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Legal options for an additional EMU fiscal capacity

NOTE



DIRECTORATE GENERAL FOR INTERNAL POLICIES
POLICY DEPARTMENT C: CITIZENS' RIGHTS AND
CONSTITUTIONAL AFFAIRS

CONSTITUTIONAL AFFAIRS

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NOTE

Abstract

The establishment of an additional EMU fiscal capacity is one of the core ideas for the further development of the EMU towards a genuine economic and monetary Union. This note indicates the legal options for the implementation of an additional EMU fiscal capacity. This covers implications of EU budget law, the legal implications of the idea of “contractual arrangements” and institutional implications of possible further developments of the additional fiscal capacity into a euro area stabilisation instrument.

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List of Abbreviations

- EBA** European Banking Authority
- EC** Treaty on the establishment of the European Community
- ECB** European Central Bank
- ECJ** European Court of Justice
- EDF** European Development Fund
- EIB** European Investment Bank
- EMU** Economic and Monetary Union
- MIP** Macroeconomic Imbalances Procedure
- OHMI** Office for Harmonisation in the Internal Market
- TEU** Treaty on European Union
- TFEU** Treaty on the Funtioning of the European Union

Executive Summary

The idea of establishing an additional EMU fiscal capacity with an own central budget is one of the core ideas in the debate on how to create a “genuine economic and monetary union”. What in concrete terms is to be understood by an additional fiscal capacity is rather vague and covers a wide range of options. On the one hand, it can be understood as an additional fund that assists participating (eurozone) Member States in their efforts to enhance their competitiveness. This could be reached by the conclusion of so-called “contractual arrangements” by Member States with the EU. Those Member States that comply with what they promised to do in these “contractual arrangements” are eligible for financial assistance from that fund. If a Member States fails to comply the fund could withhold financial assistance. By this mechanism, the additional fiscal capacity can be understood as an incentive-based enforcement measure for a Europeanised economic policy.

On the other hand, the additional fiscal capacity can be understood in broader terms as “an insurance-type mechanism between euro area countries to buffer large country-specific economic shocks”. Such an understanding requires extended revenue for the budget of the additional fiscal capacity. It requires certain conditions for payment and an extended administration which was called by the proposals a “Treasury”. The European Council did not mention this understanding in its conclusions of 14 December 2012.

There are several legal options for the implementation of an additional EMU fiscal capacity that covers such a wide range of implementation options. This note distinguishes for the assessment of the legal options between the budgetary implications, the legal implications of the “contractual arrangements” (which is the core issue of the incentive-based understanding of the additional fiscal capacity) and the institutional implications of further developments of the additional fiscal capacity.

The additional EMU fiscal capacity can be implemented within the EU budget. A differentiation of revenue and expenditure with regard to a group of Member States is possible under EU budget law. Certain revenue can be assigned to a certain budget line. Such earmarked revenue is not part of the Multiannual Financial Framework. It appears also to be possible to implement the additional fiscal capacity outside of the EU budget. In this situation, however, the European Parliament must have supervisory rights over the budget of the fiscal capacity comparable to those under EU budget law. Otherwise the European Parliament’s budgetary rights that are protected under EU budget law would be circumvented.

“Contractual arrangements” between Member States and EU institutions can be understood either as international law Treaties, contracts governed by private or public law or legally non-binding Memoranda of Understanding. An overall assessment of the legal framework of EU law only allows an understanding of “contractual arrangements” as legally non-binding “Memoranda of Understanding” that serve as cause for payments. With regard to international law Treaties it is already doubtful whether the EU has the competence to conclude Treaties with its Member States as the Treaties provide for legal bases to adopt regulations, directives and decision that address Member States. The conclusion of international law Treaties would either undermine the legislative procedure foreseen by the existing legal bases or the principle of conferral if there is no legal basis in the Treaties. The proposals themselves only refer to an endorsement of the national parliament where appropriate under national procedures and not to a ratification as required by international

law. A comparison with the existing secondary law and, in particular, with the Macroeconomic Imbalances Procedure shows that the conclusion of “contractual arrangements” does not provide for any additional legal consequence for the concluding Member States. Member States under the corrective arm of the Macroeconomic Imbalances Procedure have to present a corrective action plan that is monitored by the European Commission and whose non-compliance has legal consequences which include fines. “Contractual arrangements” that shall contain the measures proposed by the corrective action plan only give access to an additional financial support by the fiscal capacity. Member States that are not under the corrective arm of the Macroeconomic Imbalances Procedure are supposed to include measures comparable to a corrective action plan into their “contractual arrangements”. Non-compliance has, however, no further consequences except for the possibility for the fiscal capacity to withhold payments. This shows that “contractual arrangements” are not intended to create additional legal obligations for Member States and resemble therefore legally non-binding “Memoranda of Understanding”.

Further developments of the additional EMU fiscal capacity require new revenue and challenge the institutional framework and balance of the EU. Revenue can be generated either by contributions from Member States or new own resources such as an own EU tax. Whilst contributions could be introduced under existing EU law, an own EU tax whose purpose is to generate revenue for the EU can not be established under the EU Treaties. Existing EU law requires payments to EMU Member States to be subject to a strict conditionality. However, the European Commission needs to be adapted to its possible new role as EU Treasury. Democratic accountability of the European Commission acting as EU Treasury also requires changes in the institutional set-up.

In sum, the debate on the additional EMU fiscal capacity raises important questions for the further development of the EMU towards a genuine economic and monetary union. Certain elements of the ideas proposed by the four Presidents and the European Commission can already be realised under the existing Treaties. EU budget law, in particular, requires a strong involvement of the European Parliament when implementing the additional EMU fiscal capacity.

Background and Aims

On 26 June 2012 the president of the European Council proposed in the report “Towards a genuine economic and monetary union” under the title of “an integrated budgetary framework” the creation of an additional EMU fiscal capacity. Since then the idea was further developed by two more reports presented by the four Presidents (Herman van Rompuy, President of the European Council, in collaboration with José Manuel Barroso, President of the European Commission, Jean-Claude Juncker, President of the Eurogroup, Mario Draghi, President of the European Central Bank) on 12 October 2012 and on 5 December 2012. The European Commission presented, furthermore, some ideas on the additional EMU fiscal capacity in its “Blueprint for a deep and genuine economic and monetary union – Launching a European Debate” (COM(2012) 777 final/2). The European Council picked up the idea of an additional EMU fiscal capacity in its conclusions of 14 December 2012 under the name of a “solidarity mechanisms”.

The purpose of this note is to assess the legal options for the possible implementation of such an additional EMU fiscal capacity and the institutional implications of it. The proposals made by the four Presidents as well as the blueprint of the European Commission are the basis for this assessment.

1. THE ADDITIONAL FISCAL CAPACITY: DIFFERENT CONCEPTIONS

1.1. The development of the idea of a “fiscal capacity”

1.1.1. Proposals made by the President of the European Council on 26 June 2012

The report “Towards a genuine economic and monetary union”, presented by the president of the European Council on 26 June 2012 proposed initially under the title of “an integrated budgetary framework” the creation of an additional fiscal capacity (van Rompuy 2012a: 6):

“A fully-fledged fiscal union would imply the development of a stronger capacity at the European level, capable to manage economic interdependences, and ultimately the development at the Euro area level of a fiscal body, such as a treasury office. In addition, the appropriate role and functions of a central budget, including its articulation with national budgets, will have to be defined.”

1.1.2. Further developments in the interim report of 12 October 2012

The interim report of 12 October 2012 specified that the fiscal capacity “would support new fiscal functions which are not covered by the multiannual financial framework.” In order to implement it, “ways to develop this capacity within the framework of the EU and its institutions will have to be examined.” The functions of the fiscal capacity could be “to facilitate adjustments to country-specific shocks by providing for some degree of absorption at the central level” and “structural reforms that improve competitiveness and potential growth” without “water[ing] down the compliance with fiscal rules and fiscal discipline in individual Member States”. The fiscal capacity should, finally, have an “ability to borrow” (van Rompuy 2012b: 5).

