

European Interview

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## «European federalism has to be established ...»

European Interview with Didier Reynders, Belgian Deputy Prime Minister and Finance and Institutional Reform Minister

**1. The sixth reform of the State in Belgium offers greater power to the regions, notably regarding social and economic management. Observers believe that this agreement will lead to the formation of a government, but on the basis of a multifaceted programme composed by political parties with extremely different affinities. Political affinities seem to be increasingly distinct in the north and the south of the country. How do you see the future of Belgium?**

This has been a permanent bet, ongoing for the last forty years, with increasing transfers of competence towards the federal entities. Since the 1970's Belgium has been in a state of constant change: there have been more important reforms than the present one, notably that of the 1970's which led to the notion of community. Ten years later the notion of the region emerged. Belgium is permanently deepening under pressure from the north of the country, and mainly, regarding economic and social domains. This consists in the belief that regions have to take on greater responsibilities and need to be more autonomous. This phenomenon is evident elsewhere in Europe, whether it is in Catalonia, Bavaria or in the North of Italy. There are many examples of wealthier regions, who want to transfer less to those in difficulty. In their opinion these measures are temporary, because at some point the regions in distress have to recover on their own and assume their responsibilities. The same applies to what the press qualifies as the "stingy" European countries, which do not want to raise their contributions to the European budget any further.

With the new reform in Belgium, we are counting on settling typical, painful issues that bring the linguistic communities into conflict. This is an old debate but the aim is that we now have to say that each region passes to action. Wallonia and Brussels will have the means to manage their own economic and social policies; it will be up to them to show they can recover and catch up on average economic development. We have not reached the last phase of the reform and pressure in the north will stay strong to move onto the next stage.

Will other stages one day force debate over the end of the country as some fear? It comes up more and more frequently. We still have to overcome issues concerning the transfer of competences in which the federal level will remain competent in terms of everything of major importance: foreign affairs, defence, justice, taxation, some security tasks of the police, a share of solidarity with social security. The transfer will be ever greater towards the regions. It is a bet. Whatever shape the reform might take over the next few years, there will be extremely high pressure from the north and this will continue to grow. The only way to stop it, is for Brussels and Wallonia to make structural reform regarding for example, the employment market or the ageing population, which could change economic development greatly. If these regions do not take greater responsibility for themselves and they do not accept this, then tension will be increasingly great. This has been the case in Catalonia for example, with regard to southern Spain. A real capacity to make change has to be demonstrated. This is the real issue at stake.

Brussels is both a Belgian region (Brussels-Capital), the country's capital and a European capital, home to the HQ's many institutions. The Brussels region must be able to play multiple roles, including the transfer of means that are issued at a federal level. It is destined to work more with Flanders and Wallonia and to develop new partnerships. The Brussels region is oriented towards services, and the headquarters of many major groups are concentrated there. The European Commission could also try to give greater value to the city as the main seat of its institutions. In terms of the Belgian question, Brussels has to work with its "hinterland". This is a geographical area that is bigger than the area the city covers itself, but which gravitates around Brussels. For example Brussels airport that lies 14 km from the city centre is in Flanders. This is the case for a great number of activities. So a solution has to be found to include a wider economic and social zone around Brussels. This extends beyond the 19 communities that make up the city. Of course this debate is interminable, because the area is considered to be sacrosanct. There is no question of making the

region bigger from a geographic point of view. I believe that whatever happens, the Brussels region will have to work in a wider framework. It is a major challenge, because the format of action still has to be found.

So, we are at a stage of the process. From the outside this seems dangerous. But consider the European Union, which, in spite of the crises, is moving forwards. It has established peace, the free movement of people, economic prosperity and it has achieved extraordinary results in an institutional system that is constantly changing. Belgium is the same kind of laboratory, but on a smaller scale.

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**2. European countries are structurally in debt. In a period of national and international uncertainty what would you like to say to citizens and also to the markets about the country's stability, as the ratings agencies are threatening to downgrade Belgium? What are the indicators promulgating optimism or pessimism?**

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If we are realistic we cannot hide the fact that there is cause for concern. An increasing share of the population is suffering the consequences of the crisis which is a deep one, and this is emerging in various ways. I understand the "indignants", but as a political leader I have to turn this into reform. Our country is in debt, but in 1993 Belgium was indebted to a total of around 130 GDP points. At the same time France and Germany lay at 40 to 45 points of the GDP. At present, including the post-crisis period, we dropped below the 100 points mark, so we have reduced our debt by 40 points in 15 years. France and Germany have 40 points more. Therefore it is possible that some countries are doing better than we are but we are moving in the right direction. Structurally, we have covered two thirds of the road, whilst others have failed – this is a reason for optimism.

