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THE EUROPEAN UNION IN THE FACE OF THE SOVEREIGN-DEBT CRISIS

COMMUNITY INSTRUMENTS AIMED AT COUNTERING THE SOVEREIGN-DEBT CRISIS

To the end of the 2010s, the European Union developed several anti-crisis instruments. They comprised the mechanism for the coordination of national macroeconomic policies, the procedure launched in the case of excessive budget deficit and the bail-out ban. All three instruments were created under the Maastricht Treaty signed at the beginning of 1992, and the procedure for excessive budget deficit was additionally regulated by the Stability and Growth Pact.

The Maastricht Treaty introduced Article 103 to the Treaty establishing the European Community (TEC), under which the Council of the European Union adopts (by qualified majority of votes) recommendations specifying general guidelines for macroeconomic policies of Member States and the European Union.[1] At the same time, the Council is authorised to formulate recommendations for Member States whose policies are incompliant with the approved guidelines or constitute a threat to the effective functioning of the Economic and Monetary Union.

Under the Maastricht Treaty, Article 104c was also added to the TEC. The provisions of that article regulated the procedure launched in the case of excessive budget deficit.[2] The objective of this revision was to counteract the emergence of such deficits in EU Member States, and especially in Eurogroup members. Article 104c specified the operation procedure for community bodies (the European Council and European Commission). Moreover, Article 104c also outlined regulations on possible sanctions on Member States that were incapable of bringing the deficit situation to an end.

The Treaty of Maastricht also contained the protocol that specified, among others, the reference values that, if exceeded, would constitute the basis for measuring excessive deficit volume. These reference values were as follows:

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[1] After the consolidation of TEC, i.e. after the implementation of all the amendments introduced by the Lisbon Treaty, this is Article 121 of the Treaty on the functioning of the European Union (TFEU).

[2] Currently, this is Article 126 of TFEU.

- a deficit-to-GDP ratio of 3% (calculated in market prices),
- a debt-to-GDP ratio of 60% (calculated in market prices).

In the Stability and Growth Pact, the excessive budget deficit procedure was extended. The Pact was introduced under the pressure of the Federal Republic of Germany, which feared that some states (especially Belgium and Italy) would not adhere to convergence criteria in the area of finance, and would not implement the fiscal policy based on solid and sustainable foundations. The Pact encompassed five acts of law: resolution of the European Council adopted at the meeting held in Amsterdam on 16 June 1997, and four regulations of the Council of the European Union. In the resolution, the EU Member States undertook to obtain budget balance or surplus in the mid-term, and to apply measures directed at the fulfilment of this objective. On the basis of these regulations, the preventive and corrective arms of the Pact were specified.

The cornerstone of the preventive arm is to ensure that the budgets of EU Member States are regularly monitored by the Commission and the Council of the European Union. This supervision is to be carried out by evaluating the stabilisation programmes of Eurogroup members and the convergence programmes submitted by the remaining EU Member States. In the case of a negative evaluation of a programme of a given Member State, the Council is authorised to issue (in compliance with the recommendations of the Commission) “an early warning” to this Member State.

The corrective arm obliges Member States to comply with the obligation to undertake immediate actions aimed at improving their budget situations upon exceeding the 3% budget deficit. If an Eurogroup member does not implement appropriate corrections to the specified deadline, sanctions may be imposed.[3]

According to the no-bailout rule (Article 104b of TEC, currently Article 125 of TFEU), Member States bear responsibility for financing their national liabilities. This responsibility is not borne by the Community or other Member States. This individual liability has been to persuade EU Member States to pursue “healthy” budget management and avoid excessive budget deficits.

THE EU’S REACTION TO THE BUDGET CRISIS IN GREECE

In the second half of 2009, the Greek government disclosed data confirming the appalling condition of Greece’s public finances. In 2009, the Greek budget deficit reached (according to initial calculations) 12.7% of Gross Domestic Product (GDP), and public debt went up to 120%. In the first half of 2010, Greece would have to take

[3] The preventive and repressive arms of the Pact were discussed on the basis of: B. Mucha-Leszko (2007), *Strefa euro. Wprowadzenie, funkcjonowanie, międzynarodowa rola euro*, Lublin, pp. 178--179; E. Kawecka-Wyrzykowska, K. Michałowska-Gorywoda, *Unia Gospodarcza i Walutowa*, in: J. Barcz, E. Kawecka-Wyrzykowska, K. Michałowska-Gorywoda (2007), *Integracja europejska*, Warsaw, pp. 294-295.

out loans worth EUR 40 billion to service its debts. That would be a very difficult task as Greek securities had very low ratings.[4]

Greece struggled with the public finance crisis for many years already. The crisis was due to three factors. Greece developed a most costly pension system in Europe, which resulted from the relatively low retirement age (61.4 years) and a relatively long life expectancy (82.6 years for women, and 77.4 years for men). The second factor was the numerous privileges for employees (especially in the public sector, which employed ¼ of the Greek labour force), e.g. premiums for punctual arrival at work, reimbursement of transport costs and additional free days. In fact, it was impossible to lay an employee off. Premiums were given to employees and pensioners on Christmas and Easter.[5] The third factor consisted in the low interest on credits and loans that was not corrected for many years.

The European Union became aware of the emergence of the public finance crisis in Greece for the first time in 2004, when it discovered that the statistical data it received from Greek authorities had been regularly forged. For that forgery Greece should have been heavily fined. However, the European Union resigned to do so as it assumed that imposing a fine would only increase the already high budget expenditure. EU politicians assumed that Greece's membership in the Eurogroup would reduce debt repayment by 2% to 3% of GDP and, consequently, decrease Greek public expenditure and deficit. Greeks, however, allocated their savings to consumption and thus the debt did not decrease. It was in 2004 when the European Commission launched proceedings against the violation of the TEC by Greece which forged its statistical data.[6] After some time, those proceedings were halted and thus the Commission proved it did not act rigorously. Forgeries of the statistical data did not cease after 2004. The instruments foreseen in the Maastricht Treaty and the Stability and Growth Pact turned out to be ineffective.

In response to the serious budget crisis in Greece, the European Union decided to take some harsh steps towards this Member State at the beginning of 2010. It obliged the Greek government to submit reports on its savings policy to the European Commission at least every three months. The anti-crisis plans of the Greek government were analysed. The first plan, whose objective was to bring the budget deficit to the level of 8.7% of GDP in 2010, and 2.8% in 2012, was approved by Eurogroup finance ministers in February 2010. It foresaw an increase in taxes, cuts in budget expenditure, freezing of public servants' salaries and the introduction of salary caps for those with highest income.[7]

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[4] *Cf. Banken halfen bei Verschleierung von Schulden*. http://www.faz..net; *Pięć krajów, które mogą pogrążyć Europę*, "Dziennik. Gazeta Prawna" 12-14.02.2010, p. A9.

[5] *Cf. Grecy znowu strajkują, bo rząd zmusza ich do dłuższej pracy*, "Gazeta Wyborcza" 16.07.2010, p. 26; *Chocholi taniec Greka Zorby*, "Dziennik. Gazeta Prawna" 2-4.07.2010, p. A19.

[6] *Cf. Banken halfen...*, http:://www.faz..net; *Grecka tragedia, europejscy widzowie*, "Gazeta Wyborcza" 6-7.03.2010, p. 18; H.-J. Axt, *Odyssee einer Eigendynamik – Wie aus dem Griechenland-Schock eine Euro-Krise wurde*. "Südeuropa-Mitteilungen" no. 3/2010, p. 15.

