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Financial Solidarity: Ethics of the EU's Financial Response to the Coronavirus Pandemic

Violeta Perea Rubio

Abstract This paper evaluates economic relief packages introduced as an initial response to the first wave of the coronavirus pandemic in Europe between March and June 2020. The support funds were approved by the European Commission and processed by its financial mechanisms, such as the European Central Bank (ECB), European Stability Mechanism (ESM) or the European Investment Fund (EIF). The Next Generation EU economic rescue mechanism saw the first shift to full financial grants. These grants show a big step towards a fiscal union, moving from the already established monetary union of the Euro. Because of the gravity of the pandemic, for the first time in EU history the EC has taken on mutualized debt. After both outlining and evaluating the ethics of these first-wave responses, an in-depth ethical analysis of mutualized debt in the EU is carried out. Ultimately, the EU demonstrated financial collective sovereignty through the mutualized debt solution, securing the natural rights of the collective EU citizen whilst simultaneously respecting the socio-political sovereignty of each individual member state. The paper concludes that big steps were taken towards greater ethical financial solidarity in the EU.

Europe became the epicentre of the Coronavirus pandemic in mid-March 2020. This led to the complete lockdown of most European countries, restrictions on freedom of movement between EU member states, and the first humanitarian crisis on EU soil since its formation as the European Economic Community (EEC) in 1957. By summer 2020, COVID-19 had infected over 18 million and killed 700,000 people worldwide. By August 2nd 2020, there have been over 1.6 million cases and 183,000 deaths in the EU (including the UK).

Eurostat estimates a 6.4% GDP drop in the EU for 2020, the biggest drop on record. Spain is the worst hit with an 9.1% year on year drop in fourth quarter GDP. Thus, the EU is facing its first humanitarian crisis and its worst economic crisis. The EU has had to take unprecedented measures in order to maintain unity and solidarity, and protect European citizens' health, lives and welfare. This directly brings together moral dilemmas with consequence on health and livelihood with financial decisions.

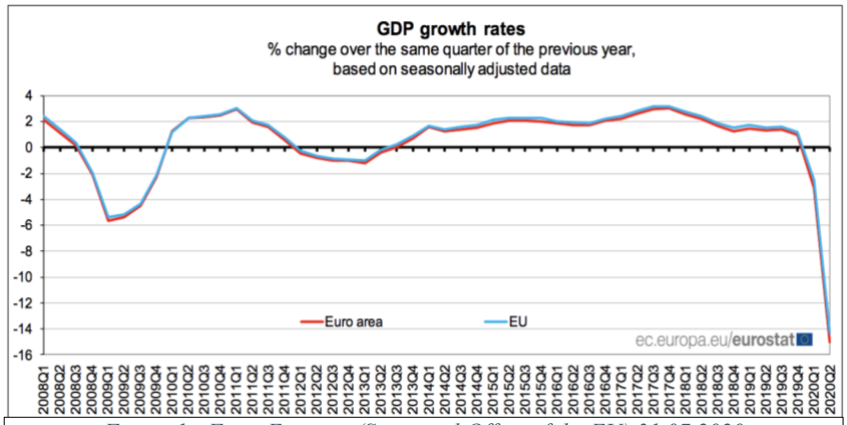


Figure 1 - From Eurostat (Statistical Office of the EU) 31.07.2020 https://ec.europa.eu/eurostat/documents/2995521/11156775/2-31072020-BP-EN.pdf/cbe7522c-ebfa-ef08-be60-b1c9d1bd385b

This paper evaluates the various economic relief packages approved by the European Commission and processed by its various financial mechanisms, such as the European Central Bank (ECB), European Stability Mechanism (ESM) or the European Investment Fund (EIF). The financial aid is divided by short-term emergency relief and long-term economic relief planning – including the 2020-2027 EU budget. Through analysing the ethics of mutualized debt in the context of the EU's emergency relief, it concludes that big steps have been taken towards greater ethical financial solidarity in the EU.

