

# **Europe: Looking for a New Model**

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# EUROPE: LOOKING FOR A NEW MODEL \*

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## ABSTRACT

More than fifty years after the Schuman Declaration, Europe is still far from a real Political Union. Europe faces an important imbalance between the two sides of the integration process, appearing as an important actor in the international economic scenario, but as a minor actor in the international political arena.

In this paper, we start by arguing that the “small steps” strategy that led the European Union (EU) until the present situation is no longer sufficient to let the Union efficiently overcome its present deficits and challenges. So, we call for an important change in the institutional and economic organisation of the EU, towards a model of largely decentralised federalism.

Examining the present challenges for the EU and the characteristics of the Draft Constitution/Constitutional Treaty for Europe, and comparing the main existent federal systems, we argue that the new “Constitution” is not enough to give the EU a strong voice both in the political and the economic areas.

In this context, we discuss the design of an adequate institutional framework for the political organisation of the EU, presenting an alternative proposal based on the characteristics of a truly federal system, also as its consequences in what concerns the design and implementation of European economic policies.

**KEYWORDS:** European Union, Political Union, Federalism, Fiscal Federalism, European Constitution

**JEL-CLASSIFICATION:** F02, F15, H77

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*“In its present shape, the EU is more than a mere alliance of Nation-States. But it is also far from being a fully developed political system with a democratically legitimised government of its own. The Union has remained at this halfway house between confederacy and federation much longer than both the optimistic and the pessimist theorists of European Integration would have thought possible in the 1950’s and early 1960’s. However [...] new factors seem to increase the pressure towards political integration. As a result, Europe will have to deal with increasing tensions between the urgency of effective central regulation and the equally compelling need to respect the cultural diversity and institutional autonomy of its nations and regions.”*

*(Fritz Scharpf)*

## **1. CHALLENGES AND DEFICITS: WHY DOES EUROPE NEED A NEW MODEL?**

Many analyses recently made on the situation of the European process of integration converge on the idea that the EU is at crossroads, facing the emergence of a relevant set of fundamental challenges: the need to consolidate the important results of the economic integration process<sup>1</sup>; the need to have an effective answer to the questions posed by the increasing globalisation<sup>2</sup>; the need to promote employment and competitiveness; the need to efficiently deal with the problems urged by the enlargement to 25 countries; the need to implement a real common external policy; or the need to promote the participation of the citizens in the process of integration, thus increasing its democratic legitimacy.

In this context, it becomes possible to recognize the existence of three fundamental “deficits” in the EU. First, a deficit of competitiveness and growth, as it is clear that the objective of turning Europe as the most competitive area in global terms until the end of this decade (Lisbon Strategy) is far from the possibility of being achieved. In fact, Europe has been facing a long period of poor economic growth<sup>3</sup>, with important consequences in social terms, which must be overruled in the near future so to avoid putting in danger some achieved results.

Secondly, there seems to be a deficit of political weight. The poor capacity of common intervention in the resolution of serious international problems (even when they were occurring in the European territory), together with the inexistence of a unique international

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<sup>1</sup> This process has been successful until our days, as Europe almost reached the top of economic integration, with a single currency and coordination of other macroeconomic policies. However, some important problems remained, such as the way to make this coordination more effective, the questions related to fiscal harmonisation or the problems concerning the sustainability of social security. For a brief review of these questions, see Alves (2001).

<sup>2</sup> On the consequences and problems derived from the increase globalisation see, for instance, Sassen (1998) and for a more radical view Guéhenno (1995).

<sup>3</sup> In some countries, even periods of economic recession...

representative of the EU, shows clearly the maintenance of a Europe that has relevant economic power but fails to have a truly political soul. This situation lies on the inexistence of a truly Political Union and a “single voice” in the international arena and effectively constrains the weight and the options of Europe in the World, a situation whose importance has increased with the war on Iraq<sup>4</sup> (and more generally, with the war on terrorism) and the division faced by the Member-States.

Finally, there seems to be a deficit of participation, legitimacy and democracy. It is related to the lack of adequate scrutiny of the Commission and the Council, the reduced importance of the Parliament (even if its powers have been lately reinforced) and the ambiguity that still marks the assignment of competences between Member-States and the Union and also marks the transfer of competences from Member-States to the Union<sup>5</sup>. These elements may be counted as the main reason why citizens have an inadequate perception of how the Union is functioning and how responsibilities are committed to each actor. The consequences of this situation may be found in the growing indifference of the citizens towards integration in Europe.

