

THE POLITICAL DILEMMA OF THE ECONOMIC AND MONETARY UNION

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Abstract

This article examines the political dilemma faced by the Economic and Monetary Union decision-makers with regards to fiscal policy co-ordination. It argues that two alternatives are available: national fiscal policies, constrained by budgetary rules at a central level, or a federal fiscal system. The operation of both of these options is discussed in accordance with the Optimal Currency Area theory and with reference to the monetary union in Europe. The former proves to be feasible, but not desirable; whereas the latter is desirable, but not feasible.

INTRODUCTION

A monetary union without an accompanying economic and fiscal policy union would prove a house of cards that would collapse with every gust of wind.

(Schiller in Dyson and Featherstone 1999:292)

Having decided to move to the third stage of the monetary integration process in Europe in January 1999, the European Union's member states took a gamble³⁹ hoping for a buoyant future. The euro was meant to reinforce the process of an "ever closer union" and guarantee robust economic growth in the years to come. However, so far the gamble has not paid off as the performance of the Economic and Monetary Union (EMU) over the last five years has been a bitter disappointment. Some of the blame can be put on the European Central Bank (ECB), which pursued an extensively restrictive monetary policy that kept the interest rates uncomfortably high,⁴⁰ and the membership countries themselves, especially the core countries like Germany and France, who failed to introduce the

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³⁹ See M. Obstfeld "Europe's Gamble" (1996).

⁴⁰ Although it has to be stressed that the interest rates have been brought down to historically low levels.

needed structural reforms. However, none of the above are mentioned as often as the Stability and Growth Pact (SGP) as the main reason for EMU sluggishness. Although it is widely accepted that fiscal stimulus is not the best long-term route to growth, it is the Pact's inflexibility that is held responsible.

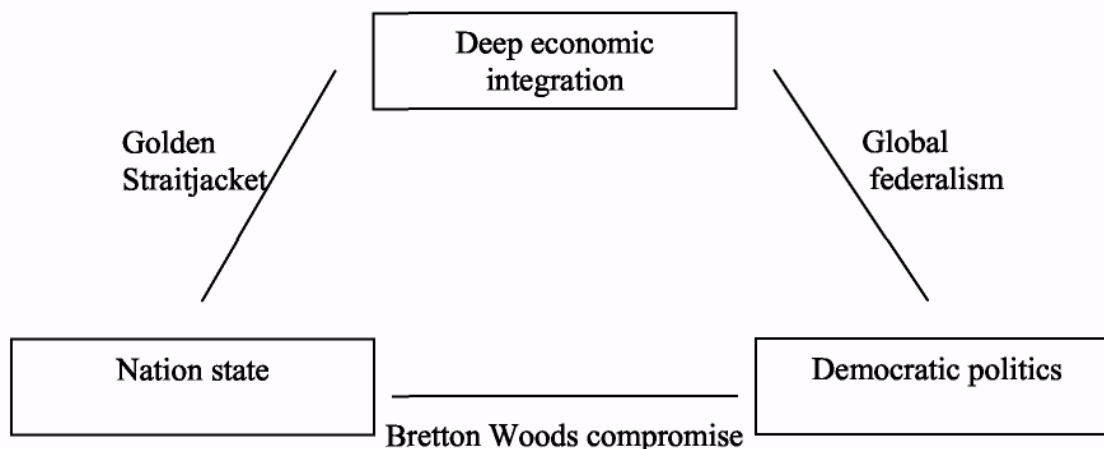
Moreover, the establishment of the EMU brought about a very bizarre policy mix in Europe consisting of a centralised monetary policy accompanied by national fiscal policies. The implementation of the SGP, aiming at securing a viable policy mix, proved to be inefficient. Therefore further development of a European State, based on the embryo of the monetary union, requires in the first place an amendment to the fiscal policy co-ordination rules. Such an action, though, must be backed by a clear recognition of the political project implicit in EMU and development of a fully fledged political arena (Boyer 2000:25, 88).

Taking into consideration the above facts, this article looks at the fiscal aspect of the monetary union in Europe. It envisages a political dilemma facing the EMU decision-makers who are bound to choose between democratic politics and national self-determination as far as fiscal policy of "Euroland" is concerned. By taking the Optimal Currency Area (OCA) theory as a point of departure, it concentrates both on the current co-existence of national budgets and the case of fiscal federalism and discusses the viability of both of these solutions.