Immediate Measures: Better Late Than Never

Redirecting Funds

The immediate aid received from the EU to individual member states centred around medical equipment, the financing of it, and ensuring the Single Market was upheld despite growing uncertainty over stock capacity. The majority of the early EU financial responses consisted in the repurposing of already existing European Commission (EC) funds within the budget (2014-2020). For example, funding for the RescEU stockpile, launched on March 19th to "support Member States facing shortages of equipment", had an initial budget of €50 million, where 90% would be financed by the EC as a grant and the remaining 10% would be paid for by individual member states requesting the aid. The money used to fund the European Commission's portion was taken out of the EU Civil Protection Mechanism budget. This is set in the Multi-annual Financial Framework (MFF). The 2014-2020 MFF granted the European Commission's Humanitarian Aid and Civil Protection (ECHO) department €7.1 billion for the 7 years, out of which the Covid RescEU funding was taken. In the MFF for 2021-2027, agreed on by the EC on the 21st of July, the RescEU budget will increase by €2 billion (Hans).

Another case of the repurposing of left-over funds from the 2014-2020 MFF budget was the EC's unlocking of €1bn from the European Fund of Strategic Investment (EFSI) as a guarantee for the European Investment Fund (EIF). Using this money, the EIF promotes banks and lenders to grant liquidity to European small to medium size enterprises (SMEs) by issuing "special guarantees" as incentive, helping over 100,000 of these enterprises. This was announced on the 16th of March as an immediate response to lockdowns spreading across Europe, starting with Italy's national lockdown on the 10th of March, followed by Spain's on the 14th. This guarantee allowed for €8 billion in potential financing to help these businesses. The EIF guarantee worked to incentivize banks of member states to support SMEs despite increase liquidity risk. Liquidity risk arises when a company – in this case, SMEs – is unable to sell its assets (ie. a shop-owner's product) in exchange for cash (liquidity) at market value because of a failure of the market, meaning the company is unable to meet its short-term financial demands. The market failure in the COVID-19 crisis was simply a lack of buyers as a result of the lockdown on general movement and non-essential commerce.

Many more instances of repurposing funds from the central budget through amendments were used as a short-term safety net for businesses, workers and the economy. However, the magnitude of the economic strain and impact coronavirus had, is having, and will have on EU member states means these 'leftover' funds are insufficient. Hence, new mechanisms of loans and grants had to be developed both for the short-term and the long-term in order to have access to greater funding.

The immediate repurposing of pre-existing funds is ethical under all evaluations. A moral dilemma could rise if there were various different emergencies taking place where the repurposed funding would directly lead to a lack of funding for another emergency. Luckily, this was not the case. Under an utilitarian analysis it was clear that most people would benefit if the funds were repurposed to account for emergency COVID-19 relief at the start of the pandemic. Nevertheless, the funding available at the early stages of the pandemic was insufficient to account for the scale of the emergency. The delay in developing unique mechanisms that would 'unlock' greater funding because of a lack of consensus between the EU member states showed a shortcoming in moral solidarity through the lack of immediate financial solidarity. The longer the delay – which is discussed in the following section – the greater the negative impact, thus the greater immorality if following a utilitarian perspective.

Pre-Existing Conditions

The lack of a pre-existing and self-sufficient EU budget for the prevention, planning and aid in case of a Public Health Crisis shows a negligence which directly led to greater harm of the population. Norman Daniels evaluates the medical ethics with regards to emergency preparedness. This is directly linked to finance ethics in that medical ethics needs to be supported by funding. Daniels states "the best preparation for major emergencies is a properly functioning public health system that makes appropriate allocation of resources for both emergencies and ordinary needs" (Daniels). The lack of a properly functioning public health system in many countries in the EU is a direct consequence of unethical cuts in financing of public health seen across Europe since the 2008 financial crisis and 2011 debt crisis. Martin Schirdewan, Member of the European Parliament (MEP) representing Germany, found that the EC made 63 individual demands for member states to cut spending on public healthcare or increase privatization of healthcare between 2011 and 2018 (See Figure 2, Schirdewan). Thus, as a result of stringent austerity measures from the EU since the 2008 crisis, public health preparedness was lower leading to greater immediate damage from the pandemic. Retrospectively, this was a clear failure of EU public finance ethics in making national health systems more vulnerable to collapse.