## **2. DEFICITS AND PROPOSALS: GOING FOR A FEDERAL MODEL?**

These three deficits are the reflex of a disquieting idea: six decades after the Second World War and even after several important steps achieved in the course of the process of integration, it has not yet been possible to build an area of real European solidarity and a true feeling of being European (i.e., of being part of a supranational community). In fact, nationalisms still have large weight in decisions and that means that the actual model of functioning of the EU (based in the “small steps” strategy, together with a recent intergovernmental deviation) is impotent to effectively face the new challenges and inefficient at the moment when EU needs to become not only an important economic voice but also a relevant political voice in the international arena.

In our opinion, the first step to find how EU might be able to overcome the important imbalance between the economic and the political side of integration (and so to deal with the above mentioned deficits) would be a credible analysis around a new and adequate model for EU, with consequences in its political and economic organisation.

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<sup>4</sup> Note, for instance, that during the war in Iraq (March to May 2003) there were no common decisions about this subject, just like it was not the main international problem...

<sup>5</sup> Cf. Alesina and Perotti (2004). On legitimacy and democracy see also Scharpf (1999).

The choice of this model would be based in the analysis of the capacity that each possible alternative shows facing two essential binomials. On one side, the binomial “unity / diversity”, corresponding to the need of creating efficient conditions to a unique intervention in areas that are clearly supranational, without threatening the preservation of European diversity. On other side, the binomial “flexibility / commitment”, corresponding to the need of creating capacity on Europe to accommodate in a easy way some relevant changes that may occur in the future (in terms of enlargement or in terms of deepening), without threatening the preservation of some common important values (namely those that really distinguish the European project).

Applying these criteria of analysis to a vast set of alternative models<sup>6</sup> that have been proposed for the EU (Europe *à la carte*, multi-speed Europe, European Directory, Europe with variable geometry, Europe with flexible integration, European Federation, etc.), we would conclude that only these last two models would be able to permit the achievement of the main goals of Europe. The other ones would suggest the disintegration of the European project or at least mean a change towards a situation where there is no equality amongst Members (which is contrary to the original guidelines of the project).

Adding to this conclusion the clear advantage of federalism upon flexible integration in what concerns the true formation of a political entity, the respect that the principles of federalism<sup>7</sup> assure to national autonomy, the success that the implementation of federal models have shown in developed countries and/or in countries with a high level of cultural, ethnic or linguistic diversity, and the presence of a federalist idea in the genesis of the European Communities<sup>8 9</sup>, it becomes clear why we opt for a federal model, regarding it as the necessary change in the institutional and economic organisation of the EU.

### **3. COMMON FEATURES OF THE PRINCIPAL EXISTING FEDERATIONS**

As a first step to design and describe a possible federal model for Europe, we take a brief look at how the main principles of federalism have been implemented in some of the main existing federations. Considering the cases of the United States, Germany and Switzerland, a first

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<sup>6</sup> For a brief description of the main features of these models, see Dewatripont *et al.* (1995).

<sup>7</sup> Autonomy; subsidiarity; participation; cooperation; guarantee. For a general description, see Héraud (1995).

<sup>8</sup> For a history of the federalist idea in Europe, see Sidjansky (2000).

<sup>9</sup> In 1950, Schuman, one of the “founding fathers” of the EU project, considered the creation of the Economic Community of Coal and Steel as the first concrete step towards a European Federation, which would be “indispensable to the preservation of peace” (Schuman, 1963).

important conclusion is that there is no such thing as a “one and only” model of federalism. For instance, the United States correspond to an illustration of a system where the separation of powers is perfectly defined, with “*each power being independent, superior and inferior to the others, by an organised set of checks and balances*” (Schmitt, 1999). On the other side, Germany shows a system where the Member-States (Lander) reveal vigorously their existence and autonomy, leading to “*a strange combination of decentralisation of autonomous bureaucracies with substantive harmonisation of policies and highly developed procedural uniformity*” (Lehmbruch, 1996).