[7] *Cf. EU kontrolliert Griechenlands Finanzen*, "Kieler Nachrichten" 4.02.2010, p. 1. *Banken halfen....*; *Greece faces EU grilling over catastrophic deficit*. htttp://www.dw-world.de; *Greek financial crisis causes euro to hit five-year low*. http://www.dw--world.de

In February 2010, the European Commission, as well as some other Member States, e.g. France, worked on reaching an agreement in the European Council on the financial aid for Greece.[8] A consensus was not reached because of Germany's position. Germany also tried to prevent the debate on the financial support at the European Council's meeting in March 2010. That position of the Federal Republic resulted from several reasons. Chancellor Merkel feared that if the decision reached was favourable to Greece, then other Member States would also demand financial aid. Merkel also wanted to check whether Greece would actually implement the savings plan. Another reason was the great concern over the economic situation of Greece expressed by the German public opinion. The international financial crisis was to affect Germany's economy; the economic growth was to fall to -5% in 2009, and the budget deficit and public debt were to amount to -3% and 72.7% of GDP respectively. The majority of the German public opinion believed that Germany could not provide Greece with financial support. Another important reason were the upcoming May elections in one of the largest lands of the Federal Republic of Germany, namely North Rhine-Westphalia.[9]

France and Spain insisted and Germany resigned from opposing the debate on financial aid for Greece at the March meeting of the European Council. At the time both France and Spain had financial difficulties themselves. In 2009, their budget deficits amounted to -7.5% and -11.2% of GDP, respectively. The plan presented by Germany had a decisive impact on the resolutions adopted by the Council. According to that plan, the International Monetary Fund (IMF) was to participate in the Greek bail-out programme and the credits would be granted not by the European Union, but by Eurogroup members. Moreover, that solution would only be used as the last resort and at the consent of all Member States.[10]

It should be noticed that the European Council departed somewhat from principles of the economic policy given in the Treaty on the functioning of the European Union, i.e. from the no-bailout principle. Germany probably intended to minimise the divergence from Treaty provisions. That is why they postulated that Greece receive credits from other Eurogroup members only as the last resort.

The decisions of the European Council crystallised during the video conference of Eurogroup finance ministers on 11 April 2010. It was decided that in 2010 Greece could receive credits worth EUR 30 billion from Eurogroup members. Germany was to provide EUR 8.4 billion and France was to ensure EUR 6.3 billion. Interest on the loans would amount to 5%, i.e. it was to be much lower than market interest

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[8] *Cf.* H.-J. Axt, *op. cit.*, p. 15.

[9] *Cf. Od Frau Europa do Madame Non*, "Gazeta Wyborcza" 27-28.03.2010, p. 2; *Weltkonjunktur und deutsche Konjunktur im Winter 2009*, "Kieler Diskussionsbeiträge" no. 470/471, Institut für Weltwirtschaft an der Universität Kiel, 2010, p. 62.

[10] *Cf. Rettungsplan für Athen steht*. http://www.faz,net; *Mistrzów w płaceniu zalewa*, "Dziennik Gazeta Prawna" 2-5.04.2010, p. M8.

rates. The International Monetary Fund intended to make an additional contribution of EUR 15 billion.[11]

The public finance crisis in Greece worsened since the end of April 2010. The Greek government admitted that if it did not receive international credits in the coming weeks, it would not be capable of repaying its debt. Greek bonds became trash bonds.[12] In this situation, in May 2010, Eurogroup finance ministers decided (in agreement with the International Monetary Fund and the European Central Bank) that Greece would receive EUR 110 billion in loans in the years 2010-2012. Eurogroup members would contribute EUR 80 billion, and the International Monetary Fund EUR 30 billion.[13]

Taking such a decision was possible thanks to a long-term reform and savings plan negotiated with Greece by representatives of the European Commission, the ECB, and IMF specialists. The main objective was to consolidate Greece's public finances which would consist in decreasing the budget deficit from -13.6% of GDP in 2009 to less than -3% in 2014. The programme stipulated that benefits for public sector employees would be lowered, pension bonuses lifted, structural reforms (e.g. of the labour market) implemented, and consumption taxes would be increased further.[14]

In May 2010, the European Central Bank decided to acquire loans (especially on the secondary market) issued by Eurogroup members hit by the sovereign-debt crisis.[15] The activities undertaken by the ECB contradicted the EU legislation, chiefly Articles 123 and 127 of the Treaty on the functioning of the European Union. The former article would not allow for the European Central Bank or national central banks to acquire debt securities directly from Member States as that could affect the process of reducing national budget deficits. Therefore, it follows from Article 123 (by implication) that it is prohibited to purchase such securities on the secondary market. Article 127 specifies, *inter alia*, the objectives and basic tasks of the European System of Central Banks. The main goal of that institution is to maintain price stability while acquisition of debt securities encourages inflation, especially if issuing securities is connected with money printing.[16] The European Central Bank, however, perceived its actions to be exceptional.

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[11] Cf. *Pakiet unijnej pomocy uskrzydlił rynki*, "Dziennik Gazeta Prawna" 13.04.2010, p. A15; *Za długi Grecji zapłacą Niemcy i Francja*, "Dziennik Gazeta Prawna" 13.04.2010, p. A15; *Griechische Finanzkrise*, http: //de.wikipedia.org/wiki, p. 4.

[12] *Cf. Grecja nad przepaścią*, "Gazeta Wyborcza" 28.04.2010, p. 26 (Purchase of trash bonds is a high risk endeavour.)

[13] *Cf.* http://www.welt.de/wirtschaft/article; H.-J. Axt, *op. cit.*, p. 17; *Griechische Finanzkrise*..., p. 4.

[14] *Cf. Internationaler Rettungsplan für Griechenland beschlossen*, "Frankfurter Allgemeine Zeitug" 3.05.2010, p. 1; *Nach Einbindung der Finanzwirtschaft ist Paket für Athen so gut wie geschnürt*, "Frankfurter Allgemeine Zeitung" 3.05.2010, p. 11.

[15] *Cf. Die EZB wird zum Problemfall*, http://www.wiwo.de, p. 2.

[16] *Cf. Notenbanker in Not*. http://www.spiegel.de, p. 1.

ESTABLISHMENT OF THE EUROPEAN STABILISATION MECHANISM AND THE EUROPEAN FINANCIAL STABILITY FACILITY

Despite the adoption of the decision to provide Greece with financial aid, interest rates on loans granted to other Eurozone states with very high budget deficit levels, i.e. Spain, Portugal and Ireland (Table 1), were on the rise. Investors withdrew from those countries and their credit markets like they retreated from Greece. Banks started to limit co-funding, and the inflow of US dollars to European banks decreased. The exchange rate of the euro went down (e.g. in relation to the US dollar).[17]

At first glance it might seem paradoxical that Ireland entered the group of Member States suffering the budget crisis, as it is a highly developed economy. In 2009, its GDP per capita amounted to EUR 35,700 and was 31.3% higher than the Eurozone average.[18] The high budget deficit in Ireland resulted the Irish government's decisions to allocated notable funds to support Irish banks. Irish banks experienced a difficult situation due to the international financial crisis. In that situation, Chancellor Angela Merkel put forward two important proposals. She postulated that Eurozone member states with high debts be excluded from the Monetary Union and demanded that regulations on bankruptcy of Member States be drafted.[19] Those postulates were not supported by other Eurogroup members since many had high debts (see Table 1).

Nevertheless, the heads of state and government of the Eurogroup Member States reached an agreement on the establishment of the European Stability Mechanism (ESM) at their meeting on 9-10 May 2010. They found legal justification in Article 122 of the Treaty on the functioning of the European Union as Paragraph 2 of Article 122 reads: "Where a Member State is in difficulties or is seriously threatened with severe difficulties caused by natural disasters or exceptional occurrences beyond its control, the Council, on a proposal from the Commission, may grant, under certain conditions, Union financial assistance to the Member State concerned".

The ESM involved credits amounting to EUR 750 billion and coming from three sources. The first source was the EU budget and its contribution was to amount to EUR 60 billion. The second were bonds worth EUR 440 billion issued in the capital markets by a special purpose vehicle – the European Financial Stability Facility (EFSF). All Eurogroup members bear joint responsibility for EFSF credits. The third source consisted of IMF loans with value up to EUR 250 billion. Obtaining a loan was dependent on the result of negotiations between the Member State in difficulties and the EU-IMF duo on the implementation of reform programmes, and the interest rate was to be lower than on capital markets.[20]

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[17] *Cf.* H.-J. Axt, *op. cit.*, p. 21; *Europäischer Stabilisierungsmechanismus*, http://de.wikipedia.org.

[18] *Cf.* Eurostat, *Europe in figures. Eurostat yearbook 2011*, p. 46.

