

# Democratic Inputs versus Output-Oriented Governance: The ECB's Evolving Role and the New Architecture of Legitimacy in the EU

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*This article examines the relationship between European integration and democratic governance during the eurozone sovereign debt crisis. It does so by analyzing the evolving policies of the European Central Bank (ECB) against the backdrop of tension between input and output legitimacy in economic and monetary union. This tension makes the ECB's actions a test case for understanding the functioning of supranational output legitimacy in a time of economic crisis. The evidence shows that the ECB stayed focused on outputs and pursued a strategic policy to prompt governments to create new treaties providing bailouts in return for conditionality. Hence this new legal-political architecture is also analyzed but in the context of how input legitimacy is institutionalized at a time of a "constraining dissensus." What this shows is that political constraints did not prevent the emergence of a new architecture of legitimacy, although this remains beholden to a national model of input legitimacy. The result is a disconnect between de facto Europeanization of fiscal decision making and de jure national implementation measures. Consequently, the relationship between integration and democratic governance is more complex than ever with input legitimacy likely to play a disruptive role in the future. In particular, the national debt brakes introduced via the Fiscal Compact mean that the tension between output and input legitimacy may well play out at the national level as well as EU-wide.*

## **Introduction: Democratic Inputs versus Output-Oriented Governance**

The eurozone sovereign debt crisis, which occurred after the 2008 global financial crisis, is perhaps the hardest challenge the EU has faced (Moravcsik 2012). Although it is a multifaceted policy problem, this crisis above all revealed the eurozone's vulnerability to having bad bank debt spill over into a wider sovereign debt maelstrom. This structural weakness stemmed from the fact that the European Monetary Union (EMU) established a single currency without an accompanying banking union, let alone a fiscal union (Lane 2012). The EU's response involved tackling both the banking (or private debt) side of the crisis as well as the sovereign debt problem by, *inter alia*, creating a bailout fund for member states, establishing a new treaty that further restricted national borrowing capacity alongside an evolution of the European Central Bank's (ECB) monetary policy.

While the origins of the problem and the efficacy of the hastily cobbled-together solutions have been—and will continue to be—much discussed (e.g., Sadeh 2012; Shambaugh 2012; Hall 2012), this article examines a different, less-studied element of this crisis. The analysis explores the way the ECB interacted with demands stemming from national politics in the debate over what could and should be done to rescue the EMU. Throughout the protracted eurozone crisis, the EU faced what is presented here as a fundamental contest over the legitimacy of decision making when taking steps to shore up the EMU. Central to this contestation were competing claims made by actors and institutions that legitimately represented the interest of the eurozone and how far this could trump individual national interest.

Reprising the analytical categories of Fritz Scharpf (1999), the article highlights how bearers of national “input legitimacy” (elected politicians and governments) challenged the preferences and decisions of “output legitimacy” (oriented institutions, notably the ECB). According to Scharpf’s model, policies and policy making can be legitimate by virtue of the benefits they produce, which constitutes in his terminology “output legitimacy” (Ibid.). In the context of EMU, as well as of EU governance more broadly, decisions may thus be legitimate not because citizens have had a role in shaping them, but “because they effectively promote the common welfare of the constituency in question” (Ibid., 6). This form of legitimacy contrasts with “input legitimacy,” stemming from preferences expressed via political participation, namely citizens actually voting for parties with specific policies. Consequently, when policy preferences between elected and unelected actors differ, there is the possibility of tension between these two forms of legitimacy.

Indeed, this tension between democratic inputs and output-oriented governance has been present from the outset of the EMU. In particular, the ECB has been treated as a classic instance of delegation for the sake of making interstate commitments credible (Dyson 2009), making this non-majoritarian, technocratic institution a bearer of output legitimacy and, therefore, subject to few democratic channels of accountability (Amentbrink 1999; Berman and McNamara 1999). However, as the article demonstrates, during the eurozone crisis the ECB came under great EU-wide political pressure to carry out bond market and other forms of intervention. Moreover, it often had to fulfill its role as guardian of the euro in the absence of political consensus, notably when bailout terms were being negotiated with countries such as Greece.

The first core wager of this article then is that studying the evolving role of the ECB, combined with the politics behind the adoption of two new treaties (the so-called Fiscal Compact, formally the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union, as well as the European Stability Mechanism treaty), offers up fundamental insights into the relationship today between European integration and democratic governance. The very ingredients of the EU response—huge sums committed for bank and sovereign bailouts counterbalanced by unprecedented top-down macroeconomic policy conditionality—are politically highly salient aspects of democratic politics. This saliency means the eurozone crisis is a test case for understanding the functioning of supranational output legitimacy in a time of economic crisis. In particular, the actions of the ECB demonstrate a strategic logic for encouraging political actors to find consensus over fiscal policy and bailouts, which were the *quid pro quo* for implementing nontraditional monetary policy.

