

A Fiscal Capacity for the Eurozone: Constitutional Perspectives



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IN-DEPTH ANALYSIS

Abstract

This in-depth analysis, commissioned by the European Parliament's Policy Department for Citizens' Rights and Constitutional Affairs at the request of the AFCO Committee, considers from a constitutional perspective the introduction of a fiscal capacity for the Eurozone. After explaining the constitutional asymmetry of Economic & Monetary Union, and surveying several recent proposals to establish a fiscal capacity, the in-depth analysis explains in comparative perspective how other federal unions by aggregation such as the United States and Switzerland are endowed with centralized fiscal stabilization tools and discusses how such a fiscal capacity could be established in the Eurozone, considering issues of legal bases, governance and accountability, as well as possible windows of opportunities to introduce it post-Brexit.

ABOUT THE PUBLICATION

This research paper was requested by the European Parliament's Committee on Constitutional Affairs and commissioned, overseen and published by the Policy Department for Citizen's Rights and Constitutional Affairs.

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LINGUISTIC VERSION

Original: EN

Manuscript completed in February 2019
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LIST OF ABBREVIATIONS

ECB	European Central Bank
EFSF	European Financial Stability Facility
EFSM	European Financial Stability Mechanism
EISF	European Investment Stabilization Function
EMU	European Monetary Union
ESM	European Stability Mechanism
EU	European Union
GDP	Gross Domestic Product
IMF	International Monetary Fund
MFF	Multi-annual financial framework
SGP	Stability and Growth PAct
UK	United Kingdom
US	United States of America

EXECUTIVE SUMMARY

The Treaties commit the European Union (EU) to establish an Economic and Monetary Union (EMU), but this project remains incomplete. The Treaty of Maastricht created an asymmetric EMU – fully federalizing monetary policy whilst leaving economic policy decentralized – and the legal and institutional responses to the euro-crisis have not fundamentally changed this status quo. For this reason, a growing number of calls has been made at the highest institutional level in favour of endowing the EMU with a fiscal capacity, that is a Eurozone budget that can be deployed as a stabilization tool in case of asymmetrical economic shocks.

The purpose of this in-depth analysis is to examine the introduction of a fiscal capacity in the Eurozone from a constitutional perspective. Comparative analysis reveals that federal unions formed by the aggregation of pre-existing states, such as the United States of America (US) and Switzerland, have developed a fiscal capacity at the central level to support their currency unions.

The in-depth analysis claims that the EU currently has the legal authority to set-up a Eurozone fiscal capacity without a need for treaty change, as already proposed by several EU institutions and member states. Nevertheless, the in-depth analysis explains that it is crucial that a Eurozone fiscal capacity be funded through genuine supranational own resources, rather than inter-state transfers, and this raises challenges given the unanimity requirement in EU tax policy. Moreover, a Eurozone fiscal capacity would have to be based on effective and legitimate governance and accountability mechanisms – through a Treasury authority subject to proper democratic control by the European Parliament. Despite these challenges, the in-depth analysis suggests that the EU has a window of opportunity to introduce a Eurozone fiscal capacity as a result of Brexit, since the United Kingdom withdrawal from the EU compels reforms of the EU revenue and expenditures system.

Ultimately, a fiscal capacity is crucial to complete EMU, and as the example of federal unions like the US and Switzerland highlights, this can be achieved through legal and institutional reforms driven by political leaders at times of economic necessity.

1. INTRODUCTION

Pursuant to Article 3(4) TEU, the European Union (EU) “shall establish an economic and monetary union whose currency is the euro”. Nevertheless, to this day Europe’s Economic and Monetary Union (EMU) remains incomplete: since the Maastricht Treaty of 1992, in fact, EMU has been built on an asymmetry between monetary and economic affairs, and the euro-crisis and the responses to it have not fundamentally altered the status quo. In particular, while for the member states that adopted the euro as their currency monetary policy has been fully federalized, the EU still lacks fiscal tools to cushion asymmetric shocks which may arise in the Eurozone. Because member states have lost control over their currency and are subject to tight fiscal constraints, however, they have limited capacity to take counter-cyclical responses to economic busts.