The content of Country-Specific Recommendations from the Commission under the Stability and Growth Pact and the Macroeconomic Imbalance Procedure 2011-2018

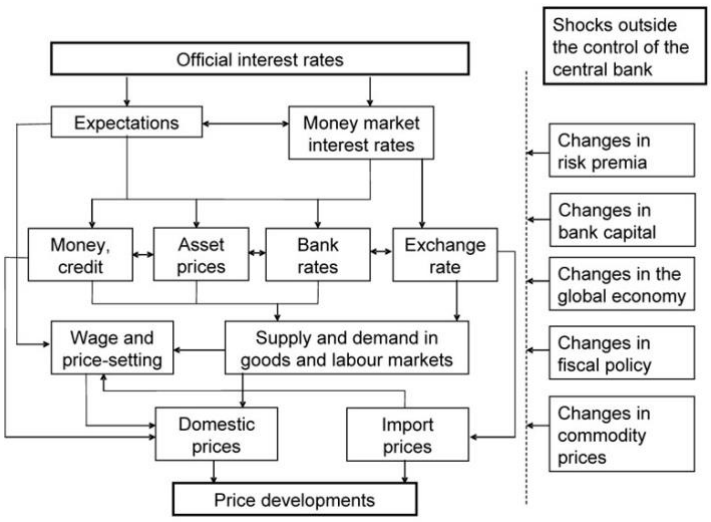
NUMBER OF MEMBER STATES RECEIVING INSTRUCTION FROM COMMISSION

YEAR	Increasing pension age/ cuts to pension funding	Spending cuts on healthcare/ privatisation of healthcare	Suppression of wage growth	Reducing job security/workers' bargaining rights	Reducing support for unemployed, vulnerable or people with disabilities
2011	14	2	7	5	8
2012	13	3	6	7	10
2013	15	10	6	9	6
2014	17	16	13	10	9
2015	13	9	8	3	3
2016	10	8	4	2	3
2017	10	5	4	2	3
2018	13	10	2	0	3
TOTAL:	105	63	50	38	45

Pandemic Emergency Purchase Programme

Financially, the ECB created the Pandemic Emergency Purchase Programme (PEPP) worth €750 billion. It is a temporary asset purchase programme of both public and private sector securities. This monetary policy aimed at minimizing the risks to and stabilizing the monetary policy transmission mechanism resulting from the pandemic. Through the PEPP, the ECB purchases bonds from corporations and countries within the Eurozone without limiting eligibility. The PEPP is a temporary measure, repeatedly emphasized by the ECB, expected to terminate by the end of 2020. This deadline was later expanded to June 2021, demonstrating the flexible and responsive approach to monetary policy taken by the ECB.

The PEPP budget was increased on the 4th of June with an additional €600 billion. In practice, the PEPP 'relaxed' eligibility allows the purchase of securities issued by countries and corporations with low credit ratings, such as the Greek



Monetary policy transmission mechanism. Source: European Central Bank

Government. The maturities of these securities range from 70 days to 30 years.

The leniency of monetary policy demonstrated by the quick turnover of the PEPP to complement pre-existing asset purchase programmes shows financial solidarity among central European institutions. This measure removes eligibility requirements thus acknowledging the symmetric shock of the pandemic. It removes any sense of blame for the greater financial impact of the pandemic in certain countries, extending aid to all.

To Grant or to Loan – That is the Question

The main debates in the development of an EU financial relief package have revolved around the question of whether to grant or to loan aid, the debate of the so-called 'coronabonds'. It is important to clearly define and outline the differences between a *grant* and a *loan*, which although obvious in definition, is more complex in practice, particularly within a federal framework like the EU's.