At the same time, changes in the legal-political structure of EMU made to resolve the sovereign debt crisis offer novel insights into the constraints on integration imposed by democratic inputs. The context behind these constraints is not just the emergency of the financial crisis, but also the growth of what Liesbet Hooghe and Gary Marks (2009) call a “constraining dissensus” facing the EU. This theory suggests that increased national political contestation over European integration makes EU policy making and treaty reform more uncertain and harder to undertake. The reason for these difficulties is that elites are split over how to pursue integration, while citizens are wary about justifications or arguments in favor of greater integration. In these circumstances, the expectation is that there is a lack of input legitimacy (both national and pan-European), which makes it harder to generate the consensus necessary for the development of greater supranational competences.

The second goal of this article is to analyze the legal-political architecture of the EMU in order to assess how input legitimacy is institutionalized following the new treaty changes, with particular attention placed on the way democratic inputs affect policy choices designed to fix the sovereign debt crisis. Of special interest here is the extent to which input legitimacy is embedded within a national, as opposed to a supranational, setting and how this relates to satisfying voter demands about retaining national control over fiscal policy. In this context, contestation over how input legitimacy should be articulated is treated as a way of testing

whether the presence of a constraining dissensus did in fact disrupt attempts to proceed with further integration during the eurozone debt crisis.

Overall, the article links together the interactions of the ECB, national political elites, and ordinary voters, demonstrating the relationship between integration and democratic governance is more complex than ever. To this end, the argument proceeds as follows. The theoretical framework used to conceptualize the tensions in the governance of EMU and the EU more generally is put forward in the first section. What follows in the second section is the analysis of how the need to resolve the sovereign debt crisis highlighted the way that input and output legitimacy rub against each other without the latter yielding to the former, notwithstanding superficial appearances to the contrary. Finally, the last section shows how the retention of a national model of input legitimacy—begotten by a constraining dissensus—is increasingly at odds with the Europeanized decision making system underlining the new bailout system. The article concludes by reflecting on what these developments mean for the role of input legitimacy and the effects of the constraining dissensus in the future political economy of European integration.

### **Theoretical Framework: The Two Tensions in Democratic Governance in the EU**

The EU's democratic practices have long been a vexing topic, with much scholarly ink spilled over whether European integration has created a fundamental democratic deficit (Føllesdal and Hix 2006) or if the EU should be absolved of such stigma (Moravcsik 2006). This debate over a deficit of democracy is broadly framed in terms of how far the EU mimics nation-state style democratic practices (Ibid.), whereas the aim here is not to compare different ways of institutionalizing political accountability. Instead, this article explores the tensions inherent in EU legitimacy arising from the response made to the eurozone crisis. These tensions exist because of multiple claims of democratic accountability and legitimacy wielded by actors within the EU system (Coultrap 1999; Glencross 2012).

In this context, Scharpf's notion of the twofold nature of democratic legitimacy is particularly useful for understanding dilemmas of EU democracy characterized by competing claims to legitimacy and its use in holding EU institutions to account. The output versus input model of legitimacy is essential for understanding one of two fundamental tensions within EU democratic governance, that is, the rivalry between bearers of output legitimacy, focused on policy effectiveness and with a longer-term perspective afforded by not having to seek electoral mandates, and bearers of input legitimacy, whose preferences and priorities reflect the partisan results of elections. Hence technocratic, unelected institutional actors such as the commission, courts, and the ECB, whose legitimacy comes from delivering policy results, see their decision making challenged by political actors.

Another way of conceptualizing this split, using the analysis of delegation pioneered by Giandomenico Majone (2001), is between majoritarian institutions (e.g., parliamentary bodies) and non-majoritarian institutions (e.g., courts or specialized agencies). In the EU, national majoritarian institutions have delegated certain policy competences to expert, non-partisan institutions such as the commission or the ECB on a fiduciary basis (Ibid.). That is, a fiduciary or trustee acts not as an agent—doing the bidding of the delegating body—but as an independent body responsible for making sure the principals stick to their treaty commitments.

This tension between delegating institutions and the trustees to which they have delegated certain policy competences is not just a question of rivalry between majoritarian and non-majoritarian bodies over competence or jurisdiction. In addition to their separate mandates (electoral versus delegated), these institutions have separate time horizons, as illustrated by the Court of Justice's jurisprudence designed to create conditions for long-term change in the EU legal system rather than scoring immediate political points (Alter 1998). Political bodies are inevitably affected by time inconsistency, i.e., their preferences are dynamic, based on changing voter inputs. In this context, the EU's apolitical, non-majoritarian bodies are designed to avoid time inconsistency by being purposefully detached from short-term

electoral exigencies. This separation allows trustees to take decisions necessary for long-term policy success, thereby generating a credible and binding order that national governments cannot overturn for the sake of short-term gains.

The bearers of output legitimacy, such as the commission or the ECB, have long time horizons likely to clash with the short-term interests of national governments or with the European Parliament. This does not mean supranational apolitical bodies are completely aloof from public sentiment and the broader political climate. For instance, the ECB “has a strong interest in finding ways to be perceived . . . as accountable and transparent (and within a wider EMU cum EU governance system, responsive) and . . . as acting effectively on behalf of the interest of European or eurozone citizens (output legitimacy)” (Torres 290). Consequently, a moment of crisis such as that experienced by the eurozone since 2010 can be framed as an overt contest between output and input legitimacy and one that reveals how the two interact in practice.

