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Tectonic shifts in the EU's institutional system

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Summary

| | |
|---|-----------|
| Abstract | 4 |
| 1. Introduction | 5 |
| 2. The key elements of the response to COVID-19 | 6 |
| 2.1 Initiation of a new asset purchase programme | 6 |
| 2.2 Suspension of the fiscal rules | 6 |
| 2.3 Creation of an unemployment insurance scheme and an ESM crisis support credit line | 7 |
| 2.4 Establishment of the Recovery and Resilience Facility | 7 |
| 3. Continuity and change in the European Union | 9 |
| 3.1 Continuity | 9 |
| 3.2 Change | 9 |
| 4. Different lenses to look at the shifts | 11 |
| 4.1 Inter-institutional balance | 11 |
| 4.2 Euro-national parliamentary system | 12 |
| 4.3 EU Economic Governance | 13 |
| 5. Evolution or revolution? | 15 |
| 5.1 Evolution | 15 |
| 5.2 Revolution | 16 |
| 6. Conclusion | 17 |
| Bibliography | 19 |
| Author information | 22 |
| About Luiss School of Government | 24 |
| Submission Guidelines | 25 |
| SoG Working Papers | 26 |

Abstract

The EU's current fiscal and economic response to COVID-19 contains several different elements, including the agreement on a € 750 billion Recovery and Resilience Facility. Criticised by some as "too little too late" and hailed by others as a "Hamiltonian moment", this paper uses three different institutional lenses to look at the institutional shifts that this response entails. The measures affect the inter-institutional balance by strengthening both the European Commission and the national governments in the Council while the European Parliament as well as national parliaments have been mostly side-lined. In addition, the response stops further Euro area integration and pushes back differentiated integration. All this amounts to tectonic changes which were unconceivable a year ago.

1. Introduction

At the beginning of 2020, nobody would have predicted that any fundamental changes in the EU's institutional system might happen soon. The Conference on the Future of Europe was an exciting idea, but mostly an empty shell. Germany and France had put their ideas into a non-paper and the EU institutions were defining their positions on how the Conference should work and what its tasks should be. No big institutional changes were imminent. Discussions about them were expected to take place at the Conference on the Future of Europe later in 2020.

When COVID-19 was starting to hit Europe in February and March 2020, the initial responses were national. Very soon, however, many decision-makers recognised that the EU had to give a massive financial response in order to reduce the economic impact of the pandemic. The agreement to mobilise € 750 billion at the European Council summit in July 2020 became a very significant development, not only financially, but also institutionally.¹ The Next Generation EU (NGEU) package greatly increases the amount of money that is distributed during the Multiannual Financial Framework (MFF) for 2021 to 2027. The envisaged creation of own resources and debt issued by the EU means that the impact of these decisions will last beyond the 2020s. The governance mix for the recovery fund that mostly involves the European Commission and national governments is also an institutional innovation.

This paper is structured as follows: It presents the key elements of the EU's response to COVID-19 and then discusses continuity and change in the European Union. The next two sections propose three different lenses to look at these shifts and they assess the evolutionary versus revolutionary aspects of what has happened. According to the definition in the Merriam Webster dictionary, *tectonic* means "having a strong and widespread impact"². Shifts that are tectonic should therefore have major consequences, produce material changes, alter existing practices significantly or lead to substantial re-arrangements. The paper concludes that there are indeed tectonic changes in the EU's institutional system. Enhancing its legitimacy and accountability must therefore be discussed at the forthcoming Conference on the Future of Europe in order to put concrete remedying measures into place as quickly as possible.

¹ The scientific analysis of the EU's response has already started, for instance with respect to whether it constitutes a "critical juncture" in the transformation of the EU (Fasone and Lindseth 2020: 22-30).

² "Tectonic", Merriam-Webster Dictionary, <https://www.merriam-webster.com/dictionary/tectonic> (last accessed 30 October 2020).

2. The key elements of the response to COVID-19

The fiscal and economic side of the EU's response to COVID-19 was sometimes criticised as “too little too late”. It consists of several key elements which are now briefly discussed one after the other: The ECB's asset purchase programme, the suspension of fiscal rules, the creation of an unemployment scheme and an ESM crisis support credit line as well as the agreement on the Recovery and Resilience Facility (RRF).