Simply, a grant is a form of financial donation whereby the recipient is not obliged to repay the borrowed money. Usually, grants are given under certain strict conditions within the EU. The standard rule for grants from EU central budget to individual member states are as follow: (1) Transparency and non-discrimination in the process; (2) Nationality rule and country eligibility; (3) No-profit rule, i.e. countries may not use the grant to fund an action which generates profit; (4) Co-

financing between grant and beneficiary; (5) Non-cumulation.[1] In terms of management, standard EU grants give two options: direct management or indirect management. The former gives grants under the condition the project receiving grant aid is overlooked and directed by the EU whereas indirect management requires a third-party partner to perform as the contracting authority. The difference with grants in times of coronavirus however, is that they are not coming from already EU-held money in the central budget. Instead, because of the unexpected and urgent need of large amounts of funding, the European Commission needs to borrow money from the international capital markets through bonds and enter into debt, either mutualized debt (shared across member states evenly) or not – another central point of conflict and division in the resolution of the COVID-19 financial crisis.

On the other hand, a loan requires a repayment at a certain interest rate. Before the pandemic, the EU had one main loan programme for its member states facilitated through the European Financial Stability Mechanism (EFSM). Two other loan programmes are directed for assistance to partner countries that are non-EU member states. In all loan programmes, the European Commission issues bonds on the international capital market on behalf of the EU using its position as a top-rated borrower. Then, the EC lends this money to the member state in financial need with the same interest rates they were given as a result of the EU's top-rated position, a significantly better rate than those available to the member state if it were to issue its own bonds. Thus, the EC facilitates better deals for its member states, but nevertheless requires re-payment of the loan, as opposed to grants.

From the beginning of the pandemic, the question in the EU of whether to give out loans or grants was central in the planning of financial relief packages. This primarily centred around two key packages: the early package in April (SURE, EIB, ESM) and the much greater Next Generation EU package approved on the 21st of July alongside the new MFF budget for 2021-27. The debates surrounding both packages and the division between member states help outline the key moral questions.

Divided Europe: Initial Blaming

Yet, these programmes were greatly delayed because of growing divisions within the EU, diminishing their potential maximum benefit. Throughout March and April, European member states entered into polarized debates over the nature of EU centralized financial aid. This created a 'north-south' divide within the EU. The 'northern' countries were primarily led by The Netherlands, with Germany moving away from this position as the pandemic continued, and becoming a

[1] See https://ec.europa.eu/international-partnerships/grants_en for outline of standard EU granting practices.

central mediator. The southern countries were led by France together with Spain, Italy, and Portugal among others. The frugal northern states were against grants and mutualization of debt. In contrast, the southern states urged financial solidarity to combat the symmetric shock. This debate led to the delay in agreements on potential financial solutions and aid, prolonging any agreement by over a month at the most critical points of the pandemic.

The "coronabond" the southern countries asked for would require mutualized debt taken out by the EU and distributed to member states in need through grants, not loans. This would mean states with stronger economies in the EU – like Germany - would contribute more to the mutualized debt and benefit less from it. This issue created opposition to mutualized debt from the 'frugal' states. They demanded strict eligibility requirements and implementation measures for member states wishing to access loans from the European Stability Mechanism. Thus, they proposed a recovery scheme alarmingly similar to the one proposed to Greece during the 2011 sovereign-debt crisis involving stringent austerity measures. In arguing for the sole use of the ESM, without the creation of another unique body to meet the demands of this unique crisis, the frugal states wrongly suggested there was a fiscal element to the crisis caused by the pandemic, implying fiscal mismanagement took place in the worst-hit countries, such as Spain and Italy. This indirectly blames countries worst affected by the external and unpredictable shock of the pandemic. Indeed, in the midst of the pandemic, Dutch Finance Minister Wopke Hoekstra called for an "investigation" into potential financial mismanagement in these countries since the 2008 crash, further implying blame for the blame-less situation that is a pandemic as an external phenomenon.

Why is this blaming unethical? Blame implies moral responsibility over actions and consequences. However, an action or consequence has to be blameworthy. Because of the external, unexpected, and symmetric nature of the pandemic, the consequences are not blameworthy. Much like US President Trump tried to directly blame China, the aspect of blameworthiness in this situation is reduced to unethical and unjust scapegoating. Scapegoating is the singling out of person or group with unmerited blame leading to negative outcomes. Miranda Fricker's theory of blame outlines three key considerations: "(1) facts about the blamer, (2) facts about the blaming interaction itself, (3) facts about person being blamed" ((Tognazzini and Coates). A key consideration for the person being blamed is the extent to which she has moral agency. In the case of the pandemic, there is minimal moral agency. Individuals can be blamed for the management of the pandemic as it develops, however placing blame from the outset merges the just blameworthiness on free action (ie. management of lockdowns, cuts on healthcare) with the unjust blame on the external, un-agented, shock of the pandemic. Thus, the blame underpinning much of the opposition to common EU funding of coronavirus relief at the beginning of the pandemic was unethical and unfounded.