[19] *Cf. Europäischer Stabilisierungsmechanismus...*

[20] *Ibid.*

Table 1

Share of budget deficit in national GDPs of Eurogroup members in 2009 and 2010

Country	Year	
	2009	2010
Austria	-3.5	-4.4
Belgium	-6.0	-4.8
Cyprus	-6.0	-6.0
Estonia	-1.7	-1.0
Finland	-2.5	-4.0
France	-7.5	-7.6
Germany	-3.0	-3.3
Greece	-15.4	-9.6
Italy	-5.3	-8.4
Luxembourg	-0.7	-4.2
Malta	-3.8	-3.7
The Netherlands	-5.4	-5.6
Portugal	-9.3	-7.9
Slovakia	-7.9	-5.8
Slovenia	-5.8	-6.8
Spain	-11.1	-9.4

Source: J. Boysen-Hogrefe, D. Groll, B. Van Roye, J. Scheide, *Konjunktur im Euroraum kommt nur schwer in Fahrt*, in: *Weltkonjunktur im Frühjahr 2011*, "Kieler Diskussionsbeiträge" no. 488/489, p.44.

The EFSF was established on 7 June 2010. On the same day, the EFSF entered into a framework agreement with the Eurogroup members regarding the conditions under which it would finance and grant loans. The ratification of the agreement by all Eurogroup members was finalised at the beginning of December 2010. Some difficulties were encountered only by Slovakia. They were overcome after centrist and rightist parties won parliamentary elections there and the government headed by Iveta Radičová was appointed.[21]

[21] *Cf. EFSF Rahmenvertrag zwischen Königreich Belgien, Bundesrepublik Deutschland, Irland, Königreich Spanien, Französische Republik, Italienische Republik, Republik Zypern, Grossherzogtum Luxemburg, Republik Malta, Königreich der Niederlande, Republik Österreich, Portugiesische Republik, Republik Slowenien, Slowakische Republik, Republik Finnland, Hellenische Republik und European Financial Stability Facility. 7 Juni 2010,* p. 2; *Europäischer Stabilitätsmechanismus,* http://de.wikipedia.org.; *Staatsschuldenkrise im Euroraum*, http://de.wikipedia.de; *Parlamentwahl in der Slowakei*. http://de.wikipedia.de

FINANCIAL ASSISTANCE TO MEMBER STATES AFFECTED BY THE PUBLIC FINANCE CRISIS

At the end of November 2010, Ireland was the first Eurogroup member to request financial assistance from the EFSF. It was not capable of repaying its debts as the profitability of the bonds it issued was too high. The European Union and the IMF granted Ireland a credit line of EUR 85 billion of which EUR 35 billion was to be allocated to the banking sector and the remaining EUR 50 billion to meeting the needs of the Irish government. Credit interest amounted to 5.8%. Ireland obtained financial aid on condition that it would undertake actions aimed at facilitating economic growth, introduce budget cuts and increase taxes which would enable reducing its budget deficit from approximately 32% of GDP in 2010 to 3% of GDP in 2015.[22] Portugal filed a request for financial support from the EFSF in April 2011. Portugal's decision resulted from the same reasons that made Ireland seek financial aid. Portugal's negotiations with the EU and the IMF ended in an agreement on the financial aid programme reached at the beginning of May 2011. The agreement foresaw, *inter alia*, that Portugal would get a credit line of EUR 78 billion. The interest on the loans was relatively low. In the case of IMF loans, the interest was to amount to 3.25% in the years 2011-2013 and in the four following years to 4.25%. The cost of the loans obtained from the EU was similar. Portugal undertook to lower its budget deficit from 9.1% of GDP in 2010 to 5.9% in 2011 and 3.0% in 2013. To this end, Portugal was to take numerous actions: raise selected taxes, shorten the period of entitlement to unemployment allowances, reduce public subsidies to private companies and CIT discounts, and privatise selected enterprises.[23]In addition, both Ireland and Portugal were assisted by the European Central Bank which acquired their bonds on the secondary market.[24]

It is worth noting that of the two Member States, only Ireland improved its public finances, which was largely the result of the measures adopted by the European Union. The Irish government intended to become independent of international aid as soon as possible.[25] The improvement of the condition of Irish public finance was brought about not only by the implementation of the agreement with the European Union and the International Monetary Fund, but also resulted from the level of development of the Irish economy. Ireland has a modern economy where services prevail, but at the same time it has a well-developed industrial production sector that generated 23.9% of the country's gross added value in 2009.[26]

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[22] *Cf. EU-Minister beschließen Irland-Hilfe*. Http:://www.manager-magazin.de/politik/welt-wirtschaft, p. 1; *Irland bekommt 85 Milliarden von der EU*. http://www.welt.de, pp. 1-2; *Bruksela łagodzi zasady bailoutu*, "Dziennik. Gazeta Prawna" 7.03.2011, p. A8.

[23] *Cf. 78 Milliarden Euro Notkredite für Portugal*, "Frankfurter Allgemeine Zeitung" 5.05.2011, p. 9; *Lizbona pożycza na niski procent*, "Dziennik. Gazeta Prawna" 6-8.05.2011, p. A9.

[24] *Cf. Bundespräsident Wulff kritisiert EZB wegen Kauf von Staatsanleihen*, http://www.derwesten.de, p. 1.

[25] *Cf. Ihr Krisenländer, schaut auf Irland*, http://www.sueddeutsche.de/wirtschaft, p. 2.

[26] *Cf.* Eurostat, *Europe in figures. Eurostat yearbook 2011*, p. 48.

In Greece, the situation of public finances did not improve in the least. The financial support programme did not help, nor did the assistance given by the European Central Bank. It is worth noting that Greece obtained successive tranches of funds disbursed under the assistance programme after long talks with the so-called troika, i.e. with the representatives of the IMF, the European Commission and the ECB. The Bank mainly purchased Greek bonds.[27]

In Greece, the public finance crisis deepened in the first quarter of 2011. Budget inflows decreased in relation to the first quarter of 2010 by 5.1% (from EUR 12.362 billion to EUR 11.732 billion). At the same time budget expenditure increased by 23.79% (from 16.687 to 20.657 billion). The budget deficit went up by 106.4% in this period (from EUR 4.325 to 8.925 billion). Even if the salaries, benefits and pensions of public servants were reduced to zero, Greece would still suffer budget deficit in the first quarter of 2011. Greece could repay its debts only until July 2011.[28]

That appalling condition of Greek public finances was also a consequence of the acute economic crisis. The pace of economic growth fell by 5.5% in the first quarter of 2011 in comparison to the first quarter of 2010. None of the EU Member States experienced such a low economic growth rate.[29] The economic crisis was caused by reduced national demand and the outdated structure of the Greek economy. National demand decreased due to the implementation of the savings and reforms. The economy structure had a serious disadvantage: the share of industrial production was too low and the food industry had the biggest share. In 2009, Greek industry generated only 13.3% of the national gross added value.[30] Had Greece had a strong industry sector, it would have a positive impact on national demand (by stimulating investment demand) and exports.

As the Greek public finance crisis worsened, in March 2011 the heads of state and government of Eurogroup members decided to lenify the conditions of the support programme. The repayment period was extended from 3.5 to 7.5 years, and interest was reduced from 5.2 to 4.2. At the same time, Greece undertook to take some actions to lower its budget deficit, i.e. to widen its privatisation programme and introduce a debt brake.[31]

The financial standing of Greece was the topic of the Eurogroup finance ministers' meetings held in April and May 2011. Although the ministers were prone to provide Greece with further aid, the meetings did not produce any effects. Most ministers, especially French Minister Christine Lagarde, opposed the mild debt conversion postulated by representatives of Luxembourg and Germany (J.-C. Juncker

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[27] *Cf. Die EZB wird zum Problemfall*, http://www.wiwo.de, p. 2.

[28] *Cf. Fakten zur Griechenland-Debatte*, http:://www.querschuesse.de, p. 2; *Streit über griechische Sparbemühungen wird schärfer*, "Frankfurter Allgemeine Zeitung" 30.05.2011, p. 11.

[29] *Cf.* Eurostat. *Newsrelease, euroindicators nr 127/2011*, http://epp.eurostat.ec.europa.eu

[30] *Cf.* Eurostat, *Europe in figures. Eurostat yearbook 2011*, p. 48.