This state of affairs has been increasingly identified as a weakness of the EMU, and a growing number of calls have been made at the highest institutional level in favor of endowing the Eurozone with a fiscal capacity – that is a budgetary instrument, funded through new resources, that can be deployed by EU authorities to stabilize the economy in case of asymmetric shocks, e.g. by preserving given levels of public investments or covering rising costs of unemployment benefits. In fact, as the comparative analysis reveals, all other mature currency unions have fiscal tools at the federal level that allow the central government to take action in case of economic recessions. In particular, the case of the United States of America (US) and Switzerland – two federal systems constituted by the aggregation of pre-existing states – is telling: in both these federal unions, through a long and incremental process, the central government has acquired the fiscal resources and the legal power to undertake an economic policy in parallel to the one of its component states.

The purpose of this in-depth analysis is to analyze the establishment of a fiscal capacity for the Eurozone from a constitutional perspective. The focus of this contribution is on the legal – rather than the economic – dimension. Others have discussed and explained the economic rationale for setting up a fiscal stabilization function for the EMU. This work, instead, examines how a fiscal capacity could be brought to bear in the EU by considering the possible legal bases, funding mechanisms, and rules of governance and accountability. As the in-depth analysis claims, the current EU constitutional framework already allows taking important steps towards the creation of a fiscal capacity, and Brexit – the decision of the United Kingdom (UK) to withdraw from the EU – actually opens a window of opportunity to this end. Nevertheless, as the in-depth analysis suggests in light of comparative insights, the proper design of a Eurozone budget is a pre-condition for its success: in particular, it is crucial that such a fiscal capacity be funded by real own resources, rather than state transfers, and subjected to mechanisms of democratic legitimation.

The in-depth analysis is structured as follows. Chapter 2 underlines the original asymmetry of EMU, and explains how the legal and institutional reforms adopted in response to the euro-crisis have not fundamentally altered this. Chapter 3 maps the proposals that since 2012 have increasingly been made at the highest EU institutional level to overcome the asymmetry of EMU, by establishing a fiscal capacity for the Eurozone. Chapter 4 adds a comparative perspective to the analysis by overviewing how federal systems by aggregation such as the US and Switzerland have developed fiscal tool to tackle asymmetric shocks emerging in their unions. Chapter 5, then, considers how a fiscal capacity for the Eurozone could be established in the EU in the absence of a political federation and discusses from a constitutional perspective the legal bases, funding mechanisms and rules of governance and accountability of such a budget. Chapter 6, finally, concludes the analysis suggesting that a window of opportunity to endow the Eurozone with a budget, provided there is the political will to complete EMU.

2. EMU: AN ASYMMETRIC ARCHITECTURE

EMU has been characterized since its inception by an asymmetry between the economic and the monetary dimensions. The euro-crisis which hit the Eurozone starting 2009, and the legal and institutional responses adopted to tackle it, have not fundamentally changed this state of affairs.

2.1. The original settlement

The Treaty of Maastricht created an asymmetric EMU. While in the run-up to the intergovernmental conference that resulted in the establishment of the EU both policy-makers¹ and academics² had emphasized the importance of integrating in parallel both monetary and fiscal policies, the Treaty of Maastricht resulted in a compromise:³ on the one hand, the M of EMU (monetary policy) was fully federalized while, on the other, the E of EMU (economic policy) remained decentralized, subject to a number of fiscal rules and mechanisms of intergovernmental coordination.

On the monetary side, the Treaty of Maastricht paved the way for the adoption of the euro as the currency of the EU. The majority of EU member states – with the exception of the United Kingdom and Denmark, which secured an opt-out to maintain their national currencies⁴ – transferred their monetary sovereignty to the EU, establishing a fully-fledged federal institution – the European Central Bank (ECB) – to govern the single currency.⁵ The ECB, which is an EU institution,⁶ was tasked with the specific mandate to maintain price stability (an objective it identified as a level of inflation below, but close to 2% per year) and protected by the interference of national governments or private actors by a strong guarantee of independence.⁷ This institutional architecture operated as the background for the introduction of the euro, which started circulating as the currency of 12 EU member states in 2002, and progressively expanded to encompass today 19 EU member states.