Yet the input/output (majoritarian/ non-majoritarian) tension interacts with another fundamental tension within EU democratic governance, one that emerges from the multilevel or compounded nature of this polity. Within member states themselves there is a growing tension between political elites and ordinary voters, which in turn is destabilizing attitudes toward integration among national elites (Hooghe and Marks 2009). This trend contrasts with the situation at the start of the European integration process when questions about how it should be organized and what policies should be pursued were kept largely separate from national politics. Diplomatic deals cut by political elites were insulated from publicity and public opinion, a feature known as the “permissive consensus” (Lindberg and Scheingold 1970). This consensus rested on two elements of trust: citizens’ trust in political elites’ ability to devise a mutually beneficial system of governance that could secure peace, strengthen the state, and increase prosperity, and elite trust that economic integration could achieve all these goals.

It is the spread of EU competences that has increased the salience of the integration dimension in national politics (Schmidt 2005; Hooghe and Marks 2009). This added saliency has challenged both elite consensus and citizens’ permissiveness toward accepting greater integration. This trend, as well as that of increased media coverage, began with the 1992 Maastricht Treaty (Hooghe and Marks 2009), which was hugely contentious in many countries. Since this time, mainstream political parties have been forced to reconsider their stance on integration, often revealing internal divisions on a subject they for good reason tried to avoid debating (Eijk and Franklin 2004).

Overall, mainstream parties are increasingly divided over what stance they should take on integration as they are confronted by fringe parties able to mobilize Eurosceptic opinion, especially in European parliamentary elections (Mair 2007). Electorates increasingly question the need for further conferral of competences to the EU. The result is that bearers of input legitimacy (i.e., parties and leaders) are subject to a “constraining dissensus,” whereby what they can do at the EU level is increasingly scrutinized and challenged in national politics (Hooghe and Marks 2009). This “dissensus” operates as a domestic constraint on the kind of deals elites can make to solve EU policy problems, thereby adding an extra complication to the tension between elected and unelected institutions.

However, the major threat posed by the constraining dissensus articulated within member states is that of rejecting not just output legitimacy—rule for the people, whether by unelected institutions or diplomatic deals made by EU political elites—but also input legitimacy stemming from other countries. Instead of having a single political community, or demos, the EU consists of multiple democratic communities or peoples, which is why it has been described as a “demoicracy” (Nicolaidis 2004) or “compound democracy” (Fabbrini 2007), rather than a plain democracy. The separate peoples do form, to a degree, a single European-wide democracy through representation in the European Parliament and the supra-majority voting procedure in the council (Coultrap 1999). Yet these compound or aggregated elements coexist

alongside distinct national democratic practices such as elections to establish governments and sometimes referendums on EU matters.

Hitherto, EU democratic governance has accommodated the existence of more than a single democratic political community, leading to the messy coexistence of multiple accountability claims made in the name of different definitions of the people (Glencross 2012). In this context, the growth of a constraining dissensus raises more than just the thorny question of where the hierarchy of democratic legitimacy resides in a multi-layered polity, i.e., at the member state level or not (Ibid.). The attempt to enshrine a national vision of input legitimacy at the same time as reinforcing the non-majoritarian macroeconomic regulatory environment risks creating an even greater division between the preferences stemming from input legitimacy and the rules pursued for output reasons. Therefore the eurozone crisis provides an opportunity to study the interaction of both these tensions as manifested in battles not just over the ECB's interpretation of its output legitimacy mandate, but also the clashes over how to institutionalize new rules for bailing out countries and ensuring the future stability of the euro.

### **Output Legitimacy and the ECB's Evolving Monetary Policy**

As explained above, output legitimacy relates to a non-majoritarian institution's ability to promote the common welfare of a particular constituency. In the case of the ECB, the output that is rendered legitimate by policy effectiveness—rather than electoral inputs—is price stability (low inflation), from which other macroeconomic benefits flow. This goal is laid out in Article 127 TFEU as the “primary objective” of the European System of Central Banks, although this goal coexists with the more general tasks of coordinating monetary policy for the eurozone, managing foreign exchange for the euro, and supporting “the general economic policies in the Union.” The delegation of monetary policy to an independent central bank in this fashion is a development associated with the rise of the “regulatory state” from the 1970s onward (Majone 1996). This model replaced government efforts to manage demand on the premise that central bank independence is the most effective way of controlling inflation, either through instrument independence or goal independence (Fischer 1995).

Yet the payoff from this act of governmental delegation is limited to the degree that fiscal policy can affect price stability (Woodford 2000). In this context, central banks are proponents of fiscal discipline, which explains the German Bundesbank's insistence on the adoption of a Stability and Growth Pact (SGP) during the Maastricht negotiations for EMU (Marsh 2009). As part of the means to secure price stability, fiscal constraints such as those imposed by the SGP (total debt of no more than 60 percent of GDP and annual deficits of less than 3 percent) are designed to convince investors to lend money to governments at sustainable interest rates. When the terms of the SGP had to be jettisoned as a result of the 2008 global financial crisis—necessitating bank recapitalization and leading to sudden tax revenue shortfalls—it was precisely governments' ability to borrow sustainably that was called into question (Shambaugh 2012).