The interim report also presented the idea of “individual arrangements of a contractual nature” which euro area Member States should conclude with “EU institutions” “on the reforms promoting growth and jobs”. The content of these contractual arrangements “could be linked to the reforms identified in the country-specific recommendations of the Council and built on EU procedures, such as the corrective action plans under the excessive imbalances procedure or the economic partnership programmes.” At this stage, the idea of the contractual arrangements was not yet linked to the idea of the “fiscal capacity” (van Rompuy 2012b: 7).

1.1.3. The blueprint of the European Commission

On 28 November 2012 the European Commission presented its blueprint for a deep and genuine economic and monetary union. The European Commission split the idea of the President of the European Council on the “fiscal capacity” into two: A “Convergence and Competitiveness Instrument” (European Commission 2012: 21) and a “proper fiscal capacity for the euro area” (European Commission 2012: 27 and 31).

1.1.3.1. Convergence and Competitiveness Instrument

The Commission merged the idea of “contractual arrangements” with the idea of a “fiscal capacity” in the “Convergence and Competitiveness Instrument”. Euro area Member States

entering into a contractual arrangement with the Commission could get financial support for “reform packages that are agreed and important both for the Member State in question and for the good functioning of EMU”. If the Commission finds ex post that a Member State did not fulfil its duties under the contract the financial support can be withheld. According to the Commission the instrument “could be set up in principle as part of the EU budget” and be established by secondary law on the basis of either Article 136 TFEU (if it reinforces the Macroeconomic Imbalances Procedure (hereinafter: MIP) under Regulation (EU) No 1176/2011) or of Article 352 TFEU by enhanced cooperation. The instrument could be financed by either a commitment of the euro area Member States or by a legal obligation to that effect enshrined in the EU’s own resources legislation “as assigned revenues” (European Commission 2012: 22).

1.1.3.2. A proper fiscal capacity for the euro area

The fiscal capacity for the euro area should be a further development of the “convergence and competitiveness instrument”. It shall, however, rely solely on own resources. Such a fiscal capacity should probably include “the capacity to borrow and issue bonds” (European Commission 2012: 32). Its tasks could be to “support adjustment to asymmetric shocks, [facilitate] stronger economic integration and convergence and [avoid] the setting up of long-term transfer flows” (European Commission 2012: 31). A stabilisation instrument built on the fiscal capacity “could provide an insurance system” (European Commission 2012: 32). The Commission then presents two different schemes on how such a stabilisation mechanism could work: Either as an asymmetric shock absorption capacity or as a counter-cyclical economic tool (comparable to the US unemployment benefit system). In order to realise such a fiscal capacity, Treaty changes are needed such as at least the creation of an explicit legal basis for its establishment, creating a corresponding, dedicated budgetary and own resources procedure and creating a new taxation power at the EU level, or a power to raise revenue by indebteding itself on the markets (European Commission 2012: 33).

1.1.4. The final report of the President of the European Council of 5 December 2012

In his final report the President of the European Council summarised the development of the idea on the “fiscal capacity”. Following the Commission blueprint the final report distinguishes between “financial incentives” for Member States that “enter into arrangements of a contractual nature with EU institutions” and “an insurance-type mechanism between euro area countries to buffer large country-specific economic shocks” (van Rompuy 2012c: 7). With regard to latter the final report distinguishes two possible approaches for its function: A macroeconomic approach “where contributions and disbursements would be based on fluctuations in cyclical revenue and expenditure items” (van Rompuy 2012c: 8) and a microeconomic approach that would work “as a complement or partial substitute to national unemployment insurance systems” (van Rompuy 2012c: 9).

1.1.5. Conclusions of the European Council (13/14 December 2012)

In its conclusions the European Council only referred to the “fiscal capacity” in its form of “financial incentives” for Member States concluding contracts with EU institutions on structural and fiscal reforms. The second type of “fiscal capacity” was not mentioned anymore. There shall be “solidarity mechanisms that can enhance the efforts made by the Member States that enter into [...] contractual arrangements for competitiveness and growth.” These “contractual arrangements” are “individual arrangements of a contractual nature with EU institutions [...]”. Such arrangements should be differentiated depending on Member States’ specific situations. This would engage all euro area Member States, but non

euro Member States may also choose to enter into similar arrangements" (European Council 2012: 5).

1.2. Distinctive elements of the conceptions

In order to properly assess the legal options for an implementation of the idea of an "additional fiscal capacity" the following elements should be distinguished:

- The **budgetary element**: The budget of the fiscal capacity can be designed differently (either included into the EU budget or as a separate fund). The chosen budgetary design has institutional implications with regard to the involvement of the European Commission when implementing the fiscal capacity and of the European Parliament when controlling the fiscal capacity.
- The **conditionality element**: In order to receive financial assistance from the fiscal capacity Member States have to meet certain conditions, in particular, the conclusion of "contractual arrangements". The answers to the question of the legal nature of these "contractual arrangements" (international law Treaties, private law contracts or Memoranda of Understanding), of who concludes these arrangements on behalf of the EU following which procedures, of how these arrangements are implemented and of who controls these implementations have different institutional implications.
- The **development element**: All conceptions include as starting point a fiscal capacity that grants financial assistance for Member States that concluded "contractual arrangements" with EU institutions. They differ, however, with regard to the further development of the fiscal capacity. Further developments of the additional fiscal capacity perpetuate a two-speed Europe of the euro area and the non-euro area, require major Treaty changes and challenge the functioning of EU institutions made for the whole EU but taking over more and more tasks for the euro area Member States.

2. LEGAL OPTIONS FOR AN ADDITIONAL FISCAL CAPACITY WITH REGARD TO BUDGET LAW

Budgetary implications of the additional fiscal capacity are closely linked to the way how it is supposed to be implemented (2.1). The legal framework of the existing Treaties will already eliminate some of the possible ways of implementing the fiscal capacity (2.2) which allows for a final view on the budgetary implications and the associated institutional implications (2.3).

2.1. Different ways of implementing the fiscal capacity

Implementing the fiscal capacity can either be realised by means of the Community method according to which the Commission implements the budget for the additional fiscal capacity controlled by the European Parliament and the Council (2.1.1), or by a fund outside of the EU budget, which is either implemented by the European Commission (2.1.2) or a new separate agency (2.1.3).

2.1.1. Community method: New own resource within EU budget

The use of the “Community method” would require including the budget for the additional fiscal capacity into the EU budget. This could be realised by creating a new own resource, which has to be financed by contributions of the Member States participating in the fiscal capacity, and a new budget line for financing the functions of the fiscal capacity. As a part of the general EU budget the budget for the additional fiscal capacity would be implemented by the European Commission and supervised by the European Parliament and the Council. This requires, in principle, an integration of the fiscal capacity into the multi-annual financial framework as Article 312(1) TFEU states that the annual budget of the Union shall comply with the multi-annual financial framework unless the fiscal capacity is subject to an exception provided for in the financial framework.

2.1.2. Fund outside of the EU budget implemented by the European Commission

The budget for the additional fiscal capacity could also be a fund outside of the EU budget, which is implemented by the European Commission. The European Parliament could give discharge for the financial management. This way is based on the model of the European Development Fund (hereinafter EDF). The European Parliament could, furthermore, take on a supervisory role comparable to the one that it has with regard to the general EU budget.