However, a comparative analysis of the features of the main existing federations also reveals some common characteristics systematically present in implemented models of federal organisation. Among them, we should stress the following ones, as they would also constitute the main features of a true federal model in Europe:

- The existence of a Constitution, that defines the principal goals of the Federation and the relations between the different levels of power; the Constitution may assume different degrees of complexity, mainly because of historical and cultural reasons<sup>10</sup>;
- The existence of a clear assignment of competences and powers to the Federation and the Member-States: in the United States, there is an explicit enumeration of the competences assigned to the federal power; in Germany, there also is an explicit enumeration of those areas of exclusive competence of the Federation, together with the enumeration of the areas of concurrent competence; in Switzerland, an important portion of the constitutional text is concerned with the division of competences, explicitly defining the areas of exclusive competence of the “Confederation” and the areas where it can also intervene;
- The existence of a clear separation of powers at the federal level: this is particularly clear in the case of the United States, with a major part of the constitutional text devoted to this question; the principle is also observed in Germany, but the President is indirectly elected and their competences are truly limited; also in Switzerland this principle is implemented, but there is a clear preponderance of the Parliament (“Assemblée Générale”) and the President is not really visible, as the Federal Council is a collegial entity;
- The existence of a bicameral legislative power, with a Chamber that represents the “interest of the population” and another one that represents the “interest of the constituting

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<sup>10</sup> Compare, for example, the simplicity of the Constitution of the United States with the complexity of the Swiss Constitution.

entities”<sup>11</sup>. In the majority of the existing Federations, directly elected members compose the first one, the composition being determined by some proportional relation with the number of inhabitants of each Member. The second chamber is composed by an equal (or almost equal) number of members representing each constituent.

- The existence of a Supreme Court, together with the supremacy of the federal law;
- The existence of a guarantee of fundamental rights (civil, political, economic, juridical and even social rights): the first chapter of German and Swiss Constitutions is concerned with this matter; in the United States, their guarantee appeared later, on the *Bill of Rights*;
- The consecration (and observance) in the constitutional text of all the principles of federalism.
- The existence of a significant federal budget, which represents an important part of the GDP of the Federation, meaning that there are “sufficient” proper resources to implement federal policies and to use them for stabilisation and redistribution programs.

#### **4. THE DRAFT CONSTITUTION FOR EUROPE: WHY IS IT NOT ENOUGH?**

Having in mind the need to overcome the challenges and deficits mentioned on section 1, the evolution towards a federal model proposed on section 2 and the main common features of the political organisation in existing federations presented on section 3, now we turn to the analysis of the capacity of the proposed Draft Constitution to effectively put Europe in a more developed and solid trend.

Let us start by a brief recall of the genesis and the original goals of this document. In December 15, 2001, the European Council in Laeken adopted a declaration on the future of the EU, assuming the compromise of becoming more democratic, effective and transparent. The simplification of the instruments of the Union and the definition of a clear assignment of competences among the Union, its institutions and the Member-States, were two of its main goals. An original Convention was called to play a principal role, the designing of a “Constitution” for Europe.

Although in the first months, the work of the Convention seemed to lead the final result toward something very close to a federal model, the later intervention of some countries resulted in a solution that stays clearly beyond that.

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<sup>11</sup> The Chamber of Representatives and the Senate in the United States; the Bundestag and the Bundesrat in Germany; the National Council and the States Council in Swiss.

To evaluate this result, at the light of what we concluded on section 2, it is important to point what seem to be the most important changes proposed by the Draft Constitution<sup>12</sup>:

- It gives EU juridical personality (art. 6);
- It promotes an assignment of competences between the Union and the Member-States, defining areas of exclusive competence of the Union (art. 12), areas of shared competence (art. 13) and areas of support from the Union (art. 16), together with the reinforcement of the principle of subsidiarity (art. 9 and Protocol on the application of the principles of subsidiarity and proportionality);
- It integrates the Chart of Fundamental Rights as a “constitutional” text (Part II);
- It reinforces the importance of the coordination of economic policies (art. 14) and calls for a real Common External and Defence Policy (CEDP), eventually leading to a common defence (art. 15);
- It creates an area of European freedom, security and justice (Part III, chapter IV);
- It defines the procedures related to a possible abandon of the Union (art. 59);
- It does not change the principles of the institutional framework of the EU (art. 18°), although it creates the figure of the President of the Council (art. 21 - elected by its pairs and responsible for the coordination the work of the institution and for the external representation of the Union – in some cases...) and the figure of the European Foreign Affairs Minister (art. 27 - first responsible for proposals and the execution of the CEDP); it also calls for a reduced number of effective commissioners, giving all the countries the right to have one commissioner but not necessarily with executive functions (art. 25)<sup>13</sup>;
- It increases the number of areas where decision is taken by qualified majority and changes the pattern of this majority, introducing a more efficient criterion than that of the Nice Treaty (art. 24)<sup>14</sup>.