The eurozone sovereign debt crisis, where a succession of countries (Greece, Ireland, Portugal, and Cyprus) were frozen out of the international bond markets and investors got nervous about Spanish and Italian debt, forced a complete overhaul of the EMU. This eventually entailed scrapping the infamous no-bailout clause (which prohibited mutual debt assistance) and reconfiguring the SGP. In addition, a range of political actors called upon the ECB to help not just the general EU economy but specific governments that were punished by the bond markets as the SGP was hollowed out completely.

Output legitimacy encountered input legitimacy in terms of debating the proper role and necessary emergency actions of the ECB. However, actors imbued with input legitimacy have no practical direct levers to control the ECB, whose independence from political interference was a *sine qua non* of monetary integration for the German government at Maastricht and thereafter. Since the very goal of price stability is enshrined in the EU treaties, this objec-

tive is in effect “constitutionalized,” meaning that it is not part of and subject to ordinary EU political decision making (Bartolini 2010). Only a revision of the treaties—a highly unlikely possibility—could alter this hierarchy of priorities. Nevertheless, in a moment of crisis, the internal decision-making process of the ECB did allow for responsiveness to a novel and potentially catastrophic scenario. It is this responsiveness that needs to be examined in order to understand the functioning of output legitimacy at a time of great policy uncertainty when elected actors sought to influence ECB decision making. In particular, it is important to focus on the strategies followed by the EU’s central bank in order that long-term goals superseded short-term political desiderata.

#### *External Pressure and the Implementation of Non-Standard Policies*

The ECB’s Governing Council, regrouping the governors of the central banks from across the eurozone countries, as well as a six-member executive board, is the key decision-making body of this institution. In May 2010, as the sovereign debt crisis erupted in Greece, the Governing Council took a radical decision to purchase government debt on the secondary market (i.e., from banks and other financial institutions). This bond buying was designed to relieve pressure on governments facing high interest rates for financing their debt, providing them with more time to make the policy adjustments needed to improve public finances and thus reassure investors.

Direct purchases from governments are illegal under the EMU rules. ECB intervention in the secondary market (a policy enthusiastically pursued by the Bank of England and the Federal Reserve), though not formally prohibited, remains nonetheless highly controversial. This is because of the supposed inflationary risk of flooding markets with this money, as well as the legal uncertainty surrounding a move that could be considered contrary to the spirit of the no-bailout clause (Article 125 TFEU). As a result, the establishment of the Securities Market Program (SMP), eventually involving the purchase of circa £75 billion of government debt, led to serious internal conflict within the Governing Council. (Though it was only the April 2011 resignation of the president of the Bundesbank, Axel Weber, that made public the level of internal dissent over SMP.)

Indeed, SMP—reauthorized in 2012 under the guise of the potentially much larger Out-right Monetary Transactions (OMT)—was only one of several “non-standard measures” (Torres 2013) adopted by the ECB in response to the deepening eurozone sovereign debt crisis. The other major policy was the provision of extraordinary liquidity to ailing eurozone banks, which began earlier in May 2009. Already in July 2009, ECB President Jean-Claude Trichet described the effects of its unconventional measures as akin to the quantitative easing pursued by British and American central banks (Trichet 2009). Nevertheless, these initial policy measures were succeeded in late 2011 by a second, long-term refinancing operation, followed by a third in February 2012. Time and again, therefore, the ECB acted during the crisis in a way that eased the pressure on governments who were on the hook for bank recapitalization and at risk of having to pay higher interest rates on debt. This remarkable evolution in monetary policy is a testimony to pragmatism, but was it also a response to the innumerable demands for ECB activism by bearers of input legitimacy?

External pressure on the ECB came notably from politicians in Mediterranean Europe, with figures from both the left and the right in France notably asking for a change in monetary policy. Already in 2007 the presidential candidates Nicolas Sarkozy and Ségolène Royal had called for reform of the ECB’s statutes to include a commitment to growth and employment (Esch and Jong 2012). In the summer of 2008, just before the financial crisis hit, France assumed the rotating presidency of the Council of Ministers, which Sarkozy used as a platform to denounce interest rate hikes from the ECB, which feared inflationary pressures. This criticism came to naught because of the insulation of the ECB from political control, although it was a sign of things to come as mounting bank debts forced sovereigns in the eurozone to desperate volumes of borrowing.

In 2011, Sarkozy applied great political pressure to change the composition of the Executive Board as Jean-Claude Trichet stepped down from presiding the ECB. This paid off at least to the extent that it prevented Axel Weber from becoming president. In terms of policy substance, the French president also asked the new ECB president, Mario Draghi, to announce unlimited bond-buying operations—assuming public lender of last resort functions (Grauwe 2011)—on the secondary markets to contain contagion effects on Italian and Spanish public debt. Indeed, the practice of banks using ECB liquidity to purchase government debt in countries facing hikes in borrowing costs entered financial parlance as a “Sarkozy trade.” Naturally, these moves put Sarkozy at odds with Angela Merkel, so much so that on 24 November 2011 the two leaders publicly declared to stop airing their divergences over the ECB’s role in public, a clear sign of the dissensus operating behind the scenes amongst the EU elite.