2.1 Initiation of a new asset purchase programme

The European Central Bank (ECB) announced the Pandemic Emergency Purchase Programme (PEPP) as a temporary asset purchase programme of private and public sector securities with an envelope of € 750 billion on 18 March 2020 (increased by € 600 billion to a total of € 1,350 billion in June 2020). The programme is another non-standard monetary policy measure to counter the serious risks posed by the COVID-19 outbreak.

After an initial hesitation, this measure reassured the financial markets. The ECB, “arguably the most federal institution in the EU” (Dehousse 2020: 17), had to act like it had already done in the Euro crisis on this basis of its existing capabilities and similar to a lender of last resort. Given the limitations of monetary policy measures and considering that the programme may have “once again pushed the ECB's competences to their outer limits” (Fasone and Lindseth 2020: 24), the central bank subsequently called for firm macroeconomic measures in order to mitigate the consequences of COVID-19.

2.2 Suspension of the fiscal rules

In response to COVID-19, one of the first Economic Governance decisions was to *de facto* suspend the fiscal rules. Two clauses in the Stability and Growth Pact offer the possibility to deviate from the rules and to undertake budgetary measures if member states face exceptional circumstances. The COVID-19 crisis qualified for the “unusual events clause”, but the Commission proposed to use the more far-reaching “general escape clause” which was triggered when the Ecofin Council endorsed the Commission's Communication (European Commission 2020a). The Commission furthermore enacted a flexibilization of state aid and of the use of cohesion funds (see Fasone and Lindseth 2020: 25).

In order to give member states fiscal leeway and to avoid a situation where all of them would find themselves under Excessive Deficit Procedures, this was a necessary step. Although member states and Commission stressed their commitment to respecting the Stability and Growth Pact, the pact will not be reintroduced any time soon and certainly undergo significant changes. The implication is a full-scale departure from the EU's previous fiscal surveillance framework which Vivien Schmidt (2020) characterized as "governing by the rules and ruling by the numbers".

2.3 Creation of an unemployment insurance scheme and an ESM crisis support credit line

The "Support to mitigate Unemployment Risks in an Emergency" (SURE) programme was set up in April 2020 as a temporary instrument to support member states in protecting employment with loans from the EU of up to € 100 billion. Similar to the European Financial Stability Mechanism (EFSM) of 2011, the Commission will issue bonds on behalf of the EU and is already concluding agreements to pass them on to individual member states.

Furthermore, the Eurogroup also agreed in April 2020 that the European Stability Mechanism (ESM) will provide a Pandemic Crisis Support (PCS) credit line of up to 2% of GDP "to support direct and indirect healthcare, cure and prevention related costs due to the COVID-19 crisis" (Eurogroup 2020a).

As both schemes come without significant political or economic conditions, the national socio-economic policies pursued under those new credit lines are different. The previously imposed conditionality that the Troika imposed on creditor countries in the Euro crisis with the great distortions that this regime introduced (see Fasone and Lindseth 2020: 16) now seems to have disappeared completely, because "such loans would be free of the usual strict conditionality" (Fasone and Lindseth 2020: 26). No country has applied for PCS yet, so the implementation of this promise remains to be seen in case of the ESM.

2.4 Establishment of the Recovery and Resilience Facility

The RRF is at the heart of the crisis response. The initial breakthrough came at the European Council meeting of 23 April 2020 which asked the Commission to develop a recovery fund. It then presented its proposal on 28 May 2020 (European Commission 2020b). It has been coupled with the next MFF which had been under negotiation in early 2020. Before COVID-19 led to Europe-wide lockdowns, the European Council had not been able to reach an agreement on the mid-term budget for 2021 to 2027. This offered the opportunity to put the MFF and the recovery fund together. They amount to a total of € 1.8 trillion. The

European Council reached an agreement on the MFF and on the NGEU package, whose main component is the RRF, at its meeting from 17 to 21 July 2020 (European Council 2020).

Large-scale debt borrowing (€ 750 billion) by the EU on the financial markets and a large share of grants (€390 billion), i.e. real financial transfers to member states, alongside loans (€ 360 billion) are unprecedented steps. The money will be spent over several years, with less than 10% of the grants disbursed in 2021 and 15% in 2022 (European Central Bank 2020). The allocation of these funds involves distributive choices between member states and economic sectors (see Crum 2020: 10-11) and although the total amount represents less than 3% of the EU's GDP, some member states are likely to receive higher shares of their GDP.