On the economic side, however, the Treaty of Maastricht did not accomplish any major transfer of powers from the member states to the EU institutions. In fact, member states did not delegate powers to the supranational institutions, and EMU was born without a fully-fledged federal budget. Rather, member states maintained control over their budgetary policies – albeit accepting to subject them to mechanisms of coordination. On the understanding that in a currency union the economic policy of each member states was a matter of common concern,⁸ EU member states decided to create an institutional framework – reflected in the establishment in 1997 of the Eurogroup: the informal gathering of Finance Ministers of the EU member states which use the euro as their currency⁹ – in which they could coordinate their national budget policies. At the same time, in order to avoid cases of moral hazard and minimize the risks of negative externalities, the Treaty of Maastricht backed-up the decentralized economic framework with two legal tools.

First, the Treaty of Maastricht entrenched the so-called Stability and Growth Pact (SGP), a set of legally-binding mathematical rules¹⁰ designed to ensure that member states would run sound national budgetary policy. Specifically, the SGP compelled EU member states adopting the euro as their currency to maintain an annual budget deficit of below 3% of gross domestic product (gdp), as well as to reduce their overall public debt to 60% of gdp. Moreover, the SGP introduced surveillance procedures as well as a possible correction mechanism to sanction member states running excessive

¹ Jacques Delors, 'Report on Economic and Monetary Union in the European Communities' (Publication Office of the EC 1989) 89.

² Barry Eichengreen, *European Monetary Unification* (MIT Press 1993).

³ Markus Brunnermaier, Harold James & Jean-Pierre Landau, *The Euro and the Battle of Ideas* (Princeton UP 2016).

⁴ See today Protocol No. 15 and Protocol No. 16.

⁵ Tommaso Padoa Schioppa, *The Euro and its Central Bank* (MIT Press 2004).

⁶ Art. 13 TEU.

⁷ Art. 282 TFEU.

⁸ Art. 121(1) TFEU.

⁹ See today Protocol No. 14.

¹⁰ See today Protocol No. 12.

deficits.¹¹ In particular, the Commission was vested with the responsibility to monitor member states budgetary policy, with the possibility to propose measures (including, in the extreme case, fines) in cases of serious deviation from the rules – which had however to be adopted by the Council by qualified majority.

Second, to enhance the credibility of the SGP, the Treaty of Maastricht also codified a no-bailout rule, geared toward excluding any form of debt mutualization vis-à-vis member states which, due to their unsound budgetary policy, were unable to service their debt. In fact, the no-bailout rule both prohibited EU institutions and member states from providing financial stability support to countries in distress,¹² and banned the ECB from coming to the rescue via its monetary policy of Eurozone member states which faced a budget crisis.¹³

2.2. The euro-crisis and the responses to it

The original architecture of EMU endured more or less unchanged for the first decade of the euro's life. However, the crisis quickly exposed the weaknesses of the original EMU constitutional settlement, and prompted a number of major legal and institutional responses. In fact, precisely the deficiencies of EMU transformed a financial crisis into an existential challenge for the EU, to the point that the survival of the euro as a currency union was itself at a point in question. Yet, through their concerted action, the EU institutions and the member states managed to address at least the most immediate effects of the euro-crisis by reforming the constitutional architecture of EMU. In particular, as it has been pointed out in the scholarly debate,¹⁴ three main legal and institutional responses to the euro-crisis took place.

First, EU institutions and member states acted to strengthen the budgetary constraints on the understanding that the lax enforcement of the SGP was the main cause of the euro-crisis. To this end, in 2011 and 2013 the EU institutions amended EU fiscal rules with the adoption of several new EU regulations and directives – the so-called “6-pack”¹⁵ and “2-pack”¹⁶ – which strengthened both the preventive and corrective arms of the SGP, among others by enhancing the Commission surveillance power over member states budget laws and introducing a reversed qualified majority rule in the Council as a condition to block Commission's proposals to sanction disobedient member states. Moreover, 25 out of the then 27 EU member states adopted in 2012 a treaty outside the EU legal order – the Treaty on Stability, Coordination and Governance in the EMU, generally referred to as the Fiscal Compact¹⁷ – which compelled signatory parties to introduce a balanced budget amendment within their national constitutional system, and further tightened the deficit rule which states had to respect in drafting their budget laws.

