European Economists for an Alternative Economic Policy in Europe

Better Institutions, Rules and Tools for Full Employment and Social Welfare in Europe

Memorandum 2002

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Summary

1. The practical ***collapse of the Stability and Growth Pact*** is the most recent public demonstration of the complete failure of European economic policy. In recent years the European Union has been unable to assess and foresee correctly the problematic development of the European economy, and unable to organise a positive impact on growth, employment and welfare. The reasons for this policy failure lie in its extremely narrow theoretical approach to economic development and in the rigid institutional arrangements underpinning this approach.

2. The ongoing work of the ***European Convention*** has largely ignored this failure and has sought to preserve and reinforce the underlying ideology and institutional structure. It has displayed hostility to the concept of a specific European social model, which has not even been on its agenda. If these tendencies prevail the result will be a long lasting weakness in economic development and a further demolition of historical social achievements in Europe. It would also impede the integration of the Eastern and Central European Countries in a comprehensive all-European development strategy.

3. As an alternative to this unattractive perspective we propose a thorough reform of European economic and social policy. Reform should be guided by the objectives of full employment, social equity, welfare for all and ecological sustainability as cornerstones of a ***European Social Model***. Concrete strategies to achieve these objectives must be exposed to a broad public debate and a democratically legitimised process of setting priorities and correcting errors.

4. Proposals for a stronger economic policy orientation towards a European Social Model

4.1. The basis for a more democratic and efficient macroeconomic policy should be strengthened:
- The European Parliament and national parliaments should be more involved in economic policy co-ordination.
- The mission of the European Central bank should be broadened to include full employment and sustainable growth
- The EU budget should be raised to 5% of European Gross Domestic Product by 2007
- Tax competition should be eliminated through harmonisation of corporate taxation and mutual information about foreign capital income

4.2. The basis for a stronger European commitment to social welfare should be created
- All members of society should have the unconditional right to decent living resources
- Minimum standards for social expenditure should be introduced
- The public social security systems and particularly the pension systems should be maintained and improved, and no part of them should be privatised.

4.3. Public services in Europe should be strengthened and not be subordinated to the neo-liberal logic of unfettered competition. Ways to achieve this purpose are the definition of national derogations from European competition law, the definition of a framework directive or even a common platform of minimum standards for services of general interest.

4.4. In financial market regulation the public interest must be enforced. This requires the protection of publicly owned, mutual and cooperative institutions from predatory competition and the strengthening and consolidation of supervisory structures in the EU. Also the Takeover Directive should be reformulated so as to take into account the interests of employees, local communities and small and medium enterprises.

1. Self-Immunisation, False Optimism and Continued Austerity amidst Growing Uncertainty: The Broad Economic Policy Guidelines (BEPG) 2002

The current year 2002 has seen repeated downward revisions of official forecasts for economic growth and employment and upward revisions for unemployment in the EU. The substantial growth of 2,75%, predicted in the BEPG 2001, did not take place and the strong recovery expected for this year did not materialise either. Economic growth remains between one half and one per cent and therefore much too low to prevent unemployment rising again. General weakness is compounded by an extraordinarily high wave of dismissals particularly by those corporations in new technologies, telecommunications, media and financial services, which only a few years ago were regarded as the spearheads of the "New Economy" and the basis for the "knowledge-based society" which, according to the Commission, would make Europe the world's most competitive region by 2010. It is now clear that much of the New Economy was not well founded and that the dynamics of financial speculation have led to a build-up of large overcapacities in these areas, driven by an obsessive emulation of the American model of shareholder capitalism.

The present economic fragility is all the more worrying because the EU cannot count on external stimulus to offset the lack of domestic demand. The situation in the US is very unstable and close to recession, and in Japan the long lasting stagnation continues. For the first time in more than twenty years there is a real danger of a deflationary spiral in the world economy.

However, for the European Commission and ECOFIN, none of this gives cause for concern, let alone a reason to review and revise the theoretical basis of their forecasts and policy recommendations. Instead of taking seriously the dangers inherent in the present situation and of recommending strong economic policy responses, they chose the way of self-immunisation by refusing to recognise reality. The key EU economic policy document, the Broad Economic Policy Guidelines (BEPG), sees the EU "at the brink of an economic recovery" as a result of "the swift and decisive response of economic policy, sound fundamentals, a restoration of confidence allied with the unwinding of the impact of a series of adverse economic shocks". Since there is no particular problem the European authorities see no need for a review or a revision of policies. The complacency of the BEPG comes close to absurdity when they state - in a situation of uncertainty and declining investment - that "the commitment to price stability has fostered a culture of stability, reducing uncertainty and promoting wage moderation, thereby providing a necessary basis for an investment-friendly environment". This is a shameful declaration in view of the uncertainty brought about by financial markets, greatly enhanced by the misconduct of a large number of firms.