2.1.3. Fund outside of the EU budget implemented by a new separate agency

A new separate agency implementing the budget for the additional fiscal capacity could be created either on the legal basis of Article 352 TFEU in enhanced cooperation of the participating Member States or on the basis of an international Treaty between the participating Member States. Within the concept of the creation of a new agency the type and degree of supervision can also be distinguished: It can be either an own budget committee, which is separate from the European Parliament and the Council and which is composed by representatives of the participating Member States (modelled after the “Office for Harmonisation in the Internal Market”), the European Parliament discharging the financial management of the agency without supervising the implementation or the European Parliament as a supervisory body comparable to the EU budget.

2.1.4. Summary table on possible concepts

		Implementing body	
		European Commission	Agency
Supervisory body	European Parliament (supervision comp. to EU budget)	Community method	Model EBA
	European Parliament (discharging the financial management)	Model EDF	Model modified EDF
	Budget Committee (composed by Member States)	<input type="checkbox"/>	Model OHMI

2.2. Legal framework

The legal framework sets limits to the above-mentioned concepts. In order to realise the fiscal capacity outside of the EU budget the Treaties should provide for an appropriate legal base or should not prevent the conclusion of an international agreement (2.2.1). Once the fiscal capacity could be established outside of the EU budget the question arises as to whether such a fiscal capacity would not infringe EU budget law and, in particular, the principle of unity of the EU budget and its completeness (2.2.2) and if there is any possible design of the fiscal capacity outside of the EU budget that would constitute a permissible exception to this principle (2.2.3). Finally, a possible solution within the general EU budget would require that a differentiation between Member States in the EU budget is legally possible (2.2.4).

2.2.1. Legal basis for the establishment of a fund outside of the EU budget and an implementing agency

A legal basis for the establishment of a fund outside of the EU budget and of an agency, which implements it, can be found in Article 352 TFEU. The functions of the fund as proposed by the President of the European Council serve to attain a “sustainable development of Europe based on balanced economic growth” and to safeguard the “economic and monetary union whose currency is the Euro”; objectives mentioned by Article 3 TEU.

Besides an action based on Article 352 TFEU, participating Member States could also establish the fund on the basis of an international Treaty. The principle of sincere cooperation in Article 4(3) TEU requires, however, that Member States shall give a legal action under the Treaties and by using enhanced cooperation priority over the conclusion of an international Treaty outside of the EU framework.

2.2.2. General principle of unity of the EU budget and its completeness

The core rule of the financial provisions of the Union is Article 310(1) TFEU according to which “all items of revenue and expenditure of the Union shall be included in estimates to be drawn up for each financial year and shall be shown in the budget.” This general provision is specified by the regulation on the financial rules applicable to the general budget of the Union¹. Art. 4(1) of the 2002 regulation as well as Art. 2(c) of the 2012 regulation define “budget” as “the instrument which, for each financial year, forecasts and authorises all revenue and expenditure considered necessary for the Union”.

These provisions establish the principle of unity of the EU budget. This principle requires that *all* revenues and expenditures of the Union are part of *one* EU budget. It forbids any kind of separate or subsidiary budget within the EU framework. The principle of unity includes the completeness of the EU budget which requires that the one EU budget which is established under the principle of unity is complete and includes *every* predictable revenue and expenditure of the Union.

¹ The current regulation is the Council Regulation (EC, Euratom) No 1605/2002 which is repealed by the Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council.

2.2.3. Exceptions to the general principle

Exceptions to the principle of unity of the EU budget and its completeness can nevertheless be found. These are:

- The European Investment Bank
- The European Central Bank
- The European Stability Mechanism
- certain Union agencies
- The European Development Fund
- Borrowing-and-lending operations entered into by the Union
- Expenditure resulting from implementation of enhanced cooperation

In general, these exceptions are highly questionable. However, there can be exceptions as the scope of application of Article 310(1) TFEU requires that the revenue and expenditure in question are those of the "Union". Any revenue or expenditure that is not of the "Union" is not subject to the EU budget law.

This view has been confirmed by the European Court of Justice in its judgment of 2 March 1994 on the European Development Fund (ECJ 1994). The ECJ found in this judgment that the EDF is a fund that has been set up by the Member States and not by the Council and that accordingly the expenditure is assumed directly by the Member States and not the Community. Therefore, expenditure of the EDF is no expenditure of today's Union under Article 310(1) TFEU. The Member States had the competence to set up such a fund since "the Community's competence in that field is not exclusive. The Member States are accordingly entitled to enter into commitments themselves vis-à-vis non-member States, either collectively or individually or even jointly with the Community" (para 26).

Every exception, however, restricts the budgetary powers of, in particular, the European Parliament. An exception to Article 310(1) TFEU has to be interpreted narrowly as the purpose of Article 310(1) TFEU is the protection of the budgetary powers of the Council and, in particular, the European Parliament. The Treaties have very delicately balanced the participation rights of the European Parliament and the Council in the Union's budgetary procedure with the decision-making procedure under Article 314 TFEU, the discharge duty of the Commission towards the European Parliament under Article 319 TFEU and the adoption of the financial rules regulation in the ordinary legislative procedure under Article 322 TFEU. Especially the strong position of the European Parliament as the representative of the Union citizens (Article 10 TEU) exercising budgetary functions jointly with the Council (Article 14(1) TEU) could be undermined by a restrictive interpretation of Article 310(1) TFEU which would allow separate budgets within the EU framework but outside of EU budget law. The Council as the representative of the governments of the Member States does not need a comparable protection as Member States' governments are also involved in the decision on public spending outside of the Union framework. It could, however, be otherwise if not all the Member States which participate in the Council take part in decisions on public spending.

Furthermore, with the Lisbon Treaty entering into force the core provision of Article 310 TFEU replaced former Article 268 EC and extended its scope of application. Whilst Article 268 EC referred to all items of revenue and expenditure of the "Community" and to certain parts of certain policies of the former Union Article 310(1) TFEU applies to the Union as a whole and abolishes by that every formerly known budgetary differentiation within in the EU framework.

In order to further assess possible exceptions with regard to their applicability to possible configurations of the fiscal capacity an in-depth analysis of the existing exceptions to the principle of unity of the EU budget and its completeness is needed.

2.2.3.1. Exceptions based on a legal personality separate from the European Union

The EIB (Article 308(1) TFEU) and the ECB (Article 282(3) TFEU) have their own budgets because of their legal personality which is granted by the Treaties and separate from the legal personality of the European Union (Article 335 TFEU). A consequence of this legal personality is the financial autonomy of the EIB and the ECB. This exception to the principle of unity of the EU budget and its completeness appears to be acceptable as the Treaties provided for the legal personality and the financial autonomy of these institutions.

The same reasoning was applied to the financial autonomy of Union agencies. Those agencies were founded on the basis of Article 352 TFEU and were granted an own legal personality. A series of these Union agencies have their own budgets, which are separate from the EU budget, and an own budget committee, which is separate from the European Parliament and the Council. This committee is composed by representatives of the Member States and sometimes also of the Commission, which are instructed to supervise. If the Union pays a subsidy to this Union agency this subsidy is a part of the general budget of the EU. All other revenues are not considered to be revenues under Article 310(1) TFEU and are therefore outside of the EU budget. Examples for these kinds of Union agencies are:

- Office for Harmonisation in the Internal Market (cf. Articles 138 et seqq. of Regulation (EC) No 207/2009)
- Community Plant Variety Office (cf. Articles 108 et seqq. of Regulation (EC) No 2100/94)
- European Aviation Safety Agency (cf. Articles 59 et seqq. Of Regulation (EC) No 216/2008)

The creation of own budgets which are separate from the general EU budget for Union agencies is, however, problematic with regard to Article 310(1) TFEU. The reasoning which was used for the EIB and the ECB cannot be applied to Union agencies. Whilst the separate legal personality of the EIB and the ECB was granted by the Treaties and, by that, by the same source that granted a legal personality to the EU, the legal personality of Union agencies derives from secondary law. Secondary law is based on competences that are conferred upon the Union and, by that, the legal personality of Union agencies derives from the legal personality of the Union. This is confirmed by the regulation on the financial rules applicable to the general budget of the Union. Art. 185 of the 2002 regulation as well as Art. 208 of the 2012 regulation apply this regulation to Union agencies. This regulation is based on Article 322 TFEU and specifies Article 310 TFEU. It can therefore only be applied to revenue and expenditure of the Union. If the Union agencies, however, are separate from the Union, the regulation on financial rules could not be applied to those agencies.

