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Relaunching the EU

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About the CER

The Centre for European Reform is a think-tank devoted to making the European Union work better and strengthening its role in the world. The CER is pro-European but not uncritical.

We regard European integration as largely beneficial but recognise that in many respects the Union does not work well. We also think that the EU should take on more responsibilities globally, on issues ranging from climate change to security. The CER aims to promote an open, outward-looking and effective European Union.

Dedication

This report is dedicated to the memory of our dear friends and colleagues Clara Marina O'Donnell (1983 – 2014), Philip Whyte (1966 – 2015) and Stephen Tindale (1963 – 2017).

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Summary

The time is ripe for EU reform. The Union has weathered the worst of its multiple crises – on the eurozone, migration and refugees, and Brexit – while economic growth has picked up. Emmanuel Macron has emerged as a strong leader alongside a re-elected Angela Merkel. Now is the time to revamp the EU so that it improves its economic performance, provides more security and tackles some of the issues that matter to citizens. This report looks first at the need for new policies, and then at the EU's structures and institutions.

We examine the interlinked challenges of the neighbourhood policy, migrant flows, the Schengen border and internal security. We suggest how the EU could play a more effective role in tackling the root causes of migration, handling the refugees who arrive in Europe and thwarting terrorists. For example, the EU should work more closely with the source countries of migrants, offering bigger incentives for them to hold on to and take back their people. It should lay the groundwork for setting up reception centres outside the EU where legitimate claims for asylum can be processed, and it will need a workable scheme for distributing those granted the right to enter. The EU should also join up its main security databases so that it can better police its asylum system and keep track of potential terrorists and other criminals.

We then turn to eurozone governance. Despite the eurozone's improving performance, problems persist, such as high levels of debt and unemployment in some countries, and divergent economic performance. The answer need not be the large-scale centralisation of economic decision-making in EU or eurozone institutions. But important incremental changes are needed, such as strengthening the banking union; amending the European Central Bank's mandate; and building a framework to ensure stable growth of aggregate demand in the eurozone as a whole. The EU should leave most economic policies to member-states, except when their consequences adversely affect others in the currency union, as is the case for Germany's current account surplus and the non-performing loans of Italy's banks.

We argue that the EU would have a greater appeal to citizens, especially the young, if it became more involved in several specific areas:

★ Ensuring that EU member-states respect the rule of law;

★ Combating the corruption that plagues some member-states;

★ Establishing rules to prevent large multinational firms avoiding tax;

★ Making it easier for workers to move around within the EU; and

★ Encouraging investment in renewables and the green economy.

The report then looks at the future shape of the EU. There are competing visions: Jean-Claude Juncker wants to see every member take part in every policy, while Emmanuel Macron has suggested several tiers of membership. Given the differing preferences and objectives of the 27, Macron's more flexible model is more viable in the long term. It would also enable the EU to revive the stalled enlargement process, by offering 'membership minus' to suitable countries. As for the neighbourhood policy, which has so far failed to create a 'ring of friends' around the EU, Brussels needs to increase its offer – for example by asking some neighbours to join particular policies. Britain could one day envisage rejoining the outer tiers of a more differentiated EU.

The EU cannot feasibly undertake a major revision of its treaties in the foreseeable future. But it should be able to fix the euro's problems with new inter-governmental treaties, just for eurozone members. As for the EU's institutions, the European Commission has lost the trust of some governments because of the perception that it is increasingly dependent on the European Parliament. It should return to an equidistant position between the Council of Ministers and the Parliament. National parliaments should play a greater role in EU governance. It is time to transcend the traditional battle between *communautaire* and inter-governmental thinking. The EU cannot succeed without both federal institutions and a major role for governments; they must work together.

Introduction

People often talk about the need to reform the EU, and lament the slow pace at which it changes. However, the prospects for reform over the next few years are particularly propitious. On the one hand, many European leaders recognise that the EU has never faced greater challenges. It needs to make itself more attractive to voters, improve its economic performance and modernise its institutions. On the other hand, the chances of achieving change are better than usual: France has elected the EU-enthusiastic Emmanuel Macron as president; Germany has re-elected the experienced and authoritative Angela Merkel; and both Brexit and Trump have created feelings of solidarity and strength of purpose among key EU leaders. Europe's leaders are making big and bold speeches proposing radical change.[1] This report examines both the policies and the institutional reforms that could help to relaunch the EU.

As the Union's leaders contemplate its renewal, they will be aware of its many achievements, on which they can build. The EU is one of the most successful peace projects in human history – it is virtually inconceivable that its members would resort to war against each other. NATO has played an essential role in defending Europe against external enemies, but the EU has been decisive in reconciling France and Germany and in curbing other long-standing animosities between European countries. For example, in recent years Germany and Poland have had strained relations, as have both Slovakia and Romania with Hungary, but these countries would not contemplate resolving disputes by force.

The enlargement of the EU from the original six members to the current 28 (soon to be 27) has helped to spread not only a zone of peace and security across the continent, but also prosperity. The EU's single market and regional aid programmes have helped to raise living standards across much of the Union, in particular in its poorer regions. The EU has also set an example to the rest of the world by opening its markets and importing more than any comparable trading bloc or country; its trade-weighted average tariff is lower than that of almost all other major economies. Together with its member-states, the EU provides

1: See for example Emmanuel Macron's speeches in Athens on September 7th 2017 and at the Sorbonne in Paris on September 26th, and European Commission President Jean-Claude Juncker's State of the Union speech in Brussels on September 13th 2017.

more development aid than any other country or grouping. The EU has helped to make Europe a single space for sciences and the arts, for example by supporting scientific research, musical and cultural projects, and exchange programmes between universities. These are positive achievements that deserve to be acknowledged.

And yet EU leaders know that their club suffers from serious problems of image and substance. Many voters assume that the EU does very little to help them deal with the issues that matter in their daily lives. In particular, the EU does not appear to counter the economic insecurity and the feeling of a loss of control that worries people. Nor does it seem to contribute to citizens' physical security: the EU finds it hard to stem the flows of immigrants from other continents, provide reassurance that the Schengen zone's external border is strong, or prevent terrorists from moving freely around inside that area. The EU's institutions sometimes seem remote and ineffective.

Underlying this malaise is the concern that the liberal, democratic values that most European leaders (and EU institutions) hold dear are in retreat. Externally, the Union is surrounded by powers that are more-or-less hostile to the EU and what it stands for – Trump's America, Putin's Russia and Erdoğan's Turkey. These leaders' disdain for openness and their authoritarian instincts chime with the anti-liberal movements that are strong in several parts of the EU. As Ivan Krastev has written:

> "A passing glance at China, India and Russia, not to speak of the vast reaches of the Muslim world, makes clear that both ethnic nationalism and religion remain major driving forces in global politics. Europe's post-modernism, post-nationalism and secularism make it different from the rest of the world, not a harbinger of what necessarily awaits it. What is also visible in the context of the refugee crisis is that national loyalties, once considered dead and buried, are back – with a vengeance – in contemporary Europe. In recent years, Europeans have come to realise that although the EU's political model is admirable, it is unlikely to become universal or even spread to its immediate neighbours."[2]

As the EU enters its seventh decade, a number of difficult issues threaten to weaken it or even tear it apart.

★ Brexit is not a one-off problem, but the symptom of a wider

2: Ivan Krastev, 'After Europe', University of Pennsylvania Press, 2017.

disorder: in many countries, large numbers of people want to kick the establishments and elites which profit from and support economic and social openness and diversity. Since the UK referendum, anti-EU nativists have suffered reverses in the Netherlands and France, but they are currently polling well in Italy and may soon join the Austrian government. Right-wing populists with a eurosceptic bent are in power in Poland and Hungary. In countries such as France, Germany and Austria, only the bravest politicians are willing to argue the case for free trade, such is the hostility of many voters. The departure of the UK removes an influential voice in favour of extending the European single market and free trade. The negotiation of Brexit may end up creating bad blood among European leaders and divert them from tackling other pressing challenges. Moreover, Brexit is damaging the EU's global standing. The remaining 27 members will find it harder to formulate credible foreign and defence policies without Britain's global outlook (rivalled only by that of France); and to implement them without the UK's diplomatic, development and defence capabilities. Meanwhile the crisis in Catalonia – exacerbated by both secessionists acting illegally and Madrid's ham-fisted response – threatens to draw in the EU.