When it became increasingly obvious that several countries would not be able to keep to the limits for public deficits laid down in the Stability and Growth Pact (SGP) of 1997 and that some governments seem – very reasonably - willing to increase public expenditure to stimulate growth regardless of the public deficit, the Commission responded in a chaotic way. Although it announced its determination to open formal procedures against Portugal and possibly Germany because of excessive deficits, it also proposed to postpone the time horizon for the achievement of balanced budgets. While some public declarations held that the SGP should be interpreted in a flexible way, the president of the Commission qualified the pact as "stupid", thereby endorsing the repeated critique which we have formulated since its adoption in 1997.

However, it is clear that the collapse of the SGP has not provided an incentive to the Commission for a critical re-examination of the theoretical assumptions underlying its policy orientation. This divorce from empirical evidence and reality is a *political* scandal which is very costly for millions of people. The continuing dogmatism of highly paid scientific personnel is also a *scientific* scandal. In this context we want to stress that in our previous memoranda our critical analysis of the situation and our assessment of the prospects for the EU under prevailing economic policies were much more realistic than the position put forward in the BEPG. But the Commission does not bother to take notice of such critiques, let alone enter into an open public debate about its economic priorities and how to achieve them.

The institutional and ideological arrangements behind the failure of European economic policy are laid out in the Treaties of Maastricht and Amsterdam and in the SGP. The coming enlargement of the EU could have been taken as an occasion to correct this problematic basis. Instead, the opposite is happening. The European Convention, whose task is to design a new constitution-like Treaty of the EU by next summer, seems determined to confirm and reinforce the misguided and harmful principles of economic and social construction in the Community. The Convention's proposals for economic governance in the enlarged EU maintain the very narrow mission and the almost complete lack of democratic accountability of the European System of Central Banks (ESCB). They leave no room for a more proactive European fiscal policy – either through an enlarged and flexible European budget or through more comprehensive policy cooperation between member countries. The social dimension of an enlarged Europe, or the specific European social model, which is invoked in political speeches and corresponds to the wishes and expectations of millions of people in Europe, is not on the agenda of the European Convention. This disregard has led to open and in our view very justified protest by some of the members of the Convention and by trade unions and NGOs.

In the present memorandum we propose an alternative approach to European economic policy, based on the concept of a strong European social model, which should in our view be the main guideline for the reform of the European Union. In ***chapter 2*** we discuss the ***cornerstones*** of this European social model. In ***chapter 3*** there is a short discussion of the specific problems raised by the coming ***enlargement***, which requires in our view a comprehensive ***all-European development strategy.*** In ***chapter 4*** we present our proposals for a policy based on the concept of the European social model in four areas: ***macroeconomic policy*** (4.1.), ***social welfare*** (4.2.), ***public services*** (4.3.) and ***financial market regulation*** (4.4.). These proposals are not exhaustive and are not fully elaborated. They are the interim result of a wide debate amongst critical economists and they invite other experts and the public to respond and to broaden the debate.

2. The European Social Model – Cornerstones for an Alternative Economic Strategy in Europe

In official declarations a specific European social model is often invoked as something which has to be preserved and defended against tendencies to subordinate all aspects of social life to the rule of markets and to the imperative of international competitiveness. It is presented as an alternative to neo-liberal policies and to the emulation of the American model with its wide inequalities, its low social cohesion and the enormous economic and social pressures which it puts on the majority of the people. However, beyond this very general rhetorical appreciation the characterisation of the content of a specific European social model remains usually very vague, and practical economic and social policy has been conducted in the opposite direction - towards the US pattern.

We support the concept of a European social model and propose that basic elements of this model should be an essential part of the coming European constitution. Europe is one of the richest regions in the world with a very high potential both to enhance welfare for all people living here – and to support less developed regions of the world. But this potential is not sufficiently developed and realized. Mass unemployment, social polarisation, instability and insecurity have spread over the last two decades during which increasingly market-based orientations have dominated economic policy. We believe that this trend can only be reversed by strong public intervention and control with the objective of defining and implementing an alternative type of economic development.

Political interventions can go wrong – but they can hardly err more than private enterprises have erred during the last decade of boom and bust, with huge overcapacities in many sectors of the "New Economy" subsequently "adjusted" through deep crises and mass dismissals. Political decisions can also be distorted by fraud and corruption – but most of the fraud and corruption revealed recently was committed by private corporations. Errors in economic policy can and must be corrected by public discussion, and by democratic decisions. The costs of such corrections are considerably lower and more fairly distributed than the costs of private fraud and misbehaviour as in the ENRON case which according to a recent study will cost the public more than $200 billion.

