decision making process of the European Union, increasing awareness of the EU, and makes decision-making more transparent. All in all, it will bring the people back into the heart of the EU, and ultimately that is what EU governance should be: for and by the people. In addition, the above-mentioned studies indicates that it will also increase of the quality of the decision-output

### **Beyond Sanctions**

In addition to the alternatives mentioned prior to the Stability Bonds proposal, another alternative can be mentioned; the use of a different inducement system. In April 2011, the European Parliament approved legislation which allowed heavier sanctions to be issued to the member states of the European Union who will not sufficiently comply to the rules of the Economic Monetary Union. The heavier sanctions are supposed to solve the core issues of the economic crisis, namely the economic instability of the European economy and the debt crisis.

This system relies on a utilitarian assumption of human behavior. The targets of governmental action, in this case the member-states, are assumed to behave rationally. Acts and decisions are made according to conscious goal seeking and follow an economic calculus. To provide punishment for a undesired action (running extensive governmental debt) is expected to alter the behavior of the member-states, and induce them to choose the desired action (stringent budgetary policy).

However, time and time again economic, psychological and political studies have shown the utilitarian assumption of human behavior to be flawed (Kahneman 2002; Stone 2002). We feel the EU should practice evidence-based policy-making and take into account the consequences of these academic findings.

As is shown in these studies and amply illustrated during the Euro-crisis, markets, politicians and citizens act on the basis of emotion. Which actions are taken depend on how a message is conveyed, on one's sense of belonging; and the social and emotional as well as the

financial benefits of the act. Moreover, studies show that people respond better to a sign saying that 80% of one's peer abide by the rules (for instance throwing litter in the recycling-bin) are far more effective than a sign summing up the sanction to a rule (100 Euro fine on littering). The European Commission should use this knowledge to their advantage.

Rather than sanctioning states that do not follow the rules, rewards should be given to the ones that perform well. This may include financial rewards (a temporary discount on the member-state contribution, a bonus-subsidy for a nice economic or innovative project), however we also feel that -given the 'human' nature of humans- rewards should come in non-financial guises: why not appoint the best performing EMU-state as the next in line to preside the Eurogroup. Estland will do a fine job, and the Estonians will feel so proud to be President of their EURO.

Apart from being more effective than measures based on faulty assumptions of human behavior, we feel that going beyond sanctions will contribute to building a European demos. In addition, implementing these positive, stimulating measure will contribute to the overall image of the European Union as a positive, rewarding and stimulating force in the mind of the people, politicians and markets.

### **Conclusion and Recommendation**

In sum, we dare the European Commission to think out of the box and go beyond all current plans to solve the Euro-crisis. Call upon the people of Europe to invest in their continent and take a stake in their government finances, take account of the scientific evidence on successful governance and experiment with plans to put people back in the heart of Europe and to go beyond the negativity of sanctions. This will not only increase the effectiveness and efficiency of EU policy-making, it has the potential to build a genuine European demos, increase public awareness and support, and contribute to solving the Euro-crisis.



## 6. Overall Conclusion and Recommendations

In our recommendation, we have examined the economic political and democratic aspects of the Stability Bonds proposal, and searched beyond the measures currently being considered to solve the crisis. We come to the overall recommendations:

With regards to the stability bond proposals we conclude that both from an economic and political angle, the option of partial substitution by stability bonds is both the most feasible and beneficial. This option will have the desired calming effect on the financial markets, limits the risk for moral hazard, may be feasible without full treaty change and evens out the financial risks for member-states. In addition, it has the potential to induce further European integration at a pace acceptable to European politicians and the people.

However, we do feel it is very unfortunate that the Green Paper does not address the democratic and accountability aspects of the stability bond proposal. In order for the new stability bonds plan to work and have the desired effect, mechanisms of rendering account and of ensuring democratic control should be established and implemented alongside the stability bonds. Special attention should be given to attempts of determining ways of getting European citizens involved in the decision-making and to providing them with adequate information, so that their attitudes towards this plan are based on solid arguments and justifications. In their communication with the European people the Commission should:

- *focus on the essence of a new plan, and not on the possible methods of implementation of it; When people do understand the essence of a plan, public awareness is likely to be achieved.*
- *mention national and individual advantages and disadvantages;*
- *tell a clear story in which the common European (not national) goals are described;*
- *accept that not everyone is interested nor wants to participate.*

Finally, we want to dare the European Commission to think out of the box and go beyond its stability bond plan and come up with more innovative ways to solve the Euro-crisis. We want to make three concrete suggestions, all of which based on previous successful experience or ample academic study:

- *call upon the people of Europe to invest in Euro-bonds*
- *involve the people in EU decision-making*
- *reward good behaviour of Europe and to go beyond the negativity of sanctions.*

This will not only increase the effectiveness and efficiency of EU policy-making, it has the potential to build a genuine European demos, increase public awareness and support, and provide a proper solution to the Euro-crisis.

We hope our recommendations are useful to the Commission and will contribute to finding an adequate, timely and sustainable solution to the Euro-crisis.

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