Furthermore, and more important, financial autonomy of Union agencies undermines the control function of the general budget and, by that, the budgetary sovereignty of the European Parliament and the Council. This could only be prevented if there was a comparable control by the European Parliament and the Council over these Union agencies.

Finally, Article 310(1) TFEU addresses the “Union” as a whole. Union agencies are part of the Union even though they are autonomous. The basic act of these Union agencies state therefore “the Office shall be a body of the Community” (cf. e.g. Article 115 of Regulation (EC) No 207/2009 on the Office for Harmonisation in the Internal Market). As a part of the Union these agencies also have to be a part of Union budget.

For all those reasons modern Union agencies such as the European Banking Authority (hereinafter: EBA) provide for a budgetary control by the European Parliament comparable to the one of the general EU budget (cf. Articles 62 et seqq. of Regulation (EU) No 1093/2010 establishing a European Supervisory Authority (European Banking Authority)).

2.2.3.2. Exceptions based on tasks outside of EU's competences

Another exception is the European Stability Mechanism. Revenue and expenditure of the ESM are not included in the EU budget and are not subject to EU budget law. This is due to the fact that the tasks conferred upon the ESM are tasks that are outside of EU's competences. As a Union institution, the ESM would be in conflict with the so-called “no bail-out”-clause in Article 125(1) TFEU and, possibly, with the ban on direct public sector financing in Article 123 TFEU. Therefore, the Member States have enabled themselves to establish a stability mechanism by Primary law with the adoption of Article 136(3) TFEU. The Union is not covered by the new Article 136(3) TFEU. Due to the fact that the Treaties do not enable the Union (or, in other words, forbid the Union) to set up such a stability mechanism the ESM cannot be covered by Article 310 TFEU.²

2.2.3.3. Exceptions based on tasks with competences shared between EU and Member States vis-à-vis third countries

The establishment of the EDF outside of the EU budget was accepted by the ECJ in the above-mentioned judgment (ECJ 1994). The Court's reasoning was based on the competence categories. According to the Court's judgment in the ERTA case (ECJ 1971) if there is an exclusive Union competence “Member States no longer have the right, acting individually or even collectively, to undertake obligations with third countries” which affect rules that were based on exclusive competences of the Union. On the contrary, as long as the Union has no exclusive competence Member States are entitled to exercise their competence in a specific policy field such as development policy and to perform any obligation. The Court draws a line between competence and expenditure. If there is a shared competence which allows Member States to act outside of the EU framework then there can also be Member States' expenditure outside of the EU budget.

This reasoning of the Court which is already over 20 years old is still limited by the general rule according to which the control function of the general EU budget and the budgetary sovereignty of the European Parliament and the Council shall not be undermined. Furthermore, three specificities of the EDP have to be taken into account, which show that the reasoning applied to the EDP cannot be generalised: First, the EDP creates obligations of the Member States vis-à-vis third countries outside of the EU and not vis-à-vis other EU Member States. Second, the European Parliament has, at least, to discharge the Commission for the financial management of the EDF, excluding operations managed by

² This conclusion can be questioned after the “Pringle” judgment of the ECJ (ECJ 2012). According to the Court the establishment of the ESM was in conformity with the EU Treaties regardless of the entry into force of Article 136(3) TFEU. The ECJ did not comment on whether the Union could establish the ESM on the basis of Article 352 TFEU (para 67). This could imply that the Union could also have established the ESM within the EU framework. An action under Article 352 TFEU or under a separate international Treaty is, however, according to the ECJ at the discretion of EU Member States.

the EIB according to Article 11(8) of the Internal Agreement on the financing of Community aid (OJ L 247, 9.9.2006, p. 32). Third, every EU Member State takes part in the EDF calling themselves "Representatives of the Governments of the Member States, meeting within the Council". Therefore, even though the Council as an institution is left outside all the governments within the Council are involved in the EDF.

2.2.3.4. Expenditure resulting from implementation of enhanced cooperation as an exception?

The last specificity of the EDF triggers the question as to whether a group of EU Member States could establish such a fund. Further guidance can be found in Article 332 TFEU on expenditure resulting from implementation of enhanced cooperation. According to Article 332 TFEU such expenditure other than administrative costs entailed for the Union institutions shall be borne, in principle, by the participating Member States. The wording of this provision appears to allow that a group of Member States can establish such a fund and even to require putting it outside of the general EU budget.

The main idea of Article 332 TFEU, however, is rather that non-participating Member States should not bear costs of decisions on which they have no political influence. It is not clear whether expenditure resulting from implementation of enhanced cooperation has to be borne outside of or within the EU budget. Article 326 TFEU states in this respect that any enhanced cooperation shall comply with the Treaties and Union law and, by that, does not allow any deviation from general EU law and principles of EU budget law.

2.2.3.5. Exceptions based on tasks with competences shared between EU and Member States vis-à-vis other EU Member States

Finally, the question arises as to whether the Court's reasoning on Member States' freedom to create financial obligations vis-à-vis third countries outside of the EU framework would also be applicable to the creation of financial obligations vis-à-vis other EU Member States. In its judgment the Court paid special attention to the division of competences: As long as the Member States have the right to act they can act outside of the EU framework and create obligations outside of the EU budget. Following the same rationale with regard to an internal action Article 2(2) TFEU on the shared competences clarifies that the "Member States shall exercise their competence to the extent that the Union has not exercised its competence." In contrast to shared competences in external relations shared competences in internal affairs can create obstacles to the right of a Member State to act if the Union has exercised its competence. This difference relates to the fact that a joint action of EU Member States vis-à-vis each other competes against legislative acts under Article 288 TFEU.

As long as the Union did not exercise its competence Member States are still bound by Article 4(3) TFEU and its principle of sincere cooperation. This principle requires that Member States are not allowed to undermine the purpose of a proposed action. The ECJ has held that "Member States are subject to special duties of action and abstention in a situation in which the Commission has submitted to the Council proposals which, although they have not been adopted by the Council, represent the point of departure for concerted Community action" (ECJ 1981: para 28).

All in all, the Court's decision on the creation of financial obligations by the Member States outside of the EU framework in case of shared competences vis-à-vis third countries is, in principle, applicable to a joint action of the Member States vis-à-vis each other. This is,

however, limited by the legislative action already undertaken by the Union. Consequently, the establishment of a fund outside of the EU framework but only concerning EU Member States depends on whether and to which extent the functions this fund has to fulfil are already subject of existing or proposed EU legislation.

2.2.3.6. Summary: Fiscal capacity as a possible exception?

The establishment of a fiscal capacity outside of the EU budget can be seen as a permissible exception to the principle of unity of the EU budget and its completeness if its function can only be realised outside of the EU framework. The two functions of the fiscal capacity that the President of the European Council proposed fall partly within the EU's shared competence on social and territorial cohesion. It therefore has to be examined to which extent the two functions would undermine existing EU initiatives which can only be done on the basis of concrete proposals.

The establishment of an agency with an own legal personality would not be as such a permissible exception to the principle of unity of the EU budget and its completeness. As the purpose of not excluding Union agencies from this principle is to safeguard the budgetary sovereignty of the European Parliament an agency with an own legal personality would only be such an exception if the establishing act provides for a Parliamentary budgetary supervision that is comparable to the one in the EU budget.