¹¹ Arts. 121 and 126 TFEU.

¹² Art. 125 TFEU.

¹³ Art. 123 TFEU.

¹⁴ Federico Fabbrini, *Economic Governance in Europe* (OUP 2016).

¹⁵ See Regulation (EU) No 1173/2011, of the European Parliament and of the Council of 16 November 2011 on the Effective Enforcement of Budgetary Surveillance in the Euro Area, OJ 2011 L 306/1; Regulation (EU) No 1174/2011, of the European Parliament and of the Council of 16 November 2011 on Enforcement Measures to Correct Excessive Macroeconomic Imbalances in the Euro Area, OJ 2011 L 306/8; Regulation (EU) No 1175/2011, of the European Parliament and of the Council of 16 November 2011 Amending Council Regulation (EC) No 1466/97 on the Strengthening of the Surveillance of Budgetary Positions and the Surveillance and Coordination of Economic Policies, OJ 2011 L 306/12; Regulation (EU) No 1176/2011, of the European Parliament and of the Council of 16 November 2011 on the Prevention and Correction of Macroeconomic Imbalances, OJ 2011 L 306/25; Council Regulation (EU) No 1177/2011 of 8 November 2011 amending Regulation (EC) No 1467/97 on Speeding Up and Clarifying the Implementation of the Excessive Deficit Procedure, OJ 2011 L 306/33; Council Directive 2011/85/EU of 8 November 2011 on Requirements for Budgetary Frameworks of the Member States, OJ 2011 L 306/41.

¹⁶ See Regulation (EU) No 473/2013 of the European Parliament and the Council of 21 May 2013 on monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficits of Member States in euro-area, OJ 2013 L 140/11; Regulation (EU) No 472/2013 of the European Parliament and the Council of 21 May 2013 on enhanced surveillance of euro-area Member States experiencing or threatened with serious difficulties with respect to their financial stability, OJ 2013 L 140/1.

¹⁷ See Treaty on Stability, Coordination and Governance in the Economic and Monetary Union, 2 March 2012, [hereinafter Fiscal Compact], available at http://www.eurozone.europa.eu/media/304649/st00tscg26_en12.pdf

Second, EU institutions and member states created new mechanisms of financial stabilization for countries in fiscal stress, moving beyond a strict construction of the no-bailout rule. In particular, in 2011 the Council set up a temporary European Financial Stability Mechanism (EFSM),¹⁸ which was soon replaced by a European Financial Stability Facility (EFSF)¹⁹ – a private law entity incorporated under Luxembourg law – and then by a permanent European Stability Mechanism (ESM) – established in 2012 by an intergovernmental treaty between the Eurozone member states.²⁰ The EFSM, EFSF and ESM supported 5 Eurozone member states which had lost access to the international bond markets – Greece, Portugal, Ireland, Cyprus and Spain²¹ – giving loans subject to conditionality. Stabilization of public finances, otherwise, was complemented by new steps designed to integrate financial markets – notably the creation of a banking union, with a Single Supervisory Mechanism²² for the largest transnational banks and a Single Resolution Mechanism²³ to wind-down failing credit institutions. All this was then backed-up by policies of the ECB which, after launching a Securities Market Program in 2010 to purchase government bonds on the secondary market,²⁴ announced an Outright Monetary Transaction plan to buy state securities of countries which accepted to enter into an ESM-financed support program.²⁵

Third, complementing the developments above, the EU institutions and member states also created new governance mechanisms. In order to ensure a better surveillance of budget rules, a new European semester was created, whereby member states are now requested to submit their draft budget bill to the Commission for review before these are tabled for approval in national parliaments. And in order to manage financial support programs and secure respect for the conditionality attached to it in member states receiving ESM aid, the format of the troika – a grouping of the Commission, ECB and the International Monetary Fund (IMF) – took hold.²⁶ On top of this, the Fiscal Compact also created a brand new institution – the Euro Summit, an informal gathering of the heads of state and government of the EU member states using the euro as their currency, chaired by a full-time president²⁷ – to provide a forum for top-level discussion on the functioning of the Eurozone and its challenges.