The RRF is linked to the European Semester and to the Country-specific recommendations that have been issued there. In order to attain RRF money, Member States must submit National Recovery and Resilience Plans (NRRPs) in which they present economic reforms and public investment projects. This means, however, that “most of the choices about how the EU funds will be spent are delegated to the Member State level” (Crum 2020: 12). The RRF nevertheless represents a forceful element of the EU's response to COVID-19 whose precise arrangements are currently being negotiated between Council and Parliament.

3. Continuity and change in the European Union

The EU occasionally embarked on major treaty reforms, but generally the project of European integration has developed in an incremental way. While new treaties contained important changes, they often sealed developments that had been prepared for a long time. It is an overall mix between continuity and change that characterises the EU as a whole and also its institutional functioning.

3.1 Continuity

The EU has been confronted with many different crises since 2010. The instruments and procedures to deal with any kind of crisis, however, have remained mostly the same and reacting to a crisis has almost become a “new normal” for the functioning in the EU.

In the COVID-19 crisis, the EU institutions tried to continue “business as usual” as much as possible in a pandemic. All EU institutions moved parts of their activities online in order to continue their work. After the institutional renewal that followed the European Parliament elections of May 2019, the institutional set-up was not supposed to change.³ The European Council remained in charge of *de-facto* deciding the crisis response. The European Parliament, just like in the Euro or migration crises, was side-lined while the European Central Bank played once again a powerful role. In all these respects, there was a high degree of continuity, even if COVID-19 posed a huge challenge to the way the EU institutions had been working.

3.2 Change

Institutional change in the EU mostly happens *between* the major treaty revisions. Although there is a lot of continuity, the EU has witnessed remarkable change within a short period of time over the course of the year 2020 and without changing the EU treaties or creating a

³ Commissioner Phil Hogan, however, had to resign after not following COVID-19 rules in his home country Ireland. This led to a small reshuffle in which Valdis Dombrovskis took over the trade portfolio while Mairead McGuinness became the new Commissioner for Financial Markets.

new intergovernmental structure. However, these institutional changes largely respond to functional needs (see also Dehousse 2020: 19-20).

When the Franco-German recovery fund proposal and the European Commission's NGEU plan were presented in May 2020, some observers quickly referred to one of the founding fathers of the United States and spoke of the EU's "Hamiltonian moment".⁴ After initially being in the backseat, the European Commission played a key role in crafting the EU's response to COVID-19, and Franco-German cooperation has been quite strong.

Interestingly, but in line with the incremental development of European integration, the decisions required unanimity but no changes to the primary law and no ratification of treaty changes or new treaties became necessary. EU decision-makers deliberately avoided these risks in order to allow for a speedy response to COVID-19. Such steps have only been envisaged for a later point, for instance with respect to possible EU competences in the area of health policy (European Commission 2020e).

⁴ Financial Times, 'Is the Franco-German plan Europe's "Hamiltonian" moment?', 21 May 2020, <https://www.ft.com/content/2735a3f1-bc58-477c-9315-c98129d12852> (last accessed: 30 October 2020).

4. Different lenses to look at the shifts

The EU's response to the COVID-19 crisis is in many respects institutionally remarkable. In order to analyse the shifts that the key elements of the response entail, this paper proposes three different analytical lenses: The inter-institutional balance, the Euro-national parliamentary system (Fasone and Lupo 2016), and a broad "EU Economic Governance" perspective. These lenses are based on the idea that shifts in the EU's institutional system can impact the existing equilibrium between the institutions as well as affect the multi-level system and the functioning of one or several particular policy fields.

4.1 Inter-institutional balance

The EU-institutional system is characterised by a delicate inter-institutional balance. In terms of the influence of the main actors and institutions, the European Commission, the European Council, the European Parliament and the European Central Bank have each played a distinct role in shaping the outcomes of the crisis response. The impact of the different measures on them is also different.

It is particularly striking to see that the European Parliament, long seen as an ascending institution (Héritier et al. 2019), is struggling to shape the crisis response. This phenomenon has also been visible in the Euro and migration crises. The relative decline of the role of the European Parliament since the fate of the Spitzenkandidaten system after the May 2019 election seems to continue. Ursula von der Leyen's early promise to forge a "special relationship" between Commission and Parliament (European Commission 2019) is not only unfulfilled in terms of its key elements (Spitzenkandidaten, transnational lists, indirect right of initiative), but the Commission's work in the COVID-19 crisis response looks more like a joint Commission-Council roll-back against a Parliament which had become too assertive.⁵ In the response to COVID-19, the European Parliament might have been the victim of a quasi-separation *and* confusion of powers (see Fabbrini 2019).