Some of these points represent a positive evolution regarding the capacity of EU to deal with the new challenges. However, in our opinion, in some important areas the advances are still not enough. Our main criticisms, which also become the principal arguments for proposing an alternative view, are:

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<sup>12</sup> Please note that the articles refer to the Draft Constitution. However, almost all the changes and the lacunas that we refer in the text also apply for the approved Constitutional Treaty.

<sup>13</sup> The Constitutional Treaty asks for a reduction of 1/3 in the number of Commissioners by 2014.

<sup>14</sup> In fact, the approved criterion has become not so transparent and efficient as the one included in the Draft Constitution. However it remains more transparent and efficient than that of the Nice Treaty.

- The excessive length of the proposal<sup>15</sup>: if one main objective was to make the communitarian “law” more accessible and transparent to citizens, it has certainly failed!
- Also the length of the Chart of FR is clearly excessive: it seems that one has envisaged to put in the text all possible rights, the ones with clear dignity to be part of a constitutional text together with the others;
- Although there is an assignment of competences, it is not absolutely clear and transparent, as competences are not as explicitly listed as in German or Swiss Constitutions, leaving space for misunderstandings and juridical problems (even with the clear statement in favour of subsidiarity);
- Moreover: the exclusive competences assigned to the “centre” do not include several aspects that we would classify as clear supranational, such as external policy or fiscal harmonisation; also, these matters will still be decided by unanimity; this means that Europe will still feel a lack of political international power; i.e., there will not be an effective solution for the imbalance between political and economic sides of integration;
- At the central level, still there is not a clear and transparent separation of powers (nor a provision of two Parliamentary Chambers). Even with its competences reinforced the European Parliament would still being a minor part in the process. The way the model is designed, there is a high probability of continuing the recent intergovernmental deviation, eventually leading to an unacceptable “directory” of the big countries; the provision of a President of the European Council and the uneven distribution of votes in this institution are two of the key elements that leave the Draft model far from an envisaged model of federation and they may drive EU away from its original idea of equality among Nations<sup>16</sup>;
- At the economic level, the text does not introduce significant changes, leaving behind the problem of increasing financial resources, with the consequence of maintaining a very short central budget, and the problem of coordination of economic policies, as it only reinforces the idea that it is an important thing to be done, but does not change the complex, bureaucratic and few credible process already established in Maastricht.

The most positive aspects of the Draft Constitution seem to be those that take the EU closer to a real federal model. As the same time, its major lacunas correspond to those features where it

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<sup>15</sup> A simple comparison between the Draft Constitution and the Constitution of Germany, Swiss and, in particular, the United States is, at this level, highly suggestive.

<sup>16</sup> Cf. Devuyt (2004), on the intentions of the Member-States when negotiating the Constitutional Treaty.

fails the way towards a Federation. As we above argued, progress on transparency, efficiency on decision-making and accountability of responsibilities are not entirely achieved with the proposed model<sup>17</sup>, keeping some of the major reasons for the so-called “democratic deficit”.

As a result, the Draft Constitution may be considered as a positive step, but also as an insufficient step to take the citizens closer to the integration process, turning off the “democratic deficit”, and to give EU a political dimension compatible with its statute of economic potency. I.e., there is a real need to go further and find a more credible and efficient alternative.

## **5. AN ALTERNATIVE PROPOSAL**

One such alternative would lie on the creation of a truly European Federation. The first step for it would be the existence of a truly constitutional text, expressing a clear supremacy of the federal law<sup>18</sup>, together with the definition of the main goals of the Union, the defence of the fundamental human rights and the clear assignment of competences among the various spheres of power.