In response to the opposition from frugal states, Ursula von der Leyen, the President of the EC, apologized for delayed action at the beginning of the pandemic, particularly regarding Italy, stating: "But saying sorry only counts for something if it changes behaviour […] we must protect each other to protect ourselves. And the truth is too that Europe has now become the world's beating heart of solidarity. The real Europe is standing up, the one that is there for each other when it is needed the most." In this, she called for the reinstating of the founding tenet of solidarity, which was being threatened by the opposition to immediate, mutualized aid. European solidarity is usually manifested in socio-political terms, as it is inscribed in the 1993 founding Maastricht Treaty: "DESIRING to deepen the solidarity between their peoples while respecting their history, their culture and their traditions." However, the pandemic has emphasized the need for economic and financial solidarity within the EU.

United Europe: Three Safety Nets

On the 9th of April, the Eurogroup put forward its first major economic package, with €540 billion as an emergency fund. €240 billion of these were available through the ESM fund as cheap credit. A further €200 billion came from the EIB to help companies and SMEs. Lastly, a €100 billion scheme known as the SURE programme (Support to mitigate Unemployment Risks in an Emergency) was created to pay wages for workers unable to work as a result of the pandemic and counter rapid peaks in unemployment. Yet, this funding was primarily made up of loans at very favourable rates, not grants, thus a rejection of pleas from countries like Spain and Italy of mutualized debt.

Countries are allowed access to up to 2% of their national GDP (as of 2019) from the ESM fund for the Pandemic Crisis Support. Support is available to all member states as opt-in. The only requirement for access to the credit line is a commitment to invest borrowed money on COVID-19 related costs. Access to the credit line will be open until 2022. To repay this loan, each individual borrowing country will need to pay a margin of 10 basis points (0.1% interest), an upfront one-off fee of 0.25% and an annual service fee of 0.005% (ESM Statistics). This repayment scheme is much lower than the ESM's usual credit lines. The loans have a maximum maturity of 10 years. This therefore removes all of the problematic conditionality previously linked to the ESM since their bailout of Greece and Ireland.

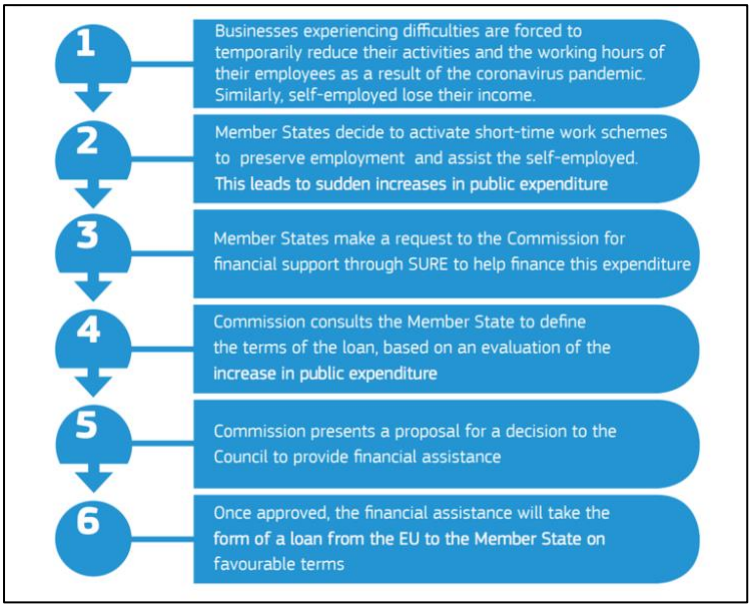


Figure 2 SURE Program

The SURE loans to help mitigate the impact of coronavirus on unemployment will be operational until December 2022. It is funded through a combination of member state contribution and EC funds. The EC will raise the majority of the funds on the international capital markets, using Europe's AAA rating to get the best borrowing deals for member states. The loan program is administered by the ECB. The loans will also be backed by guarantees from member states of up to $25 billion. This measure directly aids workers in vulnerable jobs. Repayment of loans will be offered under "favourable conditions", significantly better than if individual member states were to borrow from the capital market.