★ The massive inflows of refugees and irregular migrants originate partly in the failures of EU foreign, defence and development policy, especially in the Middle East and North Africa. The migration crisis, like the euro crisis, stems from the EU starting work on an ambitious new project but leaving it half-built. The creation of the Schengen area of borderless travel was desirable – but the mistake was to leave its external border weak and under-policed, and to neglect the drivers of migration in the EU's neighbourhood. Not enough was done to pool and co-ordinate the member-states' capacities to deal with refugees, organised crime and terrorism. When the inflows of economic migrants and asylum-seekers surged in 2015, the EU and its member-states struggled to cope. There were few proper systems in place for registering, checking and caring for asylum-seekers; sending back those not granted asylum; exchanging information on potential security risks; distributing asylum-seekers within the EU; or integrating those granted asylum into European societies. The result has been human misery, appalling public relations for the EU, and widespread (though largely unfounded) fears, fanned by nativist politicians, that the EU is 'importing Islamist terrorists'. The refugee crisis has also set government against government. A few countries, such as Greece, Italy, Germany and Sweden, have ended up hosting far more than their fair share of refugees and economic migrants. The refusal of some Central European states to take any asylum-seekers from Greece or Italy has damaged their relationships with Germany and the Brussels institutions. The flow of immigrants into Italy has boosted support for Italian populists.

★ Nearly eight years after the euro crisis began, the single currency's problems have not been fixed. The pick-up in eurozone economic growth in 2016 and 2017, and the victory of the europhile Macron in France, are encouraging. However, the next recession will test the currency union's half-built institutional structures. This is because debt levels remain high, the political and legal constraints on a relaxation of fiscal policy are powerful and the European Central Bank's (ECB's) monetary policy is near the limits of what it can achieve. Italy, which suffers from high levels of public debt, a troubled banking system and a political class that struggles to overcome the vested interests opposed to reform, is a particular worry. There are several possible reforms to eurozone governance that could put the currency union on a more stable footing – such as building a banking union with more risk-sharing and a bigger backstop to support banks in difficulty; the write-off or mutualisation of excessive public debt; or a focus on eurozone demand management, so that countries with big current account surpluses do more to stimulate growth at home and abroad. But Germany and other fiscally hawkish countries seem determined to block such schemes.

★ Outside the eurozone, there is further cause for concern. In Poland and Hungary, populist governments have taken steps towards politicising the courts, while there are questions about media diversity. The EU has failed to find a viable mechanism for making the countries concerned change their behaviour. Externally, Russia's armed forces are fighting in Ukraine and carrying out exercises close to the EU's frontier. Moscow has also interfered in the political systems of France and Germany and is well-placed to sow discord among the member-states. Russian and Turkish influence in the Balkans has grown, as the EU's has waned. The EU has struggled to cope with an increasingly authoritarian, illiberal Turkey – with which it needs to co-operate on immigration, terrorism, the Middle East and much else. The EU's neighbourhood policy has failed to convert its eastern and southern neighbours into a 'ring of friends'; several of them are in turmoil. Meanwhile the unpredictable presidency of Donald Trump – and his questionable commitment to European security, free trade and democratic values – worries many European leaders.

The first part of this report looks at some of the policies that could help to make the EU more robust. It first considers how European leaders can best tackle immediate problems, such as the neighbourhood, migrant flows and the eurozone. It then considers how the EU might become more involved in certain policy areas, to inspire support among citizens, and in particular young people. So it examines, in turn, the EU's role in promoting human rights, combating corruption, fighting corporate tax avoidance, encouraging labour mobility and boosting the green economy. The second part of the report looks at a new architecture for the EU. It argues for the Union to develop more flexible structures, so that its countries are given greater choice over which policies they take part in. Finally, the paper looks at what treaty changes are required, and what reforms the EU institutions may need.

Part one: New policies

Migration and security

The neighbourhood and migration

A lot of European citizens are reluctant to see EU institutions play a bigger role in their lives. Yet several of the biggest problems confronting Europe – such as those affecting the neighbourhood, migration and the euro – cannot be solved without the member-states working together and allowing the EU to play a greater role.

The EU faces serious challenges in dealing with the boatloads of people travelling from North Africa towards the EU – almost 95,000 landed in Italy from Libya in the first eight months of 2017, though the numbers dropped in the late summer and early autumn. The possible resumption of flows from Turkey into Greece is another worry (those flows halted because Turkey and the EU reached an agreement in March 2016, and because several Balkan and EU countries closed their borders in the months preceding that deal). The wars in Afghanistan, Iraq and Syria, plus poverty in South Asia and sub-Saharan Africa, have driven hundreds of thousands of people towards the EU; no end to those conflicts or the other drivers of migration is yet in sight.

But migration is not the only problem in the EU's neighbourhood – indeed, it is often a symptom of other problems. The EU has struggled to create stability beyond its borders. In the eastern neighbourhood, two of the six countries in the EU's Eastern Partnership, Azerbaijan and Belarus, are autocracies, while most of the six suffer serious problems of corruption. Though the EU has signed association agreements with Georgia, Moldova and Ukraine, implementation will take time and is unlikely to transform their prospects in the way that EU membership did for Central Europe.

In the southern neighbourhood the situation is even worse. The 'Arab Spring' of 2011 brought hopes of change in a region that had long suffered from authoritarian regimes and under-development. Instead, Libya and Syria have become failed states; Egypt has reverted to military rule and mass repression; and other countries have made limited if any progress. Only Tunisia has managed to establish a fragile democracy, though it is threatened by Islamist extremism. Large numbers of refugees and economic migrants have travelled to Libya from sub-Saharan Africa because of conflict, repression or the lack of opportunities at home. The chaos in Libya has enabled gangs of smugglers to send boatloads of people towards Europe.

The EU needs to prioritise the development of a new neighbourhood policy, as a way of reducing both security threats and migration pressures. Invented in 2003 by then Commission President Romano Prodi, the European neighbourhood policy was supposed to create what he termed a 'ring of friends' around the EU. But it has largely failed, in three ways:

★ The EU has not offered big enough incentives – in terms of trade, aid, freer movement and stronger political ties – to motivate the countries concerned to make the economic and political changes that would enable them to move closer to the EU. With some partial exceptions (such as Georgia, Ukraine and Tunisia), many of the neighbours have turned away from the EU rather than become its friends. One erstwhile star performer of the neighbourhood policy, Moldova, has recently shifted towards Moscow, in part because of gross corruption by its 'pro-European' elite.

★ The EU has not invested enough, militarily or diplomatically, in preventing state failure or seeking solutions to conflicts close to its borders, particularly in the south. The EU has largely left other actors (or sometimes no-one at all) to try to manage the Syrian war, even when it has created security threats within Europe, for example through returning jihadis. And in Libya, where France and the UK bear some responsibility for destabilising the country, the EU has again left it to the UN to try to sort out the mess, while Egypt and Russia have partially filled the power vacuum by backing the most successful warlord.

★ The EU has done too little to connect its policies for tackling instability in the neighbourhood (and in the neighbours of the neighbours) with its efforts to handle the migration crisis. Its attempts to stop migration at the external borders of the EU have often failed; but it has done too little to prevent migrants reaching those borders, and to address the drivers of migration in the countries of origin and transit.

A new neighbourhood policy should include a new approach to enlargement, which has ground to a halt. The last country to join was

Croatia in 2013 and the next one – Serbia or Montenegro? – will be lucky to join by 2025. This slow-down reflects the fact that many voters within the EU do not want to see new countries joining the club. One consequence is that Brussels' influence in the Balkans and Eastern Europe has waned.

For both the neighbourhood policy and enlargement, the EU needs to develop new forms of association that offer less than membership but much more than current policies – in terms of economic integration, aid and political ties. The idea of a 'privileged partnership', which Angela Merkel floated a dozen years ago in the context of Turkey, should be revisited. Some voters in EU countries would be less hostile to enlargement if the candidates concerned did not join some policies – for example free movement.

If the EU revived the process of enlargement, with a variety of possible outcomes (some of which would fall short of full membership); and if countries such as Morocco or Ukraine became eligible for partial membership, Brussels' influence in the neighbourhood would grow. The EU's soft power would benefit from its being seen to spread its values geographically. In the Balkans and Eastern Europe this would help to counter rising Russian and Turkish influence. Macron has made exactly this point: "If we can accept the challenges of enlargement, it is because the EU's stronger foundation will allow greater forms of differentiation."[3]

There is no politically acceptable way to eliminate the problem of people travelling over land and sea from poor countries towards the EU. But such flows can be reduced and managed. The EU needs to come up with stronger and more effective policies not only for its neighbourhood but also for its borders and its Schengen system. It has started to take some of the right steps. It has rapidly built up a European Border and Coast Guard, which is assisting the member-states. And it is seeking to negotiate 'migration partnerships' with Ethiopia, Mali, Niger, Nigeria and Senegal. In return for aid, the countries concerned are asked to constrain emigration and to take back economic migrants. There have already been some positive results, notably in Niger, though it will be many years before these partnerships make a big difference.

One of the difficulties is that some of these countries benefit enormously from the remittances sent by workers inside the EU; in

3: Emmanuel Macron, Sorbonne speech, September 26th 2017.