THE POLITICAL DILEMMA OF THE EUROZONE

In his article "Feasible Globalizations", Rodrik (2002)⁴¹ conceptualises the political trilemma of the global economy (figure 1) by arguing that "the nation-state system, democratic politics, and full economic integration are mutually incompatible. We can have at most two out of three" (Rodrik 2002:1). As a way-out, he calls for the creation of a renewed "Bretton Woods compromise", preserving some limits on integration while establishing some global rules to handle the growing interconnectedness.

⁴¹ See also Rodrik (2000).

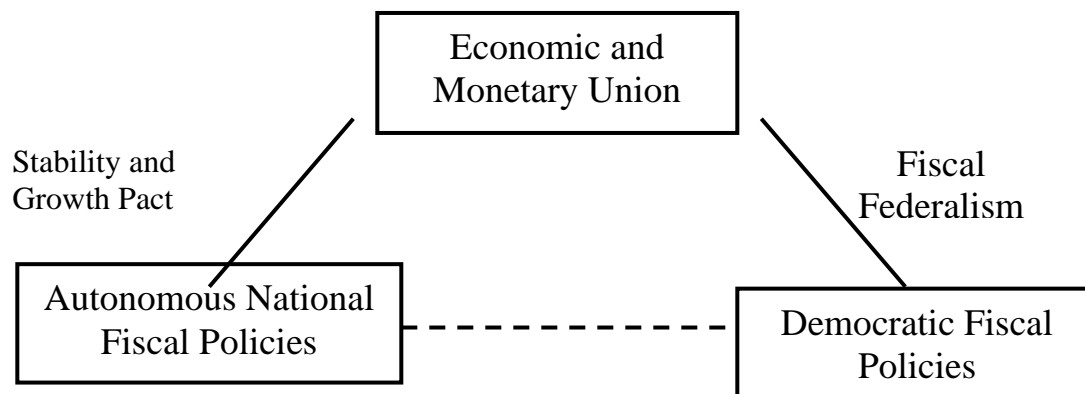
FIGURE 1. THE POLITICAL TRILEMMA OF THE WORLD ECONOMY

Source: Rodrik (2002)

The present author tries to bring this deliberation onto European grounds with special reference to the fiscal dimension of the EMU. Nevertheless, as the process of economic integration has almost been completed in Europe with the implementation of the single currency, backing out of it is not in question.⁴² Therefore there are only two options available (figure 2). We can either have a monetary union with national fiscal policies, strictly limited by fiscal constraints,⁴³ for example in the form of the existing SGP, or a monetary union with a democratic federal fiscal system. However, in order to analyse their sustainability, we first have to examine their roles in accordance with the OCA theory underpinning the concept of a monetary union.

⁴²However, as noted by Eichengreen and Frieden (2001:15): “Technically, exiting the monetary union is straight forward: the government of the participating member state needs only to restart the printing press and reissue the national currency. If a country left the monetary union because it felt that the ECB was following excessively inflationary policies, its ‘good’ domestic currency would drive out the ‘bad’ European currency. If the country instead left because it felt that the ECB’s overly restrictive policies were aggravating unemployment, it would in addition have to declare that the euro would no longer be accepted as legal tender within its borders.”

⁴³Friedman (in Rodrik 2002:15) calls such constraints the “Golden Straitjacket” that a country puts on: “Golden Straitjacket narrows the political and economic policy choices of those in power to relatively tight parameters. [...] Once your country puts on the Golden Straitjacket, its political choices get reduced to Pepsi or Coke – to slight nuances of tastes, slight nuances of policy, slight alterations in design to account for local traditions, some loosening here or there, but never any major deviation from the core golden rules.”

FIGURE 2.**THE POLITICAL DILEMMA OF THE ECONOMIC AND MONETARY UNION**

Source: Own model based on Rodrik (2002)