The second point is that we must have a balanced budget by 2015. This will be the focus of the debate over the next few weeks. Our budget has to be below 3% of the deficit, which will give us one of the best scores in the euro zone. Growth is positive and it is above that of the euro zone and it will even be over that of Germany. These are positive signs that we must show to the ratings agencies.

On the downside there is the international situation, where we note a general slowing. Chinese growth is declining, even though the scale is not the same; growth in the USA is decreasing, likewise that of

the emerging countries. The effects of the crisis are worrying. A second concern is caused by the financial structures and the sovereign debt crisis in Europe, either via country to country contagion or via the financial sector. In this context we are worried that we might have the same experience as three years ago, when one institution was unable to honour its commitments, which resulted in a confidence crisis.

With the reform we have just discussed, Belgium has decided to move towards a total change in its funding system. We must be able to show that we can still fund the debt at a federal level. There will be no disruption now. We have to show that we can return to balance and then that we can explain how funds are to be divided up between the regions, the Federal State and the communities. Belgium's challenge, like that of other countries, is to achieve budgetary balance by supporting growth, by providing reassurance and by avoiding austerity measures that impact negatively on growth and employment. Balance has to be found. Over the last few years it has worked well since growth was there. Our employment problem was not as severe as in neighbouring countries and we continue to reduce our debt.

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**3. You are one of the oldest members of the ECOFIN Council. How would you define the Council's development, its prerogatives and also how it operates with 27 members? And what about the development of the Eurogroup?**

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We have evolved from formalism to a club. It is a development which also happens within the IMF, in the Eurogroup and even the ECOFIN Council. When I joined in July 1999 people read out their papers – this seems still to go on in other Council committees! It is no longer the case now for two reasons. The first is that ministers' are constantly present. Nearly all of the ministers attend and there are many meetings. The Eurogroup and also the ECOFIN Council meet at least once a month. Hence ministers stay in Brussels for at least two days. We meet at the FMI, some come to the G20 and the G7. There are many meetings and this creates the club atmosphere. We all know each other. During the 2008 crisis I could use my mobile and quite freely call my European colleagues in the same way as I call my Belgian colleagues. We are in permanent contact, discussion is more open.

The second reason is that by managing issues like the financial crisis, having emergency meetings etc

... we no longer have time to turn up with a written paper, but we negotiate, discuss and exchange ideas in a bid to find solutions. We are moving towards more dialogue. Also when the task force chaired by Herman Van Rompuy was set up, it comprised Finance Ministers only. Firstly, because we mainly speak a lot about finance and above all, because these ministers are used to meet regularly.

However, there is one slight drawback to this club for me as a European, convinced about the European community method – and which is, that it is extremely inter-governmental. We have created a single currency, a central bank but we have left the budgets in the hands of the States. Moreover the Euro Group is not included in any of the treaties – this has been done externally in the annexes. It has become more integrated with the Lisbon Treaty, but this still is not enough. It is no longer the Commission that is so evident, even though it makes many declarations. It has been behind many texts, but with regard to major issues we feel that the Franco-German couple wanted to leave its mark each time and put proposals forward. Only then do the Member States meet, in the Euro Group or within the Council. This is an inter-governmental development. I would like it to be included in the treaties and that we set up a more community-like structure.

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**4. The crisis has shown that the economic governance of the euro zone could be improved and that more unity and common governance are vital. Federalism, which was more theoretical in the past, is no longer a taboo. However, although the idea is better accepted now, differences still exist with regard to methods and amongst other things about how the euro zone is to be piloted. Who is the most legitimate to pilot the machine? Can the Commission stand as the natural manager of European economic governance?**

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The Franco-German couple naturally has a role to play, because when it comes to drawing up new tools, the States have to agree. This couple plays a positive role as a driving force, because they are the two most important economies in the euro zone and we need agreement between these two powers to move on. It must not simply develop into a board of management or into intentions. It is not just about providing impetus, but about leading. We have to find balance. However, in the economic and monetary area, we have to find a federal organisation. In Belgium in 2001, I put

forward an idea of European taxation that was rejected by all my counterparts. I see that things are changing. Michel Barnier and a number of leaders now talk of federalism.