[31] *Cf. Euro-Rettungsfonds wird ausgeweitet*, http://www.wiwo.de, p. 1 and p. 2; *Pakt dla euro w wersji light*, "Gazeta Wyborcza" 14.03.2011, p. 25.

and W. Schäuble). That solution was also criticised by the representative of the European Central Bank. The French government and the ECB believed that rating agencies would consider the shifts in maturity dates to be a sign of bankruptcy with consequences difficult to predict. Wolfgang Schäuble proposed that Greek debts should be reduced and costs borne by private creditors. That suggestion was also criticised by most ministers. It was debated whether it was reasonable to adopt a new bailout programme that would provide Greece with further credits.[32]

Those differences in opinions had an impact on the Eurogroup finance ministers' meeting of 14 June 2011 in Brussels. An important step toward overcoming disagreements was the compromise reached by Chancellor Merkel and President Sarkozy in Berlin. They arrived at a conclusion that the participation of private creditors in saving Greece should be voluntary.[33] At the next Eurogroup meeting held on 20 June 2011 in Luxembourg, Eurogroup finance ministers reached some agreement on the next bailout programme for Greece. They decided that it would be financed from public and private sources. Creditors would (voluntarily) invest the income on expiring bonds in new Greek debt securities.[34]

The new (second) bailout programme for Greece was agreed on 21 July 2011 at the meeting of heads of state and government of the Eurogroup members in Brussels. It covered the years 2011-2014 and amounted to EUR 109 billion in total. That amount was to be disbursed by the EFSF and the IMF. EUR 34 billion was to meet the need to refinance the Greek debt, EUR 20 billion to increase the capital of Greek banks, EUR 35 billion to pay risk insurance as private creditors were to join the programme, and EUR 20 billion to buy Greek loans from private creditors.[35]

The participation of private creditors in this programme was to be voluntary. They could sell Greek loans or accept extension of the maturity date of securities. The loans would be purchased by EFSF at market price decreased by a specified sum. According to calculations of summit participants, private creditors would incur losses of EUR 12.6 billion in total. The banks announced that they would trade matured Greek loans for new loans with very distant maturity dates and a high degree of safety.[36]

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[32] *Cf. Sanfte Umschuldung für Griechenland rückt näher*, "Frankfurter Allgemeine Zeitung" 18.05.2011, p. 9; *EU zörgert mit weiteren Hilfen für Griechenland*, "Frankfurter Allgemeine Zeitung" 17.05.2011; *EU plant sanfte Umschuldung für Griechenland*, "Frankfurter Allgemeine Zeitung" 18.05.2011, p. 1; *Grecja się pali. Czy także zatonie?*, "Dziennik. Gazeta Prawna" 16.060.2011, p. A7.

[33] *Cf. Euro-Staaten ringen um Hilfen für Griechenland*, "Frankfurter Allgemeine Zeitung" 15.06.2011, p. 1; *Private Gläubiger sollen freiwillig Griechenland retten helfen müssen*, "Frankfurter Allgemeine Zeitung" 18.06.2011, p. 1.

[34] *Cf. Griechenland kann auf Abwendung des Staatsbankrotts hoffen*, "Frankfurter Allgemeine Zeitung" 21.06.2011, p. 1; *UE mówi jednym głosem. Będzie pomoc dla Grecji*, http://wiadomości.onet.pl, p. 1.

[35] *Cf.* A. Belke, Ch. Dreger, *Das zweite Rettungspaket für Griechenland und Perspektiven für die Europäische Zentralbank*, "Integration" no. 3/2011.

[36] *Cf.* A. Belke, Ch. Dreger, *op. cit.*, p. 215 and p. 216.

The programme also contained a series of provisions that were to streamline the servicing of the debt by Greece. Those provisions also applied to Ireland and Portugal. In result, the maturity date of future EFSF loans was extended from 7.5 to at least 15 years and at most 30 years, with a 10-year grace period. Interest on the loans was to be 3.5%. The credits were to be granted on very friendly terms.[37]

At the summit held in Brussels on 26-27 October 2011, the heads of state and government of Member States belonging to the euro area revised the second Greek bailout adopted in July 2011. The funds were not to exceed EUR 100 billion in total. It was decided that Greece's debt would be reduced by 50%, which was a (potentially) significant factor allowing Greece to overcome its public finance crisis in the future. That was why the arrangements were praised by Prime Minister George Papandreou.[38] They enabled the simultaneous launch of negotiations between the Greek government and the Institute of International Finance (IIF) that represented private creditors. The talks were not easy. The issue of the percentage by which the Greek debt should be reduced was disputed as well as the interest rate on loans granted by private creditors. According to the Greek government, the interest rate should amount to about 4% while the private creditors demanded 5%.[39] The agreement reached specified that the Greek debt held by private creditors would be reduced by 53.5%, and the interest rate would not exceed 3.65%.

The EU, the ECB and the IMF announced that the final adoption of the new bailout programme was dependant on whether the Greek parliament would pass the reform and savings package. The package was adopted by Greeks on 13 February 2012. Finance ministers of the Eurogroup member states could thus decide in favour of the second bailout programme for Greece at their meeting on 20-21 February 2012. The financial aid was to amount to EUR 165 billion of which 35 billion was the money transferred in the first bailout programme for Greece. It was decided that the second programme would be financed by the EFSF first and from mid-2012 by the ESM. Some funds were to be provided by the IMF. However, the amount of the IMF's contribution was not specified. In the statement by Eurogroup finance ministers the contribution of the IMF to the implementation of the programme was mentioned as notable.[40]

It was decided to allocate EUR 85 billion, of the EUR 165 billion fund, to strengthening the capital of Greek banks, EUR 50 billion to the service of the debt, and the remaining EUR 30 billion to insure loan exchange.[41] Eurogroup finance ministers reg-

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[37] *Ibid.*, p. 215.

[38] *Cf.* C. Colombier, *Zu wenig Europa im Reformpaket des Europäischen Stabilitäts- und Wachstumspakts*. "Die Volkswirtschaft. Das Magazin für Wirtschaftspolitik" no. 11/2011, p. 5; *Schuldenschnitt: Geschenk von den oder für die Banken*, http://www.abendblatt.de, p. 1.

[39] Cf. *Ateny bliżej bankructwa. Przerwa w negocjacjach z bankami*, "Gazeta Wyborcza" 14-15.01.2012, p. 8.

[40] Cf. *Parlament billigt Sparprogramm*, www.faz.net; *Die Griechenland-Hilfe im Überblick*, http://www.faz.net, pp. 1, 3 and 4.

[41] Cf. *Die Griechenland-Hilfe im Überblick...*, pp. 3 and 4.

ulated the decrease of the Greek debt in accordance with the agreement reached between the Greek government and the IIF. Private creditors were to renounce 53.5% of their receivables from Greece. That meant that Greece's debt would decrease by EUR 107 billion (from EUR 350 billion to EUR 243 billion). In return for the remaining receivables, private creditors would receive short-term loans of EUR 93 billion payable by the EFSF, as well as new Greek bonds of EUR 63 billion. The maturity of the latter was to amount to 30 years.[42]

Eurogroup finance ministers obliged Greece to adopt several parliamentary acts by the end of February 2012. Those acts were to come into force in the same year. They were to cover cuts in healthcare expenditure, the minimum wage cut, cuts in state spending and employment in public services, as well as a pension reform and cuts in various subsidies.[43]

ESTABLISHMENT OF FURTHER FACILITIES AIMED AT COUNTERACTING THE SOVEREIGN-DEBT CRISIS

Solutions adopted at the beginning of May 2010 were but temporary measures aimed at reducing the already apparent public debt in Eurozone member states. That is why it proved necessary to extend the range of tools for combating the debt and to establish permanent facilities. Thus the European Council, at its meeting held on 28-29 November 2010, pointed to the need for the introduction of a permanent anti-crisis mechanism that would guarantee financial stability of the entire euro area and to the need to introduce restriction to the Stability and Growth Pact. At the same time, Eurogroup ministers, in their statement of 28 November 2010, specified general principles of the functioning of such a mechanism. That statement was approved by the European Council.[44]

The mechanism would be based on the EFSF and would provide financial support to Eurozone member states that meet strict requirements compliant with the regulations on the Instrument. The task of the mechanism would be to prevent and significantly reduce the likelihood of (financial) crisis in the future. The loans granted would be favourable and second to IMF loans in terms of their status. The Member State would receive financial aid if it implemented the strict programme for the improvement of its economic and fiscal situation, and the Commission and the IMF, in cooperation with the European Central Bank, performed a thorough analysis of its capacity to service its debt. Eurogroup ministers were to take the decision on granting the financial aid unanimously.[45]

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[42] Cf. *Die Griechenland-Hilfe im Überblick...*, pp. 1 and 2; *Banken müssen für Griechenland stärker bluten*, http://www.faz.net, p. 2.