MONETARY UNION AND NATIONAL BUDGETS

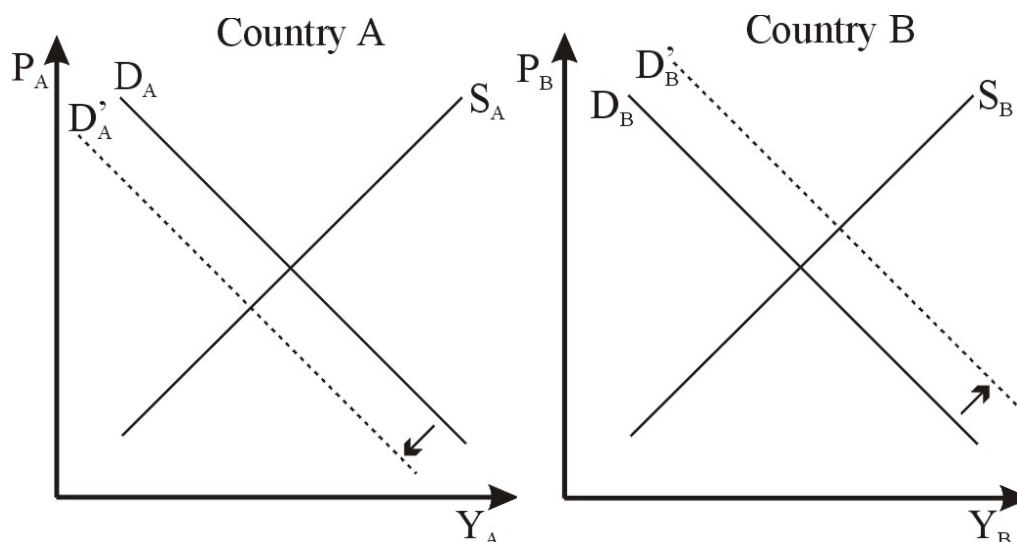
The OCA theory⁴⁴ sets up conditions that countries planning to introduce a common currency have to meet. It approaches the impact of a single exchange rate policy by taking into consideration the exposure of particular monetary union members to asymmetric shocks. It emphasises the operation of adjustment processes based on mobility of labour and wage flexibility, which enable partial or full accommodation of such shocks. Additionally, it lays stress on the high level of fiscal integration between countries or national fiscal flexibility as a further mechanism helping to restore equilibrium.

Let us assume that neither labour mobility nor wage flexibility is able to accommodate fully an asymmetrical shock, and fiscal policy is needed to restore equilibrium. To proceed with this analysis we will concentrate on the case where a monetary union, formed of two countries - Country A and Country B, is accompanied by independent fiscal policies run autonomously by the membership countries. Therefore, a negative demand shock in Country A (figure 3) will cause the budget of this country to go into deficit or will increase the already existing one, because of declining tax revenues and a rising level of unemployment payments. On the contrary, Country B will experience increasing budget surpluses or declining deficits. If capital markets work efficiently, the need for the government of Country A to borrow will be accommodated by the increasing

⁴⁴ For the original texts see Mundell (1961), McKinnon (1963), and Kenen (1969). For contemporary analysis of the OCA theory see for example De Grauwe (1997).

supply of savings in Country B⁴⁵ and the equilibrium will be restored (De Grauwe 1997:192).

FIGURE 3: AGGREGATE DEMAND AND SUPPLY



Source: P. De Grauwe (1997:6)

Based on this simplified model, an argument can be made in favour of fully flexible and autonomous fiscal policies conducted by national governments participating in a monetary union. Moreover, such a way of managing fiscal policy is in line with the principle of subsidiarity as defined by Pius XI (in Inman and Rubinfeld 1998:1):

Just as it is wrong to take away from individuals what they can accomplish by their own ability and effort and entrust it to a community, so it is an injury and at the same time both a serious evil and a disturbance of right order to assign a larger and higher society what can be performed successfully by smaller and lower communities.

As argued by Boyer (2000:88), the implementation of subsidiarity might appear to be a solution to the long-term viability of the single currency.

However, fiscal expansion may appear to be a source of shock itself.⁴⁶ First of all, increasing debt today implies higher taxes tomorrow. If factors of production are

⁴⁵ However, one has to remember that the level of these budgetary effects depends to a large extent on the degree of wage flexibility and labour mobility (De Grauwe 1997:192).

mobile, as in the case of a monetary union, the prospect of raising taxes can lead to a situation of capital flight and labour migration, thus leading to the erosion of the tax base. It would also decrease substantially the competitiveness of a particular country. Therefore, the more integrated the factor markets are, the more difficult it is for a government to increase spending (Eichengreen 1993:1335). Secondly, expansionary fiscal policies of some countries can cause a rise in the interest rates in all the member states, hence, crowd out investment. Furthermore, financial capital inflow will lead to the single currency appreciation and reduction in the competitiveness of export production (Kenen 1995:91). Lastly, there is a problem of budget deficit sustainability.⁴⁷ It is defined as follows (De Grauwe 1997:194):

A budget deficit leads to an increase in government debt which will have to be serviced in the future. If the interest rate on the government debt exceeds the growth rate of the economy, a debt dynamic is set in motion which leads to an ever-increasing government debt relative to GDP. This becomes unsustainable, requiring corrective action.