2.2.4. Possibilities of differentiation within the EU budget

Whilst it is shown that under certain conditions the establishment of a fiscal capacity outside of the EU budget could be a permissible exception to the principle of unity of the EU budget and its completeness, it remains to be assessed whether a differentiation with regard to the revenue and the expenditure within the EU budget is possible.

The general budget of the EU is financed by own resources and other revenues. The own resources are defined in the Council decision 2007/436/EC, Euratom on the system of the European Communities' own resources (OJ L 163, 23.6.2007, p. 17) (hereinafter: Own Resources Decision). These are levies and tariff duties, VAT-based own resources and GNI-based own resources. The latter is at the moment a uniform rate to the sum of all the Member States' GNIs. In accordance with the procedure laid down Article 311(3) TFEU the Union may also establish a new category of own resources that is financed by contributions from a certain group of Member States with a higher rate.

With regard to expenditure Article 6 of the Own Resources Decision states that "the revenue [...] shall be used without distinction to finance all expenditure entered in the general budget of the European Union." The wording appears to preclude any differentiation. One has, however, to distinguish the establishment of expenditure that is directly linked to a certain own resource, which is prohibited, and the establishment of new budget heading only for a group of Member States without any direct link to an own resource. The latter case is legally possible under the Own Resources Decision and the regulation on financial rules. Article 18 of the 2002 regulation on financial rules as well as Article 21 of the 2012 regulation on financial rules allows for assigning certain revenues to certain expenditures. These revenues are called "assigned revenues" and can only be used for the budget line these revenues are assigned to. The assignment can legally be made by the basic act on the assigned revenue. A new own resource could therefore increase the general budget by the amount that contributes to this new budget line.

A comparable differentiation with regard to other revenue has already been adopted with Article 10 of Regulation (EU) No 1173/2011 on the effective enforcement of budgetary surveillance in the Euro area. According to this article “the interest earned by the Commission shall constitute other revenue as referred to in Article 311 TFEU and shall be assigned to the European Financial Stability Facility.” This regulation defines payment obligations only for Euro area Member States and the EFSF to which the revenue is allocated is a body exclusively composed by Euro area Member States.

2.2.5. Borrowing-and-lending operations entered into by the Union

A special issue are borrowing-and-lending operations entered into by the Union: Article 14(2) of the 2002 regulation on the financial rules as well Article 17(2) of the 2012 regulation on financial rules state that “the Union and [Union agencies], may not raise loans within the framework of the budget.” At the same time, the Union already raised such loans with regard to balancing of payment difficulties caused by the increase in prices of petroleum products (cf. regulation (EEC) No 397/75), to assisting non-eurozone Member States which are experiencing or are seriously threatened with difficulties in their balance of current payments (cf. regulation (EC) No 332/2002) or to financing investment projects which contribute to greater convergence and integration of the economic policies of the Member States (cf. Council decision 78/870/EEC). Revenue of these loans is, moreover, considered to be other revenue of the EU budget in terms of Article 311 TFEU.

This contradiction can be explained by the fact that based on Article 352 TFEU the Union is allowed to enter into borrowing-and-lending operations for specific purposes such as the above-mentioned ones. In order to contribute to the general EU budget, however, the Union is not entitled to raise loans.

The integration of the additional fiscal capacity into the general EU budget would not prevent to provide for an ability to borrow for it. This ability must be restricted to a specific purpose and the guarantees for its borrowing-and-lending operations must be mentioned in the general EU budget. Borrowing-and-lending operations as such are not part of the general budget.

2.3. Implications of the legal framework on possible concepts for a fiscal capacity

The legal framework as set by the Treaties reduces the possible concepts for a fiscal capacity to those in which the European Parliament is a supervisory body comparable to its role with regard to the EU budget: Either the fiscal capacity is integrated into the EU budget or if outside of the EU budget it has to be established on the basis of Article 352 TFEU in enhanced cooperation between the participating Member States or based on an international Treaty between these Member States including such a Parliamentary control.

2.3.1. Integration into the EU budget

The integration into the EU budget does not require an integration of the fiscal capacity into the multi-annual financial framework although, according to Article 312(1) TFEU, the annual budget of the Union shall comply with the multi-annual financial framework. Paragraph 11 of the Interinstitutional Agreement between the European Parliament, the Council and the Commission on budgetary discipline and sound financial management (OJ C

139, 14.6.2006, p. 1) provides for an exception for “revenue earmarked within the meaning of Article 18 of the [2002] Financial Regulation” (so called “assigned revenue”): “The financial framework does not take account of budget items financed by [such] revenue.” Furthermore, the integration of the fiscal capacity into the EU budget would require an amendment of the Own Resources Decision on the basis of Article 311(3) TFEU as well as the establishment of a new budget line for financing the functions foreseen for the fiscal capacity.

2.3.2. Fund for the eurozone Member States outside of the EU budget

The fiscal capacity can also be established outside of the EU budget based on Article 352 TFEU or an international Treaty. Its implementation could be assigned to the European Commission or a new separate agency. This would, however, infringe the principle of unity of the EU budget and its completeness under Article 310(1) TFEU if the basic act does not provide for supervision by the European Parliament comparable to the EU budget. Otherwise, the establishment of the fiscal capacity outside of the EU budget would undermine the budgetary sovereignty of the European Parliament and the democratic control of the Union’s revenue and expenditure.

3. LEGAL IMPLICATIONS OF THE “CONTRACTUAL ARRANGEMENTS”

A core element of the idea of an additional fiscal capacity is the combination of the establishment of such a capacity with the conclusion of “contractual arrangements” by Member States with EU institutions. They were called “individual arrangements of a contractual nature with the EU institutions on the reforms promoting growth and jobs” (van Rompuy 2012b: 7), “contractual arrangements to be concluded between the Commission and Member States” (European Commission 2012: 42) or “mutually agreed contracts for competitiveness and growth” (European Council 2012: 5). The conclusion of such a “contractual arrangement” is seen as a necessary condition in order to receive financial assistance from the funds of the fiscal capacity.

3.1. Elements of definition of “contractual arrangements”

According to the different official documents on the idea of “contractual arrangements” the following elements on what “contractual arrangements” are can be identified:

- Concluding parties are the Member States and EU institutions/Commission;
- Contractual arrangements are included in the European Semester;
- Content is based on the country-specific recommendations adopted by the Council, based on a proposal by the Commission, under Article 121(2) TFEU;
- For Member States under the corrective arm of the MIP the Corrective Action Plan (Article 8 of Regulation (EU) No 1176/2011) would correspond to the contractual arrangements;
- For Member States under the preventive arm of the MIP (cf. Article 6 of Regulation (EU) No 1176/2011)³, the contractual arrangements would consist of an action plan similar to that required under the corrective arm;

³ Art. 6 states: “If, on the basis of the in-depth review referred to in Article 5, the Commission considers that a Member State is experiencing imbalances, it shall inform the European Parliament, the Council and the Eurogroup accordingly. The Council, on a recommendation from the Commission, may address the necessary

- The arrangement needs the “endorsement” of the national parliament where appropriate under national procedures.

There is a divergence in the official documents with regard to the mandatory nature of the conclusion of “contractual arrangements”:

- Mandatory for all Euro area Member States (European Council 2012: 5; van Rompuy 2012c: 11)
- Mandatory for Member States under the Corrective Arm of the MIP (European Commission 2012: 43)

3.2. Legal nature of “contractual arrangements”

Contracts concluded by Member States with EU institutions can be International law Treaties, Memoranda of Understanding, contracts governed by public law or contracts governed by private law.