Consequently, the pressure experienced by the ECB to adjust its policies during the eurozone crisis has come largely from outside the ordinary and highly limited accountability process behind EMU. The European Parliament, tasked with providing an annual non-binding report on the ECB’s activities, has nevertheless sought to flex its muscles through the economic and monetary affairs committee. This body questions the ECB president on a trimestral basis and has notably used this platform to advocate plowing ECB liquidity into loans to small and medium-sized enterprises. Moreover, European Parliament president Martin Schulz explicitly supported the creation of OMT in autumn 2012. The European Parliament thus followed other bearers of input legitimacy in calling for a change in policy direction by the ECB.

#### *The ECB’s Successful Strategy for Pursuing Long-Term Effectiveness*

Sometimes portrayed as a purely crisis-management response designed to “compensate for delays and set-backs in the intergovernmental creation of fiscal capacity” (Genschel and Jachtenfuchs 2013) or as “short-term measures” (Vilpišauskas 2013), the ECB’s resort to unorthodox policies is not merely a case of muddling through until market conditions improve. In particular, the introduction of a raft of policy measures seemingly in line with the demands from elected politicians calling for a loosening of monetary policy does not mark a departure from output legitimacy as it may initially appear. Looked at in detail and in relation to the political decision-making calendar, the unprecedented market interventions by the ECB were doubly strategic. They were intended to prop up the eurozone economy while also ensuring that long-term effectiveness of the EMU was not undermined by short-term political preferences for looser monetary policy. To achieve this dual objective, the ECB sought to accompany and encourage political actors in taking decisions deemed necessary for the health of the euro in the long run. Therefore, it was the strategic actions of the ECB—using its policy competences rather than relying merely on a different time horizon—that ensured supranational output legitimacy resisted the countervailing pressures of input legitimacy.

The ECB’s nonstandard policies were by no means a blank check to insulate banks and governments from the crisis in order to assuage elected actors. Rather, these measures were designed to support eurozone countries without generating moral hazard, and without relieving member states of their obligation to return to fiscal discipline as well as to increase certain kinds of financial solidarity across the eurozone. For a start, SMP was authorized by the ECB’s Governing Council only the day after the creation of a European Financial Stability Fund was announced. In this fashion, the ECB’s move to purchase government debt on the secondary markets was conditional on prior political agreement to supply emergency credit to Greece through the EFSF, i.e., to associate a political remedy with a monetary one. This not only meant transferring responsibility to the member states but also introducing stricter fiscal conditionality than is possible through the ECB emergency measures.

In its press release justifying the temporary bond-buying program on the back of the launch of the EFSF, the ECB specifically referred to eurozone countries’ commitment to meet their fiscal targets (ECB 2010). Hence, SMP was not a policy designed to please governments

under pressure by providing short-term, commitment-free succor. This concern with moral hazard explains why by autumn 2010 the ECB started to worry about banks' over-reliance on its emergency liquidity (Gabor 2013). This fear was compounded by the fact that banks were using the ECB lending to fund sovereign debt purchases—engaging in the Sarkozy trade—thereby strengthening the inter-dependence between private lending and sovereigns (Shambaugh 2012).

In response—and against the preferences of both governments and banks—the ECB acted strategically by changing track. It sought to phase out its emergency bank lending over the course of 2011, suggesting that the EFSF should take on this role while also reducing its SMP bond-purchases (Gabor 2013). At the same time, the ECB insisted on seniority (i.e., precedence in repayment) for its holdings of Greek debt, as the IMF-ECB-Commission troika negotiated a partial default to the tune of €100 billion. ECB holdings of Greek debt had risen substantially during 2010 owing to SMP. Despite the fact that this move scared off investors in other eurozone countries' debt, the ECB considered a default on its bond holdings as tantamount to an illegal monetization of public debt (as prohibited under Article 123 TFEU). The results of this return to orthodoxy were almost immediate and politically (as well as financially) damaging: Ireland and Portugal followed Greece in requesting a bailout, while Italy and Spain experienced worrying interest rate differentials thereby raising the prospect of further bailouts.

As the situation in the eurozone deteriorated 2010–11, the ECB was castigated for exacerbating pressures on government finances and failing to act as a lender of last resort to restore the market confidence necessary to finance otherwise manageable levels of public debt (Grauwe 2011). This criticism targets decisions that increased instability in the short-term, thereby jeopardizing the ability to provide long-term outputs that are legitimate by virtue of their efficacy. However, by reducing its market interventions and thereby generating market uncertainty, the ECB confronted national governments with the need to contribute themselves to the long-term viability of EMU by taking concrete measures of fiscal discipline allied with financial solidarity. Instead of yielding to external pressure from bearers of input legitimacy, the ECB shaped the strategic space to encourage the political pursuit of long-term solutions to the sovereign debt crisis. As a bearer of output legitimacy, the EU's central bank did not want political expediency to trump policy effectiveness in the long run.