For that reason, the use of fiscal policy has limits in offsetting negative economic shocks. In addition, due to the spill over effects, national fiscal policies can generate economic instability in all the members of the monetary union.

These arguments, however, were played down constantly by proponents of fiscal autonomy. De Grauwe (1996) argued that once an independent central bank is set up and the governments lose control over their central banks, the capital markets will be able to force them to fiscal retrenchment. The assumption here is that, if the capital markets work efficiently, the problem of growing indebtedness in one country will not be transferred outside its borders as the markets will attach a risk premium only to that particular country's bonds. Therefore, interest rates in other monetary union members will remain unchanged (De Grauwe 1997:198). Dornbusch (1997) points also to the provision of "no-bailout". In accordance with article 103 of the Treaty establishing the European Community (TEC):⁴⁸

⁴⁶ As argued by Obstfeld (1996:280), the fiscal expansion of the Johnson administration during the 1960's helped to bring down the Bretton Woods, whereas the German reunification can be held responsible for the 1992/1993 European Monetary System crisis.

⁴⁷ For further analysis of this problem see De Grauwe (1997).

⁴⁸ The no-bailout clause was also implemented in the "Protocol on the Statue of the European System of Central Banks and of the European Central Bank" (art. 21).

The Community shall not be liable for or assume the commitments of central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of any Member State, without prejudice to mutual financial guarantees for the joint execution of a specific project. A Member State shall not be liable for or assume the commitments of central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of any Member State, without prejudice to mutual financial guarantees for the joint execution of a specific project.

In view of the above, borrowing commitments of Member States are their internal problem, hence, any externalities of fiscal expansions are unlikely. Additionally, regardless of the above critique, von Hagen and Eichengreen (1996) argue that, in the event of financial difficulties, countries retain the possibility of raising their own taxes, which reinforces the credibility of the no-bailout rule.⁴⁹

Nevertheless, none of the above advocates seem to fully recognise the prospect of free-riding once the monetary union is in place. As the Maastricht Treaty does not allow for any country to be expelled from the EMU, a monetary union becomes a public good, and as with every public good, it is exposed to the aforementioned problems. By over borrowing, countries risk defaulting on their debt by means of stopping interest payments on the outstanding debt⁵⁰ (De Grauwe 1997:203). As an ex-post bailout is prohibited under the current readings of both the TEC and the ESCB Statute, the remaining option for the ECB is to bailout countries facing debt crisis by keeping interest rates low to lighten the debt-service burden (ex-ante bailout) (von Hagen and Eichengreen (1996). Such actions, though, might endanger the prime objective of the ECB, i.e. price stability. Therefore, fiscal rules can help to make ECB less likely to face such a dilemma (Masson 1996).⁵¹

⁴⁹ In the debate between the proponents and opponents of binding fiscal rules in the EMU, the United States monetary union experience was also claimed as supporting both positions. The former group pointed to the existence of a state's own voluntary constitutional limitations on borrowing and their usefulness, whereas the latter emphasised the joint absence of post-war defaults by state governments and of federally-imposed fiscal rules (Goldstein and Woglom 1992:253).

⁵⁰ This option is labelled in the literature as an "outright default". The other option available, an "implicit default", is achieved by creating surprise inflation and devaluation in order to reduce the real value of the debt (see De Grauwe 1997).

⁵¹ Another way of eliminating free-riding, stemming from the traditional "realist" approach, would be emergence of a dominant state, a local hegemon, willing to use its power to keep the monetary union functioning effectively on terms agreeable to all (Cohen 2001:192).