The key general principles for an alternative economic policy are public discussion and increased democratic control of and participation in the economic development process. The basis of such discussions and interventions must be publicly formulated objectives which a European social model should fulfil. In our conception there are at least four such basic objectives: full employment, social welfare, social equity and ecological sustainability.

2.1. Full employment

By full employment we mean that every person who is able and willing to work has the right to a decent job.

Since the summit of Lisbon in March 2000 full employment is again a major objective on the EU agenda. But our understanding of full employment differs considerably from that of the European Commission, the ECOFIN and most member states governments. In the official conception the attainment of full employment appears to be essentially a problem of raising the participation rate of the population of working age, pushing people to work regardless of their circumstances and of the working conditions. We are opposed to such a mechanistic view of full employment because it is void of the social substance which makes full employment a desirable goal.

This does not mean that we want to return to the concept of full employment which dominated the social democratic policy agenda during the 1950s and 1960s and which was largely based on male employment. We take into account the changes in technologies and social structures, the emerging new division of labour within families, new individual attitudes and lifestyles, widespread desires for more flexibility in working time arrangements etc. Nevertheless we believe that the following basic principles remain valid:

- Employment must be voluntary and not compulsory. It must correspond to the qualification and preferences of the person employed, and it should offer opportunities for further learning and job improvement.
- Employees should have the right to regular and permanent jobs and not be compelled to accept precarious work.
- Wages or salaries of persons working full time should allow them to lead an independent life without the danger of poverty.
- Employees must enjoy full work protection and rights against dismissal, discrimination and other arbitrary measures from the employers' side.
- All arrangements concerning flexibility in working hours and working conditions require the consent of the employees.

Full employment in this sense is a basic economic, social and political asset for society:
In *economic* terms full employment allows us to make full use of the productive potential of society and thus to enhance welfare. It is also a major contribution to a healthy public budget because it generates tax revenue and reduces public expenditure on unemployment and poverty relief.
Socially full employment is a major factor for social inclusion and integration, enhancing the individual's potential for development and self-respect, strengthening the basis for social cohesion and solidarity. Full employment also strengthens the position of workers and trade unions and can partly offset the systemic disadvantages of labour as against capital.
Finally, full employment is an important factor for *political* stability and an effective response to all kinds of political extremism and fundamentalism.

2.2. Social welfare

Social welfare includes the unconditional right for all persons to a level of material resources which allow a dignified life and access to all basic social and cultural institutions. Essential for the achievement of comprehensive social welfare is a strong and publicly maintained network of social security systems (like pensions and health care) and the provision of public services like education and child care.

A high degree of social cohesion and the eradication of poverty belong also to the declared goals of the EU. In practice, however, policy in many areas is not conducive to these goals and in some has the opposite effects. The latter is particularly true for the so-called “modernisation” of social security systems, which is basically a privatisation strategy. At present the reform of pension schemes is very high on the EU agenda. In shifting public pension systems from public Pay-as-you-go (PAYG) schemes to privately funded capital market schemes this "modernisation" exposes the living standard of future pensioners to the incalculable risks of financial markets. The recent stock market crash and the collapse of large corporations in the USA, in which major pension funds had invested a large fraction of employees’ social security contributions has impressively demonstrated that these markets are not a reliable basis for safe pensions and that crises can push many pensioners into sheer poverty. The reasons which are regularly given to justify such shifts from public PAYG schemes to private capital market schemes, are not only unconvincing but simply fallacious: An ageing population requires – if the present relative living standard of pensioners is to be maintained – a larger real transfer of future production from the working population to the pensioners – regardless of the mechanism by which this transfer is effected. We maintain that such transfers can be carried out via the public PAYG system more safely and with greater social equity. The real thrust behind the shift from public to private schemes is not any objective necessity but much more the interests and lobbying power of large institutional investors, who will obtain command over billions of private insurance contributions to invest on financial markets. It is this prospect for profit and not the problems of an ageing population which propels the modernisation of pension systems.

2.3. Social equity

By social equity we mean the absence of social discrimination and excessive inequality in the distribution of income, wealth and access to material resources, institutions and channels of democratic public discussion and decision taking.

Social equity is also on the agenda of the EU. Efforts are being made to cope with gender discrimination and to establish equal employment opportunities for men and women. But real successes have been few and far between. Gender discrimination in payment and in access to higher positions in corporations and public administration is still very strong.

In most other areas the call for more equity remains largely rhetorical because the EU has no real competence in social policy and cannot deal efficiently with growing inequalities. The instruments for redistribution in the EU – particularly the EFRE and the ESF – do have some impact on poorer countries and regions, but as a whole they are much too small to support a sustained catch-up process. In the context of the coming enlargement this lack of efficient mechanisms for redistribution will become a major obstacle to balanced development and probably also a major source of conflict within the enlarged EU.