3.2.1. Preliminary remark: Capacity to conclude contracts or Treaties

In order to conclude “contractual agreements”, the contracting parties need to have the capacity to conclude contracts or Treaties. Whilst Member States possess the capacity to conclude contracts or Treaties according to general International law EU institutions do not have such a capacity. The EU has according to Article 47 TEU legal personality which includes the capacity to conclude contracts (Article 335 TFEU) or Treaties. The same applies to the ECB according to Article 282(3) TFEU and to the EIB according to Article 308 TFEU. All other EU institutions and, in particular, the European Commission do not have a legal personality and cannot conclude contracts in their names. They can only conclude contracts on behalf of the “European Union”. The same applies to the conclusion of “Memoranda of Understanding” in order to receive stability support from the ESM: According to Article 13(4) of the ESM-Treaty the European Commission signs the “Memorandum of Understanding” on behalf of the ESM. Therefore, EU institutions cannot conclude “contractual arrangements” with Member States but only the EU.

3.2.2. International law Treaties

Taking account of the above-mentioned elements of definition of “contractual arrangements” it appears to be rather unlikely that these are International law Treaties. Firstly, it is already unclear whether the EU has the right to conclude International law Treaties with its own Member States.⁴ Article 216(1) TFEU only enables the EU to conclude agreements with third countries or international organisations but not with a Member State. This can be explained by the fact that the EU can always address Member States by means provided for in Article 288 TFEU (regulations, directives and decisions), but only within the limits of the competences conferred upon the EU (Article 5(2) TEU). The conclusion of an International law Treaty within the scope of application of a legal basis in the Treaties would undermine the legislative procedure foreseen by this basis. The conclusion of an International law Treaty by the EU outside of the scope of application of any legal basis in the Treaties would infringe the principle of conferral in Article 5 TEU. “Contractual

recommendations to the Member State concerned, in accordance with the procedure set out in Article 121(2) TFEU.”

⁴ This has to be distinguished from the case of the so-called “mixed agreements”. Such agreements are concluded both by the EU and by the Member States on the one side and third countries or international organisations on the other side in case the content of an agreement is subject to shared Union competences.

arrangements” understood as International law Treaties concluded by the EU would therefore conflict with the EU Treaties.

Secondly, the Commission blueprint referred to an “endorsement of the national parliament where appropriate under national procedures”. An International law Treaty, however, requires a ratification which is more than an “endorsement”. The “contractual arrangements” can therefore not be considered to be International law Treaties.

3.2.3. Contracts governed by public law or private law

Contracts governed by public law or private law are legally binding agreements voluntarily concluded by two or more parties containing an obligation to do or not to do for one or more of the parties and granting the other party the right to demand the performance of the promised obligation. The distinctive feature is therefore the will of the parties to legally bind them.

Taking a closer look into the official documents one cannot identify an element according to which Member States should bind themselves legally to implement the measures on which they agreed in the contractual arrangements. The contractual arrangements are integrated into the European Semester. For Member States that are under the corrective arm of the MIP the contractual arrangement equals the corrective action plan under Article 8 of Regulation (EU) No 1176/2011. Under Article 8 these Member States are bound to the corrective action plan. The Commission monitors the implementation (Article 9) and if a Member State fails in doing so, the Council can decide on surveillance missions (Article 10(4)) and, in case the Member State is part of the euro area, on sanctions (Article 3 of Regulation (EU) No 1174/2011). Under these circumstances there is no need for an additional legal obligation under a contractual arrangement.

If, furthermore, a Member State is under the preventive arm of the MIP the official documents state with regard to the content of the contractual arrangements that these would consist of an action plan similar to that required under the corrective arm. Non-compliance, however, would not lead to sanctions. The official documents therefore do not provide for any further legal consequences if such a Member State concludes a contractual arrangement.

The only consequence that is linked to the fact that Member States have concluded contractual arrangements is that they are entitled to claim financial support from the fiscal capacity.

In sum, Member States are not supposed to create additional legal obligations by concluding contractual arrangements with the EU. By consequence, the contractual arrangements cannot be qualified as contracts governed by public law or private law.

3.2.4. Memoranda of Understanding

The elements given by the official documents resemble “Memoranda of Understandings” (MoU) as provided for in Article 13(3) of the ESM-Treaty. MoU are legally not binding agreements in which the parties declare their intention to act. They can be classified as Treaties but do not require any ratification. Compliance with MoUs can be ensured by incentives, so that financial assistance is only granted if there is compliance and withheld if there is non-compliance.

The main purpose of the “contractual arrangements” is an incentive-based enforcement of country-specific recommendations in addition to sanctions where sanctions legally can be imposed (such as for Member States under the corrective arm of the MIP). Where sanctions cannot be imposed legally (such as for Member States under the preventive arm of the MIP) it is the only means of enforcement.

3.3. Legal framework for “contractual arrangements”

The legal framework for “contractual agreements” is set by Article 121 TFEU and Articles 310 et seqq. TFEU.

3.3.1. Legal framework for the conclusion of “contractual arrangements”

The conclusion of “contractual arrangements” falls within the scope of application of Article 121 TFEU and the multilateral surveillance procedure. The purpose of “contractual arrangements” is to strengthen the enforcement of country-specific recommendations under Article 121(2) TFEU. The enforcement of country-specific recommendations is, however, restricted to a warning addressed to a Member State that can be made public. Any further enforcement could therefore infringe Article 121(4) TFEU.

The incentive-based enforcement of “contractual arrangements” does not infringe Article 121(4) TFEU. Although this is an enforcement measure that is not foreseen by this Article, it does not worsen the position of this Member State in case of non-compliance with the “contractual arrangement”. Prior to the conclusion of a “contractual arrangement” this Member State would have no right to claim financial assistance as it has no right to claim it after conclusion of this contract in case of non-compliance. Legally, its position is the same with or without conclusion of a “contractual arrangement”. Therefore, an incentive-based enforcement measure would not infringe Article 121(4) TFEU.

3.3.2. No involvement of the European Parliament in the conclusion of “contractual arrangements”

As the conclusion of “contractual arrangement” falls within the scope of application of the multilateral surveillance, the European Parliament cannot take part in the conclusion of the “contractual arrangement”. The “contractual arrangements” shall have the same content as the country-specific recommendations. These recommendations are adopted by the Council, based on a proposal by the Commission, under Article 121 TFEU. A possible inclusion of the European Parliament in the conclusion of “contractual arrangements” would therefore extend Parliament rights to an area in which the Treaties do not provide for any involvement of the European Parliament.

3.3.3. No obligation on Member States to conclude “contractual arrangements”

Although the official documents declare the conclusion of “contract arrangements” to be mandatory for either Euro area Member States or Member States under the corrective arm of the MIP, there is no EU legal obligation for Member States to conclude such “contractual arrangements”. Member States remain free in declaring politically to conclude “contractual arrangements”. As these contractual arrangements are not foreseen by any EU legal act Member States, however, cannot be obliged to conclude them. A legal act establishing the additional fiscal capacity could nevertheless require the conclusion of such a “contractual arrangement” as a condition to receive financial assistance from it.

3.3.4. Implementation of “contractual arrangements”

As mentioned above the budgetary part of the fiscal capacity falls within the scope of application of EU budget law. According to EU budget law the European Parliament controls the implementation of the EU budget. Therefore, the European Parliament should be included in the decision on whether a financial incentive is granted. The incentive-based enforcement of country-specific recommendations has a budgetary impact. This budgetary impact requires an involvement of the European Parliament when implementing the “contractual arrangements”.

3.4. Institutional implications of the “contractual arrangements”

“Contractual arrangements” understood as an additional enforcement measure of country-specific recommendations with the legal nature of a legally not binding MoU whose compliance gives Member State the right to claim financial assistance from the additional fiscal capacity only has minor institutional implications:

- for the **European Commission**: The European Commission has to negotiate the “contractual arrangements” and to sign them on behalf of the EU. As their content is the same as in country-specific recommendations or in corrective action plans, the Commission is already under the legal obligation to propose certain measures under Article 121 TFEU and under the MIP. This does not entail any further obligations. Under the MIP the Commission also has to monitor the compliance of Member States under the corrective arm. Therefore, only a monitoring task with regard to Member State under the preventive arm of the MIP creates an additional task for the Commission.
- for the **European Parliament**: The European Parliament has no right to take part in the conclusion of the “contractual arrangements”. However, as the implementation has a budgetary impact the European Parliament has to control the implementation of the “contractual arrangements”. Unlike the ESM, where the European Parliament has no right to control the implementation of the MoUs, granting financial assistance from the additional fiscal capacity requires Parliamentary control as this decision falls into the scope of application of EU budget law.