The EIB's fund aims to guarantee up to €200 billion in loans to businesses and companies struggling with the pandemic. It is mainly directed to small and medium-sized enterprises (SMEs – up to 249 employees). It is financed by the contribution of €25 billion from each EU government. This shows a move away from national stimulus packages to EU-wide co-ordinated packages to stimulate the EU economy as a whole. The fund is available until the end of 2021, with room for extension. 65% of the fund is reserved for SME, 28% for non-SMEs with up to 3,000 employees, 5% for public sector entities, and 7% for venture and growth capital through the European Investment Fund (EIF). To benefit from these funds, the individual company must prove it is viable in the long-term if not for the pandemic. Repayment will be offered at the favourable rates granted to the EIF on the capital markets with its AAA rating. Thus, the majority of the early sizeable packages were financed by loans.

Next Generation EU

The breakthrough package was the Next Generation EU which saw the first shift to full financial grants. On July 21st 2020 the EU agreed to a €750 billion recovery effort through the ECB. Of this, €390 billion will be given out in the form of **grants**. The remaining €360 euros will be given out as loans to individual member states. Originally, the European Commission's proposal, backed by France and Germany, demanded €500 billion in grants, however this was reduced because of pressure from the frugal states. The grants are facilitated by a new mechanism called the Recovery and Resilience Facility. The €750 billion is financed by the European Commission who will borrow from the international capital markets taking advantage of premium rates. These grants will be distributed between 2021-2023. In terms of repayment of the **loans**, all liabilities are to be paid by December 2058.

These grants show a big step towards a fiscal union, moving from the already established monetary union of the Euro. Although Article 125 of the treaty on the functioning of the European Union states: "The Union 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", an article often used in opposition to mutualized debt, the clause "for the joint execution of a specific project" justifies the use of a mutualized debt for extraordinary circumstances that require joint execution of projects, such is the pandemic. This is the first time in the EU's history that the EC has taken on mutualized debt.

Nevertheless, because of the resistance from the frugal states some conditions have been implemented for the giving out of the grants. Firstly, each member state will need to prepare a national recovery plan for their post-coronavirus economic reform. Secondly, The Netherlands introduced a veto-like system where an individual member state can raise objections if it feels a grantee state is failing to meet their reform promises. This gives any state the power to temporarily halt financial transfers to said country whilst the EU reviews this claim. The review time can take up to 3 months, during which the country would not be receiving grants.

Alongside the Next Generation EU package, the EU approved the MFF for 2021-2027 which is also fundamental in recovery planning. The governments agreed on a €1.074 trillion budget. This budget "will also be the main instrument for implementing the recovery package to tackle the socio-economic consequences of the COVID-19 pandemic" alongside Next Generation EU, according to the European Council. The EU budget is financed primarily through member state contributions in proportion to their Gross National Income. Hence, it is often said Germany pays for the EU, as it is the country with the highest Gross National

Income. The budget is further funded by import duties and percentages of individual member states' VAT rates.

Ethics of Mutualized Debt

Why should one sovereign state pay for a less-economically stable state's economic recovery? The central moral questions surrounding the grants was the mutualization of debt wherein all member states would contribute equal relative amounts (depending on GDP). A good comparison to make for understanding the morality of mutualized debt in this extraordinary circumstance is a comparison with a tax-funded national welfare system. In most EU countries, each individual citizen contributes different amounts to the public welfare system depending on income through the income tax. If you earn more money annually, you give more money proportional to this. This follows the fundamental ethical principles of generosity (and Rawlsian distributive justice) – giving when you have excess to those who do not. Aristotle's proposes the idea of the 'golden mean' as part of his virtue ethics. The 'golden mean' pushes for the middle between two extremes, between excess and deficiency. Generosity becomes virtuous and ethical in its mediating position in the 'golden mean'; she who has excess money returns to the golden mean by generously giving to one who has financial deficiency, bringing both parties to the 'golden mean'. This is why systems like welfare states or charity organizations are ethical in attempting to bridge inequality between excess and deficiency, albeit only if there are no ulterior motifs to the generosity (i.e. power, guilt).