Nigeria, EU aid amounts to about a tenth of the value of remittances. The EU does not yet have readmission agreements with Nigeria, Ivory Coast or Guinea, all big sources of irregular migrants. It will have to increase the incentives it offers – in terms of both aid and legal routes for skilled workers into the EU – in order to win their co-operation.[4]

There may be occasions when the EU needs to deploy military power in its neighbourhood, for example to keep the peace in Libya, after any deal that brings the civil war there to an end. Current moves to increase EU countries' defence spending, and to strengthen the Common Security and Defence Policy, are welcome. So is the Commission plan for an EU defence fund, which would, if member-states agree, provide €1.5 billion a year from 2020, to be spent on developing new military technologies and equipment. The EU also hopes to activate the 'permanent structured co-operation' (PESCO) provisions of the Lisbon treaty by the end of this year. PESCO could allow an *avant-garde* group to move ahead in certain military areas.

Given Britain's departure from the club, Germany needs to spend more on defence, build its military capabilities and develop the strategic culture that would enable it to use them. France cannot lead European defence on its own. Nor should it remain the only large EU country that is willing and able to undertake combat missions that benefit the security of the EU as a whole – as it has done in the Sahel region. Given the quality of Britain's armed forces – and its desire to remain closely engaged in this area – the 27 should look for ways of associating the British closely with EU defence structures, and enabling them to take part in EU operations.[5]

4: Luigi Scazzieri and John Springford, 'Can the EU make deals with third countries to curb migration?', CER policy brief, October 2017.

5: UK government, 'Foreign policy, defence and development: a future partnership paper', September 2017.

Internal security

The EU needs to join together its internal and external security policy. At home, it should focus on strengthening borders, catching criminals and terrorists, and processing migrants who have entered the EU, including the identification and resettlement of those with a legitimate claim to asylum. Despite significant progress over the past couple of years, the EU does not yet perform these tasks very well.

One way to cut the horrific number of deaths and disrupt the business model of the people smugglers, at least partially, would be to offer genuine asylum-seekers more legal ways of entering, without their having to embark on a dangerous maritime trip (although economic migrants with sufficient funds would still turn to smugglers). The EU should seriously consider establishing reception centres in countries of transit or origin, for example in Morocco, Libya (if and when it is peaceful), Mali or Niger. The EU would have to make this financially advantageous for the country concerned. Teaming up with the UNHCR and the International Organisation for Migration, the EU should work closely with the host government to ensure decent standards in the reception centres, and to prevent the people inside them creating security problems. This is particularly important in the case of Morocco, which though a significant source of jihadists has a government keen to reap the rewards of co-operating with the EU.

If the EU succeeds in reducing the flow of migrants at its sources (or at least, in neighbouring countries), it will still need to deal with those who have already arrived. The EU is seeking to reform the so-called Dublin regulation, which tries to ensure that claims for asylum are processed in the country of first arrival in the EU. The system effectively broke down under the weight of numbers in 2015, with front-line countries (and Greece in particular) unable to cope.

The Dublin system can only operate successfully if (a) applications are processed quickly; (b) those without a legitimate claim to enter the EU are removed quickly; and (c) asylum-seekers are not left as the responsibility of a small number of member-states. In an effort to address the problems with the Dublin system, the Commission has tried, without much success, to force all member-states to accept quotas of asylum-seekers from Italy and Greece.

Asylum requests made in reception centres outside the EU – and in the 'hot spots' already established in Greece and Italy, which will need to remain open for a while – should be processed and managed by a fully-fledged European Asylum Agency (in June 2017, EU leaders reached a political agreement to transform the current European Asylum Office, which merely supports national governments, into an agency). This will only be feasible when the EU has made progress towards harmonising its rules on asylum, covering the criteria for assessing claims, the appeals system, returns policy and distribution mechanisms. The agency will need sufficient resources to process applications and enough autonomy to distribute successful applicants to Schengen countries through a quota scheme.

The Commission should accept that there are different ways in which member-states can help to deal with the migration crisis. Those that refuse to take refugees should be allowed to contribute in other ways, such as providing cash payments or border guards. But there will probably still need to be a system of incentives and penalties to ensure that the Schengen system functions properly in the future. The aim would be to ensure that countries on the external border of the Schengen area manage their section effectively, drawing on the help of the new European Border and Coast Guard and other EU agencies where necessary; and that countries not on the front line show solidarity with those that are, whether by taking in their share of refugees or contributing to border security. Countries that managed the border negligently, or refused to bear their share of responsibility for looking after refugees, would face the possibility of suspension from the Schengen area. Creating a mechanism for suspending or readmitting a Schengen member would require treaty change.

Another part of the answer to managing the migration crisis is to speed up returns of those denied asylum. Italy, which took 180,000 people from boats in 2016, returned only 6,000 of them. The EU as a whole is more effective: in 2016, 46 per cent of the 494,000 non-EU citizens ordered to leave the EU departed.

Speedier returns will require more investment in personnel and processes. The EU should offer more help to EU governments, which could hand over much of the task of repatriation to an EU Asylum Agency.

European governments need to modify their own laws so that there are fewer legal obstacles to deportation (while remaining compliant with the 1951 refugee convention). The EU and its governments should also step up co-operation with countries of origin and transit, for example via the migration partnerships already referred to. There will be times when the EU has to offer both positive and negative incentives to governments, to encourage them to take returnees.

The Commission is taking steps in the right direction. In September 2017 it proposed spending €500 million to resettle 50,000 refugees from camps in Africa and the Middle East. It also proposed pilot schemes to encourage member-states to take skilled workers from states that work with the EU to restrict illegal migration. And it suggested boosting the capacity of the European Border and Coast Guard to carry out returns.

The EU needs access to good data, enabling individuals to be identified, so that it can manage migration, for example by preventing failed asylum-seekers from trying again with a new identity or in a new country. It also needs access to data so that it can detain suspected terrorists or other wanted individuals. Indeed, better use of data is a *sine qua non* for Schengen's survival.

The EU has half-a-dozen important databases, including the Schengen Information System (SIS, which handles criminal information), the Visa Information System and the Eurodac finger-print database for asylum-seekers, while the member-states' 'Prüm' system allows the exchange of national data on finger-prints and DNA. But these databases are not connected. They are often inaccessible to national police services, Europol or the officials checking passports on borders.

The problems are technical, legal and political. Data privacy legislation prevents the transfer of information between databases, and bans the use of data for any purpose other than that for which it was originally collected. Libertarian politicians (including many MEPs) oppose changing these laws. But if the EU is serious about demonstrating that it can win the fight against cross-border crime and terrorism, it needs to create a single agency that brings together these databases.

The EU's eu-LISA agency, set up in Strasbourg in 2012, is well placed to take on this integrating role. It describes itself as the 'European Agency for the operational management of large-scale IT systems in the area of freedom, security and justice'. In April 2017 – in response to terror attacks in Paris and Brussels – ministers from Schengen countries decided to strengthen their border code, by requiring EU citizens entering Schengen to be checked against the SIS and relevant Interpol databases (this led to delays for tourists at some airports in August 2017). But officials on the border still lack easy and quick access to all the databases. Hence the need for a single, centralised system, with safeguards to prevent abuse.

Given the expertise that the British have in areas such as policing and counter-terrorism, mechanisms should be found to allow them to contribute to the EU's work on security after Brexit – for example, by finding ways for Britain to remain plugged into Europol, the Schengen Information System and the European Arrest Warrant.[6]

6: See three CER insights by Camino Mortera-Martinez: 'Good cop, bad cop: How to keep Britain inside Europol', May 2017; 'Hard Brexit, soft data: How to keep Britain plugged into EU databases', June 2017; and 'Arrested development: Why Brexit Britain cannot keep the European Arrest Warrant', July 2017.

The eurozone

The current economic upturn in the eurozone is proving to be more durable than many had expected. Barring an international economic shock, the eurozone appears set for at least a couple of years of decent economic growth. The ECB is continuing to provide the de facto public debt guarantees and the stimulus that are keeping the eurozone together, albeit with unemployment too high and inflation too low.

But there is no doubt that the failure of the euro to provide economic prosperity across the whole eurozone, exacerbated by what some perceive as a lack of democratic accountability for eurozone decision-making, has nourished eurosceptic sentiment in parts of the EU. The euro's problems have damaged the reputation for competence of governing pro-EU centrists, pitted creditor against debtor countries and contributed to the feeling among some voters of powerlessness.

There is currently much optimism that the election of the reformist, strongly pro-EU Macron in France, and the re-election of Merkel for a fourth term in Germany, bodes well for Franco-German relations and the cause of eurozone reform. Despite her worse-than-expected election score in September, and the need to form a coalition that includes the fiscally hawkish Free Democrats, Merkel seems likely to go along with some of Macron's ideas – such as creating a eurozone budget, and turning the European Stability Mechanism (the eurozone's bail-out fund) into a European Monetary Fund – at least to a modest degree.

Three broad approaches to reform are under discussion. They would all put the eurozone on a more stable footing, but probably only one of them is both politically and economically viable.