The European Central Bank was able to rely on its autonomy and independence in order to put its new asset purchase programme in place. Christine Lagarde acted like Mario Draghi

⁵ As negotiations on MFF and RRF are still ongoing, this is only a preliminary assessment.

in the Euro crisis and could use the toolkit of non-standard monetary policy measures that had been developed back then, despite fierce opposition – for instance from the German Constitutional Court.

4.2 Euro-national parliamentary system

National parliaments have not been at the forefront of the discussions on the response to COVID-19 either. Governments were generally “more influential and less controlled” (Rozenberg 2020: 5) than they would have been under normal circumstances. In addition, there is currently little evidence for a real emphasis on integrating parliamentary involvement into the different tools that constitute the EU’s fiscal and economic response to COVID-19. The different instruments foresee some involvement of the European Parliament, but this is partly still under negotiation and could be enhanced further. The same applies to national parliamentary involvement, for instance over NRRPs.

A major concern regarding the role of national parliaments in fiscal and economic issues has been that rules and orders from the supranational level would shrink their decision-making space in these areas. The existence of a common currency (with the need to limit spill-over effects and to ensure convergence) justified the creation of tools like the Stability and Growth Pact. However, these tools remained contested over the years. Now it is no longer the EU that is constraining national parliaments, but the EU is removing obstacles to spend, is creating flexibility and even funnelling additional money to member states. This is clearly imposed by an economic necessity again.

In the COVID-19 crisis, national parliaments now see themselves marginalised by their own governments: Major decisions are being taken by the Heads of State or Government in the European Council once again and they have long had difficulties to scrutinise these summits (see Hefftlar et al. 2013).

However, there is a clear potential for better parliamentary scrutiny of NRRPs, compared to the previous National Reform Programmes of the European Semester, because more is at stake. National parliaments should scrutinise the NRRPs at least as properly as national budgets. This is in their own self-interest as well as in the interest of the European Parliament, other national parliaments and the EU taxpayer, because the debt created for the RRF is supposed to be repaid by new EU-wide own resources. The lukewarm parliamentary scrutiny of Stability or Convergence Programmes and National Reform Programmes (see Hallerberg et al. 2018) is no blueprint for NRRPs.

It would therefore be more necessary than ever to remedy the structural and procedural weaknesses of both the European Parliament and national parliaments with new intertwined Euro-national parliamentary procedures (see Fasone and Lupo 2016). This could help to reduce the information asymmetries and create an “exchange of information and best practices [...] with a view to foster their individual and collective ability to scrutinize” (Fasone 2019: 7).

4.3 EU Economic Governance

A first and very important development for EU Economic Governance is that the RRF completely revamps the European Semester. This annual cycle of fiscal and economic policy coordination and surveillance produces non-binding Country-specific recommendations for national economic reforms which up until now have largely been ignored by member states. The draft RRF regulation now establishes a clear link between these Country-specific recommendations and the new funds. However, the Semester was, as Ben Crum argues, “never set up for the purpose of monitoring the allocation of funds” (Crum 2020: 10). Given that the RRF has clear economic policy objectives for the EU as a whole, the non-binding governance structure of the European Semester is indeed not suitable to steer the process. This is recognised by the Commission’s proposal to suspend certain elements of the Semester (2021 Country-specific recommendations for member states that submit a NRRP).

On the continuum between conditionality and rubber-stamping, the NRRPs are “meant to be a contract whereby money is intended to serve certain goals, and the EU checks that the conditions to achieve them are in place” (Pisani-Ferry 2020). The drafting, assessment and decision on NRRPs, however, lacks clearly well-defined opportunities to ensure that pan-European elements are part of these programmes. These can only be anchored in the political objectives of the RRF regulation and in the Annual Sustainable Growth Strategy of the European Semester which will continue to annually set overall economic policy objectives for the EU (Crum 2020: 14).

A second major development is that prior to COVID-19 the main emphasis in EU Economic Governance was on strengthening the Euro area. The Budgetary Instrument for Convergence and Competitiveness (BICC), a new budgetary instrument for the Euro area (with a total amount of only € 17 billion for the entire period from 2021 to 2027), was agreed in October 2019. In May 2020, however, the European Commission withdrew the proposal that it had drafted on this basis. The momentum for further integrating the Euro area, for developing the ESM into a Eurozone Treasury or for setting up a Eurozone Parliament (Kreiling and Larhant 2016; Lupo 2018) has faded almost completely.

