Analyses OSW

CENTRE FOR EASTERN STUDIES 12.09.2012 www.osw.waw.pl

Germany can ratify the European Stability Mechanism and the fiscal compact

Kamil Frymark

On 12 September the Federal Constitutional Court (FCC) in Karlsruhe ruled on motions aimed at blocking the ratification of the following three laws: the law establishing the European Stability Mechanism (ESM), the law relating to the fiscal compact and the law which makes it possible to adopt the European Council Decision amending Article 136 of the Treaty on the Functioning of the European Union (TFEU) with regard to a stability mechanism for eurozone member states.The court rejected the motions on the condition that an international legal reservation which would specify that German loan guarantees would be limited to a level set under the ESM at 190 billion euros and another reservation made that it is necessary for the Bundestag to agree to any increase of this amount. The court's verdict is not the final decision about the unconstitutionality of the laws relating to the ESM, the fiscal compact and the amendment to Article 136 of the TFEU but only enables the president to ratify these agreements without the need to wait for the final verdict in this matter. The court's decision means that the fundamental barrier to the ratification of the ESM has been removed.

The political and legal background

The negotiation of the fiscal compact has been one of Germany's key demands in the search for solutions to the problems with the eurozone. This pact, which was adopted by the leaders of the 25 EU countries on 2 March, is set to guarantee budget consolidation and to force the introduction of structural reforms in member states. It will be possible for the pact to enter into force after it has been ratified by 12 out of 17 countries of the euro zone. For the ESM, it is necessary that eurozone countries which can ensure in total 90% of its capital ratify the related law. Berlin guarantees the largest part of the capital – 27.1%, therefore without the participation of Germany the mechanism will not come into force. Germany is the only country still to ratify the ESM.

In order to adopt the agreements relating to the ESM and the fiscal compact on 29 June a two thirds majority of the votes in both chambers of the German parliament was required. This majority was ensured by deputies from opposition parties – the SPD and the Green Party as they had received a guarantee from Chancellor Angela Merkel that Germany would be striving for the introduction of a tax on financial transactions in the EU. Merkel furthermore guaranteed that after the fiscal compact has been launched Germany will see

the introduction of a system of transfering potential fines to the federal government which have resulted from excessively high indebtedness of a part of the federal states. A section of the CDU/CSU/FDP coalition deputies were against the adoption of the ESM and the fiscal compact by Germany and voted against them. The ratification of the laws by Germany required the signature of the federal president. Joachim Gauck, however, delayed his decision until the verdict of the Federal Constitutional Court was issued as he took into consideration the court's earlier verdict of 19 June which stated that it was necessary to provide more information to the Bundestag about Germany's European policy issues.

The court's verdict

The FCC's verdict is temporary and will be in force until a verdict is reached at a later time in the main proceedings in the matter of the unconstitutionality of the ESM and the fiscal compact and the amendment to Article 136 of the TFEU.

When justifying the verdict the judges stated that the guarantee in the form of an international legal reservation made by the German government that the stipulation that the amount of the loan guarantees may not exceed a level of 190 billion euros is a necessary condition in order for these laws and the amendment to the TFEU to be ratified. The court also made a reservation that the change in the German contribution to the ESM is possible exclusively upon the agreement of the German representative in the ESM who, prior to that, has to obtain agreement from the Bundestag. Furthermore, the German government is set to guarantee that the obligation of the confidentiality of ESM officials will not affect the Bundestag's right to information in the area of the ESM’s activity. The court also decided that Germany has to clearly state that, should the reservations made by Berlin prove ineffective, Germany will quit the ESM. The judges emphasised that the verdict does not question the rationale behind using legal and financial means by the government in order to combat indebtedness and to boost the economy, but only to their compliance with the constitution. The choice and the selection of methods to counter the crisis remain within the mandate of politicians. Nor does the verdict affect the European Central Bank’s decision of 6 September which makes it possible to buy in unlimited quantities of state bonds. The FCC will look into the complaint made in this regard together with the remaining submissions regarding the main proceedings (see Appendix).