Increasing inequality has been a major feature of developments in Europe. The wage share in national income has fallen throughout the Union during the last two decades; the concentration of income and wealth, already high in the 1980s, has in most countries risen further during the 1990s. While disparities in per-capita income have slightly diminished *between* countries, they rose *within* most countries, so that the gap between the better-off regions and the poorer regions in the EU has in fact widened. In some countries homelessness has become a real problem for hundreds of thousands of people. In most countries, young people are particularly badly affected by unemployment and poverty.

2.4. Ecological Sustainability

By ecological sustainability we mean that the exploitation of natural resources should not be extended beyond their capacities of renewal and that the emission of waste into the environment should not exceed its absorption capability.

The consequences of a long-lasting disregard of ecological imperatives have recently been demonstrated by increasingly frequent catastrophes such as floods and storms. Common European projects are needed to contain and reduce wasteful, harmful and energy-intensive production. Ecological sustainability requires, in the first place, a far reaching restructuring process in several core areas of economic and social reproduction: decentralisation of energy provision, greater use of renewable energy sources, attractive public transport infrastructure, less use of chemical fertilizers and other pollutants in agriculture, construction of low energy housing etc. During this process, reductions in ecologically harmful production would be offset by increased expenditure and employment, and therefore growth in the sustainable fields. The changing composition of GDP towards services also creates potential for a shift towards more sustainable patterns of development. The promotion of these comprehensive structural changes should be a high priority for the EU. But so far – apart from some minor advances – it has not been able to overcome the powerful lobbies of the chemical, the automobile, oil and other industries and to enforce a healthier environment for its citizens.

3. Eastern Enlargement - Challenge and Perspective for the European Social Model

Political change in the eastern part of Europe opened the way to eastern enlargement. This is a unique opportunity for East-West reconciliation, to end centuries of controversy between countries and to create a Europe of peace and social progress.

The European Commission has proposed to the December Copenhagen Council that in 2004 eight Central and Eastern European Countries (CEEC) plus Malta and Cyprus should become members of the EU. This is an event of great historical importance. It is also a big challenge for the European social model. The low level of productivity and income in the CEEC necessitates specific measures to make the European social model work for these countries, too, and to prevent the persistence of an eastern periphery, subordinated to the rules of the internal market but excluded from the benefits of the social model.

It has been shown that, even in the “old” EU, the objectives of the social model are insufficiently realised and that thorough reform is required. One of the basic principles should be, that the ***club-approach***, which dominated the accession negotiations and imposed unconditional acceptance of existing EU rules on the CEEC, be replaced by an ***all-European development approach***.

The enlargement is first of all a political action that can strengthen democratic change and economic and social progress in the new member states and also have positive effects on the rest of Eastern Europe. It opens new opportunities for all partners, East and West, but also involves significant risks. Existing member states gain access to CEEC markets with 82 million people. The eastern countries have a large growth potential, natural resources, well educated labour forces and good educational, health and social systems. The enlargement creates opportunities for higher and more stable growth rates in the Union as a whole, and opens up new areas for investment. For the eastern countries accession provides a unique opportunity to accelerate development, adjust and modernise their economies and thus improve the living conditions of the population.

The years of comprehensive systemic change involved a deep transitional crisis. Although recovery has by now started in all countries of the region and reconstruction of their economies is under way, the basic problem for a smooth enlargement process is that the development level of the new members is much lower than the Union's present average. According to the Commission's latest progress report the average per capita income of five central European countries (the Czech Republic, Hungary, Poland, Slovenia and the Slovak Republic) was only 53 percent of the EU average in 2001, that of the three Baltic States 37 percent, and that of Bulgaria and Romania 28 percent, calculated in purchasing power parities. For comparison, the GDP per capita of Greece, Portugal and Spain, the three poorest countries among the 15 existing members, was 78 percent of the Union's average in 2000. Thus GDP per capita in all candidate countries is below that of the poorest member of the Union, and country differences among the eastern countries are much larger than among the present member states. These *quantitative* differences demonstrate a *qualitative* difference in the economic conditions of the candidate countries, so far neglected in the economic strategy of the Union.

In the negotiations for accession, candidate countries were required to adopt all the Union's values and provisions, and they did so. However, the difference in levels of development is so great that growth rates which are twice as high as in the EU15 are needed for the next decades to diminish the existing gap and to bring the CEEC up to the level of the lowest-income countries among the 15. This cannot happen, if the Maastricht criteria are applied to the new members. The persistence of disparities on the present scale between East and West will, sooner or later, lead to intolerable tensions and conflicts.