The only path towards strengthening the Euro area dimension in the response to the COVID-19 crisis is related to the Euro area recommendation of the European Semester. Eurogroup President Centeno concluded in June 2020 that this recommendation “could be a natural avenue to reflect a legitimate Euro area dimension to the Recovery and Resilience facility, without adding layers of complexity to the governance process” (Eurogroup 2020b: 2). One important consequence of the COVID-19 response will probably be a strengthening of the *economic* part of the Economic and Monetary Union which has so far primarily been a monetary union with only some economic coordination.

5. Evolution or revolution?

Referring back to continuity and change in the EU and based on the insights that the three lenses to analyse the shifts have provided in the previous sections, how far-reaching do these shifts seem as of now?

5.1 Evolution

Cristina Fasone and Peter Lindseth explain that NGEU does not lead to a Europeanisation of taxation authority and that EU debt issuance itself is also not new. The magnitude of the debt to be issued and unresolved questions, however, bring the EU, even if it “has not yet crossed the Rubicon, [...] right up to its banks” (Fasone and Lindseth 2020: 29).

In addition, the different elements of the response largely rely on existing institutions and toolkits. The European Commission had envisaged to revise the fiscal rules of the Stability and Growth Pact even before the pandemic started to hit Europe. An unemployment insurance scheme had been discussed for a long time. The creation of a bigger budget had long been the dream of federalists and Eurocrats. Some ideas have prevailed after being in the pipeline for a long time.

Procedurally, the NRRPs are closely aligned to the European Semester. The relationship between the three logics inside the European Semester – national parliamentary involvement, surveillance mechanisms and ownership (see Kreilinger 2016) – is redefined in the newly-designed governance mode for the RRF: On the one hand, parliamentary involvement is still not prescribed or recommended while the surveillance component (even though already non-binding in the Semester) is further reduced. On the other hand, ownership notably by national governments is greatly enhanced. These examples show an evolution and a gradual shift of existing policies and practices.

5.2 Revolution

Taken all together, however, this paper argues that the crisis response amounts to a revolution. Actually, an executive revolution, because it is a revolution for which nobody could vote in the European Parliament elections of May 2019, less than a year before the pandemic. There have been very few parties with far-reaching ideas like expanding the budget on the ballot paper. Nothing of this kind had been debated at the forefront of the electoral campaign. The policies and measures that are now being put in place were not supported by a majority of voters in May 2019. True, COVID-19 was unforeseeable and the crisis required a quick and decisive response. But from the point of view of the democratic legitimacy of those decisions, this is worrying. In view of its huge redistributive effects, the EU must ensure that its response to COVID-19 is sufficiently legitimised.

While there is wide-spread public support for the measures, one of the lessons from the Euro crisis is that the risk of a public backlash against such measures is big, both in creditor and recipient countries. Such a constellation has already emerged with the group of the “Frugal Four” (Austria, Denmark, Sweden and the Netherlands).

Contrary to its way of dealing with the Euro crisis, the EU took real steps towards creating what had been called a “macroeconomic union” by Simon Hix (2014), although still one with a democratic deficit. In addition to its other tasks, the Conference on the Future of Europe will have to be a place where the decisions that were taken in response to the crisis are openly discussed and explained. When it comes to many of the follow-up decisions, for instance the one on which own resources to create for the EU and how exactly to design such new taxes (see also Fasone and Lindseth 2020: 29-30), the Conference will have to put an emphasis on involving citizens in these questions and not make them an exercise of intergovernmental bargaining. The mantra “no taxation without representation” still applies.

6. Conclusion

This paper tried to shed light on the recent developments that re-shaped the institutional system. The EU's fiscal and economic response to COVID-19 has indeed led to shifts that are having a strong and widespread impact.

Above all, there are significant changes to the post-Lisbon equilibrium between the three major institutions – Commission, Parliament and European Council – regarding their relative power : the European Parliament has been clearly side-lined in the response to COVID-19. Moreover, multi-level governance is affected through a much weaker Euro-national parliamentary system and a strengthening of the executives at the expense of the legislatures. Finally, the functioning of fiscal and economic policy coordination and surveillance as well as the development of Euro area governance is altered substantially: The entire austerity and conditionality discourse was shelved and the scope of Economic Governance quickly expanded to all 27 member states.