Mutualized debt helps reach the virtuous 'golden mean' through similar means as welfare systems which EU countries already have in place. As with the MFF EU budget, each member state's financial input is determined by its own national GDP. Those with higher GDPs, like Germany and France, contribute the greatest amount to the budget, or to the Next Generation EU scheme, and receive the same in return, oftentimes needing less in return. The Next Generation EU Scheme likewise helps reach the 'golden mean' between the different, unaccountable shocks of the pandemic on different countries in the EU as well as the disparity in financial means. This is what other relief tools, like the RescEU, did with medical stockpile to help countries with deficiency of equipment and excess in the impact of the pandemic. However, the mutualized debt brings this from material generosity to explicit financial generosity. Thus, the mutualized debt implicit in the Next Generation EU Scheme is a striking example of ethics in public finance. The objection to mutualized debt during a pandemic when extraordinary circumstance means greater disparity between those in excess financially and those in deficiency is therefore, unethical.

A European Social Contract

Furthermore, one can argue there is a European Social Contract, a moral contract alongside the administrative and political contract of a country joining the EU. Indeed, the Maastricht Treaty established the 'Citizenship of the Union' as its key tenet. Thus, in entering the EU, an individual in any member state has a symbolic dual citizenship: that of her native state and her collective EU citizenship. However, this arguably creates conflicting 'contracts' and conflicting loyalties. Should an EU leader aim to protect her own national citizens' rights and health over that of the EU citizen collective or vice versa? The question of EU citizenship and the extent to which there is a European Social Contract in the Hobbesian sense is problematized in cases of emergency lending to poorer states.

For Hobbes, a social contract is the "mutual transferring of rights", as voiced in his seminal work *Leviathan* (1651). Yet, within a society, this is mediated through a sovereign authority, either "sovereign by institution" or "sovereign by acquisition". The EU problematizes this sovereignty which Hobbes deems fundamental to the fruition of the contract in creating two coexisting sovereignties – the sovereignty of the EU and that of the member state. Although the EU emphasises it respects the sovereignty of member state over that of the institution, in moments of crisis, this is tested when the need of collective action arises. Yet, this conflict of sovereignties in times of emergency can be resolved by separating distinct sovereignties: the financial/economic sovereignty and the socio-political sovereignty. This separation arguably took place in the final collective decision for large-scale mutualized debt in resolution of the developing economic crisis. The main opposition revolved on conflicting sovereignty and loyalty. Leaders felt they needed to prioritize their own national citizens' health and safety over that of the collective EU citizens. This led to the initial closure of borders and bans on transporting certain material, such as PPE, threatening one of the key tenets of free trade and movement within the EU. Both frugals and the 'southern' states had their own national citizens' rights to health prioritized over that of the EU citizen. However, where the former voiced this through hesitancy to extend a hand financially, the latter desired the health of EU citizens in general in order to secure rights for their own national citizen. Ultimately, the EU demonstrated the need for financial collective sovereignty through the mutualized debt solution in order to secure the natural rights of the collective EU citizen whilst simultaneously respecting the socio-political sovereignty of each individual member state.

The Future of the EU's Financial Solidarity

Although at the beginning of the crisis it seemed the EU was failing to live up to its promise of solidarity and protection to its EU citizens in its failure to take immediate action to help the worst affected member states like Italy, the agreement on the mutualization of debt through the Next Generation EU plan shows it was ultimately able to demonstrate financial solidarity. Hopefully, this continues in the

future and changes the EU's attitudes towards mutualization of debt as an ethical financial tool to display generosity, solidarity and uphold the rights of all EU citizens alike.

All statistics used in this paper are from the European Commission official statements on the website unless otherwise specified.

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