The first model, popular with federalists, would lead to a much more integrated eurozone and a political union. This would entail a sizeable common eurozone budget with its own revenues and common debt issuing (so-called eurobonds), as well as shared sovereignty over national fiscal policies; fully integrated banking and capital markets, including common rule-making and a large common fund to help resolve failing banks; increased fiscal transfers to poorer regions to help them grow inside the common currency; and a strong role for a central eurozone 'government' to co-ordinate economic policies and structural reforms across all countries using the currency.

Such a federal eurozone would be the best outcome economically, but is probably unachievable politically. Many member-states are wary of giving significant new powers to eurozone or EU institutions. Public and political opinion, in Germany in particular, remains very resistant to the pooling of fiscal sovereignty that would be required. Such reforms would also require major treaty changes, which most governments will not countenance, at least in the short term.

The second possible reform, frequently mentioned by fiscal disciplinarians, would be the creation of a 'responsibility union', with a return to the treaty's original idea of a strict no bail-out rule. Member-states would be forced to default on their debts if they became unsustainable; the knowledge that bond defaults were possible would supposedly lead markets to impose discipline on governments that borrowed too much. However, the experience of emerging market debt crises suggests that such market discipline could well be erratic and unreliable. Higher interest rates for struggling countries would also worsen the divergence between eurozone economies during downturns; weak economies need lower, not higher interest rates, to recover.

Moreover, the possibility of a government defaulting would mean that banks could not be allowed to hold their national government's bonds in large amounts. Otherwise, a government default would trigger financial and economic collapse, and the likely exit from the eurozone of the member-state concerned. Of course, a government default would still be economically disruptive, even if banks held only modest amounts of their home government's bonds, but at least it would not lead to a euro exit.

If the eurozone became serious about enforcing a no-bailout rule, its fiscal rules could be scrapped, since the costs of a default would mostly be borne by the defaulting member-state itself. Such an arrangement would go some way to returning fiscal policy to national control, and in the process restore national democratic accountability. Policy on structural reform would also remain a national responsibility.

However, such a bold move to a strict no-bailout world would require a grand bargain on debt forgiveness and bank restructuring: current debt levels in countries such as Italy are too high, and many banks are loaded with their national government's bonds. Without debt forgiveness and large-scale bank restructuring, financial markets would quickly call Italy's place in the eurozone into question.

In terms of macroeconomic management, the euro would become de facto a fixed-exchange rate regime, as opposed to a true currency union: countries would be prone to 'sudden stop' capital flight, meaning that in a crisis capital would quickly drain away from a country, forcing it into a severe recession. Countries would try to insure their economies against such episodes by hoarding foreign assets and reducing public debt, counting on other countries to create the demand their economies needed. Macro-economically, this would be a big step in the wrong direction.

The third and most promising model would be to improve the macro-economic and financial governance of the eurozone, in deficit and surplus countries alike, but by centralising only the policies that matter most for the currency union's stability. The ECB would need a more flexible and bolder mandate, similar to that of the US Federal Reserve, so that it could tackle shortfalls in eurozone aggregate demand in a timely and effective fashion. It would also need to be able to act as lender of last resort to banks and governments. That is something it has been doing since the crisis began, but only reluctantly and under the threat of legal challenges, since such a role is only implicitly covered by its current mandate.

Fiscal policy could remain a national responsibility, but the eurozone would need to ensure that fiscal policies were strongly counter-cyclical in both booms and downturns, and that the aggregate eurozone fiscal stance was appropriate. The current rules-based system – involving the 'stability and growth pact' and much EU legislation – is not up to the job. There would need to be bolder institutional changes, such as the creation of strong independent national fiscal councils that would work like central banks to make sure fiscal policy was macro-economically sound; and a strong eurozone fiscal council, to ensure that fiscal policy in the eurozone as a whole was set appropriately. A common eurozone budget would help, too, particularly at times when monetary policy alone was struggling to revive the economy.

Banking and capital market policies would need to be very tightly integrated, including, for bank resolution, a common backstop with greater capacity than the current Single Resolution Fund. Such tight integration and risk-sharing in times of crisis would help to ensure that both banking and capital markets could absorb economic shocks rather than concentrate them in one ailing country. Banking and capital market integration would also allow firms and households access to affordable finance, curbing the impact of the state of their local economy or the debt levels of their sovereign on borrowing costs.

Concerning economic policies, EU institutions would only need to play a role to the extent that a policy had a strong macroeconomic or financial impact across the eurozone. That would apply, for example, to the policies needed to tackle current account imbalances such as Germany's large surplus or non-performing loans in the Italian banking system. Structural reforms in general, such as those affecting labour or product markets, are often portrayed as the silver bullet to solve the eurozone's problems. But they are fiendishly difficult to get right, involve many areas that are of secondary concern for other eurozone countries and are often politically very sensitive. The eurozone is right to encourage structural reforms but should ultimately leave them to national democracies.[7]

In the long run some of these changes would require new institutions, which would need to be made more accountable to eurozone citizens. Treaty changes would be needed. A more tightly integrated eurozone could develop its own democratic accountability, for example by creating a eurozone parliamentary chamber – an idea that Macron has floated. This could consist of national parliamentarians or MEPs, or a combination of both. Such a chamber could elect a permanent eurozone finance minister with powers over, or a supervisory role for, fiscal policy co-ordination, the various fiscal councils, banking and capital markets policies and a eurozone budget.

7: Christian Odendahl, 'We don't need no federation: What a devolved eurozone should look like', CER report, December 2015.

New roles for the EU

Enforcing the rule of law

The EU has powerful instruments for ensuring that countries wishing to join respect its values, through the 'Copenhagen criteria' that applicants must fulfil, and Article 49 of the Treaty of the European Union (TEU), which sets out the legal procedure for accession. But the EU does a poor job of maintaining democratic standards among its own member-states. If it performed this task better, it would be more inspiring to its own citizens and to those in neighbouring countries.

In theory, the EU has several instruments which should help it to influence a member whose commitment to democratic values is in doubt. Unfortunately, none of them is working properly.

First, the European Commission can launch infringement proceedings when an EU government breaks European law and in the process threatens EU values such as democracy, equality, respect for human rights and the rule of law (these values are set out in Article 2 of the TEU). But if the government concerned has not breached any specific EU law, the Commission cannot act.

Second, the EU can determine that a member-state has breached democratic values and ultimately, under Article 7 of the TEU, suspend some of its rights as a member-state, including its voting rights in the Council. The problem, however, is that the European Council must first decide unanimously (minus the alleged violator) that there has been a "serious and persistent" breach of democratic values. It is more than likely that at least one EU government would block such action, however bad the alleged violation of European values. Some countries may object to the principle of sanctioning member-states for bad behaviour; others may trade their support for the miscreant's backing in some other field.

Third, the Commission has established a 'rule of law framework' which helps to fill the gap between infringement proceedings and the 'nuclear option' envisaged by Article 7. This instrument starts with a dialogue between the Commission and the member-state concerned. If the Commission is not satisfied with the outcome of the dialogue or the implementation of its recommendations, it can propose that Article 7 be activated.

Poland and Hungary are cases in point. The EU has failed to persuade their current governments to change course and show more respect for the rule of law. The European Commission activated the rule of law framework against Poland in January 2016. But the Polish government knows that the Commission would struggle to get the European Council to agree to suspend its voting rights in line with Article 7 (Hungary and the UK, at the very least, would back Poland) and has rebuffed the Commission's recommendations.

But when the EU turns a blind eye to bad behaviour in its own member-states, it undermines its power of example and its international standing. The EU plays an important role in championing democratic values and the rule of law in its eastern and southern neighbourhoods. Its ability to argue credibly in favour of its principles will be seriously weakened if it cannot enforce its own standards internally.

So the EU should give its Fundamental Rights Agency (FRA) a greater role in enforcing the rule of law in member-states. The FRA, based in Vienna, currently provides independent, evidence-based advice on fundamental rights to EU institutions and governments. Its management board consists of independent experts (one is appointed by each member-state, one by the Council of Europe and two by the European Commission). But its opinions are not binding and the FRA cannot take enforcement action.

The FRA produces high-quality research and is well plugged into all 28 national human rights protection systems. It already works closely with civil society and ombudsman institutions in all member-states. But it should start systematic and regular monitoring of democratic standards in the 27. It should also take over the Commission's role in assessing concerns about democracy and the rule of law in member-states like Poland or Hungary. This would help to depoliticise the current process. The Polish government, for example, has accused the Commission of triggering the rule of law framework for political reasons. Governments might find it harder to justify criticising the judgment of an agency run by experts.

The FRA's opinions should provide the basis for a mandatory debate in the college of commissioners, the European Parliament and the Council of Ministers about triggering Article 7. If these institutions decided to reject an FRA recommendation, they should explain their reasoning in writing to the European public.