[43] Cf. *Die Griechenland-Hilfe im Überblick...*, p. 4.

[44] *Cf.* European Council, 16-17 December 2010, *Conclusions*, pp. 2 and 8; *So soll der Euro gerettet*, Http://www.ftd.de/politik/europa

[45] *Cf.* European Council, 16-17 December 2010, pp. 8 and 9 (The Eurogroup is a group within which Eurozone members coordinate their economic policies).

On 15 December 2010 at the Bundestag, Chancellor Merkel outlined conditions that the new mechanism would have to meet. The number of those conditions was higher than that the number of conditions in the statement of the Eurogroup ministers. It would be an (anti-) crisis mechanism for the Eurozone states so their sovereignty rights would not be transferred to the European Union. Financial aid would be granted if the entire Eurozone was jeopardised. The IMF would participate in supporting Member States experiencing financial difficulties. Private creditors would participate (on a case-by-case basis) in counteracting crisis situations and if any Member State was threatened by insolvency, they would be obliged to make a financial contribution. Starting from 2013, clauses concerning creditors' participation were to be included in agreements on all new loans taken by Member States in trouble.[46]

Once Member States agreed on the need to establish a permanent anti-crisis mechanism, the European Council (16-17 December 2010) could call on the Eurogroup ministers and Commission to complete their work on an international agreement by March 2011. The agreement was to be the basis for the new mechanism. It was agreed that its introduction would require an amendment to the Treaty on the functioning of the European Union and that the mechanism would replace the EFSF by mid-2013.[47]

To the end of 2010, methods of combating the financial crisis started to be disputed by some Member States. Belgium spoke in favour of increasing the volume of EFSF credit lines. In fact, the volume already amounted to EUR 250 billion as it was necessary to provide credit insurance. Most Member States were, however, against any increase in the EFSF volume, which was still apparent at the summit held on 16-17 December 2010.[48] Luxembourg and Italy were for the employment of Eurobonds, i.e. bonds jointly issued by a European debt agency that would allow for covering in full or in part the demand of Eurozone members for funds. Eurobonds would be beneficial especially for countries with low ratings, as the interest rate would be based on the average rating of all EU Member States.[49]

Chancellor Merkel opposed solutions supported by Belgium, Luxembourg and Italy. She believed that the founding treaties would not allow for Eurobonds. She also argued that the flat interest (on Eurobonds) for all Eurozone members would not

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[46] *Cf. Merkel legt Neun-Punkte-Plan vor*, http://www.faz.net, p. 4; *Regierungserklärung von Bundeskanzlerin Merkel zum Europäischen Rat am 16. und 17. Dezember in Brüssel*, http://www.bundesregierung.de, pp. 1-2.

[47] *Cf. European Council*, 16-17 December 2010, *Conclusions*, p. 1 and p. 2; *"PermanenterKrisenmechanismus" ab 2013*, http://www.faz.net, pp. 1-2.

[48] *Cf. Merkel gegen neue Notmassnahmen*, http://manager-magazin.de; *"Permanenter Krisenmechanismus ab 2013...*, pp. 1-2; *Mehr Geld, weniger Zinsen*, "Frankfurter Allgemeine Zeitung" no. 61, 14.03.2011, p. 14.

[49] *Cf. Merkel gegen neue Notmassnahmen*, http://manager-magazin.de; *Euro-Anleihen: Darumgeht es*, http://www.heute.de/ZDFheute.

persuade Member States to implement savings and painful reforms.[50] At the meeting of the European Council held on 16-17 December 2010, also France, Sweden and Austria opposed Eurobonds.[51]

The position of the German Chancellor on Eurobonds was fiercely attacked by the President of the Eurogroup, Luxembourg Prime Minister Jean-Claude Juncker. He accused Angela Merkel of "unrefined thinking" and "non-European conduct".[52]

At the turn of 2011, Germany proposed "a pact for competitiveness". The German government wanted to use the pact to overcome (in the long-term), the financial crisis in the Eurozone. The pact was to introduce "a debt brake" in Member States belonging to the euro area. That brake was to be modelled on Germany's anti-crisis instrument. Other measures involved adjustment of retirement age to demographic data and freezing the automatic indexation of salaries against inflation. Other goals included mutual recognition of school and professional certificates, establishment of national banking systems of combating the crisis and uniform CIT. The effects of the implementation of the pact would be evaluated by means of objective criteria, i.e. labour unit cost, stability of public finance and minimum rate of investment in R&D, education and infrastructure. The German government foresaw the application of financial sanctions on Member States that would failed to comply with the provisions of the pact. According to the Chancellor, the legal basis for sanctions was Article 136 of the Treaty on the functioning of the European Union. Under this Article, EU Member States could decide whether a given Member State pursued wrong policies and should be fined. In order to prevent further divisions in the EU, the German government invited also non-Eurozone members to join the pact. Under the pact, the economic policies of Member States would be coordinated to an extent. Merkel called the above "an economic government".[53]

It is worth noting at this point that, in Germany, the pact did not meet with full support of the ruling coalition. FDP politicians were against the introduction of the common CIT which, according to them, would lead to the end of competitiveness in the area of taxes. President of the European Council Herman Van Rompuy and, to a large extent, Nicolas Sarkozy opted for the adoption of the pact.[54]

At the beginning of 2011, the unwillingness of most Member States to increase the volume of EFSF credits waned. Germany also altered its position, whereby Minister Wolfgang Schäuble insisted on a solution opposite to that promoted by President of the European Commission José Manuel Barroso, i.e. to link the changes to

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[50] *Cf. Merkel gegen neue Notmassnahmen*. http://manager-magazin.de

[51] *Cf. Merkel sieht EU auf dem Weg zu gemeinsamer Wirtschaftsregierung*, http://www.faz.net, p. 2.

[52] *Cf. Merkel legt Neun-Punkte-Plan vor*..., p. 3 and p. 4.

[53] *Cf. Frau Merkel serviert schwere Kost*, "Die Welt", 4.02.2011, p. 4; *Merkel ängstigt Europa Schwache*, "Die Welt" 5.02.2011, p. 9; *Deutschland will bald Beschluss zu EU-Koordination*, "Frankfurter Allgemeine Zeitung" no. 26, 1.02.2011, p. 13; *Das große Euro-Tohuwabohu*, "Frankfurter Allgemeine Zeitung" no. 26, 1.02.2011, p. 13.

[54] *Cf. Deutschland will bald Beschluss zu EU-Koordination*..., p. 13.

the EFSF with other planned reforms of the currency mechanism.[55] At the same time, Schäuble opposed the tendency of some Member States to pass the costs of increasing EFSF credit capacity to the Federal Republic of Germany and other EU Member States of highest creditworthiness such as Austria, Finland, France, the Netherlands and Luxembourg.[56]

On 4 February 2011, another meeting of the European Council was held. It was dedicated to the struggle against the sovereign-debt crisis. The participants agreed on numerous projects constituting elements of a large reform package. The proposals included, *inter alia*, the drafting of specific proposals by the Eurogroup aimed at strengthening the EFSF, work on designing operations of the (permanent) European Stability Mechanism and the pact for competitiveness.[57]

The proposal of the pact was presented by the German Chancellor in agreement with President Sarkozy. At the meeting, some of the proposed provisions of the pact were heavily criticised. The most criticised provisions included e.g. the postulated harmonisation of the CIT rate. Cyprus, Ireland, Slovakia and the Netherlands were against this solution.[58] Cyprus, Ireland and Slovakia had low CIT rates.[59] Belgium and Luxembourg opposed the suggested abandonment of adjusting salary scales for inflation. In Belgium, salaries rose more slowly than labour effectiveness. That is why the cancellation of salary indexation had no economic grounds. Luxembourg politicians doubted whether that solution would improve the economic situation in their country.[60]

Austria and the Netherlands were against the EU regulating retirement age. Austria justified its position by stating that its economic situation was good.[61] Most Member States frowned at Germany's postulate to introduce debt anchors to national constitutions. EU institutions criticised EU Member States for attempting to coordinate their economic policies practically excluding the European Commission and the European Parliament from this process.[62]

Eurogroup finance ministers managed to reach an agreement on some elements of the permanent ESM formula at the meeting of 15 February 2011. They decided that their member States would contribute EUR 500 billion to the mechanism. Ad-

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[55] *Cf. Finanzminister wollen Rettungsschirm erweitern*, "Frankfurter Allgemeine Zeitung" no. 14, 18.01.2011, p. 2.