In our memoranda we have regularly criticised key elements of the economic policy of the EU. We have argued that this policy impedes economic activity and employment in the EU-15. This applies even more to the CEEC. To impair growth in these countries will also lead to negative repercussions on the present member states. To avoid this we need to correct the misguided rules and to reform what at present is an excessively rigid framework for economic policy in Europe.

4. Better Institutions, Rules and Tools for the European Social Model

Thorough changes are needed in the institutional framework and in the rules for economic and social policy in the EU. The current revision of the Treaty by the European Convention is going in the wrong direction. Instead of this aberration we need:

1. A framework for a more democratic and efficient macroeconomic policy.
2. A stronger commitment to social welfare particularly in the area of pensions
3. A stronger and more democratically organised public sector and
4. Enforcement of the public interest in financial markets.

4.1. A framework for a more democratic and more efficient macroeconomic policy

Eliminating the democratic deficit in economic policy co-ordination. The EU economic policy co-ordination framework is fragmented, complex and opaque. Its democratic legitimacy is limited, so that decisions are taken on an intergovernmental basis, while the

European Parliament participates in only two, out of five, co-ordination processes and only in a consultative capacity:

"At the European level, the Parliament for the time being has no formal role in co-ordinating economic policies. The strengthening of the economic co-ordination instruments must go hand in hand with a greater degree of involvement by the European Parliament, with the exact role depending on the instruments being considered, and remaining mindful that the management of economic policy is not a matter for the legislative areas. Similarly, co-operation between the European Parliament and the national parliaments needs to be stepped up" (COM(2002) 247 final/22-5-2002/p.10)

In contrast to this declaration, the actual proposals of the Commission limit themselves to streamlining the policy co-ordination process. The issue of the democratic legitimacy of economic policy co-ordination is not even addressed. And, the role of the ECB is taken as given. The co-ordination problems created by a false dichotomy between economic and monetary policies are not considered. Both the role of the EP and that of the ECB have to be examined and adjustments made to render economic policy formulation and co-ordination more democratic and more rational. In particular, the EP should have greater weight in the co-ordination process, along the lines of its participation in the Community budget process. Also national parliaments have to be included in the co-ordination process at least on a consultative level. Finally it should also be kept in mind that strengthening democracy means involving the public in debates on economic priorities much more than is now the case.

Amending the Stability and Growth Pact. In a deteriorating economic climate policy needs to be reoriented, with full employment as its central objective and with monetary and fiscal policies directed towards this goal. Immediate measures are necessary and possible to stimulate output and employment. But more ambitious medium-term reforms are also required to avoid inadequate rates of development, more unemployment and more exclusion. It is also necessary to democratise European macroeconomic policy and to make it more efficient.

The basic weaknesses of the arrangements surrounding the euro have become obvious in the past year. The economic slowdown has lowered tax revenues and pushed up budget deficits, often towards the 3 per cent limit imposed by the SGP. It should have come as no surprise that economic slowdown would test the 3% limits. It is of course a matter of regret to the advocates of the SGP that 'fiscal discipline' has been undermined, and the credibility of the pact brought into doubt. But there is still a threat that wrong policies will be imposed: if national governments are forced to cut budget deficits in the years ahead, then production will be held back and high unemployment will persist.

It is time for some fundamental changes to the Stability and Growth Pact – to stop it becoming the Instability and Stagnation Pact. Imposing a 'one size fits all' fiscal policy (with balanced budgets over the cycle and an upper limit on deficits of 3 per cent of GDP) prevents national governments from adopting fiscal policies appropriate for their countries. The minimum requirement would be to give national governments enough room for efficient anti-cyclical measures in a framework of European coordination and the further prospect is to use close and flexible policy co-ordination in the Eurogroup and Council as the alternative to the rigid SGP.

Broader objectives for monetary policy. The objectives of the ECB should be reformulated to include a target for growth and full employment, following the model of the US Federal Reserve. It is difficult to reduce the democratic deficit here, because there is no supranational policy authority with clear legitimacy. But it is possible to increase the responsibility of the ECB to the European Parliament and to the Council and to broaden and intensify its dialogue with national political authorities. The ECB would keep its operational independence but with a broader set of objectives (to include full employment and sustainable growth) and with accountability.

Co-ordination between monetary policy and national fiscal policies should be much more effective, and focus on high levels of sustainable economic activity. There must be a move away from the subordination of national fiscal policies to the artificial budgetary limits imposed by the Stability Pact and to the dictates of the ECB. A stronger Euro-group could become the interlocutor of the ECB with regard to monetary policy. If the principle of the BEPG, that the strategic choices of governments should lead to pluriannual programmes for public finances, is to be of any use, the content of the Policy Guidelines must be widened. Monetary policy should be explicitly included and the effects of policies conducted by other countries should be taken into account to assess the gains from co-ordinated action. Strong policy coordination is also necessary to combat tax evasion, criminal transactions and money laundering.