EU leaders could also give the European Court of Justice (ECJ) a bigger role in enforcing the rule of law in the member-states. Today, the Court can only review whether the procedural requirements set out in Article 7 have been followed. The Commission should be empowered to take before the ECJ any member-state which it considers to be violating the fundamental rights set out in Article 2. It should be able to act in this way – drawing on the opinion of the FRA – even when the member-state concerned has not breached any particular EU law.

Such a reform would require treaty change and would certainly be controversial. And any move to strengthen the FRA's role in the rule of law procedure would require unanimity among the member-states. But whatever the difficulties, European leaders must not duck the challenge of ensuring that the EU remains true to its basic values.

Fighting corruption

In recent years, demonstrations and popular revolts in countries like Egypt, Georgia, Moldova, Romania and Russia have shown that even in places with endemic corruption, people do not like to see businessmen or politicians enrich themselves at the expense of the rest of the population. In its member-states and in its neighbourhood, the EU could enhance its popularity by doing more to support good governance. In the process, it could also increase the resilience of democratic institutions.

'Corruption' is a term that covers a multitude of sins, not all of which should be the EU's business. The EU should not make the mistake of trying to ensure that no policeman takes a bribe in return for not issuing a speeding ticket, or that no planning officer ever accepts a gourmet meal from a developer. But it should do more to tackle large-scale corruption, state capture and money-laundering, all of which undermine confidence in government.

The Commission made an error in deciding not to update its 2014 report on corruption in the member-states, claiming – bizarrely – that no update was needed. The last Commission President, José Manuel Barroso, had come up with the good idea of an anti-corruption report every two years.

Eurosceptics often claim that the EU itself is corrupt; but the evidence shows otherwise. Though far from perfect, the EU's institutions are generally good at identifying and preventing significant internal cases of corruption. Where EU funds may be at risk, the European Anti-Fraud Office (OLAF) investigates suspicious activity and has been able to recover significant sums of money for the EU's and the member-states' budgets. However, the EU's auditors often find problems with EU funds disbursed by member-states. Twenty member-states have now signed up to plans for establishing a European Public Prosecutor's Office (EPPO), designed to investigate and prosecute fraud and other crimes affecting the Union's financial interests. The Union should become bolder at confronting bad practice in member-states.

The EU could make a significant impact on corruption at the national level:

★ It could make the principles of open government mandatory. While the EU institutions win praise from the Open Government Partnership (a voluntary international compact, committing governments to a certain level of transparency in the provision of data), they do little to enforce similar standards for access to government information and data in the member-states. This makes it difficult for citizens to ensure accountability in decision-making and spending.

★ It could establish common standards for financial transparency for public officials. Ironically, the EU has pressed Ukraine to put in place a system for officials to declare their income and assets to the public, when many member-states do not insist on a similar level of openness. Voters should know that politicians and officials are paid by the state and working on behalf of the state (or the EU, in the case of the EU institutions), rather than on behalf of third parties in the shadows.

★ It could do more to counter money-laundering. Successive anti-money laundering directives have been implemented inconsistently by different member-states. Enforcement is patchy and penalties vary widely. Tough US anti-money laundering penalties have often had more effect on the behaviour of European financial firms than the enforcement of EU rules. The EU's 4th Anti-Money Laundering Directive was adopted in 2015, and entered into force in June 2017. The Commission has already put forward proposals to strengthen the directive, including through greater transparency on the beneficial ownership of companies. The EU's Data Protection Supervisor has objected to some of them, concerning public access to data, though they would give investigative journalists and anti-corruption NGOs important tools for identifying suspicious activity. The EU could do more to ensure that national monitoring systems treat suspect behaviour consistently, that information (for instance on the abuse of shell companies) is shared effectively and that all member-states penalise financial institutions and money-launderers for illegal activity.

★ When EU funds are involved, the Union should do more to ensure that member-states (and neighbours that benefit from EU-funded programmes) investigate and where necessary prosecute and penalise corruption cases according to consistent standards. The creation of the EPPO might not have been unnecessary if all member-states had dealt in the same way with the misuse of EU funds, or corrupt procurement on EU-funded projects.

Tough measures to combat corruption could win support from eurosceptics and EU-enthusiasts alike.

Tackling corporate tax avoidance

One reason why citizens have perceived Europe's economic system as unfair, especially since the financial crisis, is that a lot of companies get away with paying very little tax – while some of them have been bailed out with taxpayers' money. A number of multinationals, notably those deriving their revenues from the internet, have found clever ways of limiting their tax obligations – often aided by governments eager to attract jobs and investment.

A certain amount of tax competition between jurisdictions can be desirable, since it puts pressure on governments not to grow public spending excessively. It may also help economically weaker regions or countries to attract capital and talent. But the situation in Europe has moved beyond what is desirable and is threatening to undermine public finances.

The problem is that tax policy is national, so that any EU initiative requires unanimity. The VAT system of indirect tax has been harmonised within the EU to facilitate cross-border trade. But the taxation of labour, capital and companies remains a patchwork of different systems, rates and loopholes. EU harmonisation has so far been limited to avoiding unnecessary double taxation. International efforts, such as the OECD's recent 'base erosion and profit shifting' (BEPS) programme, designed to prevent the erosion of tax bases through improper corporate behaviour, have led to some progress at the global level. But if Europe cannot set an example by creating a fair, multinational tax system inside the EU, global efforts are likely to fall short, too.

In order to create a fair European tax system, the EU needs to do three things. First, the EU should push ahead with plans for a 'common consolidated corporate tax base' (CCCTB), which aims to harmonise not tax rates but the bases on which rates are calculated. Such a scheme would close corporate tax loopholes and also set down rules for determining what share of profits should be taxed in which country; its rationale is that tax should be paid to a country in proportion to the company's assets, employees and revenues in and from that country. Companies should no longer be able to shift profits for the purpose of avoiding taxation.

Seven national parliaments have rejected this scheme. If those opposed cannot be brought on board, the Commission should pursue the CCCTB via 'enhanced co-operation' – a coalition of the willing – in the hope that it sets a standard that other member-states will sign up to in the long term.

In September 2017 a group of countries led by France proposed a new scheme for taxing digital firms' revenues, rather than profits, in order to limit their scope for avoiding tax. Though Germany, Italy and Spain support this idea, many other member-states do not. The idea is worth exploring but is politically and technically more complicated than the CCCTB, in part because many of the companies concerned are non-European.

Second, the EU needs to become a champion of fair taxation both at home and in international forums. As a start, the EU should agree on standards for fair taxation that all its member-states vow to follow, and conduct regular reviews of their tax systems in terms of fairness, efficiency and progressivity. Given that tax policy remains national, the commitment of substantial political resources to 'soft' measures such as common standards and reviews is necessary.

Third, the taxation of banks, financial institutions and financial markets should be made a European responsibility, at least within the eurozone. This would not only help to integrate European banking and capital markets, but also provide a source of revenue for the Single Resolution Fund (which may be called on to bail out a bank in trouble). The fund could then promise to recover losses to the public purse from bank bailouts by imposing higher taxes on financial markets and institutions in the future.

A lot of European voters, including those who are generally critical of the EU, large corporations and globalisation, would be happy to see large companies paying their fair share of tax.

Encouraging mobility

One of Europe's historic failings, compared to the US, has been its people's lack of mobility. Migration – both within the bloc's member-states and between them – is significantly lower than in the US. This is one important reason why Europe is poorer than North America: workers have been unable or are unwilling to move to where the best-paid jobs are.

In the years after 2004, migration within the EU rose significantly. Millions of people moved from Central and Eastern European member-states in search of higher wages in Western Europe. And in the years after the 2008 financial crisis, high rates of unemployment in Greece, Spain, Ireland, Italy and Portugal pushed up the numbers of migrants again. Free movement has been a useful safety valve, even though the level of intra-EU migration remains lower than in the US.

A higher and less cyclical rate of migration, with experienced and highly-skilled workers moving as much as younger, less-skilled ones, would help to raise living standards in Europe. And there are many steps the EU could take to encourage the cosmopolitan mixing that would instil a stronger sense of European identity.

The Erasmus scheme of university exchanges has been expanded so that 5 per cent of university students now study in another member-state. But that number could be doubled, raising the proportion of young Europeans who speak a second or third language and have the beginnings of a social network in another European country. Erasmus has been extended to apprentices and other non-university students, but rates of participation in these schemes are much lower; the EU should provide more money, language teaching and administrative support so that colleges and companies can offer young people increased opportunities to work and learn elsewhere.

It is still too difficult for migrants to have their professional qualifications recognised in many member-states. Take Germany, where there are dozens of regulated professions for which other EU countries do not require equivalent qualifications – for example, engineering. And many countries are slow to approve professional applications. Prior experience should count towards recognition. In areas where professionals are unlikely to cause harm to other people or the environment, a 'silence is consent' rule would allow them to work if bureaucrats take too long in assessing applications.

Another deterrent to migration is that would-be movers often find it difficult to carry their pension, health and welfare rights with them. This is because entitlement and residency rules differ from country to country, and the bureaucracy can be confusing and intimidating for applicants.