The problem is that we chose to create the euro zone originally with 11 members, now 17, to create an independent European Central Bank with one goal – that of controlled inflation even though it has to take on other responsibilities – but we have allowed the States to manage their budgets. For some States the single currency meant that they entered into federalism without realising it, a bit like Mr Jourdain. They are starting to realise it now. What should this lead to? It means an authority that is able to manage the euro zone's budget, in the same way that the Central Bank manages monetary matters. Budgetary matters could be given to the Commission, if we decided to do so or to a Finance Minister, comparable to the role Ms Ashton plays in terms of foreign policy. Nevertheless this minister could only work with elements that require multilateral agreements, as was the case with Schengen and the modification of the Treaties. It must be able to take budgetary decisions in the place of and instead of the States. There are two ways to do this: either with a European budget – and it will take time before the EU has a budget that allows it manage the economic policies of the various countries. One day maybe the main share of budgetary work will lie in European hands and no longer in those of the States. The other way would be to have a European authority, which apart from making recommendations to the States can sanction them as it sees fit. Everyone agrees to do this for Greece. The 17 States of the Euro Zone must realise that if we set this up for Greece then it could be applied to anyone at any time. But in 2004-2005 when France and Germany were struggling, they asked for greater flexibility rather than requesting integration. Are we prepared to say: let's move towards greater integration and if a country slips by the wayside, will Europe take decisions in its place? Of course in Greece, but in each of the Eurozone countries. This is the area of budgetary integration: the ability to impose decisions on a country which has derailed.

Integration must go hand in hand with the treasury. One day it will be euro-bonds or the enhancement of European capability. We discuss this within the task force. I have been asking for euro-bonds but the strongest countries say "we are going to pay higher interest rates to help struggling countries, without having the guarantee that they will adapt". Some want

euro-bonds to cover solidarity, whilst others want the capability to act to be boosted. At the end of the day both are required in my opinion. I don't know with what we shall start but we shall have to accept developments in both directions. The ideal situation would be for the Commission to play this role, but then the Commission would have to acquire greater legitimacy over the next few years. For example, I would like the President of the Commission to be elected by universal suffrage or initially by members of parliament.

From an economic point of view, we need a European authority to manage budgetary policy, as the Central Bank takes care of monetary policy, with a real capacity to act. This means having the capability to act and to cover funding requirements. These two authorities ought to be able to say: we have taken decisions in Greece; we're putting the budget back on track. That is real federalism, but federalism still has to be accepted as far as budgetary matters are concerned. During an intermediary phase there could be a Finance Minister who is truly autonomous, but in the long run it would be logical for the Commission to govern the zone even if we know that its composition and legitimacy are not be the same as a national government. For there to be development in Europe a major change has to take place.

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**5. The tools to help countries in crisis exist (the European Financial Stabilisation Fund etc ...) but are these adequately adapted to the present crisis? How might they be improved?**

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We experienced the same situation three years ago. The States have had to react, then came European coordination. We have established a financial reaction capability that is sufficiently strong to put an end to all types of speculation. Under the French Presidency of the European Union in 2008, Europeans heard a new word in the fight against the crisis; trillions. The best way to react is to show that in the face of financial speculation, we have pockets that are deep enough to stop this. We did this at the time of the bank crisis. When it comes to supporting States, we are not as ambitious and more cautious. We spoke of trillions of € in 2008, now we are speaking of hundreds of billions of € for the European facility. Belgium's guarantee totals

34 billion €. This is a lot of money, around 10% of the GDP. In 2008 I signed a guarantee of 90 billion € for Dexia bank! The euro zone represents a third of this.

The person in charge of the Council must be able to say clearly to the markets: I have adequate power to act to resist any kind of speculation – otherwise it is impossible. I understand my German friends: no one wants unlimited ability to act if there is no real power to act on the budgets. Look at the USA. California is virtually bankrupt. It could almost take part to the G8 as an independent State and yet its financial state has almost no effect on the markets! Why? Because there is a Federal Reserve, a Secretary of State, a Congress and also Federal Authorities. The whole world is concerned about Greece which represents 2% of the GDP, whilst no one mentions California. This isn't normal, except if we believe that Greece is being attacked individually with regard to its debt and threatens to infect neighbouring countries, because it does not have the capacity to react immediately.

The euro is not struggling. It is a strong currency, which is reaching high exchange rates (1.33) whilst it started off at 1.17. It has even fallen to 0.8. The euro is used as a reserve in several Central Banks; it is used in international contracts. The drawback is that we cannot manage this zone from a budgetary point of view.