Paradoxically, the fact that the ECB soon backtracked and went all out in its pursuit of unconventional measures actually further demonstrates this strategic intent. This interpretation is borne out by the ECB's role in negotiations over the European Stability Mechanism, which had its first iteration in July 2011 based on a March agreement by the European Council. The ESM deal was based on a strengthening of the SGP—part of the so-called “six pack” of measures for improving fiscal health in the eurozone—in line with the ECB's preference for member states to provide temporary financial support rather than fiscal transfers (ECB 2011). It was this political decision, providing borrowing facilities in return for conditionality, that prompted the ECB to extend SMP in April 2011 to purchase Italian and Spanish debt.

The ECB clearly preferred a long-term political-fiscal remedy to a purely monetary one, even at the cost of prolonging instability in the short-term. Indeed, the previous pattern seen with the SMP was repeated soon after the ESM deal, as ECB President Trichet expressed concerns over the robustness of the revised SGP rules and continued to point the finger at national fiscal mismanagement, something that ought not be remedied by monetary policy (Gabor 2013). This criticism, alongside market skepticism about the size of the ESM, was the context for a modified ESM announced by the European Council in February 2012.

In the new version, the ESM was associated with the so-called Fiscal Compact. This was highly significant as the Fiscal Compact ties provision of emergency financing (including funds going directly to bank recapitalization) to the introduction of national debt brakes to provide medium- and long-term fiscal discipline. It was precisely this more robust version of conditionality that gave the ECB the confidence to establish the OMT—designed as a much

larger program than the SMP—in August 2012. That is, the OMT purchases of government debt are dependent on that country having requested help from EFSF/ESM and thus subject to strict fiscal conditionality.

Finally, the ECB's actions in the context of the bailout for Cyprus also point to the overarching dual strategy that has characterized the institution during the crisis: an unwavering commitment to fulfill a mandate based on output legitimacy and a desire to facilitate political agreement on long-term reforms. As the sovereign debt crisis struck the eurozone, Cypriot banks used the ECB liquidity to purchase high-risk Greek debt—offering the high returns needed to afford the high interest rates used to attract rich depositors from outside the EU. The ECB pulled the plug on this unsustainable funding model in March 2013, when it gave Cyprus and the EU/IMF a deadline by which to agree a bank recapitalization loan or else lose access to emergency liquidity assistance. In other words, the ECB forced the hand of political actors whose indecision ran counter to taking the drastic measures necessary to save a (possibly contagious) run on Cypriot banks and overhaul the Cypriot banking model.

There is ample evidence to suggest that the ECB's actions—although ostensibly focused on achieving short-term outcomes—were designed to meet long-term objectives rather than to yield to calls for change from bearers of input legitimacy. Moreover, the ECB acted strategically throughout 2010–13 to accompany and encourage political actors—even when its inaction made short-term conditions more unstable—in taking decisions deemed necessary for the health of the euro in the long run. What remains to be seen then is how far the requisite political consensus was affected by the presence of a constraining dissensus across the multiple levels of the EU polity.

### **Input Legitimacy, the Constraining Dissensus, and the Post-Bailout Architecture**

As noted in the introduction, the eurozone crisis provides an opportunity to see not just the tension between output and input legitimacy over monetary policy but also exactly how input legitimacy is institutionalized in the new legal-political architecture the ECB wanted to see put in place. The spread of a “constraining dissensus” amongst EU member states means that the insulation of national politics from questions about the merits of integration or how it should be organized is now over (Hooghe and Marks 2009). This situation increases the difficulty of reaching consensus over new treaties, especially when this requires electorates to accept a further transfer of competences in salient areas such as macroeconomic policy. In this context, the expectation about the behavior of national politicians is twofold. As well as being tempted to reassure skeptical voters by insisting that input legitimacy—especially as articulated at a national level—trumps output-oriented policy making, national leaders will also operate under increased domestic constraints when it comes to transferring new competences to the EU. This section analyzes the extent to which the presence of a constraining dissensus affected the governance architecture created, as per the desires of the ECB, to stabilize the EMU.

To explore this topic, it is necessary to move beyond chronicling instances where bearers of input legitimacy in various countries challenged the choices of output-oriented institutions and existing macroeconomic rules. Instead, the analysis scrutinizes the nature of input legitimacy—notably according to how it defines the political community that provides democratic inputs—institutionalized in the evolving legal-political architecture. What has to be ascertained is whether the influence of the constraining dissensus has been felt in the way input legitimacy is institutionalized and the difficulty present in agreeing to two new treaties: the European Stability Mechanism and the so-called Fiscal Compact. That these treaties were signed and ratified already shows that consensus remains possible among EU elites, even though sixteen EU countries experienced a change in government in the years 2010–12. To measure the potential impact of a constraining dissensus requires a fine-grained analysis of the provisions of these new treaties.

### *The European Stability Mechanism*

First, it is useful to explore the structure of the European Stability Mechanism and how this relates to various conceptions of the political community (or communities) that generates input legitimacy. The ESM was established in 2012 (in its second guise), prompted by the ECB, as a permanent fund to provide emergency loans to countries that ratify the Fiscal Compact. Overall, its mode of functioning suggests that input legitimacy is considered in compounded terms, albeit with certain qualifications, meaning that it is via pan-EU democratic inputs that bailouts should operate. In this case, elite consensus has prevailed over dissensus.