[56] *Cf. Finanzminister Schäuble gegen einseitige Belastung für Deutschland*, "Frankfurter Allgemeine Zeitung" no. 15, 19.01.2011, p. 9.

[57] *Cf.* European Council, *Conclusions*, 4.02.2011, pp. 12-13.

[58] *Cf. Jagd auf den Yeti*, "Der Spiegel" 14.02.2011, p. 25; *Szczyt państw strefy euro przypomni o jej kłopotach*, "Rzeczpospolita" 5-6.03.2011, p. B3; *Merkel ängstigt Europa Schwache...*, p. 9.

[59] In Cyprus, the CIT rate was 10%, in Ireland 12.5%, and in Slovakia 19%. *Cf. Firma w UE*, http://www.ck.agh.edu.pl.

[60] *Cf. Jagd auf den Yeti...*, 14.02.2011, p. 25; *Niemcy są pewni, że potrafią wypełnić pustkę po Brukseli*, "Dziennik Gazeta Prawna" 10.03.2011, p. A11; *Ein Pakt für Wettbewerbsfähigkeit*, http://www.ksta.de, p. 2.

[61] *Cf. Merkel ängstigt Europa Schwache...*, p. 9.

[62] *Cf. Frau Merkel serviert schwere Kost...*, p. 4.

ditionally, the IMF was to provide EU 250 billion, and non-euro EU Member States were to make voluntary contributions.[63]

In response to the strong criticism of the pact on competitiveness expressed by some Member States, President of the European Commission José Manuel Barroso and President of the European Council Herman Van Rompuy prepared a compromise document consulted with Eurozone members.

The authors of the document refused to abandon salary indexation and to mutually recognise school and professional certificates. At the same time they postulated that Member States should be capable of implementing the remaining proposals of Chancellor Merkel (e.g. regarding retirement age) in the form of declarations of intent. As a result, German proposals were notably weakened. According to José Manuel Barroso and Herman Van Rompuy, Member States were to discuss the implementation of their obligations at one of the annual summits of heads of state and government. The document also contained recommendations on the pay policy in the public sector and improvements in pay indexation where it was applied.[64]

The "Pact for the Euro", drafted to a large extent on the basis of the document of compromise delivered by the two EU politicians, was adopted without much dispute at the European Council meeting of 11 March 2011. The principles and objectives of the Pact implementation were described in the Pact. The main goals were to foster competitiveness and employment, contribute further to the sustainability of public finances and to reinforce financial stability. When formulating the objectives, reforms which were priorities were pointed out. It was decided, after the document drafted by José Manuel Barroso and Herman Van Rompuy, that each year Eurozone members would decide on concrete actions on the European Council's forum.[65]

At the meeting held on 11 March 2011, the heads of state and government of the euro area devoted much time to discussing the (permanent) ESM and EFSF. They drew many important conclusions. They agreed that the ESM would be capable of granting loans of EUR 500 billion in total and that financial aid would be provided at the request of a Eurogroup member on condition that such an intervention would be assessed as necessary for the stability of the entire Eurozone. The decision on ensuring financial aid would be taken unanimously, and financial aid would be dependent on close adherence to a designed macroeconomic adjustment programme. Eurozone heads of state and government also decided that the EFSF would achieve its full capacity to grant loans of EUR 440 billion in total upon the launch of the (permanent) EMS. That meant that they consented to the granting of additional warranties securing credits. Only Finland opposed those decisions.[66]

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[63] *Cf. Schäuble: höhere Belastung durch Euro-Krisenfonds*, "Frankfurter Allgemeine Zeitung" no. 39, 16.02.2011, p. 9.

[64] *Cf. Merkels Pakt ist kein Pakt mehr*, "Frankfurter Allgemeine Zeitung" no. 51, 2.03.2011, p. 12.

[65] *Cf. Kritik am Euro-Kompromiss aus Koalitionsfraktionen*, "Frankfurter Allgemeine Zeitung" no. 61, 14.03.2011, p. 1; *Conclusions of Eurozone heads of governments and stated of 11 March 2011*, pp. 5-12.

[66] *Cf. Konkluzje szefów państw lub rządów strefy euro...*, pp. 4-5; *Der endgültige Euro-Krisenfonds steht*, "Frankfurter Allgemeine Zeitung" nr 69, 23.03.2011, s. 10.

Member States kept working on the restricting conditions and measures of the Stability and Growth Pact. EU finance ministers made the decision at their meeting on 15 March 2011. As followed from the adopted provisions, Member States would be punished not only for budget deficits, but also for incurring debt and negative turnout balance on current accounts. Member States with a debt-to-GDP ratio exceeding 60% would be obliged to reduce the difference between the debt and the reference value by 1/20 every year. Should the European Commission decide that the negative turnout balance on current accounts was too high, the Commission would be entitled to launch appropriate proceedings.[67]

Member States subjected to excessive deficit, debt or negative debit balance procedures would have to submit a deposit amounting to 0.2% of their GDP. If a Member State fails to improve its financial standing, the deposit will be turned into a fine. It would be difficult for Member States to avoid sanctions, as they could only be waived by a resolution of the Council of the European Union passed by a majority of 2/3 of votes.[68]

While debating the (permanent) ESM, the "key" according to which Eurozone members would participate in the financing of that mechanism was a highly controversial issue. According to Minister Schäuble, Slovakia and four other Eastern European Member States demanded a different division of financial obligations, arguing that the criteria preferred by the German Minister would be an excessive financial load.[69]

Germany decided to make concessions which allowed to reach an agreement on ESM regulations at the meeting of Eurogroup finance ministers on 22 March 2011.[70] Finance ministers considered the new mechanism to be a new international financial organisation modelled after the International Monetary Fund.

It was decided that the mechanism would dispose of funds amounting to EUR 700 billion, EUR 80 billion of which would be contributed by Member States and constitute its share capital. The remaining EUR 620 billion would encompass warranties of Member States and capital on demand. Generally, contributions to the ESM were to be calculated according to the principles adopted by the ECB in regard to shares in its basic capital. In regard to Central and Eastern European Member States, the strength of their economies would be taken into account as otherwise contributions of these countries would be too high. Half of the share capital was to be contributed in 2013. The last provision was the outcome of a compromise negotiated by Minister Schäuble. The mechanism would have the capacity to grant

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[67] *Cf. EU-Stabilitätspakt wird schärfer*, http://www.faz.net

[68] *Cf. EU-Finanzminister billigen Reform*, http:://www.manager-magazin.de/politik; *EU-Finanzminister beschließen strengeren Stabilitätspakt*, http://www.euractiv.de

[69] *Cf. EU streitet über Hilfsfonds und Irland*, "Frankfurter Allgemeine Zeitung" no. 68, of 22.03.2011, p. 11.

[70] *Cf. Der endgültige Euro-Krisenfonds steht...*, p. 10.

credits of EUR 500 billion in total and it would aim to strengthen its activities by involving the International Monetary Fund. Eurozone members experiencing financial difficulties would have the possibility of using credits, if that was necessary for maintaining the financial stability of the entire euro area. The debtor would have to meet rigid requirements on economic and fiscal policies. Interest on the loans would be similar to that applied to IMF bailout loans, i.e. it would be lower than the EFSF interest. The ESM would enjoy privileged status in relation to all other creditors, i.e. its receivables would have to be satisfied first.[71]

At the meeting of 24-25 March 2011, the European Council adopted an action package aimed at overcoming the financial crisis in the Eurozone. The Pact for the Euro was included as some non-euro Member States entered into that agreement, i.e. Bulgaria, Denmark, Lithuania, Latvia, Poland and Romania. For this reason the Pact was named the "Euro Plus Pact".[72]

The effectiveness of the Pact is dependent on the nature of actions it will promote. Of course, the Pact should support real reforms that lead to the rationalisation of state expenditure and elimination of obstacles to economic growth.