To encourage mobility, the EU could explore optional Union-level 'regimes' for pensions, social security and health insurance, for workers who move from one EU state to another. These would enable European citizens to transfer accrued pension rights, as well as unemployment and health insurance, into EU schemes. These EU regimes would be able to draw upon prior social security and pension contributions to member-states, and would require continued contributions thereafter – although the EU scheme's users would be exempted from paying contributions to national schemes. And these regimes would pay out according to their own rules, irrespective of the country of residence. The more mobile among EU citizens would certainly welcome such reforms.

Boosting Europe's green economy

The biggest energy policy challenge facing EU member-states is how to guarantee the availability of low-carbon electricity that is affordable for households and competitive for businesses. To this effect, EU energy legislation has aimed to achieve three things: to make it easier to trade and invest across EU borders, to promote low-carbon energy, and to ensure member-states show solidarity when one of them faces a threat to its energy supplies. This has not been without success: interconnections between national energy grids have burgeoned; investment in renewable energy sources has risen steadily as the cost of wind and solar has become increasingly competitive with fossil fuels; and member-states have become less dependent on Russian gas supplies. But business investment as a whole remains far too weak to bring about the needed shift to a low carbon economy.

Fixed capital investment fell steeply during the financial crisis, and has not yet recovered. Following a decade of weak investment and consumer spending, Europe's capital equipment and consumer goods are increasingly obsolete. Consumer spending is now picking up a bit but there is sizeable pent-up demand: for example the EU's car fleet is older than it has ever been. Despite the strong rise in investment in renewable electricity generation across the EU in recent years, investment in energy infrastructure as a whole has been weak. Although overall carbon emissions have fallen over the last decade, this has happened in the context of very weak economic growth, especially industrial activity. And emissions from some sectors, such as transport and buildings, have continued to rise.

The EU needs a major push to link up member-states' electricity grids. An EU-wide, interconnected network of national energy systems would help member-states to save on investment in generating capacity and to enhance their energy security. It would also help them to manage the challenges of low-carbon energy systems that are increasingly dependent on intermittent supplies of renewable energy. For example, an integrated network would connect solar energy capacity in the south to wind power in the north, and make it easier to access the energy (and energy storage) potential of Norwegian and Swedish hydro-electric power.

The EU's Emissions Trading System (ETS) was supposed to drive investment in low-carbon power generation and factories by setting a price for carbon. But the ETS has failed because carbon prices have been too low to affect investment decisions. This is because both weaker than expected economic growth (and hence energy usage), and faster than expected deployment of renewables, have created a surplus of emission allowances. The EU has agreed to cut the number of available allowances, but not by anything like enough to bring about the needed increase in carbon prices.

Rather than continuing with a system that struggles to generate the necessary price signals, the EU should scrap the ETS and replace it with a carbon tax, which should then be raised progressively over time. There could be exemptions from this tax in order to prevent the offshoring of heavy industry to locations with laxer environmental standards, as well as transition periods for members currently dependent on coal.

The EU should also agree on stricter regulations for consumer goods and buildings. For example, it should agree on a cut-off date of 2035 for the phasing out of the sale of combustion-engine cars, and introduce an aggressive scrappage scheme to remove the most polluting cars, buses and trucks from European roads. The EU should also tighten environmental standards for new buildings – the existing regulations requiring that new public buildings be 'near zero energy' by 2018, and houses by 2020, contain too many loopholes. And the current regulations do not cover the existing stock of buildings, which can never meet the energy-efficiency of new buildings but should nevertheless be required to meet considerably higher standards. The modernisation of the existing stock of buildings would cut emissions significantly and provide a big economic stimulus.

The strategy outlined here would meet four objectives: it would kick-start business investment and consumer spending, generate tax revenue, accelerate the decarbonisation of the EU economy and reduce European dependence on Russian gas. The EU would show that it can deliver real economic and environmental benefits to citizens, including younger people, and help to rebuild support for closer political integration.

Part two: New European architecture

A more flexible Union

The EU needs to become more flexible, so that its members need not sign up to all the same policies. The EU's institutions have long opposed this principle, on the grounds that too much 'variable geometry' could boost 'inter-governmentalism' and undermine their own position. They have subscribed to the orthodoxy that almost all EU members will ultimately join the euro and the Schengen area. However, Britain's vote to leave has helped some policy-makers to recognise that in an EU of 27 members, which have very different objectives, not everybody will be willing to sign up to everything. Indeed, some projects – such as co-operation on defence or a European Public Prosecutor – may work better with a smaller number of committed countries involved.

This principle of differentiation featured in Commission President Jean-Claude Juncker's March 2017 white paper, as one of his five models for the future of the EU: "In a scenario where the EU-27 proceeds as today but where certain member-states want to do more in common, one or several 'coalitions of the willing' emerge to work together in specific policy areas." (Juncker has subsequently made clear that he rejects this scenario.) A few days after the publication of the white paper, Angela Merkel, François Hollande, Paolo Gentiloni and Mariano Rajoy – the then leaders of Germany, France, Italy and Spain, respectively – met in Paris and praised the idea of a multi-speed Europe.

A distinction needs to be made between 'multi-speed' Europe, the idea that all countries remain committed to the same objectives, but some travel quicker than others; and 'multi-track Europe', the idea that not every country has to sign up to the same objectives. During his renegotiation of the terms of Britain's EU membership – which concluded in February 2016 – Prime Minister David Cameron pushed for the right to different destinations, not different speeds. Italy backed Cameron's initiative. However, France, Germany and the Commission ensured that he did not achieve a great deal. What he did secure was a provision that the treaties' commitment to "ever closer union" need not apply to the UK. He also obtained another change that applied to all members: "The references to ever closer union among the peoples are therefore compatible with different paths of integration being available for different member-states and do not compel all member-states to aim for a common destination." Britain's departure means that the document enshrining the results of the British renegotiation has no legal standing, but some of its ideas remain pertinent.

The Commission white paper of March 2017 referred to neither multi-speed nor multi-track and blurred the distinction. It is time for EU leaders to state openly that the 27 do not and will not share all the same ambitions and objectives. President Macron seems willing to take the lead. He told his ambassadors that they "should contemplate a Europe based on several formats, go further with all those who want to move forward, without being held back by the states that want – and that is their right – to advance slowly or not as far." He added that the EU needed to escape a "constricted framework in which we would have to move forward…with the agreement of 27 states, or do nothing, or with the agreement of 19, or do nothing."[8]

Such thinking has already encountered flak, from both traditional federalists and eurosceptic Central Europeans. The former see the departure of the UK as an opportunity to push for a more uniform and integrated Union. Thus in his State of the Union address in September 2017, Juncker argued that every member-state should join the euro, the banking union and the Schengen area.[9]

Several Central European countries also dislike the idea of a multi-track Europe, fearing that it would lead to them being treated as second-class. Thus Poland's president warned in September that "if EU membership became less attractive for countries that are thrown out of the first decision-making circle, then this moment…will be the actual beginning of the end of the Union." He continued: "Sooner or later the societies of states that today view the EU positively…will feel rejected and support for the EU will decline [leading to] further Brexits."[10]

Therefore proponents of flexibility need to emphasise that a core group will not exclude any member wishing to join which meets objective criteria. And smaller groups should be transparent about what they

8: Emmanuel Macron, speech to French ambassadors, Paris, August 29th 2017.
9: Jean-Claude Juncker, State of the Union speech, Brussels, September 13th 2017.
10: Andrzeg Duda, speech in Krynica, September 5th 2017.

do, in order to ensure that a differentiated EU does not become a fragmented Union.[11]

In fact if the EU made several policies optional, including membership of the euro, it would probably suit the current Polish government very well. The orthodoxy that every country must join the euro risks fueling anti-EU populism in some places. Greater flexibility would help to defeat the eurosceptic narrative that the EU is an all-powerful juggernaut intent on imposing a uniform model of integration onto an entire continent.

Despite the opposition to greater flexibility in some quarters, Macron's arrival may well herald a less uniform EU. Italy is sympathetic to his thinking on flexibility. Together with Angela Merkel, who won Germany's election in September, Macron plans to push ahead with eurozone integration, as discussed earlier in this report. The eurozone will become more distinct from the rest of the EU, with more of its own institutions. Joining the euro will become an even more demanding undertaking than it is already. Sooner or later many EU leaders will recognise that some member-states are ill-suited to euro membership and that others – such as Sweden and Poland – will just not want to join for the forseeable future.

In this new, more flexible European Union, the most important distinction will be between the countries in the euro and those outside it. The eurozone has problems that need fixing, but these should not and need not spill over into the wider EU. Indeed, as the eurozone strengthens and develops its own institutions, it will inevitably become quite distinct from the EU. So it is important to ensure that two classes of EU member do not emerge: the future institutional arrangements must ensure that the eurozone countries do not gain a privileged position within the wider Union.