FISCAL CONSTRAINS ON NATIONAL BUDGETS IN THE EMU

The above analysis suggests that fully flexible national fiscal policies of monetary union members may be unsustainable in the long-run. Hence, constraints on them seem to be interpreted as safeguards for the Union's credibility. However, in the case of the EMU, the "Golden Straitjacket" was put on countries even prior to the euro introduction. Initially, it took form through the Maastricht convergence criteria⁵² which were meant to secure the establishment of a deeply rooted "stability culture" that would ensure a viable monetary union and enable the ECB to produce stable prices at low real costs (Winkler 1995). Nevertheless, once it appeared that the third stage of the EMU would be composed of a wide number of countries, the fear of free-riding intensified. It led to the implementation, mostly on the German insistence, of the SGP obliging Member States to "respect the medium-term budgetary objective of close to balance or in surplus" (European Council 1997). It also set out the borderline for the budget deficit at the level of 3% of the GDP⁵³ and gave the Council the right to use sanctions amounting to 0.5% of the GDP against countries that are found in breach of the Pact.

Both the Excessive Deficit Procedure, which is a part of the Maastricht Treaty, and the SGP itself, reflect the "structure [of the EMU] that is preoccupied by a 'sound money' view, in which the central risk is perceived to be a 'debt trap'" (Dyson 2000:9). They try to bridge the gap between economic rationale, calling for a closer co-operation of economic policies, and political feasibility. As noted by Tsoukalis (2003:157):

We have created a European single currency with a weak and unbalanced institutional structure, and rigid rules to compensate for those faults. This is what was politically feasible at the time, and the architects of EMU went for it, postponing several difficult decisions – only half-consciously perhaps, since their design closely reflected current economic fashion.

Such a feeble structure may, however, jeopardise the outcome of the monetary integration process.

⁵² For the analysis of the Maastricht convergence criteria see for example Winkler (1999) and De Grauwe (1997).

⁵³ The German preoccupation with the reference value of 3% of the GDP seemed to be theoretical and artificial as no theory supported such a precise figure (see Dyson and Featherstone 1999:9).

The SGP has recently come under severe criticism. It has been renamed the “Stupidity Pact” after the President of the European Commission, R. Prodi, called it stupid (*The Economist* 2002a), and “The Instability and Depression Pact” (*The Economist* 2002b). Moreover, De Grauwe (2002) sees it as a vote of no confidence by the European authorities in regards to the strength of the member countries. According to him:

It is quite surprising that EU-countries have allowed this to happen, and that they have agreed to be subjected to control by European institutions that even the International Monetary Fund does not impose on banana republics (De Grauwe 2002).

Although a requirement of some fiscal constraint within the EMU is widely recognised, the Pact has failed to strike a right balance between the need for rules and flexibility. According to De Grauwe (1997:206-9), “the stability pact has been guided more by the fear of unsustainable debts and deficits than by the need for flexibility”. It is too inflexible, especially at a time of economic slowdown when it forces countries to tighten fiscal policies in the situation of falling tax revenues as their economies slide into recession. It has also failed to distinguish properly between cyclical and structural factors (*The Economist* 2003). Moreover, the reference value of GDP 3% appears to be arbitrary and “could hamper the operation of the automatic stabilisers and thus increase the volatility of output” (Beetsma 2001:24).⁵⁴ Additionally, in November 2003 the SGP appeared to be unenforceable. After it has been breached for two consecutive years by France and Germany, the majority of the Member States voted against the recommendations of the Commission that wanted to initiate the Excessive Deficit Procedure against both of them. In fact, the decision of the ECOFIN Council meant the abolishment of the Pacts rules.

At the very least, the SGP should be redefined in terms of the fiscal balance adjusted over the economic cycle which would give governments a bit more room to respond to a slump (*The Economist* 2002b). It also has to pay more attention to the aggregate fiscal stance. As argued by Buti et al. (2002: 11), “the aggregation of nationally-determined fiscal policies may not result in an optimal fiscal stance at the euro area level... and may not be suitable to ensure an adequate policy mix”. Such an inappropriate fiscal stance may occur even without violation of the Pact.⁵⁵ Reform of it should also eliminate the disincentives to government

⁵⁴ See also Eichengreen and Wyplosz (1998).

⁵⁵ For more on the reform of the SGP see De Grauwe (2003) and Buiter (2003).

investment in infrastructure and human capital, created by the current rules, which are said to be crucial for boosting long term economic growth (De Grauwe 2003). Remodelling the Pact, however, would not remove the “Golden Straitjacket” circumscribing autonomy of national fiscal policies. Therefore, it appears to be worthwhile to consider the option of fiscal federalism in Europe.⁵⁶

MONETARY UNION AND FISCAL FEDERALISM

Let us recall the assumption made earlier in the text: a monetary union, formed by two countries, Country A and Country B, experiences an asymmetrical shock (figure 3) that neither labour mobility nor wage flexibility is able to accommodate fully, and fiscal policy is needed to restore equilibrium. However now we suppose that both countries, apart from centralising their monetary policy conduct, have also centralised a substantial part of their national budgets. Thus, the centralised budget will work as a shock absorber. The decline in tax revenues in Country A will be offset by the increase in transfers from the central budget, whereas the tax revenue increase in Country B will be accompanied by the decline in spending of the central budget. In this way equilibrium will be restored. The main difference between a centralised budget and national fiscal policies is that in the former case the country does not have to increase its external debt and face the prospect of servicing it in the future (De Grauwe 1997:191-192).