Taking account that the situation of the EU is particularly different from those of the “success cases” earlier mentioned, and that it becomes almost impossible in Europe (and even not desired) to change the pattern of the existence of Nation-States with relevant roles<sup>19</sup>, the federal European model would assume an original form<sup>20</sup>, perhaps in line with the idea of a “Federation of Nation-States”<sup>21</sup>.

This model would observe several main features. First of all, a relevant degree of autonomy for the constituting entities, together with a significant degree of decentralisation in the assignment of competences, as these conditions stand for the maintenance of a reasonable relevance of the traditional Nation-States, the proximity of the decisions to the citizens and the reinforcement of democracy in the European project.

The model would also promote an equal treatment of Member-States and their citizens, the respect for the European fundamental values (including, in particular social values), the

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<sup>17</sup> Cf. Baykal (2004).

<sup>18</sup> This is not clear in the Draft Constitution and in the debate related with it, as there still some discussion on if the document is a truly Constitution or just another Treaty, this time a Constitutional Treaty.

<sup>19</sup> Cf. Fischer (2000).

<sup>20</sup> This originality would not be a surprise, as the European integration process has been evolving with original steps and as there is no general and universal model of federation.

<sup>21</sup> Please note that several politicians use(d) this concept, which was proposed some years ago, not always referring to the same model.

development of a real European citizenship (leading to the creation of a truly “conscience of being European”) and the creation of new financial resources for the Federation (generating a real federal European budget).

We believe that a model of this kind would represent a necessary solution for maintaining efficiency in an enlarged EU, an essential solution for preserving unity in fundamental questions, together with the respect of national, regional and local diversity, and a crucial step for further development of the European ideal. In this context, the following items present a brief discussion of some relevant issues concerning a possible European federal model.

### **5.1. Political and institutional organisation**

The new model will have to be consecrated by a real Constitution that defines the EU as a “Federation of Nation-States”, whose main goals are political and economic stability, peace, prosperity, security, justice and the defence of liberty and human rights. Underlining these aspects, this Constitution should stress, in its initial chapters, the importance of human rights as well as the respect for political, economic and social values that clearly distinguish the European tradition from the American tradition.

The preamble and the initial chapters of this Constitution should also stress two other elements, because of their symbolism and/or their practical consequences. First, it should be underlined that the creation of a European Federation responds to the will of an increased union without threatening an enlarged autonomy of national entities and their sovereignty: a formula like “*the people of Europe and respective Countries (...) establish the following Constitution (...)*”, similar to the one included in the Swiss Constitution, would be a good sign. Secondly, the consecration of the principles of federalism should be clear, in particular those concerning the autonomy of the constituents, the subsidiarity in public intervention, and the juridical guarantee.

In what concerns the assignment of competences and taking account the desire of a large decentralisation, only the questions that are clearly supranational should become exclusive reserve of the federal institutions. Among them, we would count the external policy of the Union (including commercial policy), the issues concerning internal security and preservation of the single market (including the questions on fiscal harmonisation), the monetary policy and the definition and use of the federal (enlarged) budget.

In other areas, the intervention of central power would be possible but subsidiary, taking place when the matter seemed relevant for common interest or when there were no doubts about positive results from a central intervention (like in the conception and financing European networks of communication and telecommunication). Finally, in some matters, federal power would be able to launch indicative or binding goals, conditioning the actuation of Member-States. In any case, federal powers should leave an ample margin of manoeuvre for Member-States.

Following the examples earlier mentioned, the assignment of competences would include the explicit consecration of the federal exclusive competences and the areas of concurrent competences, leaving all the other competences to national (and regional and local) entities, as the only way to create a largely decentralised federation.

Finally, in what concerns the institutional organisation, there should be some kind of “revolution”, comparing to the present situation. It should observe clearly the principle of separation of powers, the features being closer to the German or the Swiss model than to the American one, mainly in what relates to the executive power.

Legislative power would be totally assumed by the parliamentary institution, here named as “Federal Assembly” and having two Chambers, so following the example of the main existing Federations. The first Chamber would be named European Parliament and result from the direct transformation of this present institution. As it happens today, directly elected deputies, according to electoral circumscriptions defined by the Member-States, would compose it. Allowing for more efficiency, the number of deputies would have to be reduced comparing to the actual Parliament. Each country would be assigned with a number of deputies proportional to its population. However, to avoid the hypothesis of some small countries have no deputies, there would be fixed a minimum number of deputies.