A more differentiated EU would in some ways be more complicated. There would be implications for budgets and accountability. Some groupings of countries might want to have their own budgets, as well as their own parliamentary bodies (consisting of MEPs and/or national parliamentarians). President Macron wants the eurozone to have its own budget and to be scrutinised by MEPs from the eurozone alone.

Flexibility would also make the Union more attractive to some potential applicants. For example the United Kingdom would be more likely to

11: Agata Gostyńska-Jakubowska and Christian Odendahl, 'A flexible EU: A new beginning or the beginning of the end?', CER insight, May 2017.

want to rejoin the EU one day, if it could move into an 'outer circle' of members that did not have to join the euro, Schengen and perhaps some other policies; the same would apply to an independent Scotland. Senior Turkish officials are enthusiastic about the concept of partial membership. "If the UK can join an outer tier, why cannot Turkey?" said one. "The EU has become too big and needs a different format….We could become a different kind of member."[12]

In addition to the euro, Schengen, policing and defence co-operation – all policy areas that currently allow some member-states to opt out – one could extend the same principle to the databases that facilitate co-operation on security, the harmonisation of corporate taxation or new arrangements for the sharing of intelligence, amongst other policies. But for the EU to function smoothly, there would have to be a minimal number of policies that all members stayed involved in, such as the single market, competition policy and trade, environmental rules and foreign policy.

The concept of greater flexibility for EU members could be combined with the new approach to enlargement and the neighbourhood – privileged partnerships and so on – discussed in the first section of this report. Flexibility could make it easier for the EU to resume the process of enlargement in Eastern and South-Eastern Europe, creating an outer circle of members that would not be expected to join the euro, Schengen and perhaps some other policy areas – at least for a long transitional period, until existing members were convinced that the countries concerned could meet all the requirements.

All this would present challenges to the EU's legal order, which the institutions will, rightly, seek to protect like hawks. The EU will insist that if some non-members are allowed to take part in policies such as defence, trade or parts of the single market, they must accept its rules and the jurisdiction of its courts.

In the very long run, more flexible structures could allow the ideas floated in August 2016 by a seminal Bruegel paper to return to the agenda. The Bruegel proposal would allow non-EU states to forge 'continental partnerships' with the EU.[13] They would be in the single market and consulted on its rules. They would have to follow ECJ rulings but not necessarily EU rules on free movement. Such ideas could allow countries such as the UK, Norway, Switzerland, Ukraine and Turkey to move closer to the EU without becoming full members

12: Private comment at the CER/EDAM/ECFR Bodrum roundtable, October 8th 2017.
13: Jean Pisani-Ferry, Norbert Röttgen, André Sapir, Paul Tucker and Guntram Wolff, 'Europe after Brexit: A proposal for continental partnership', Bruegel, August 2016.

(though each of those countries would probably wish to move closer in very different ways).

Nick Clegg, the former British deputy prime minister, makes a similar argument in his recent book:

> "The EU itself is not a fixed thing. It changes all the time.… It has an elastic capacity to accommodate huge differences between different countries under one roof. That versatility can help, once more, to reincorporate the UK within the EU, but on a more settled basis – not within the inner core of the EU, but not cast out to the political wilderness either. An accommodation, most especially on the vexed question of free movement, can be found as the EU develops into an ever more distinct union of 'concentric circles'."[14]

At the moment neither the EU nor the UK is ready for such an accommodation. In several years' time, when the UK has experienced the chill winds of solitude, and when EU governments have realised that keeping the UK at arms' length is not in their interest, the situation may be different.

14: Nick Clegg, 'How to stop Brexit', Bodley Head, 2017.

Treaty change and institutional reform

The planning, negotiation and ratification of the constitutional treaty, which became the Lisbon treaty, took about ten years. Ever since, most EU governments have been very wary of further treaty change; EU rules mean that a single country can wield a veto. If the governments did draw up a new treaty, several of them, notably Denmark, the Netherlands, Ireland and (possibly) France, would have to hold referendums, with the likelihood that one or other country would vote it down. The subject of major treaty change has therefore been avoided in recent years; governments have gone for temporary fixes or mini-treaty changes, which do not require referendums.

But treaty change cannot be postponed for ever. In May 2017, Macron broke with the position of his predecessor and said that treaty change was no longer taboo. When she met the new French president in Berlin, Merkel said that she did not rule out a new treaty. But she also said that the EU first needed to work out a road map of what it wanted to achieve; only then should it consider which mechanisms were necessary to deliver change. Macron's advisers talk similarly of a new EU treaty as being likely at some point, but only if and when it becomes the only way of achieving the reforms required.

The case for the EU taking on new powers (especially for the eurozone), and therefore ultimately for a new treaty, is strong. But how can the difficulty of ratification be overcome? Could the rules on treaty revision be amended, so that a single country can no longer block change? Not easily, because such an amendment would in itself require a treaty change, which would have to be agreed unanimously.

So what course should European leaders pursue? Given the current state of popular opposition to the EU in some countries, they should probably avoid going for a full-blown treaty change, on the model of the Lisbon treaty. But there is a precedent for changing the rules on eurozone governance. In December 2011, David Cameron vetoed a treaty change that sought to tighten EU rules on budgetary discipline.

The other countries then bypassed that veto by concluding an inter-governmental treaty, with a different procedure for ratification: it would enter into force when 12 eurozone members had ratified it. That meant no one country could block the change. In the end 25 euro and non-euro member-states ratified and adopted the 'fiscal compact'. The eurozone has also benefited from other inter-governmental treaties of limited scope, such as the one signed in 2011 that established the European Stability Mechanism (ESM), a bail-out fund, and another signed in 2014 that set up parts of the banking union's Single Resolution Mechanism.

Inter-governmental treaties on EU matters are not ideal (especially for tidy legal minds) but can work smoothly alongside the Union's treaties. The fiscal compact, for example, prescribes a role for the Commission and the European Court of Justice in policing its rules. In the long term, European leaders intend to integrate the fiscal compact (and the other inter-governmental eurozone treaties) into the EU treaties – just as the inter-governmental Schengen treaty of 1985 was later folded into the EU treaties. More of these inter-governmental treaties could allow the rules of the eurozone to be changed quite speedily.

The wider EU also needs reform, if rather less urgently than the eurozone. However, a major treaty change for the 27 should wait for the euroscepticism which has taken hold in many parts of Europe to subside. When the EU has overcome many of its current difficulties, and improved its standing with voters though reform, new treaties and referendums can be contemplated.

In the meantime, the EU's institutions need attention. Indeed, improving the institutions would help to make the EU more effective and thus augment its popularity.

Since its golden age in the time of Jacques Delors, the European Commission has grown weaker vis-à-vis the member-states. It no longer sets the agenda that the member-states follow. The reasons for this weakening are manifold, and mostly structural (through some weak leadership in recent decades has not helped).[15]

One problem is that the gravity of the challenges the EU has faced in recent years – such as the eurozone and refugee crises – has required the mobilisation of resources that only national governments can

15: See Charles Grant and colleagues, 'How to build a modern European Union', CER report (Chapter 1), October 2013.

provide. That is why the Commission alone lacks the credibility to lead the work on EU reform, though it must be closely involved.

Another is that successive treaty changes have boosted the powers of the Parliament, making the Commission increasingly dependent on it. The Commission has started to see itself as a political government, accountable to the Parliament. The highly problematic *Spitzenkandidaten* system, by which the candidate of the most successful party in the European Parliamentary elections becomes Commission president, has encouraged this dependency. The sway of the Parliament over the Commission has encouraged the latter to become – as Juncker has proclaimed – more 'political'. In some ways that may be desirable. However, a Commission which is too political and too close to MEPs risks losing the credibility to fulfil its technical functions properly. It is because of the perception that the Commission is slack in policing the EU's rules that the German finance ministry wants the ESM to supplant the Commission's role in managing the eurozone.

The Commission's leaders need to make more effort to emphasise their independence from the Parliament. When Juncker became president, he said that he would position the Commission equally between the Parliament and the Council. But that is not how it turned out. Some commissioners are afraid of crossing the Parliament, lest powerful MEPs make their life difficult. As one commissioner put it: "The Parliament is a constant, physical presence, pulling the Commission towards it; yet on the other side of us the Council is ephemeral and hardly present, since ministers go home after meetings."

To take just one specific example of this sway, in 2012 a group chaired by Erkki Liikanen (the Governor of the Bank of Finland) drew up a report on European banking. The commissioner responsible, Michel Barnier, supported the report's ideas of partially separating investment from commercial banking, and of increasing bank capital requirements. But the Parliament, responding to some deft corporate lobbying, ensured that the report was largely buried. Another, more general example is that the Parliament has often pulled the Commission towards larger and larger EU budgets, against the wishes of many member-states.