4. INSTITUTIONAL IMPLICATIONS OF FURTHER DEVELOPMENTS OF THE FISCAL CAPACITY

Although the conclusions of the European Council of 13/14 December 2012 did not mention any further development options for an additional fiscal capacity, the final report of the President of the European Council (van Rompuy 2012c: 8) and the blueprint of the European Commission (European Commission 2012: 31) addressed this question: They were referring to “an insurance-type mechanism between euro area countries to buffer large country-specific economic shocks”. This could be either as an asymmetric shock absorption capacity or as a counter-cyclical economic tool (comparable to the US unemployment benefit system).

Besides the question as to whether such further developments are economically convincing (cf. in this respect Wolff 2012) questions with regard to institutional changes are to be raised. Institutional implications are to be assessed in relation to the replies to the following

key questions for the direction that a further development of the additional fiscal capacity might take:

- Sources of **revenue**: An extended version of the additional fiscal capacity requires either new sources of revenue or an extension of existing sources of revenue. Sources of revenue can be contributions by Member States (which entails the question on which basis these contributions are to be calculated and if they should be modified in case a Member State is either hit by an asymmetric shock or failed to reach certain reform and budget targets), own resources such as a proper EU tax (e.g. the financial transaction tax) or loans (which requires an ability to borrow which is not allowed for the current EU budget but not completely forbidden for specialised funds, c.f. 2.2.5, p. 18). If a further developed fiscal capacity should be based on an own EU tax revenue or on loans a proper administration such as a Treasury needs to be established.
- Conditions for **payment**: The payments can be made unconditional and only be based on certain macroeconomic indicators. Reaching the indicator triggers payments to this Member State. The spending will remain national. The alternative would be to earmark payments for a defined purpose (such as unemployment). Spending is then defined at EU level. The first option only requires proper administration at EU level and democratic control of the legal act that defines the macroeconomic indicators. The second option confers also the spending on the EU level. This requires an enhanced democratic control of the spending by EU institutions.
- Decision-making for **authorising payments**: Payments can be automatic or based on discretion. If payments are automatic the mechanism establishing the automatic payment requires a legal act that should be co-decided by the European Parliament and the Council. If payments are based on a discretionary decision this discretionary power must be assigned to a certain body (European Commission or a specialised body) and the use of this discretionary power must be democratically controlled by the European Parliament.

4.1. What is legally possible under the existing Treaties?

Elements of these options for a further development of the additional fiscal capacity can already be realised under the existing Treaties. The legal options for the sources of revenue of such an extended version of the fiscal capacity (4.1.1) are to be examined followed by an assessment of possible legal bases for payments (4.1.2). Guidance for the conditions of payment (4.1.3) and decision-making for authorising payments (4.1.4) can also be found under the existing Treaties.

4.1.1. Sources of revenue

The extension of existing sources of revenue or the introduction of new sources of revenue for the extended additional fiscal capacity can be implemented by amending the Own Resources Decision according to the procedure laid down in Article 311(3) TFEU.

Contributions by Member States require a distinction between Member States participating in the additional fiscal capacity and those which do not. Such differentiation within the EU budget is, in principle, legally possible (cf. 2.2.4). It can either be done by including a differentiation in the correction mechanisms foreseen by Articles 4 and 5 of the Own Resources Decision. In this case the contributions by Member States would be calculated on

the basis of GNI. Or a new category of contributions could be included in the Own Resources Decision for participating Member States with a different calculation basis.

Financing by loans is currently forbidden for the general EU budget. It is, however, under the existing Treaties legally possible for specialised funds (cf. 2.2.5). If this also applies to a specialised fund, that exceeds a certain share of the EU budget and could therefore be considered as a circumvention of the prohibition for the general EU budget to be financed by loans, is, however, questionable.

An own EU tax can be introduced under the existing Treaties in two steps: Firstly, the EU tax has to be established on a legal basis. Secondly, the own EU tax has to be included as a new own resource in the Own Resources Decision according to the procedure laid down in Article 311(3) TFEU. Article 311 TFEU does not provide for any legal basis to establish taxes.

The Union can adopt measures in tax matters on the basis of Article 113 TFEU concerning indirect taxes, Article 115 TFEU concerning direct taxes, Article 192(2)(1)(a) TFEU concerning environmental taxes, Article 194(3) TFEU concerning energy taxes and Article 352 TFEU. Article 115 TFEU only serves as a basis for tax legislation by means of directives. An own EU tax can only be created by means of a regulation. Article 113 TFEU is not restricted to directives but requires a "harmonisation of legislation". The establishment of an own EU tax can hardly be considered as a "harmonisation". Although the ECJ decided that the establishment of an own EU agency can be done by means of regulation on the basis of Article 114 TFEU, that requires "approximation", such an establishment is only possible "in order to facilitate the uniform implementation and application of acts based on that provision" (ECJ 2006: para 44). As long as the establishment of an EU agency (or tax) facilitates an existing EU legal act it can be based on "harmonising" legal bases. An own EU tax, however, cannot be considered as an "annex" to an existing EU legal act. It is not "harmonisation" in terms of Article 113 TFEU. Articles 192 and 194 TFEU allow for the adoption of "provisions" (Article 192 TFEU) and "measures" (Article 194 TFEU) if they are "primarily of a fiscal nature". This includes regulations. Except for those very specific fields, the only remaining legal basis for the establishment of an own EU tax would be Article 352 TFEU. There can be, however, no legislation based on Article 352 TFEU if an overall assessment of all possible legal bases results in the conclusion that legislating on the basis of Article 352 TFEU would amount to a circumvention of the division of competences between the EU and Member States. The Treaties only provided for a possibility to adopt "measures" in very specific fields (environment and energy). In all other fields of taxation it only provides for harmonisation of Member States' legislation and the adoption of directives. This means, conversely, that the Treaties do not provide for any legal basis for an own EU tax which cannot be circumvented by relying on Article 352 TFEU (Mayer & Heidfeld 2011: 375).⁵

This finding is supported by the fact that the introduction of an own EU tax requires an enhanced democratic control which is not foreseen by the existing legal bases in tax matters. Articles 113 and 115 TFEU only require a consultation of the European Parliament and Article 352 TFEU only requires consent by the European Parliament. Taxation, however, requires representation. The creation of a future legal base for an EU tax whose purpose is to generate revenue for the EU needs a complete involvement of the European Parliament

⁵ This could be seen differently with regard to the introduction of the financial transaction tax if the main purpose of this tax is not to generate revenue for the EU but a steering effect with regard to financial transactions. The introduction of a financial transaction tax as a Member States' tax whose revenue is assigned partly or completely as an own resource of the EU budget remains, however, possible under the existing Treaties.

and special rules on taxation in Primary law (comparable to a financial constitution) (Waldhoff 2012: 12).

4.1.2. Legal basis for payments

A legal basis for payments can be found in Article 352 TFEU as long as payments are necessary in order to attain one of the objectives set out in the Treaties and provided that the Treaties either do not contain any specific competence or do not exclude any EU competence.