The above analysis gives us a reason to claim that the creation of a monetary union should be accompanied by the implementation of fiscal federalism between the countries considered.⁵⁷ The theory of fiscal federalism states that:

...the central government should have the basic responsibility for the macroeconomic stabilisation function and for income redistribution in the form of assistance to the poor. [...] In the absence of monetary and exchange rate prerogatives and with highly open economies that cannot contain much of the expansionary impact of fiscal stimuli, provincial, state, and local governments simply have very limited means for traditional macroeconomic control of their economies (Oates 1999:1121).

⁵⁶ See for example Korkman (2001), Grahl (2001) and the references therein.

⁵⁷ This argument was raised originally by Kenen (1969).

Three distinct functions are being assigned to fiscal federalism (Eichengreen 1993:1337): first, the equalisation function that allows the low-income regions to continuously receive transfers from the rest of the federation;⁵⁸ second, the stabilisation effect that causes the federal tax liabilities of all regions to go down and transfer receipts to go up once all regions enter recession simultaneously; and third, the regional co-insurance function that allows for the increase in the net transfers from the federal budget to a country that enters a recession not experienced by the rest of the federation members, i.e. a country hit by an asymmetrical shock. The last effect is meant to be a necessary component of a viable monetary union.

FISCAL FEDERALISM AND THE EMU

The problem of fiscal co-ordination in the future monetary union in Europe was brought to light during the work of the Werner Group in the 1970's. The MacDougall Report (Commission 1977) suggested the creation of a centralised European budget capable of containing potential asymmetrical shocks. It recommended a three-stage approach (Hitiris 2003:101):

- “pre-federal integration, with a Community public sector taking up 2-2.5% of Community GDP;
- federation with a small Community public sector, 5-7% of GDP;⁵⁹ and
- union with a large Community public sector, 20-25% of GDP.”

Lack of “political homogeneity” at that time to justify such a move was seen as an impediment on the road to a deeper fiscal integration (Hitiris 2003:101). The Delors Report (Commission 1989) reinforced that call by arguing in favour of the establishment of a powerful fiscal shock absorber at the central level, in order to deal with asymmetrical shocks (Kletzer and von Hagen 2001:2). However, none of these claims have been reflected in the Maastricht Treaty.

The debate on fiscal mechanisms in the future monetary union in Europe rests to a large extent on the United States experience. The study of Sala-i-Martin and Sachs (1992), argues that the existence of a federal tax system was the reason behind the

⁵⁸ In the European Union the effect of equalisation is addressed by the notion of cohesion (Eichengreen 1993:1337).

⁵⁹ It has to be remembered that “the Report was considering a monetary union among a smaller and less heterogeneous group of countries than the current members of EMU” (Kletzer and von Hagen 2001:17).

viability of the dollar exchange rate, and found that approximately 40% of the one-dollar shock in a particular State is absorbed by the Federal Government.⁶⁰ Also Bayoumi and Masson (1995) support this view by taking into consideration the case of both the American and Canadian fiscal systems.⁶¹ A more recent study by Kletzer and von Hagen (2001) calls not only for the introduction of fiscal federalism, but an advanced co-ordination of economic policies. It argues that:

...the adoption of a common currency among a set of highly integrated regions implies that governments of these regions should no longer regard policies aiming at structural reforms of their local goods and labour markets as matters of purely regional concern (Kletzer and von Hagen 2001: 37).