Nevertheless, the legal and institutional measures adopted in response to the euro-crisis have not fundamentally tackled the original asymmetry of EMU. In fact, if especially the constitutionalization of budgetary constraints has centralized powers in the EU,²⁸ this has happened on the basis of a 'surveillance model',²⁹ in which the EU enjoys no fiscal capacity of its own but has invasive oversight power on the budgetary policies of the member states. It is in this context that growing calls have been made in favor of developing a fiscal capacity for the Eurozone.

¹⁸ Council Regulation No. 407/2010/EU of 11 May 2010 establishing a European financial stabilisation mechanism OJ 2010 L 118/1.

¹⁹ Decisions of the Representatives of the Government of the Euro Area Member States Meeting within the Council of the EU, ECOFIN, 9 May 2010. Doc. No. 9614/10.

²⁰ See Treaty Establishing the European Stability Mechanism [hereinafter ESM Treaty], 25 March 2011, available at <http://www.european-council.europa.eu/media/582311/05-tesm2.en12.pdf>

²¹ In fact, Spain never lost access to market financing but raising money was becoming increasingly expensive. The ESM assistance package for Spain was unlike those of other programme countries. The money was used for the only purpose of restructuring several country's banks. <https://www.esm.europa.eu/assistance/spain>

²² See Council Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions, OJ 2013 L 287/63.

²³ See Regulation (EU) No 806/2014 of the European Parliament and of the Council establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Bank Resolution Fund and amending Regulation (EU) No 1093/2010.

²⁴ Decision of the European Central Bank of 14 May 2010 establishing a securities markets programme (ECB/2010/5), [2010] OJ L124/8.

²⁵ European Central Bank, Press release, Technical Features of Outright Monetary Transactions, 6 September 2012.

²⁶ See also European Parliament resolution of 13 March 2014 on the enquiry on the role and operations of the Troika (ECB, Commission and IMF) with regard to the euro area programme countries, P7_TA(2014)0239.

²⁷ Art. 12 Fiscal Compact.

²⁸ Federico Fabbrini, 'The Fiscal Compact, the Golden Rule and the Paradox of European Federalism', (2013) 36 *Boston College International & Comparative Law Review* 1.

²⁹ Alicia Hinarejos, 'Fiscal Federalism in the European Union: Evolution and Future Choices for EMU', (2013) 50 *Common Market Law Review* 1621.

3. OVERCOMING ASYMMETRY: PROPOSALS FOR A FISCAL CAPACITY

Proposals to establish a fiscal capacity to strengthen EMU have been made at the highest level by ad hoc groups established to reflect on the future of EMU, as well as by the European Commission, the European Parliament and the member states themselves.

3.1. High-level groups

The first reference to the term 'fiscal capacity' appears in the so-called Four Presidents Report – a document entitled "Towards a Genuine Economic and Monetary Union" and drafted by the President of the European Council in cooperation with the Presidents of the Commission, the ECB and the Eurogroup. In particular, while in its June 2012 inaugural report³⁰ the President of the European Council Herman van Rompuy had already suggested that "[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 [T]reasury office,"³¹ it is in the interim October 2012 report that the idea of fiscal capacity is first articulated and presented. In its discussion about the next pillars of EMU reform – a Banking Union, a Fiscal Union, an Economic Union and a new framework for democracy, legitimacy and accountability – the report stated that "strengthening [fiscal] discipline is [...] not sufficient" and suggested that "[i]n the longer term, there is a need to [...] go beyond the current steps to strengthen economic governance to develop a fiscal capacity for the EMU."³²