The second Chamber, here named as “European Senate”, would be composed by an equal number of representatives of each Member-State<sup>22</sup>. Half of them would be directly elected by national Parliaments and the other half would be designated by national governments. This figure would allow each Member State to be represented on the legislative process, as well as an increased participation of the national parliaments, resulting on an evolution of the actual European Council.

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<sup>22</sup> The equality in the representation of each Member State better corresponds to the ideal that inspired the process of European integration since its beginning.

The “European Government”, composed by a President and a number of ministers, would assume executive power, and would command the federal administration. This government would result from an evolution of the existing European Commission and its President would be elected by the Parliament, starting with a proposal approved by the Senate. The other Ministers would be chosen by the President, all team being later approved by the Parliament, institution that would have the competence to vote motions of rejection. This way of nomination of the European Government would somehow preserve the actual form, but goes further on conferring homogeneity to the all team and responsibility to the Parliament<sup>23</sup>.

The President would have the responsibility of coordinating all the action of the government and would be the representative of the European Union in the exterior, this way solving one of the most important present problems of the common external policy.

The competence to initiate any legislative process would be assigned to each of the Chambers and to the Government. Federal laws (and other juridical instruments) would have to be approved by the two Chambers. If one proposal would be approved by the Parliament and rejected by the Senate, it would be possible to re-approve it on the first Chamber if voted by a majority equal to those that defeated the proposal in the Senate. This German-like solution would better defend the European interest. Qualified majority or simple majority, depending on the issues, would be the rule for decision. Referendum would be allowed but its use would be restrained to some questions of very high European relevance<sup>24</sup>.

Finally, juridical power would be organised in a German-kind way, following the European tradition. It would comprise the European Constitutional Court, federal courts included in the Constitution and national courts. The European Constitutional Court would be the result of an evolution of the existing European Court of Justice and it would represent the supreme guarantee of the juridical system, interpret the Constitution and decide upon divergences between different jurisdictions.

## **5.2. Consequences on the economic organisation**

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<sup>23</sup><sup>23</sup> As an alternative, it would be possible to consider a direct election of the President by all Europeans. Even if this solution would probably lead to an increase interest of the citizens in European matters, it would have a major inconvenient, as it would confer the elected President an enormous political power, giving rise to potential important conflicts with the legislative institution. So, a German-kind solution appears to be preferred, the “President” corresponding to the figure of the “Chancellor”.

<sup>24</sup> We do not defend the assignment to the referendum regime of a degree of importance similar to the one it has in Switzerland.

If a change in political organisation towards a federal structure occurs, it would also call for some significant changes in the way that economy is organised. In particular, the definition and the execution of all kind of public policies would also suffer important transformations, as they would have to adequate to the “rules” of federalism, in this case of “fiscal federalism”<sup>25</sup>.

In the area of “economic federalism” we find a large number of consensual points, even if some polemical ones subsist<sup>26</sup>. In particular, we observe that the main conclusions of the “fiscal federalism” theory<sup>27</sup> would be largely compatible with the political ideal of a largely decentralised Federation composed by the “former” Nation-States and with the need of creating a “European economic government” responsible for the competences assigned at this level to the Federation.

Decentralisation would also be the principle to be followed in what relates to the supply of public goods. As Oates (1972) suggested in a general case, also in Europe only general and supranational public goods would be supplied at a central level. The defence constitutes the typical example, but some other areas would benefit from some degree of centralisation, including the fields of transports, communications, environmental protection and technological research.

The redistribution policies would be an area of shared competences among different jurisdictions. The objectives related to an increased harmonisation of income among countries and regions would be achieved by a combination of coordination of policies and inter-regional compensatory transfers.

The European budget would have an important increase, as the only way to give the federal government enough capacity to deal with macroeconomic stabilisation and also to effectively intervene in other fields. Own financial resources should be increased and that could be achieved by an adequate tax assignment and distribution of revenues among the multi-levels of government<sup>28</sup>.