Nevertheless, the implementation of fiscal federalism faces at least two major problems as far as the current European Union budget is concerned. First and foremost, it is too small. The budgetary ceiling rests at the level of 1.27% of the GNP and, together with the prohibition of borrowing, it makes the EU budget hardly comparable to the central budget common to federations and the provisions made by the MacDougall Report (Tondl 2000:235-6). Second, the structure of both the revenues and expenditures is far from meeting the functions of fiscal federalism. The revenue side consists of four sources. However, the GNP-based national contributions and the community's share in the VAT account for almost 82% of the total revenues.⁶² The two remaining resources include custom duties and agriculture levies (Hitiris 2003:95-96). The revenues are primarily regressive as the poorer countries generally spend a higher share of their income on consumption and are more import-dependent compared to richer members. A limited progressiveness is reflected only in the case of the GNP-based contributions (Tondl 2000:239). Almost 80% of the budget expenditures are devoted to the Common Agriculture Policy and Structural Funds. The cohesion impact of the former is rather mixed. Although within countries it has a positive redistributive impact, on average it transfers income from richer regions to the poorer ones, where higher food prices have a regressive impact on consumers, as lower income households spend a higher share of their budget on food (Tsoukalis 1997:214). The operation of the latter has a clear redistributive effect. The total transfers in the period of 1994-99 represented 0.45% of the EU GDP and are

⁶⁰ Their results were criticised by von Hagen (1992) for failing to distinguish between the equalisation and insurance functions of transfers.

⁶¹ According to their measures, the stabilisation effect is around 30%.

⁶² Data concerning the EU's general budget for 2002.

estimated to have an income equalisation effect of 5% (Commission data cited by Tsouklais 1997:204). However, it has to be noted that structural fund transfers are not used to correct income differentials, but to finance public investment in the weaker regions (Commission 1989:22).

Therefore, the implementation of the principles of fiscal federalism requires a general modification of the EU budget. As proposed by G. Tondl (2000:252-3):

The central points are the introduction of individual EU taxes, social transfers to individuals, and a sharp reduction of CAP guarantee payments in favour of other expenditure items. The management of interregional distribution, now operated by several funds, could be effected by a single, new cohesion fund.

Having such a healthy-constructed budget would allow at least for the establishment of a system of fiscal equalisation based, for example, on the German *Länderfinanzausgleich* (Kletzer and von Hagen 2001:17).

CONCLUSION

The creation of the EMU in Europe was made possible by political consensus among state leaders. It was meant to become an embryo for a future European State. However, to date the centralisation has taken place only in the monetary component of economic policy. The implementation of the SGP as an element of fiscal co-ordination has proved inefficient. Therefore, the EMU decision-makers are facing a dilemma concerning the conduct of fiscal policies in the monetary union. As neither backing out of the single currency project nor keeping fully autonomous national fiscal policies is possible, they must choose between national fiscal policies, constrained by the ‘Golden Straitjacket’ in the form of some central rules, or the federal fiscal system. This article has analysed their operation in accordance with the Optimal Currency Area theory only, which limits the validity of the agreed upon conclusions, as the problems of the EMU go far beyond the fiscal aspects. Nevertheless, it can be argued that decentralised budgetary policies are feasible, but not desirable. The recent troubles of the Euro zone’s two biggest economies, namely France and Germany, reaffirm that statement. The latter may be desirable, but it is not feasible.⁶³ Fiscal federalism has not yet won enough support in Europe to be treated as more than a theoretical

⁶³ See Rodrik (2002).

option. Still, its implementation appears to be desirable as it could help to correct the democratic deficit in the EMU. The “traditional mystique” surrounding monetary policy could be offset by more democratic accountability required in the case of the federal budget. Thus, a new institution accountable to the European Parliament is required in order to balance the domination of the ECB in the economic debate at the European level. The new born Eurogroup, consisting of finance ministers from the EMU participating countries, seems to be the natural selection (see e.g. Tsoukalis 2003). As Tocqueville predicted, writing in the first half of the nineteenth century, “in the democratic ages which are opening upon us [...] centralisation will be the natural government” (Tocqueville in Oates 1999:1145).

During the work of the European Convention, a great opportunity for changing the current readings of the treaty passed. The draft constitution, prepared by the group chaired by Giscard d’Estaing, has not changed anything as far as the excessive-deficit procedure is concerned. Another chance that is nearing on the horizon is the perspective of budget 2007-13 talks. However, a serious impediment on the road to a federal budget, and further to a European State, might be far beyond economic rationale and political commitments. A successful EMU, where both the “E” and the “M” are in place, might require a genuine sense of community among countries, defined by Keohane and Hoffmann (1991:13) as “a network form of organization, in which individual units are defined not by themselves but in relation to other units”. From that point of view, federalism has still a long way to go in Europe.

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