According to the interim report, a fiscal capacity would pursue functions which are not covered by the EU budget, the so-called multi-annual financial framework (MFF). In particular, "one of the functions of such a new fiscal capacity could be to facilitate adjustments to country-specific shocks by providing for some degree of absorption at the central level."³³ At the same time, "[a]nother important function of such a fiscal capacity would be to facilitate structural reforms that improve competitiveness and growth."³⁴ These ideas were later developed in the December 2012 final Four Presidents report,³⁵ where the establishment of a fiscal capacity was clearly linked to the creation of a "shock-absorption function" to improve the resilience of EMU.³⁶ As the Four Presidents final report clarified, the economic rationale of this instrument lay in the reduction of the impact of country-specific shock and in the prevention of contagious effects across the currency union.³⁷ Because of its "insurance-type" nature, at the same time, the report suggested alternative macro or micro economic approaches to set-up a fiscal capacity,³⁸ and emphasized that its design would still have to avoid "the risk of moral hazard inherent in any insurance system."³⁹

Moreover, the idea of a fiscal capacity – even though not the term 'fiscal capacity' itself – has been supported also in the so-called Five Presidents report "Completing Europe's Economic and Monetary Union", drafted in June 2015 by the President of the European Commission, in close cooperation with the Presidents of the European Council, the Eurogroup, the ECB and now also the European Parliament.⁴⁰ Building on the Four Presidents report, the Five Presidents report indicated the importance of creating "a euro area-wide fiscal stabilization function,"⁴¹ – although allegedly

³⁰ President of the European Council, Report Towards a genuine Economic and Monetary Union, 26 June 2012.

³¹ Ibid 5.

³² President of the European Council, Interim Report Towards a genuine Economic and Monetary Union, 12 October 2012, 4.

³³ Ibid 5.

³⁴ Ibid.

³⁵ President of the European Council, Final Report Towards a Genuine EMU, 5 December 2012.

³⁶ Ibid 5.

³⁷ Ibid 10.

³⁸ Ibid 11 (distinguishing between a macroeconomic approach, which looks at contribution to, and disbursement from, the fiscal capacity in light of fluctuations in the economic cycle; and a microeconomic approach, focused instead on specific public functions such as unemployment insurance).

³⁹ Ibid 10.

⁴⁰ President of the European Commission, Report Completing Europe's Economic and Monetary Union, 22 June 2015.

⁴¹ Ibid 14.

postponing the achievement of this objective “in the longer term.”⁴² As the report emphasized, “in case of a very severe crisis, national budgets can become overwhelmed [... and] in such situations, national fiscal stabilisers might not be enough to absorb the shock.”⁴³ For this reason, otherwise “all mature Monetary Unions have put in place a common macroeconomic stabilization function to better deal with shocks that cannot be managed at the national level alone.”⁴⁴ Hence, the report concluded with a plea in favor of an automatic stabilization mechanism which “should improve the cushioning of large macroeconomic shocks”⁴⁵ – although cautioning such a mechanism should “not lead to permanent transfers between countries”⁴⁶.

Finally, an important endorsement in favor of a fiscal capacity for the EU has also emerged from the report of the high-level group chaired by former Italian Prime Minister and European Commissioner Mario Monti,⁴⁷ which had been established by an inter-institutional deal between the European Parliament, the Commission and the Council to reflect on the future of EU own resources. Although the high-level group mostly focused on the sources of funding of the MFF, its persuasive call for a reform of the revenue-side of the EU budget bear important implication also for the spending-side. In fact, its final December 2016 report with recommendation also referred to the idea of a euro area budget “to tackle the specific characteristics of a monetary union, such as the need for automatic stabilisers, and the fiscal and budgetary policies of the participating Member States.”⁴⁸ To this end, the Monti report identified possible sources of ad hoc revenues for the euro area, and stressed that a new “budget authority, whether created within the EU institutional framework or via a separate authority such as a European treasury, would have to be created to manage the expenditure and revenue of such budget, and ensure appropriate accountability and governance.”⁴⁹