The intergovernmental ESM treaty, which operates under EU law but outside formal EU institutional structures (Bardutzky and Fahey 2013), is designed in a way that permits national parliaments in some countries to have a veto power over increasing available ESM funds. In their national implementing legislation, countries such as Germany, Estonia, and Finland have specified that parliamentary approval is required for any rise in capital contributions. In Germany, this measure became necessary following judicial review of the ESM treaty by the Constitutional Court. The latter ruled that there is a limit on how far the executive can commit German taxpayer money without the authorization of the Bundestag, which the constitution entrusts with overall budgetary responsibility (*haushaltspolitische Gesamtverantwortung*).

Significantly, however, the terms of the treaty specified that it would not require unanimity to enter into force. Article 48 provides for entry into force when ratified by member states representing 90 percent of the total capital subscription. In that sense, national political communities—whether through parliamentary or even directly democratic mechanisms—were not granted a veto on the creation of this bailout fund. At the same time, the decision-making procedure of the ESM (within the confines of funds already allocated) relies on a super-majoritarian two-thirds threshold, while also allowing a one-third blocking minority based on countries' capital share (i.e., countries representing 34 percent of the capital can block a decision).

Consequently, the ESM model is consistent with the supranational, compounded—akin to concurrent majorities (Schmitter 2000)—model of democratic decision making typically found in the council. In this way, the existence of a supposed constraining dissensus did not prevent the establishment of a bailout fund with a standard supranational form of decision making. In Ireland, the Supreme Court rejected a legal challenge over the need to ratify this treaty by referendum (as is the case for any constitutional revision), meaning that input legitimacy came in the form of parliamentary ratification through signatory states rather than via direct democracy. As noted in the previous section, the original size of the ESM and the weakness of conditionality it posed when disbursing funds meant the ECB and the financial markets were unconvinced by the nature of the 2011 diplomatic deal, which resulted from the caution of elites aware of domestic constraints. In this case, therefore, it was by virtue of the strategic action of the ECB that the effects of the constraining dissensus were overcome, and a more robust form of conditionality, in the shape of the Fiscal Compact, was adopted.

### *The Fiscal Compact*

Turning to the Fiscal Compact element of the new post-bailout architecture, it appears that this instrument bears important traces of the impact of a constraining dissensus. This is certainly the case from a British perspective, since David Cameron refused to sign the treaty, because he was concerned that without UK-specific concessions the treaty change might not muster a commons majority to enter into law (Beach 2013). Nevertheless, it was adopted outside EU law by other EU member states, but, more significantly, the Fiscal Compact is predisposed toward a national concept of input legitimacy, reflecting the domestic constraint felt by political elites when negotiating.

At the heart of the Fiscal Compact is the implementation of debt brakes or balanced budget rules, which go beyond the strictures of the SGP. According to the terms of the treaty, debt brakes have to be adopted into national (and, if so desired, constitutional) law, although

these are set to function without a supranational oversight mechanism (Dullien 2012). That is, while the Court of Justice of the EU has been granted competence to check for the actual implementation of debt brakes, it lacks the power to review their functioning. National parliamentary and/or judicial mechanisms will be responsible for the enforcement of the debt brakes in line with the principle that the national arena is responsible for budgetary decision making. Each signatory country has the ability to choose whether to politicize enforcement by using a parliamentary mechanism or delegate enforcement to courts and rely on output legitimacy.

A more supranational enforcement model was envisaged at one time, with Germany's finance minister calling in 2012 for the commissioner for economic and monetary affairs to have a direct say in national budgeting decisions. The rejection of this non-majoritarian regulatory EU-level approach to budgetary decision making is another sign of the constraining dissensus in operation, as agreement was only possible on a less sovereignty-curtailing mechanism for ensuring fiscal discipline. The result leaves national parliaments (and potentially courts) in charge of tax and spending decisions within the parameters of EU-wide fiscal rules.

And so the vision of input legitimacy enshrined in the bailout architecture rests on continued reliance on national inputs within a non-majoritarian macroeconomic regulatory environment. It is national political and judicial processes that are expected to find a way to accept and thus legitimize the supranationally decided fiscal framework as it functions in practice, with limited supranational intrusion. In another indication of the constraints facing elites seeking to pool more competences the operation of this national model of input legitimacy was initially deferred. The treaty commitment to pay back 1/20th of total debt over 60 percent of GDP can only be enforced after a three-year period from entry into force of the Fiscal Compact, i.e., not before 2016 (Dullien 2012).

This reliance on a national model of input legitimacy leaves little room for a compounded or even supranational variant—peoples deciding in common via their representatives in the European Council or aggregated together in the European Parliament. Consequently, macroeconomic policy for eurozone countries appears to rest on national decision making (to the exclusion of supranationalism) in line with the reinforced regulatory framework of the reconfigured SGP and the Fiscal Compact. Yet there remains an element of fiction in this national-oriented model of input legitimacy. This is because the imposition of stricter budgetary rules on member states is subject to a significant issue of interpretation.