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<sup>25</sup> As Oates (1999) notes, the meaning of “federalism” in Economics is not exactly the same as its meaning in Political Science. In this area, as observed, it refers to a political system grounded on a Constitution that allows for some degree of autonomy and power to all levels of political jurisdiction. In the area of Economics, we note that the public sectors are always “more or less” federal, in the sense that there are different levels of government supplying public services and performing some power of decision *de facto*. The subject of “fiscal federalism” is therefore the set of questions concerning the vertical structure of the public sector, i.e., concerning the intervention of the State itself in the economy at all different levels.

<sup>26</sup> Cf. Oates (2001).

<sup>27</sup> Development of this subject might be found in Oates (1999) or Spahn (1994).

<sup>28</sup> The creation of a new European-based tax would be considered as an alternative, in the short run.

The criteria for tax assignment proposed by Musgrave (1983) would be largely applicable, even if they have been recently subject to some criticism, particularly taking account of the empirical experience in some federations. The European government would be responsible for progressive taxation (because of the perverse effects of excessive migration), for taxes with high mobile bases of calculus (because of possible effects of distorting decisions of where to locate activities, the taxes on capital income being a good example) and for taxes whose bases are asymmetrically distributed among regions and countries (because of possible increase in geographical inequality). National and local governments would be responsible for other kind of taxes.

Let us turn again to the question of macroeconomic stabilisation. In the long run, the existence of a strong federal budget would be important for achieving this goal, as it happens in most of the existing federations. In the short run, however, as it appears politically difficult to have a European budget with the adequate dimension, an increase in the efficiency to deal with macroeconomic stabilisation requires an important reinforcement of the process of coordination of economic policies (eventually with the creation of a new supranational entity, the “economic government”).

The creation of a limited central shock-absorber mechanism<sup>29</sup>, activated in the case of asymmetrical shocks, and a profound revision of the (moribund) Stability and Growth Pact, excluding the effects of economic conjuncture and some public investment expenditures and taking account of the differences in initial situations of the Member-States<sup>30</sup>, are aspects that should be implemented in the very short run, even independently of a possible evolution towards a federal model.

## **6. CONCLUDING REMARKS**

In this paper, we have argued that the “small steps” followed by the EU until the present, together with some kind of intergovernmental deviation in the last years, is not an adequate strategy/model to let the Union efficiently overcome its present deficits and challenges. So, we called for an important change in the institutional and economic organisation of the EU, towards a model of largely decentralised federalism.

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<sup>29</sup> Some years ago, Italianer and Pisani-Ferry (1994) presented an interesting example (1994) and some developments have followed that original work.

<sup>30</sup> The discussion around the Stability and Growth Pact has increased in the last months/years, particularly due to the negative economic conjuncture and the difficulties shown by several countries to perform its rules. For an interesting discussion of pro and contra arguments, see for instance Buti *et al.* (2003) - please note that these authors largely defend the rules of the Pact. For an interesting alternative, see for instance Creel (2003).

We also argued that the changes promoted by the Draft Constitution (and by some later consensual decisions) are not enough to lead to an adequate equilibrium of the political and economic sides of the integration process and to give the EU a strong voice both in the political and the economic areas.

Staying far from a federal model, the model proposed by the Draft Constitution fails in some important areas, mainly in what concerns the possibility of having a truly unique external policy, the existence of a common budget of relevant dimension, the clarification of competences between the centre and the Member-States and also between central institutions, the consecration of a truly equality in the treatment of all Member-States and the incentive for participation of the European citizens in the process of integration.

In this context and taking account of the successful experiences of Germany, Switzerland and the United States in what concerns the design of a Federation, we tried to present an alternative proposal for the political, institutional and economic organisation of the EU. We believe that this proposal, founded on the concept of a “Federation of Nation-States”, would better allow for an efficient answer to the present challenges of the EU.

Such a “radical” change leading to a federal system would necessarily have to be legitimated by a European referendum that should take place in each one of the Member-States. The change would be effective only if approved by at least 2/3 of the voters and 2/3 of the States.

Also note that the success of such a model would largely depend on the achievement of creating a truly European citizenship. In the past, the existence of a feeling of “belongings” to a supranational community has shown as one of the key issues on the success of federal models (United States, Germany, Switzerland, etc.), as well as its non existence has led to the disintegration of other supranational entities<sup>31</sup> (Soviet Union, Yugoslavia, etc.).

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<sup>31</sup> About the ex-USSR, see, for instance, Kux (1996).

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