3.2. The European Commission

The European Commission too has made the case in favor of a fiscal capacity in response to the euro-crisis. The November 2012 Commission blueprint “For a Deep and Genuine EMU”⁵⁰ endorsed the idea of a fiscal capacity to underpin structural reforms at the national level and provide a stabilization tool at Eurozone level to support adjustment to asymmetric shocks. Moreover, following the Four Presidents report, the Commission suggested the creation of a fiscal capacity in stages, distinguishing between a short term, in which “the economic governance framework should be strengthened further by creating a ‘convergence and competitiveness instrument’ within the EU budget – but separate from the MFF – to support the timely implementation of structural reforms, on the condition that ‘contractual arrangements’ are concluded between Member States and the Commission;”⁵¹ and a medium-long term in which a real fiscal capacity for the euro area would be fully established. In this light, in March 2013 the Commission presented as a first step the introduction of convergence and competitiveness instruments, emphasizing the link between structural reform and financial support to be provided by member states.⁵²

⁴² Ibid.

⁴³ Ibid.

⁴⁴ Ibid.

⁴⁵ Ibid.

⁴⁶ Ibid 15.

⁴⁷ Mario Monti, Future financing of the EU, Final report and recommendations of the High Level Group on Own Resources, December 2016.

⁴⁸ Ibid page 67.

⁴⁹ Ibid.

⁵⁰ European Commission Communication, A Blueprint for a Deep and Genuine EMU: Launching a European Debate, 28 November 2012, COM (2012)777 final.

⁵¹ European Commission Memo, A Blueprint for a Deep and Genuine Economic and Monetary Union, 28 November 2012, MEMO/12/909, 2.

⁵² European Commission Communication, The Introduction of Convergence and Competitiveness Instruments, 20 March 2013, COM (2013)165 final.

Moreover, following the May 2014 European Parliament elections and the appointment of a new European Commission, the efforts to deepen EMU have remained a priority of the Commission.⁵³ In fact, the new Commission President Jean-Claude Juncker indicated in his July 2014 programmatic speech before the European Parliament, that he would seek to “launch legislative and non-legislative initiatives to deepen our Economic and Monetary Union [... including through] a targeted fiscal capacity at Euro zone level.”⁵⁴ And in the September 2017 State of the Union Address, he further developed on this idea, stating that the Commission would “make concrete proposals for the creation of a dedicated euro-area budget line within the EU budget.”⁵⁵

In the context of the reflection on the future of Europe⁵⁶ on the occasion of the 60th anniversary of the Treaties of Rome, the Commission brought forward further, more detailed options in favor of a fiscal capacity in EMU. In particular, building on two reflection papers on the future of EMU,⁵⁷ and the future of EU finances,⁵⁸ in December 2017 the Commission made the case for “a new budgetary instrument for a stable euro area within the Union framework.”⁵⁹ This proposal, which is part of a package to deepen EMU⁶⁰ – including also a proposal to re-integrate the ESM in the EU legal order through the establishment of a European Monetary Fund,⁶¹ and to strengthen the fiscal responsibility of the member states⁶² – advanced proposals to create a Euro area budget, to be read in conjunction with a communication on the creation of a EU Finance Ministry.⁶³ Specifically, the Commission identified four functions for such euro area budget: namely: 1) to support national reforms; 2) to foster convergence, notably for member states that have yet to adopt the euro as their currency; 3) to secure a backstop for the Banking Union; and 4) to roll-out a stabilization function as a way for preserving investment levels in the event of large asymmetric shocks.⁶⁴ The abovementioned plan was then integrated in the framework of the preparatory work for the new MFF,⁶⁵ and in May 2018 the Commission proposed to set up a Reform Support Program of 25bn€ and European Investment Stabilization Function (EISF) of 30bn€ as part of the 2021-2027 MFF.⁶⁶ In particular, the EISF would establish a counter-cyclical fiscal tool through loans that the Commission would disburse, subject to conditionality, to Eurozone states facing a sudden increase in unemployment as a way to maintain a level of public investment in a situation of economic recession.