The idea of an EU basic unemployment insurance (Dullien 2007) according to which “the fiscal capacity would work as a complement or partial substitute to national unemployment insurance systems” (van Rompuy 2012c: 9) cannot be implemented on the basis of Article 352 TFEU. Rules on unemployment insurance can, in principle, be introduced on the basis of Article 153(1)(c) TFEU as a minimum benefit system as long as it is not inconsistent with the fundamental principles of Member States’ social security systems and part of the national unemployment insurances. A complement or partial substitute to national unemployment insurance systems, however, cannot be established on this basis since Article 153(2) TFEU only allows legislation by means of directives, which require a transposition into national law. Adopting such rules on the basis of Article 352 TFEU would circumvent Article 153 TFEU. Therefore, such payments would need a legal basis to be created by a Treaty change.

4.1.3. Conditions for payment

Whilst unconditional payments based only on the transgression of certain macro-economic indicators where the spending remains national appears easier to realise under the existing institutional configuration of the EU as it would not require the establishment of an EU Treasury, such payments could infringe Article 125 TFEU. The ECJ decided that Article 125 TFEU, which addresses “financial assistance” by the EU or the Member States, is not intended to prohibit either the Union or the Member States from granting any form of financial assistance whatever to another Member State” (ECJ 2012: para 132). Article 125 TFEU prohibits, however, “the Union and the Member States from granting financial assistance as a result of which the incentive of the recipient Member State to conduct a sound budgetary policy is diminished.” Therefore, “the activation of financial assistance [...] is not compatible with Article 125 TFEU unless it is indispensable for the safeguarding of the financial stability of the euro area as a whole and subject to strict conditions” (para 136). Whilst it can be argued that granting financial assistance in order to buffer large country-specific economic shocks is “indispensable for the safeguarding of the financial stability of the euro area as a whole”, payments cannot be activated unconditionally. Therefore, unconditional payments based only on the transgression of certain macro-economic indicators where the spending remains national conflict with Article 125 TFEU.

Earmarking payments for defined purposes appears rather to be in conformity with Article 125 TFEU as understood by the ECJ. Such conditionality in which the EU level defines the spending requires, however, deep modifications of EU’s institutional structure. This could include the creation of an EU Treasury with an appropriate Parliamentary control.

4.1.4. Decision-making for authorising payments

A mechanism according to which the fulfilment of certain criteria automatically triggers payments to a participating Member States appears to be in conformity with Article 125

TFEU. Although it could be inferred from the term “liable” that “automatism” is *per se* forbidden by this provision the judgment of the ECJ in the “Pringle” case only refers to two conditions for a financial assistance to meet in order to be in compliance with the Treaties: The payment must be, firstly, indispensable for the safeguarding of the financial stability of the euro area as a whole and, secondly, subject to strict conditions. As long as the strict conditions are met, an automatism of payment appears to be possible.

A discretionary decision-making as known under the ESM-Treaty does not give rise to legal objections with regard to Article 125 TFEU. Such a political decision-making procedure requires, however, deep modifications of EU’s institutional structure, especially with regard to democratic accountability.

4.2. Establishment of a Treasury

Some of the options for a further development of the additional fiscal capacity require an enhanced administrative body in order to manage them. This is called the establishment of a Treasury by the blueprint of the Commission (European Commission 2012: 33, 38, 40) and the final report of the President of the European Council (van Rompuy 2012c: 9).

Such a task could be entrusted to the European Commission or to a separate body. Assigning it to a body separate to the Commission would, however, undermine the Commission’s position among the EU institutions, weaken the Commission’s general position within the EU administration and, by that, violate the principle of institutional balance.

The establishment of a Treasury requires an enhanced democratic accountability. This can be done in two ways:

- The Commission as a college is responsible towards the European Parliament: This corresponds to the legal situation according to Article 234 TFEU. There can be only a motion of censure on the activities of the Commission as a whole. This entails further questions that are not explored in this note: Is it still convincing that the Commission is responsible as a college if it concerns decisions which only have an impact on Member States participating in the additional fiscal capacity? Is the decision-making within the Commission according to which it shall act by majority of its Members (Article 250 TFEU) a convincing decision-making for Treasury decision? Is it reasonable to have a motion of censure against the whole Commission if there were particular wrong decisions by the Treasury? Is it an appropriate democratic control of a Treasury if a motion of censure always has to be tabled on the Commission as a college instead of a motion on the Commissioner responsible for the Treasury?
- The head of the Treasury is directly responsible towards the European Parliament and, by consequence, should be elected by the European Parliament with the possibility of a motion of censure on his activities. If the Treasury is assigned to the Commission and, within the Commission, to the Commissioner for Economic and Monetary Affairs, acting as Vice-President of the Commission, the rules just mentioned would be applied to this Commissioner. This would require a Treaty change as under the existing Treaty only the Commission as a college is responsible towards the European Parliament and no single Commissioner can be elected by the European Parliament. Such a design would conflict with the existing principle of collegiality of the Commission as described above. The purpose of the principle of collegiality is to ensure an internal checks and balances within the Commission. This lack of internal checks and balances would, however, be

outweighed by an enhanced external checks and balances exercised by the democratically elected European Parliament

5. CONCLUSIONS

The additional EMU fiscal capacity can be understood, according to the official documents, in two ways. The first is an incentive-based enforcement instrument for country-specific recommendations under Article 121 TFEU. After the conclusion of “contractual arrangements”, understood as legally non-binding “Memoranda of Understanding”, concluding Member States can receive financial assistance from the additional fiscal capacity in case of compliance. It would then be an additional enforcement mechanism. A different understanding of “contractual arrangements” would conflict with the Treaties. The revenue and the expenditure of such an additional fiscal capacity are subject to EU budget law and its principles. Accordingly, the European Parliament has to assume a supervisory role over the fiscal capacity. It cannot be part in the negotiation and conclusion procedure of “contractual arrangements” but in their implementation. A differentiation of revenue and expenditure is possible under EU budget law. Certain revenue can be assigned to certain budget line. Such earmarked revenue is not part of the Multiannual Financial Framework. Such an additional fiscal capacity can be realised under the existing Treaties.

The second way of understanding the additional EMU fiscal capacity is to be an insurance-type mechanism between euro area countries to buffer large country-specific economic shocks. Such a fiscal capacity requires own and increased revenue. Such revenue could be realised under the existing Treaties as long as these are Member States’ contributions or a share of Member States’ taxes such as a national financial transaction tax. Own EU taxes whose purpose is to generate revenue for the EU cannot be established under the existing Treaties. The institutional framework of the EU is also not adapted to such a situation. The implementation of such a fiscal capacity can be done under the existing Treaties as long as it indispensable for the safeguarding of the financial stability of the euro area as a whole and subject to strict conditions. Unconditional financial assistance which is granted only by transgressing certain macroeconomic indicators is not in compliance with the Treaties. Deciding on these payments is under such conditions a highly political question and an administrative challenge that requires the establishment of a Treasury. Such a Treasury should be established with the European Commission. Under the existing Treaties, a proper democratic accountability of such a Treasury is not possible. In sum, only elements of an additional EMU fiscal capacity understood as an insurance-type mechanism between euro area countries to buffer large country-specific economic shocks can be realised under existing EU law. Especially questions on the democratic accountability cannot be solved in a satisfactory manner and require Treaty changes.

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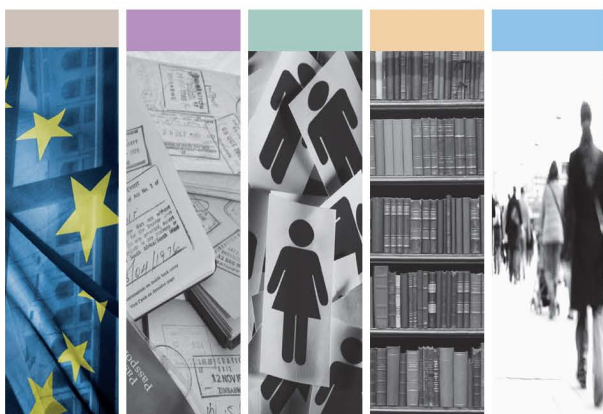
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