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**6. Support to Greece seems to be challenged by various public opinions like Finland, Slovakia and Germany in particular. How do you justify this vital, intra-European solidarity to the Belgian people? What is the best scenario in order to help Greece?**

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Solidarity is a difficult message to convey. The debate we have between the north and the south of Belgium is the same as between the north and the south of Europe. Many European citizens wonder why we should help Greece, or support Portugal? If we do not want to help them out of generosity or solidarity, then we must at least help them out of interest. If we don't help them then contagion will spread to Italy and Spain. It will affect the entire zone and the example of Dexia shows that the sovereign debt crisis is having an impact. All of those with savings and all economic activity

is being affected in Belgium, Germany and France – but it is more difficult to convey the message when it involves Greece than when it affected the Lehman Brothers bank! The second point is that we have to move forward in stages, boosting the means to act in these countries. Some want Greece to leave the euro zone. But why should not Portugal leave – why don't we build another wall and exclude the countries of Central and Eastern Europe? No -we have to move on and this is what we have to explain to Europeans. This does not mean providing endless help but protecting the euro zone by guaranteeing funding. Greece has to take steps itself or let Europe take them in its place. There will be a loss of sovereignty. This debate will be discussed over the next weeks.

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**7. The German Chancellor and the French President want to make major changes to the European treaties. What changes should be made?**

Earlier I pointed out the paths we ought to be investigating. However, there are 27 in the discussion and the procedure is a heavy one. This might be achieved via intergovernmental agreements initially, as we did with Schengen. We are moving along in stages together, with 27 of us if possible, with 17 in the euro zone. Mid or long term, we could also modify the treaties significantly. If we cannot move ahead as 27 then we can do so as 17. The case of Greece is important. We still haven't established the facility system. Greece was helped by means of bilateral loans that were approved by each Parliament. We are moving along step by step, but the aim is to achieve European budgetary federalism.

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**8. In August last the Franco-German couple launched the base for fiscal alignment on company tax. Do you think this measure was useful to enhance the economic governance of the Euro? Which countries, as they form a "hard core" could follow this innovative step? Belgium for example?**

I suggested that Benelux went in this direction and that it could join the movement – which presently depends on France and Germany. We might set up a joint tax system based on company tax. If all of the euro zone

does not follow, then France-Germany-Benelux, along with Italy, the founders of Europe, would represent an important, economically strong area,. We could work on a common tax in a geographically linked zone.

The other debate of taxation is whether one day we might accept that some taxes will be directly paid at European level. It is happening quite surreptitiously. I suggested this in 2001 and Guy Verhofstadt suggested it when he was Prime Minister of Belgium. At the European Council everyone was against it. 10 years on, many colleagues say that we should move towards a tax on financial transactions. This tax would go into the European budget and in exchange we would reduce the States' share of this, which several countries do not want to increase. Hence we would the start of a European fiscal system, even if at first it would only concern financial transactions. I am still convinced that one day the European Union should raise its own taxes. The legitimacy of political authority is based on this. In Belgium the regions want more responsibilities, but we tell them to assume this also by raising taxes, because, for citizens' opinion it is a mean to assessment of the work done by the political authorities. If they are not happy they can have their say and vote against it. This lack of responsibility is more striking on a European level, since citizens are not addressed by taxation. We do not want to admit that Europe also comprises national governments and parliaments. There has been a misunderstanding: when something negative happens it's Brussels' fault, when some positive happens it is thanks to the national government!

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**9. Does the Dexia case challenge the European stress tests? How can the dismantling of this bank be explained? Does the solution satisfy you?**

Dexia bank itself was not dismantled. There was a group with major liabilities and we have consolidated the banking activity, which meant gathering savings together and making a loan on this basis. We have taken Dexia Bank out of the group by buying all of it, 100%, and I would like the bank to undertake its job again – which is gathering savings and not finding funds on the American markets using complex products. The same idea applies in France and Luxembourg. We have

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split the traditional savings banks from the investment bank. From a general point of view, this will be one of the major issues for the banking system over the next few years. I would like us to be able to distribute tasks better through Europe. Let those who work on the markets do so with their own money and those who take savings from the citizens should be monitored and obliged to work with traditional loans. Therefore there would be a separation between savings and loans. Separate activities - this is a move forwards in banking – so that banks' solvency is no longer endangered. The stress tests are tests of solvency. Since 2008 we have known that many banks have increasingly suffered liquidity and solvency problems. We have to define the way these tests are organised. Above all I believe that we have to back up what we have already achieved during the Belgian Presidency of the Union in 2010 and likewise the capabilities of the European supervisory authorities. We now have a European banking supervisory authority. I want its powers to be enhanced, so that it can step up its supervision of the banks from a systemic point of view on a day to day basis. There is a systemic risk committee led by the President of the Central Bank. A multitude of European texts still have to be adopted. Michel Barnier is doing

a great amount of work on this and needs support, from both the Parliament and the Council. Reform is ongoing. We have set up three institutions (banks, insurance, markets), a systemic risk committee, directives have been adopted in terms of boosting supervision. However the road is still long and there is still a lot to do.



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