The fundamental ambiguity at the heart of this system is the difference between headline budget deficits and structural deficits, with the latter excluding one-off measures and the effects of the business cycle. Since both the new SGP and the Fiscal Compact are based on member states' cutting structural deficits, there is bound to be an intense definitional debate on the criteria separating headline from structural deficits. Resolving this ambiguity—a precondition for identifying compliance—is not something that can be achieved solely through national channels of input legitimacy. At least this is the evidence from the current operation in practice of this mechanism. The European Commission undertakes an annual review of national fiscal practices, alongside policy recommendations for countries subject to an excessive deficit procedure, and submits this to the Council of the EU and the European Parliament. Given the council's decision-making responsibility for enforcing the SGP, defining the actual kind of deficit any individual eurozone country has is bound to be a pan-European affair, including the input of the commission.

In this way, input legitimacy on fiscal matters is not the prerogative of national actors or institutions. This combination or compound of multiple political actors from across member states fits with the already well-noted fact that this crisis has produced a startling Europeanization of fiscal politics (Genschel and Jachtenfuchs 2013). Nevertheless, though these rules and their interpretation are the subject of supranational or compounded input legitimacy, the conceit of the Fiscal Compact's debt brake provision is that the national community is responsible for legitimizing and enforcing them. This separation suggests a disconnect between de facto Europeanization of fiscal decision making and de jure national implementation measures.

### **Conclusion: The Future Role of Input Legitimacy and the Constraining Dissensus in the EU's Political Economy**

Both the eurozone crisis itself and the EU's response to it illustrate fundamental characteristics of contemporary European integration. Never before have complicated EU policy debates played such a central role in national politics, as shown by government instability in the face of meeting EU budget rules. Equally, the response to the crisis, notably the evolution of the ECB's role and the scrapping of the no-bailout policy, shows the EU's capacity for flexibility. As is the historical trend (Moravcsik 2012), an unexpected situation revealed incompleteness in the stage of integration reached—the construction of monetary union without a banking union—and forced policy makers to respond. The need to compensate for this absence highlighted two tensions in the democratic governance of the EU: that between input and output legitimacy and that between rival national definitions of input legitimacy. In this regard, the EU response to the eurozone crisis reveals important dynamics in the relationship between democracy and integration, notably including the effects of the constraining dissensus in the political economy of European integration.

At first glance, input legitimacy, as illustrated by politicians' calls for a loosening of ECB monetary policy, altered the decision making pursued by the EU's central bank. Yet the evidence presented in section two showed that the unorthodox policies pursued by the ECB cannot be reduced to either crisis management or kowtowing to input legitimacy. The chronicle of the ECB decision making is one of pursuing a strategic policy that prompted governments to form a political consensus concerning financial solidarity and conditionality. It was only in this context that the ECB pledged to act as lender of last resort. Hence, the bearers of input legitimacy were ineffective in changing the priorities of an institution founded on output legitimacy. Indeed, the ECB's strategic interactions with EU policy elites have resulted in a policy outcome in which, despite the constraining dissensus, macroeconomic policy is increasingly Europeanized.

This Europeanization is the product of treaties that the ECB wanted to see put in place to shore up EMU. The new legal-political architecture privileges a national definition of input legitimacy, at least in the form of the debt brake system, whose operation is not supervised by supranational, output legitimacy institutions such as the Court of Justice or the commission. While it is up to national parliaments and courts to enforce the fiscal rules of the treaty, the very definition of the structural deficit and the decision to start an excessive deficit procedure are inherently supranational, EU-level processes.

From this perspective, the tension between national bearers of input legitimacy is yet to be felt fully as the enforcement mechanism of the Fiscal Compact will not apply before 2016. Thereafter, the constraining dissensus, which did not prevent—under German leadership, if not hegemony (Paterson 2011)—the adoption of more robust rules on fiscal discipline, is likely to manifest itself in the form of rival attempts to weaken or enforce these very rules. EMU is thus set to be a battleground for bearers of input legitimacy across eurozone countries over national budgetary policies. A foretaste of these clashes may be seen in the efforts of Italy and France to extend the deadline for meeting the 3 percent rule of the SGP, as well as internecine conflict within the French government over how to cut public spending. Added to this complex equation will be the role of national non-majoritarian institutions such as courts, which in many countries have been delegated the power of supervising compliance with balanced-budget rules. Consequently, the tension between output and input legitimacy may well play out at the national level, as well as EU-wide.

What is clear then is that the tensions in EU democratic governance are at the mercy of political economy, in that growth rates and public finances will determine eurozone countries' ability to abide by the new rules for macroeconomic policies. Since integration in this policy area has not been accompanied by a Europeanized form of representative politics, input legitimacy will continue to be defined in predominantly national terms. In turn, the presence of a constraining dissensus means that input legitimacy at the national level will continue to chafe

with the policies of output-oriented institutions as well as with the supranational decision-making structure of macroeconomic policy. So while, in spite of the constraining dissensus, the EMU was rescued for the present, its future prospects remain uncertain.

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