A European Employment Stabilisation Fund (of the order of 1% of EU GDP) should function as an *automatic stabiliser* by organising rapid transfers to countries facing a worse than average deterioration in employment performance. It can be financed either from the EU budget or by separate contributions from the member states. On a member state level the same function would be served by *contingency budgets*, which would be spent when performance dropped below a certain threshold.

Reform of the revenue system. The tax regime in the EU must be reformed in two ways: the federal budget of the EU must be increased, and tax competition between member states must be mitigated.

a. There is no sustainable perspective for growth and full employment without the ***creation of a federal budget*** which provides for recovery on a European level in the case of common shocks (as is the case in the USA) and for interregional redistribution to cope with asymmetries and widening disparities. Given the existing strong reluctance only a moderate increase, to a level of 5% of European GNP by 2007 can be envisaged. Even that would be a break-through. The additional revenues should be raised by (1) reforming the system of own resources, (2) introducing additional taxes and (3) giving the EU the right to incur its own public debt.

(1) We propose a progressive GDP-related EU tax with national GDP as the tax base. Richer countries pay a higher fraction of their GDP, poorer countries a smaller one. This reflects the different abilities to pay and facilitates international redistribution. (2) Additionally, a harmonized securities transaction tax of 1 % on all secondary trades in bonds, shares and derivatives should be levied; the first issuance of securities should be tax exempt. (3) To be able to react to external shocks and to finance long-term transnational investment the EU should obtain the right to issue bonds via the European Investment Bank.

b. To mitigate tax competition and promote a more equitable and efficient system of public finances the EU should harmonise in particular (1) capital taxes, (2) energy taxes and (3) currency transaction taxes. (1) The harmonization of capital taxes is indispensable because ongoing capital tax competition in the EU is eroding the revenue base in all member states. We propose the introduction and strict implementation of the world income principle for the taxation of multinational enterprises to foreclose international tax competition in company taxation. The company tax base should be harmonized and a minimum tax rate of about 45 % should be set. To avoid further tax evasion by private investors a system of mutual information on cross-border interest payments must be established immediately. (2) Member states should introduce a harmonized energy tax, including the energy producing sector, based on the carbon dioxide emission intensity of the energy sources used. To avoid the substitution of nuclear energy for fossil energy nuclear power must be included in energy taxation. (3) Finally, member states should levy a harmonized tax on currency transactions of 1 % (Tobin tax) with the purpose of mitigating financial instability; revenues should be transferred via the United Nations to the developing countries.

4. 2. A stronger commitment to social welfare

The long-term objective in strengthening the European welfare state is a European social constitution which gives every person living in the EU the unconditional right to those levels of income, social protection and welfare which are necessary to lead an independent and dignified life. There must also be a right to democratic participation in social life, which is equally necessary to individual independence and dignity. These basic principles should be incorporated in the new Treaty on the European Union.

One way to concretise this perspective is by a ***comprehensive set of minimum standards***. Such formulations must take national specificities into account but at the same time prevent a competitive “race to the bottom”. Minimum standards should - as we explained in our 2001 memorandum - imply that member countries must dedicate a minimum share of GDP to their welfare systems as a whole. But minimum standards should also be defined for each area of social provision.

The further development of ***social security systems***, particularly the pension and health systems which have come under attack from privatisation strategies in the EU, is of great importance. Sharp falls on European stock markets have pointed out the dangers of privately funded pension schemes and have strengthened the case against further privatisation.

We support changes in the pension system if they improve and expand the present systems and respond to the widespread dissatisfaction of pensioners who criticise the lack of funds and the often bureaucratic character of the system. The basic premise of reform is that the wellbeing of old people has to be preserved. Here we cite the declared objectives of the EU for the pension systems: '*ensure that older people are not placed at risk of poverty and can enjoy a decent standard of living; that they actively share in the economic well-being of their country and can accordingly participate actively in public, social and cultural life'* (*Joint report of the Social Protection Committee and the Economic Policy Committee on objectives and working methods in the area of pensions: applying the open method of coordination, point 1, 2002)*

Since the reforms being carried out at present have very strong regressive effects in the long run, it is of importance that *in the short run* the first alternative is to safeguard the existing public pension systems and, in some cases, to restore the previous public system after damaging changes. This can be done without the alleged problems on the financing side. Full employment is the best guarantee for financing pensions in the short run.

In the medium and long run three basic elements are widely accepted by most commentators: equity, solidarity and decommodification. Equity refers to the relationships among generations but also between the active population and the pensioners. Solidarity is required within and between generations; however, a choice must be made between the option to fight poverty and guarantee an income to all poor people (Beveridgian) or to put more emphasis on guaranteeing the maintenance of the standard of living of contributing workers (Bismarckian). Decommodification, i.e. keeping pensions away from of the market-place, where they would be traded like goods and services, can only be achieved with public systems.