Sometimes the precise impact of the shifts still remains to be seen and also depends on how provisions that are vague and open to different interpretations being used. A lot will depend on how the European Commission intends to enforce them. But the relative silence of parliaments is particularly worrying. They are vital places to debate the redistributive choices that these measures involve. In the pandemic they have successfully moved parts of their activities online and been able to scrutinise their governments domestically (Rozenberg 2020). The same is possible with respect to EU affairs. In order to create a positive impact on the individual and collective ability of legislatures to scrutinise (Fasone 2019), national parliaments and the European Parliament must start to see each other as allies in addressing the joint task of democratically controlling these new instruments: This includes strengthening the Interparliamentary Conference on Stability, Economic Coordination and Governance and enhancing their individual scrutiny tools.

As the RRF is at the heart of the EU's COVID-19 response, it should also be at the centre of parliamentary activities: First, the European Parliament should be properly involved into the RRF (see Crum 2020). Second, it could become a public forum where national decision-makers explain their NRRPs in case of doubts, similar to existing practices in the European Semester (Kreilinger 2016). And, third, national parliaments must ensure that their role in the budget process remains intact and that recovery money receives the same amount of scrutiny as ordinary national budgets.

The ongoing negotiations on the RRF between Council and European Parliament actually show a great dilemma of the tectonic shifts: On the one hand, a significant part of the EU's population has difficulties to understand why institutions are struggling about minor details of the recovery package. On the other hand, another significant part of the EU's population will not see the safeguards and control instruments as sufficient. Even though economists doubt that the size of the RRF will be sufficient when in the United States the fiscal stimulus in the financial crisis of 2008 amounted to 10% of BIP, this tension has the potential to tear the EU apart. Under such a scenario, there would then – in addition to all the problems that occurred with Brexit – also be a huge mountain of debt.

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The SoG provides its students with the skills needed to respond to current and future public policy challenges. While public policy was enclosed within the state throughout most of the last century, the same thing cannot be said for the new century. Public policy is now actively conducted outside and beyond the state. Not only in Europe but also around the world, states do not have total control over those public political processes that influence their decisions. While markets are Europeanised and globalised, the same cannot be said for the state.

The educational contents of the SoG reflect the need to grasp this evolving scenario since it combines the theoretical aspects of political studies (such as political science, international relations, economics, law, history, sociology, organisation and management) with the practical components of government (such as those connected with the analysis and evaluation of public policies, public opinion, interests' representation, advocacy and organizational leadership).

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Luiss School of Government welcomes unsolicited working papers in English and Italian from interested scholars and practitioners. Papers are submitted to anonymous peer review. Manuscripts can be submitted by sending them at sog@luiss.it. Authors should prepare complete text and a separate second document with information identifying the author. Papers should be between 8,000 and 12,000 words (excluding notes and references). All working papers are expected to begin with an abstract of 150 words or less, which should summarise the main arguments and conclusions of the article. Manuscripts should be single spaced, 11 point font, and in Times New Roman.

Details of the author's institutional affiliation, full postal and email addresses and other contact information must be included on a separate cover sheet. Any acknowledgements should be included on the cover sheet as should a note of the exact length of the article. A short biography of up to 75 words should also be submitted.

All diagrams, charts and graphs should be referred to as figures and consecutively numbered. Tables should be kept to a minimum and contain only essential data. Each figure and table must be given an Arabic numeral, followed by a heading, and be referred to in the text. Tables should be placed at the end of the file and prepared using tabs. Any diagrams or maps should be supplied separately in uncompressed .TIF or .JPEG formats in individual files. These should be prepared in black and white. Tints should be avoided, use open patterns instead. If maps and diagrams cannot be prepared electronically, they should be presented on good quality white paper. If mathematics are included, 1/2 is preferred.

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SoG Working Papers

The Luiss School of Government aims to produce cutting-edge work in a wide range of fields and disciplines through publications, seminars, workshops, conferences that enhance intellectual discourse and debate. Research is carried out using comparative approaches to explore different areas, many of them with a specifically European perspective. The aim of this research activities is to find solutions to complex, real-world problems using an interdisciplinary approach. LUISS School of Government encourages its academic and student community to reach their full potential in research and professional development, enhancing career development with clear performance standards and high-quality. Through this strong focus on high research quality, LUISS School of Government aims to understanding and influencing the external research and policy agenda.

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