Some qualifications are called for. First, we are not arguing that the Parliament's influence is necessarily malign or unproductive. The institution contains genuine expertise and sometimes takes sensible initiatives. For example it has often pushed for a deeper single market or for higher environmental and consumer standards. Thus it set up an inquiry into the Volkswagen emissions scandal, when the Commission was ignoring it. It pushed the Commission to abolish roaming charges on phones when people travel within the EU. And it insisted that the budget for the Erasmus student exchange programme expand, when other budgets were being cut.

Second, though commissioners sometimes feel dependent on the Parliament, there are times when the Commission appears to be the messenger of the big member-states, notably France and Germany – much to the annoyance of the smaller member-states. For example, until recently it took a very Germanic view of the eurozone crisis, seeking to impose strict austerity on problem countries.

The bigger picture is that many of the Parliament's leading figures appear sometimes to have lost touch with European citizens, becoming ever more focused on expanding the powers and budget of the Parliament itself and of the EU. That may be one reason why turn-out has fallen at every European election since 1979 (although in a few countries, such as Germany, the Parliament has retained considerable credibility). If and when the EU treaties are amended, the Parliament's already extensive powers need not be extended.

What is missing from the EU's current institutional balance is a meaningful role for national parliaments. MPs enjoy a legitimacy that MEPs sometimes lack – but they are often ignorant about the EU. Finding a role for them in EU governance, alongside MEPs, would help to educate MPs in how the Union works. They might then treat EU matters with a greater sense of responsibility.[16] The idea of a 'green card' could be revived, whereby a certain number of national parliaments could club together and demand EU action in a particular area; the Commission would be obliged to respond.[17]

Some national parliaments already intervene in a significant way on EU matters, such as Germany's Bundestag, which has won the right to approve the use of eurozone bail-out funds. But MPs from one country should not count for more than those from another. A eurozone assembly made up of MPs and MEPs could monitor and hold to account decision-making on euro matters. This might help MPs – including those from the Bundestag – to understand the bigger

16: Charles Grant, 'Can national parliaments make the EU more legitimate?', CER insight, June 2013.
17: Leading members of the UK House of Lords, such as Lord Boswell, have suggested this, as has a CER policy brief. See Agata Gostyńska-Jakubowska, 'The role of national parliaments in the EU: building or stumbling blocks', June 2016.

picture, and the downsides of a narrow, nationalistic approach to policy-making.

Though there is a need for new institutions, even more important is the need to transcend the traditional battle between *communautaire* and inter-governmental thinking. The EU cannot work without federal institutions and principles, such as the European Central Bank and majority voting. But neither can it function without national governments playing a major role, for example in foreign policy, handling eurozone crises or intelligence-sharing.

A principle of institutional partnership needs to be established: EU institutions should become involved when and where they can evidently add value to the capacity of member-states, for example in helping to strengthen Schengen's external border. Several leading Commission officials understand the need for a new culture of co-operation with the member-states. When important new institutions are created, such as a putative European finance ministry, they will surely – as with the European External Action Service – consist of both federal and inter-governmental elements.

Collaboration between the Commission and member-states would be easier if the original balance between the three main EU institutions was restored. The Council of Ministers should represent the member-states; the European Parliament should promote citizens' interests; and the Commission should enforce the treaties and laws, while proposing new rules, without being beholden to either of the other two institutions.

In order to emphasize the point that the Commission should be equidistant between Council and Parliament, EU leaders should scrap the *Spitzenkandidaten* system. This system makes the Parliament pre-eminent in choosing the Commission president and discourages some of the most talented potential presidents from putting their names forward.[18] In his Sorbonne speech, Macron expressed scepticism about the system, arguing that the major European parties which choose the candidates should not monopolise the debate on Europe; he said he preferred bottom-up methods and pan-European electoral lists for European elections.

EU leaders should not forget the pledge made by the European Council in 2014 to review the system for appointing the Commission president.

18: Heather Grabbe and Stefan Lehne, 'The 2014 European elections: Why a partisan Commission president would be bad for the EU', CER policy brief, October 2013.

The appointment of the next president should simply require a positive vote in the European Council and in the Parliament. Furthermore, if and when the treaties are changed, the European Council should gain the power to sack the Commission, a right which the European Parliament already enjoys.

Conclusion

> "I am a strong believer that modern political life must rediscover a sense for symbolism. We need to develop a kind of political heroism. I don't mean that I want to play the hero. But we need to be amenable once again to creating grand narratives. If you like, post-modernism was the worst thing that could have happened to our democracy. The idea that you have to deconstruct and destroy all grand narratives is not a good one. Since then, trust has evaporated in everything and everyone….Why do modern democracies refuse to allow their citizens to dream? Why can't there be such a thing as democratic heroism?"[19]

These words, from Macron, are very French, not to say Napoleonic, and will not appeal to all Europeans. But he is right to argue that it should not be left to extremists, such as nativists and jihadists, to offer appealing narratives. The EU certainly needs inspiring messages and symbols.

Whatever the narratives that Macron and other leaders may be able to construct, the EU should focus on outcomes, not processes. Voters want to see that the EU can produce results in areas that they care about. The Union therefore needs new and joined-up policies for handling the neighbourhood, refugees, borders and internal security. It needs new initiatives to improve eurozone governance and economic growth rates, as well as more effective foreign and defence policies. And it needs to take more action in certain areas that would appeal to citizens – such as boosting the green economy, encouraging labour mobility, tackling corruption in member-states, limiting corporate tax avoidance and enforcing the rule of law across the Union.

An EU that succeeded at some of those tasks, while making a better job of delivering prosperity and security, would stand a good chance of regaining the trust of European voters. To achieve better outcomes, Europe needs more integration in some areas, but not the pursuit of either federalist or inter-governmentalist dogma.

19: Emmanuel Macron, interview in *Der Spiegel*, October 13th 2017.

Macron is right to propose more flexible institutional structures because, as he knows, not everyone will buy the grand narratives that he desires. "Europe is already moving at several speeds, so we should not be afraid to say so and want it!...Let's embrace the differentiations, the vanguard…No state must be excluded from the process, but no country must be able to block those wanting to make faster progress or forge further ahead."[20]

If Macron's vision wins out against Juncker's idea of a more uniform EU, there will be positive consequences. First, the EU would be more viable in the long run, since it would be better able to contain the varying and evolving policies and priorities of its members. Second, more flexibility could enable the EU to revive the enlargement process, as Macron acknowledged in his Sorbonne speech; he noted that Balkan enlargement would spread peace and stability across the continent. And third, a more flexible and differentiated EU would be more attractive to the UK, post-Brexit. "In a few years' time the UK will be able to find its place, if it wishes, in this EU focused on uncompromising values and an effective market…In this revamped, simplified EU that I propose, I cannot imagine that the UK would be unable to find its place."[21]

For the past several years, the EU has suffered from weak and insipid leadership, as it has lurched from one crisis to another. But now, against the background of a somewhat improved economic situation, the combination of Macron's enthusiasm and intellectual creativity, and Merkel's authority and experience, bodes well for the cause of EU reform. The Union's critics have often argued that it is too inflexible to adapt and flourish. Macron, Merkel and other leaders, including those running the EU institutions, must move quickly to prove the critics wrong and prepare to relaunch the Union. The initial signs are quite encouraging.

In his insightful but pessimistic new book on the state of Europe, Ivan Krastev quotes approvingly the German poet Rainer Maria Rilke: "Who speaks of victory? To endure is all."[22] But the EU should do better than endure. It remains a unique historical experiment, even if the current geopolitical context puts it on the defensive. It must fly the flag for its values, those of the rule of law, human rights, international co-operation and global governance, as well as the combination of market economics and social justice. Although the EU is the leading champion of such values, they are not uniquely European. Europeans have discovered that these principles can deliver political, social and

20: Emmanuel Macron, Sorbonne speech, September 26th 2017.
21: Emmanuel Macron, Sorbonne speech, September 26th 2017.
22: Ivan Krastev, 'After Europe', University of Pennsylvania Press, 2017.

economic wellbeing. Many people on other continents are keen for the Union to sort out its problems so that it becomes a more outward-looking, effective and inspirational entity, better able to take on global responsibilities. A successful relaunch of the EU matters – not only for Europe but also for the cause of liberalism worldwide.

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Relaunching the EU

Charles Grant with Sophia Besch, Ian Bond, Agata Gostyńska-Jakubowska, Camino Mortera-Martinez, Christian Odendahl, John Springford and Simon Tilford

Having weathered its recent crises, the EU is ripe for a relaunch. This report suggests how the EU could better handle its neighbourhood and migrant flows. It argues that the eurozone's weaknesses can be fixed with some modest reforms. And it proposes a greater EU role in enforcing the rule of law, fighting corruption, tackling corporate tax avoidance, facilitating free movement and boosting the green economy. The report calls for more flexible EU structures: tiers of membership – with some members opting out of certain policies, and some non-members opting into others – would allow the EU to revive enlargement. In the long run, a tiered EU could help the UK to find a place in an outer rim. The report concludes with some recommendations on institutional reform.

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