Since the nature of labour markets and society have changed very substantially it may be in the interest of the population to shift public systems from a labour market to a citizenship basis. One way would be to move towards universalisation of pensions entitling all citizens to pensions regardless of their labour-market histories. A less radical way would be to complement a system based on labour by one based on citizenship. A much stronger – and controversial - variant would be to embark on the conception of a basic income for every citizen.

Different national pension systems throughout the EU might persist even in the long-term. But the EU can and should engage in a process of real convergence towards the best social policies and actively contribute towards this by establishing union-wide minimum standards.

Because of the far reaching and controversial nature of the on-going pension reform, a wide social debate should be encouraged. Most of our basic principles go against the main trends of current economic and social policy. Therefore progress will only be possible if the outlook of social and political forces changes. The problem is not technical but ideological and political.

4. 3. Reforming and Strengthening Public Services

Public services (or, in Commission terminology, "services of general economic interest") involve the supply of goods and services needed for daily life and for the exercise of basic individual rights (guaranteed access to energy, to health and health care, to transport, to communications, to education - no matter where one lives, without discrimination and on an equal basis for all). These services contribute to economic, social and geographical cohesion. They can be provided either by the public administration or, under certain conditions, by public or private enterprises. They have been a central issue in the policies of liberalisation and exposure to competition which have been pursued since the early 1990s.

Several factors are invoked to justify actual policies. Some activities, such as telecommunications, which were in the past characterised by economies of scale, have been transformed into activities with diseconomies of scale by technological change, so that it is no longer appropriate to see them as natural monopolies. The segmentation of some activities, in rail transport for example, has permitted the break-up of public enterprises into different parts, some of which could be privatised or subjected to market competition. From many points of view, these "theoretical" reasons have only been a disguise for a retreat from the notion of "public service" under the pressure of neo-liberalism and in the context of budgetary retrenchment.

The future of public services is now an issue in European integration and, more widely, in the framework of WTO negotiations on trade in services. In the founding Treaties of the EU, the basic principle was competition, but scope for "services of general economic interest" was recognised, by allowing nation states to define the fields to be covered by their public services. Since the beginning of the 1990s, the Commission has dealt with public services, not as a whole, but by taking sectors one at a time (telecommunications from 1990, then, successively, freight transport, air transport, electricity, gas, postal services). EU directives have led to a gradual opening up of each sector to competition and have narrowed the scope of public services.

Nevertheless, three factors keep open some possibility of more active intervention. The directives accept the notion of a "network", characterised by increasing returns to scale, and this can be used to argue that there are "natural monopolies" in the sectors involved so that public interventions are justified. The directives in particular sectors also recognise the need to provide a "universal" service - a "minimum set of services, of a given quality, available to everyone at an affordable price". Finally, the role of "services of general economic interest" has been reaffirmed in some of the most recent EU documents.

On the other hand, the WTO's General Agreement on Trade in Services GATS) has given rise to disturbing new constraints on public services. Countries can define exceptions and restrictions to the general rule of liberalisation. But in the regular re-examination of these exceptions every five years it is the WTO which decides whether they are still acceptable. In the case of litigation it is the "Disputes Settlement Body" of the WTO, a tribunal of very questionable democratic legitimacy, which will make the final judgement.

Several proposals for the preservation of the role of public services can now be put forward.

The first possibility would be to explicitly recognise the freedom of member states to define the scope of their own public services and how they will be delivered (how the services are to be financed, whether the enterprises involved will be public or private).

A more ambitious approach would maintain the principle of a framework directive at EU level, to define "services of general interest" and to establish democratic regulatory bodies with the participation of service users and citizens. The notion of "public service" would be wider than that of "universal service". This framework directive would then be interpreted through sectoral directives to take account of the specific characteristics of each sector. This approach would mean that liberalisation and opening up of markets would no longer be considered as the only way to bring about European integration.

A longer-term possibility would be a common European platform of "services of general interest" which would then become obligatory for all member states, with common objectives and joint interventions by EU and national regulators. In this perspective, there would be a clear framework to constrain the working of competition and the drive towards privatisation.

As regards the WTO, EU negotiators, who represent all member countries, should defend a clear concept of public services. Public services should be recognised as essential to the exercise of fundamental rights and should therefore enjoy a special status.

Finally, integration of network services needs an active industrial policy; firstly, to address the distortions which arise from liberalisation and to lay down rules for the interaction of public and private enterprises; secondly, to establish an ambitious policy for European infrastructures to increase the development potential of the EU economy as a whole.