Another part of the package was constituted by the ESM regulations agreed upon by Eurogroup finance ministers, as well as the provisions adopted by heads of state and government on increasing the EFSF's lending capacity to EUR 440 billion. The European Council, however, introduced a change to these regulations. Its amendment concerned the deadline of making cash contributions to the mechanism. They were to be made annually for five years, starting from 2013. Angela Merkel pressed for that change and by doing so, she rejected the abovementioned compromise negotiated by Minister Schäuble. The decision of German Chancellor was motivated by the position of the CDU/CSU and the FDP parliamentary groups and economic conditionalities. The adopted solution could lower a new net debt of the Federal Republic of Germany.[73]

Owing to the positions of the Federal Republic of Germany and Finland, it was not agreed when the EFSF lending capacity would be increased. Germany intended to delay its decision on additional guarantees, and Finland was still against their granting.[74]

As mentioned above, the European Council agreed at its meeting of December 2010 that the establishment of the ESM would require amending the Treaty on the functioning of the European Union. In consequence, at the meeting held on 24-25 March 2011, the Council took the decision on adding the following paragraph to Article 136 of the Treaty: "The Member States whose currency is the euro may

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[71] *Cf. Neugestaltung der Währungsunion*, "Frankfurter Allgemeine Zeitung" no. 72, 26.03.2011, p. 11; *Der endgültige Euro-Krisenfonds steht*..., p. 10.

[72] *Cf. Neugestaltung der Währungsunion*..., p. 11.

[73] *Cf. ibid*., p. 11, 6.

[74] *Cf. ibid*.; *Der endgültige Euro-Krisenfonds steht*..., p. 10.

establish a stability mechanism to be activated if indispensable to safeguard the stability of the euro area as a whole. The granting of any required financial assistance under the mechanism will be made subject to strict conditionality". The decision was to enter into force on 1 January 2013, on condition that notifications of ratification were received from all EU Member States. If that was not the case before 1 January 2013, it was to enter into force on the first day of the month following the receipt of the last of the notifications.[75]

The European Union decided – in compliance with the resolutions of the finance ministers of EU Member States – to tighten the Stability and Growth Pact. In the end, this was regulated by five regulations and one directive, i.e. by the so-called six-pack, adopted by the Parliament and EU Council at the turn of October 2011. All those legal acts entered into force on 13 December 2011.[76]

Both preventive and corrective/repressive arm regulations were made stricter. Provisions on the implementation of sanctions were introduced to the preventive arm. Sanctions were to be imposed when a given Member State failed to specify its medium-term budgetary objective. The ECOFIN adopted an appropriate resolution based on the recommendation of the European Commission by a qualified majority of votes. The penalised Member State would be obliged to submit an interest-bearing deposit amounting to 0.2% of its GDP. If a Member State provides false data on its budget deficit and debt, it would be fined an additional sanction of 0.2% of GDP.[77]

In the preventive arm, the significance of the European Commission in the decision-making process was increased. The EU Council received the power to lift the sanctions, i.e. cancel the implementation of Commission recommendations, but only if such a decision was adopted by an ordinary majority of votes.[78]

In the repressive arm, the list of cases in which the anti-deficit procedure applies was broadened. The anti-deficit procedure was to be launched if the debt of a given EU Member State exceeded 60% of GDP or was not being reduced fast enough. The anti-deficit procedure was shortened and the scale of applied sanctions was increased. Shortening the procedure was possible with rising the role of the Commission. Sanctions against a Member State that violated the binding provisions were to be applied automatically in line with the recommendations of the Commission, unless the EU Council passed a veto by a qualified majority of votes. Thus sanctions could be called "quasi-automatic". The imposed fine was a non-interest-bearing deposit amounting to 0.2% of GDP. If the Member State failed to adhere to the binding

[75] *Cf. Neugestaltung der Währungsunion...*, p. 11; European Council, 24-25 March 2011, *Conclusions*,

[76] *Cf. Neugestaltung der Währungsunion...*, p. 11; *Der endgültige Euro-Krisenfonds steht...*, p. 10.

[77] *Cf.* European Council, 24-25 March 2011, Conclusions, p. 6; *European Council Decision of 25 March 2011 amending Article 136 of the Treaty on the Functioning of the European Union with regard to a stability mechanism for Member States whose currency is the euro* (2011/199/EU). "Official Journal of the European Union" 6.04.2011, L91, p. 2.

[78] *Cf. Six-Pack tritt am Dienstag in Kraft*, http://derstandard.at.

provisions again, the deposit was to be converted into a fine. That fine would be higher if the Member State failed to comply with the recommendations of the Commission.[79]

Under the legal acts passed by the European Parliament and Council, the supervision of the macroeconomic development of EU Member States was increased, which was aimed at detecting problems as fast as possible and correcting the "harmful" macroeconomic instabilities and differences in competitiveness levels. The ECOFIN monitors the situation and is authorised, at the request of the European Commission, to provide a Member State with recommendations on how to overcome current assets imbalances. If such recommendations are not implemented, their recipient is obliged to submit an interest-bearing deposit. If the Member State continued to sabotage the activities suggested by the Council, the deposit would be converted into a fine of 0.1% of GDP.

It should be underlined that in such a case the sanctions are also quasi-automatic. The recommendations are drafted in accordance with the request of the European Commission, unless the ECOFIN rejects the Commission's request with a qualified majority of votes. The introduction of quasi-automatic sanctions has increased the effectiveness of the Commission's actions.

When adopting the six-pack, the EU Council and the European Parliament followed the regulations adopted by EU finance ministers on 15 March 2011. Some issues, however, sparked serious controversies. These were the issue of applying quasi-automatic sanctions in the preventive arm and the elimination of positive (surplus) current account balances. France was particularly not in favour of such penalties, and the Federal Republic of Germany also was not too happy with them. Germany, similarly as the European Parliament, did not opt for the elimination of positive current account balances. France had a contrary opinion on that issue.[80] The position of Germany is fully understandable – its economy is characterised by outstanding international competitiveness. At the same time, Germany's position is compliant with the basic principle of capitalism, i.e. the principle of free market competition.

Finally, a compromise was reached. France and Germany pushed through their postulates on the nature of the sanctions specified in the preventive arm of the Pact, and at the same time France revised its position concerning the issue of positive current account balance.[81]

THE DEEPENING PUBLIC FINANCE CRISIS IN THE EUROZONE AND ITS CONSEQUENCES

In the second half of 2011, the public finance crisis hit Italy while the economic situation in Spain deteriorated. The debts of both Member States grew systematically, which induced rating agencies to lower their creditworthiness. Standard&Poor's and Fitch did so at the end of September and at the beginning of 2011. In consequence,

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[79] *Cf.* C. Colombier, *op. cit*., p. 6.

[80] *Ibid*., p. 6.

[81] *Ibid*., pp. 5-6.

the interest on Spanish and Italian bonds went up notably. To provide an example: in November 2011, the interest on Spanish treasury bonds was higher than 6%.[82]

As the public finance crisis in the Eurozone worsened, Germany and France put forward a few significant (from the perspective of combating such crises) proposals at the European Council meeting of 8-9 December 2011. It was the Federal Republic of Germany which had the casting vote on their wording. Both Member States proposed the application of automatic sanctions to EU Member States that fail to keep their deficits below 3% of GDP. They also postulated the introduction of debt brakes to the national legislature of Member States, and demanded that the European Court of Justice monitors compliance with such provisions. France and Germany believed that for those proposals to enter into force, it was necessary to amend the Treaty on the functioning of the European Union. They expressed their support for the launch of the ESM already at the end of 2012.[83]

The Franco-German postulates did not touch upon the issue of introducing Eurobonds, which was favoured by France. Germany was strongly against this solution.[84] At the mentioned meeting, most Member States did not share France and Germany's opinion on the amendment of the Treaty but supported the position of the President of the European Council, Herman Van Rompuy, who suggested changing only the Protocol to the EU Treaty. The latter solution would take less time to complete and would not require ratification.[85] Finally, it was decided to enter into an intergovernmental agreement as the Member States would not consent to the terms put forward by the UK. The UK made its consent to amending the Treaty (as well as the Protocol to the Treaty) dependent on the adoption of a regulation that would exempt the UK from complying with some EU regulations on the financial market.[86]

Eurozone heads of state and government decided that the provisions on the introduction of new financial regulations to national constitutions would be included in the intergovernmental agreement. The annual structural budget deficit was not to exceed 0.5% of nominal gross domestic product. If a Member State violated that principle, the European Commission would specify the date by which the Member State should reach the admissible deficit level.[87]

At the meeting other details of the contents of the intergovernmental agreement were agreed upon. The agreement stipulated that any violation of the Stability and Growth Pact would incite specific actions unless Eurozone members vetoed

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[82] *Cf. Durchbruch bei Verhandlungen über Stabilitätspakt*, "Frankfurter Allgemeine Zeitung" 8.09.2011, p. 11.