The impact of the verdict on Germany's European and internal policies

The verdict will enable the current orientation of the Angela Merkel government regarding the response to the crisis in the euro zone to be pursued. Both the ESM and the fiscal compact reflect Germany's approach to combating this crisis. The regulations included in both documents guarantee the introduction of structural reforms and the establishment of a “budget brake” in the euro zone countries as well as stable control mechanisms and they fulfilled German expectations that the euro zone would be rescued. The fact that EU

institutions were omitted in the negotiations about the ESM and the fiscal compact also sheds light on the fact that Germany is pushing through its vision of relations between national states, the European Commission and the European Parliament.

In German politics the FCC's verdict will enable Chancellor Merkel, at least temporarily, to calm concerns in her own party. Opponents of the ESM and the fiscal compact from the CDU and CSU warmly welcomed the FCC's verdict which imposes the obligation not to exceed loan guarantees without the agreement of the Bundestag and ensuring the Bundestag the right to related information. Due to these restrictions, those Christian Democratic deputies who have been critical of the coalition's plans will be able to accept the anti-crisis solutions adopted by the government and will soften their stance in the approaching campaign for the election to the Bundestag to be held in 2013.

The fact that Germany will enter the ESM means that Angela Merkel will be able to focus on the election to the Bundestag which is being held next year. She wanted to avoid the reopening of the negotiations about the ESM should the FCC not agree on the ratification of these laws by the president as this would mean it would be necessary to become involved in European policy to a larger extent at the expense of the parliamentary election in Germany.

However, despite the present agreement on the ratification of the laws, the court's final decision may make it necessary to amend the German constitution if it turns out that its provisions do not allow further European integration to be pursued. Even before the court's verdict was reached, this requirement had been mentioned by several politicians, including Wolfgang Schäuble. In this situation the final verdict could lead to the renegotiation of the mechanism stabilising the eurozone among the 17 countries which have the joint currency. In this case Germany's negotiating position would be, however, weaker than at present, in part due to the decision recently made by the European Central Bank with regard to buying bonds on the secondary market.

Appendix

The rationale behind the complaints to the FCC

The decision made by the Bundestag and the Bundesrat on 29 June 2012 to join the ESM and the fiscal compact was first challenged by the association “More Democracy” which collected 37,000 signatures in total to back its complaint. This made it the largest constitutional complaint in Germany's history. Consecutive complaints were submitted by some opposition deputies, the Left Party parliamentary group and a CSU politician Peter Gauweiler. A complaint was also submitted by retired economics professors represented by Professor Karl Albrecht Schachtschneider who also extended their complaint to the “Six Pack”.

In the complaints it was argued that the adoption of both agreements by Germany will weaken the Bundestag's capacity to shape and control the country's fiscal policy following the possibility to provide unlimited financial guarantees to beneficiary countries for loans granted under the ESM. It will restrict the Bundestag's autonomy in this area and the

democratic control of the German budget which voters have. This reservation referred above all to the amendment to Article 136 of the TFEU since the amended article in fact removes the no-bailout clause (which prohibits the funding of debts of EU member states by other EU member states) and thus establishes a legal basis for the functioning of the ESM.

As for the fiscal pact, which sets limits of indebtedness on eurozone countries, the plaintiffs argued that its ratification will not allow this decision to be changed on grounds of domestic legislation. The introduction of related new regulations will mean moreover the breach of the TFEU. Furthermore, the Left Party challenged the mode of adopting laws relating to the ESM and the fiscal compact. In the opinion of this party, the introduction of amendments should be only possible as a result of a national referendum (on the basis of Article 146 of the Fundamental Law). The plaintiffs also raised the issue of violating the constitution in Article 20, sections 1. and 2. which on the basis of Article 79, section 3. cannot be amended. This is stipulated by the "eternity clause" which has been confirmed by the FCC in its numerous verdicts (including Solange I of 1974 and Solange II of 1986). This clause rules out the possibility of amending the constitution in the area of the fundamental rules of the functioning of the state (including democracy, the welfare state).

On Friday 7 September another complaint was submitted to the FCC by Peter Gauweiler, in which he demanded that the announcement of the verdict be postponed. Gauweiler argued that until the European Central Bank recalled its decision on buying domestic short-term bonds in unlimited quantities the FCC should delay announcing the verdict. In Gauweiler's opinion, the EBC's decision of 6 September is unconstitutional as it violates fundamental principles of democracy by excluding the Bundestag from the decision making process and goes beyond Germany's loan guarantees foreseen in the ESM. The FCC rejected Gauweiler's complaint and issued the verdict as initially planned.