4. 4. Enforcing the public interest in financial markets

Financial integration, envisaged in the Financial Services Action Plan (FSAP), is a key priority of EU leaderships. Their objective is a complete transformation of European financial mechanisms towards a structure which would give much greater weight to capital markets. This strategy is seen as a central component of the drive for European "modernisation" and "competitiveness". This flawed strategy can only exacerbate the imbalance between the social and economic sides of European construction.

The Lisbon agenda, on the basis of a most unrealistic assessment of the functioning of the US economy in the late 1990s, attempts: to accelerate the substitution of security markets for bank credit in the provision of finance; to encourage the growth of fund managing enterprises such as pension as actors on these markets; to harmonise national systems of financial regulation on a minimalist basis; and to remove legal barriers to financial transactions. The central theme of the FSAP, reemphasised by the Lamfalussy Report, has been to reduce transactions costs in the financial sphere, especially in the trading of securities.

Thus attempts are being made to bring about deep changes in many aspects of national economic systems – in corporate law, bankruptcy rules, consumer protection etc. There are also wider implications for social policy, since the financial integration project goes along with attempts to "modernise" social security structures in ways which promote a greater dependence on fund managing enterprises, particularly for pensions (cf. s.4.2.).
Closely associated with the FSAP are repeated attempts to reform and integrate European Takeover codes, so that it would become much easier to buy control of European corporations on stock markets. It is claimed, without strong evidence that such a market contributes to effective industrial restructuring. A liberalised takeover regime would have

serious consequences for job security and the place of employees within European enterprises.

The stock market debacle, the serious macroeconomic situation which followed financial collapse and the revelation of massive malpractice by US corporations demonstrate the lack of a rational foundation for the FSAP and the Takeover Directive in their present forms.

We propose a completely different approach to the EU financial sector. Integration should be based on the assertion of general interests and on a very high level of consumer protection.

One necessary aspect of this strategy is to defend publicly owned, mutual and cooperative financial institutions from predatory competition. Public interest savings and credit institutions can make big contributions, for example by resisting the financial exclusion of low income groups or by supporting activities of community interest. Competition rules in the financial sphere must take these contributions fully into account.

A second aspect of the alternative strategy is to limit instabilities in financial markets. Since market stability is not the responsibility of individual market dealers it is a public good which will be sacrificed if the present drive towards minimal regulation continues.

Thirdly, consumer protection systems should be reinforced and harmonised upwards towards a regime which prevents financial enterprises from selling products unless they have properly investigated their customers' actual interests and requirements.

Finally, the present Takeover Directive should be replaced by a European Restructuring Code which defends the interests of employees, local communities and Small and Medium Enterprises during corporate mergers and acquisitions.

5. Conclusion

In the year ahead the EU has to meet three challenges. It has to fight the threat of economic recession and of a sharp rise in unemployment and social polarisation. It has to achieve enlargement and embark on an all-European development strategy. And it has to incorporate the basic principles and institutions of the larger EU into a new constitutional treaty. In the present and previous memoranda we have criticised the neo-liberal approach and its lack of democratic anchorage. We have proposed alternative economic policies and institutional reforms, based on the guiding principle of a European social model. We do not believe that we have dealt with all aspects or solved all the problems of an alternative economic development strategy and we invite colleagues, experts, the scientific community and the public to give us their critical comments so that we can improve our arguments. But we do believe that our proposals are superior to those of the Commission, the ECB and the ECOFIN Council. We certainly ask the official authorities of the EU to respond to our arguments and to engage in an open controversial debate. But we speak above all to the social movements who are fighting against neo-liberal politics. We want to support these movements by offering our professional scientific expertise and by showing, that the arguments for prevailing policies are wrong and that the thrust behind them is not scientific validity but economic interest and political power. As we have demonstrated in this memorandum and in previous memoranda, there are alternatives to neo-liberal policy in the EU and these alternatives are in the interests of the majority. But the realisation of such alternatives is a matter not only of intellectual insight but also and above all of democratic power. This requires energetic and persistent social and political mobilisation.

To: **European Economists for an Alternative Economic Policy in Europe**

Declaration of support

I support the general direction and main arguments and proposals in the Memorandum 2002:

“Better Institutions, Rules and Tools for Full Employment and Social Welfare in Europe”.

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I would like to be informed about the regular work of the working group and be invited to their meetings.

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Please return this form as soon as possible – **not later than 30th November 2002** – by fax or e-mail to: Prof. Dr. Jörg Huffschmid, fax: +49-421-218-4597, e-mail:Huffschmid@ewig.uni-bremen.de or Jacqueline Runje, fax: +49-421-218-4597, e-mail:jrunje@ewig.uni-bremen.de .