[83] *Ibid.*

[84] *Cf. Italien und Spanien werden in die Pleite gestuft*, http://www.heise.de; *Fitch stuft Kreditwürdigkeit Italiens und Spaniens*, http://de.nachrichten.yahoo.com; *Wraca zaufanie do Włoch i Hiszpanii*, "Dziennik. Gazeta Prawna" 13-15.01.2012, p. A5.

[85] *Cf. Merkel und Sarkozy Vertragsänderung im März 2012*, http:://www.faz.net.

[86] *Ibid.*

[87] *Cf.* Sarkozy: *Wir brauchen mehr Disziplin und gemeinsames Regieren*, "Frankfurter Allgemeine Zeitung" 9.12.2011, p. 1.

such a decision by a qualified majority of votes. The agreement would also contain the principle that Member States with debt exceeding 60% of GDP were obliged to gradually decrease their debt volume. Each and every year, such Member States would have to lower the amount of debt exceeding the admissible level by 5%.[88]

Eurozone heads of state and government undertook to support the introduction of the ESM already in July 2012. They decided, together with their peers representing the remaining EU Member States, to discuss the issue and confirm their contribution of additional funds amounting to EUR 200 billion in the form of bilateral loans to the IMF within ten days.[89] The objective of the latter solution was to increase the role of the Fund in the struggle against the Eurozone public finance crisis. They agreed that the EFSF capacity to grant loans would be tripled (via leverage) to about EUR 750 billion.[90]

Negotiations on the contents of the intergovernmental agreement, i.e. the Fiscal Compact, were conducted at a fast pace. Before the European Council meeting of 30-31 January 2012, the issue of whether non-euro EU Member States would participate in the implementation of the Compact was still particularly controversial. France opposed their participation while Poland, supported by e.g. the European Central Bank, was an ardent supporter of this solution.[91] The Polish government made the undoubtedly correct assumption that if only 17 Eurozone members participated in the Fiscal Stability Treaty, then the continent would be divided into a Europe of "two speeds".

At the meeting of the European Council in the end of January 2011, the participants managed to end the dispute and reach a compromise. Generally, Eurozone Member States were to deliberate on their own, and non-euro EU Member States had the right to participate in crucial meetings on e.g. a global strategy of the Monetary Union, competitiveness of EU Member States and principles of the Fiscal Compact. In result, the European Council could write down the international agreement . At the summit, it was also agreed that the Pact would enter into force if it was ratified by twelve Member States. The Czech Republic and the UK did not intend to participate in the Compact.[92] At the meeting of the European Council, the agreement on the establishment of the (permanent) European Stability Mechanism was also written down.[93]

The Fiscal Pact was signed at the Brussels summit on 2 March 2012 by 25 EU Member States (except for the Czech Republic and the UK).[94]

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88 *Cf. Ein Europa der Geschwindigkeit*, "Frankfurter Allgemeine Zeitung" 10.12.2011, p. 2.

89 *Cf. Merkel: Gipfel ist der Durchbruch zu einer Stabilitätsunion*, "Frankfurter Allgemeine Zeitung" 10.12.2011, p. 1; European Council, *Statement by the Euro area Heads of State or Government*, Brussels, 9 December 2011, p. 3.

90 *Cf.* European Council, *Statement*..., p. 3; *"Durchbruch zu Stabilitätsunion"*, "Frankfurter Allgemeine Zeitung" 10.12.2011, p. 2.

91 *Cf.* European Council, *Statement*..., pp. 5 and 6.

92 *Cf. Was auf dem Gipfel beschlossen wurde*, http://www.spiegel.de, p. 1.

93 *Cf. Union streitet vor dem EU-Gipfel über den Inhalt des Fiskalpakts*, "Frankfurter Allgemeine Zeitung" 30.01.2012, p. 11.

94 *Cf. EU-Gipfel beschließt Fiskalpakt und ESM-Vertrag*, http://www.faz.net, pp. 1 and 2.

CONCLUSIONS

The Eurozone is troubled with the public finance crisis. The crisis first surfaced in Greece, i.e. at the beginning of the 21st century. In the years 2010 and 2011, it affected more EU Member States (Ireland, Portugal, Spain and Italy).

Many collective instruments were introduced in the European Union to combat the crisis. These included temporary and permanent measures. The former embraced financial aid programmes for Greece, the European Stability Mechanism and the purchase of loans issued by Eurozone states struggling with the sovereign-debt crisis by the ECB, while the latter included the Euro Plus Pact, stricter provisions of the Stability and Growth Pact and the Fiscal Compact. In the future, the (permanent) European Stability Mechanism would be added to the latter group of instruments. The adopted solutions have been the outcome of difficult negotiations, and some contradicted the Treaty on the functioning of the European Union.

Temporary measures did not bring about significant positive results. Only in Ireland its financial situation improved, which was also due to Ireland's modern economy structure. The condition of Greece's public finances is still very bad. At the end of 2011, the Greek national debt amounted to EUR 355 billion, i.e. 163% of GDP. At the beginning of 2012, Greece was EUR 15 billion short on funds to repay debts due, according to the estimates of the European Commission, the ECB and the IMF.

However, one should not expect the bankruptcy of Greece though many economists propose such a solution (this assessment was formulated at the beginning of 2012). Eurozone politicians are generally against the adoption of this solution. They fear consequent financial losses.[95] Generally, expelling Greece from the Eurozone has not been an option, as it would suggest to financial market players that the European Union "lets euro states fall".[96] This opinion, expressed by Volker Kauder, Chairman of the CDU/CSU group in the Bundestag, undoubtedly reflects the position of Angela Merkel's government. That is why, in the future, more bailouts would have to be provided to Greece.

Permanent instruments for combating debt might yield results in the case of most Eurozone states if they are consistently applied to achieve the set goals. It seems that the situation that occurred at the beginning of the 21st century will not repeat itself. It was in 2003, when the EU Council rejected recommendations of the European Commission to launch the procedure against France and Germany for their excessive budget deficit and thus the procedure was suspended. Instead of applying the sanctions, the Council acknowledged the unilateral obligations of both Member States to limit their budget deficits and called for improving their budget situation in 2005.[97]

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[95] *Cf. EU-Gipfel beschließt Fiskalpakt und ESM-Vertrag*, http://www.faz.net, pp. 1 and 2.

[96] *Cf.* Merkel: *Fiskalpakt ein Meilenstein der Geschichte der EU*, "Frankfurter Allgemeine Zeitung" 3.03.2012, pp. 1-2.

[97] *Cf. Schwarzer Peter*, "Der Spiegel" no. 5/2012, p. 19.

There is a risk that France and Germany will use the Fiscal Compact to harmonise taxes in the Eurozone, i.e. to introduce a single (unified) tax base and unified rates. In their letter presented at the European Council meeting of 30-31 January 2012, Angela Merkel and Nicolas Sarkozy informed that they would present proposals concerning the harmonisation of some taxes (on corporate income, financial transactions and energy sources). Some Eurozone states rightly fear that this might be the first step toward the harmonisation of the Corporate Income Tax rate.[98]

The above would be tantamount to introducing tax rates as high as those in Germany and France in the whole Eurozone, which would have a negative impact on Member States with low income tax rates. It would slow down economic growth and international competitiveness, and, consequently, hamper the struggle against growing debts.

ABSTRACT

The author presents initiatives launched by the European Union in order to overcome the financial crisis of the Eurozone member states. To meet this goal, emergency instruments were created (aid programmes for Greece, the European Stability Mechanism and purchase by the European Central Bank of loans issued by countries of the Eurozone in debt crisis) as well as permanent instruments (the Euro Plus Pact, sharpened regulations of the Stability and Growth Pact and the Fiscal Pact). Emergency measures did not bring about any substantial positive effects, since only the financial situation of Ireland improved to some extent. The state of public finances in Greece is still critical and therefore many economists suggest that this country should declare its bankruptcy. Permanent instruments to fight debt might yield the desired effects (in the case of the majority of the Eurozone countries) if they are used consistently and in accordance with their purpose.

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[98] *Cf. Durchbruch bei Verhandlungen über Stabilitätspakt*, "Frankfurter Allgemeine Zeitung" 27.01.2012, p. 2.