3.3. The European Parliament

The strongest backing for a fiscal capacity to date has come from the European Parliament. In the midst of the euro-crisis, the European Parliament was the most vocal in calling for a fiscal capacity to complete

⁵³ European Commission Communication, On steps towards Completing Economic and Monetary Union, 21 October 2015 COM (2015) 600 final.

⁵⁴ See European Commission President-elect, Jean-Claude Juncker, A New Start for Europe: My Agenda for Jobs, Growth and Democratic Change, Speech at the European Parliament, Strasbourg 15 July 2014, 7.

⁵⁵ See European Commission President, Jean-Claude Juncker, State of the Union, Brussels, 13 September 2017.

⁵⁶ European Commission, whitepaper on The Future of Europe, 1 March 2017.

⁵⁷ European Commission, reflection paper on The Deepening of Economic and Monetary Union, 31 May 2017.

⁵⁸ European Commission, reflection paper on The Future of EU Finances, 28 June 2017.

⁵⁹ European Commission Communication, New Budgetary Instrument For a Stable Euro Area Within the Union Framework, 6 December 2017 COM (2017)822 final.

⁶⁰ European Commission Communication, Further Steps Towards Completing Europe's Economic and Monetary Union: a roadmap, 6 December 2017 COM (2017)821 final.

⁶¹ European Commission proposal for a Council Regulation, on the establishment of the European Monetary Fund, 6 December 2017 COM (2017)827 final.

⁶² European Commission Communication, laying down provisions for strengthening fiscal responsibility and the medium-term budgetary orientation in the Member States, 6 December 2017 COM (2017)824 final.

⁶³ European Commission Communication, A European Minister of Economy and Finance, 6 December 2017 COM (2017)823 final.

⁶⁴ See note 59.

⁶⁵ European Commission Communication, laying down the multiannual financial framework for the years 2021 to 2027, 2 May 2018 COM (2018)322 final.

⁶⁶ European Commission Communication, on the establishment of a European Investment Stabilisation Function, 31 May 2018 COM (2018)387 final.

EMU. In November 2012,⁶⁷ the Parliament underlined how “the innovative idea of a central budget for the euro area funded by members of the euro area is now being proposed as the ultimate guarantee for [...] financial solidarity”⁶⁸ and expressed its view “that a ‘genuine EMU’ cannot be limited to a system of rules but requires an increased budgetary capacity based on specific own-resources [...] which should in the framework of the Union budget, support growth and social cohesion addressing imbalances, structural divergences and financial emergencies which are directly connected to the monetary union.”⁶⁹ In May 2013 then, the Parliament clarified that it considered the Commission proposal for convergence and competitiveness instruments as “building blocks towards a genuine fiscal capacity,”⁷⁰ and it expressed its clear wish that “this mechanism should be funded by means of a new facility triggered and governed under the Community method as an integral part of the EU budget, but outside the MFF ceiling, so as to ensure that the European Parliament is fully involved as a legislative and budgetary authority.”⁷¹ And in December 2013, the European Parliament further made the case for a “budgetary capacity which should, in the framework of the Union budget, support growth and social cohesion, addressing imbalances, structural divergences and financial emergencies which are directly connected to the monetary union,”⁷² indicating that this should be funded by real own resources.

Since the European elections of 2014, moreover, the EP has continued to push in favor of a real fiscal capacity. In June 2015, the Parliament once again reaffirmed its support for “a euro area fiscal capacity based on specific own-resources which should, in the framework of the Union budget [...] assist Member States in the implementation of agreed structural reforms.”⁷³ And in February 2017, the Parliament approved an ad hoc resolution on budgetary capacity for the Eurozone,⁷⁴ as part of a three-document package to outline its vision for the constitutional future of the EU.⁷⁵ This resolution represents the climax of a policy convergence within the Parliament – also due to the party affiliation and nationality of the two joint rapporteurs: Reimer Böge (EPP/Germany) and Pervenche Berès (S&D/France) – outlining a concrete roadmap to set up a fiscal capacity in the EU. The resolution, in particular, affirms that a fiscal capacity is needed to complement the transfer of monetary policy to the EU level, and that this should be created in addition to the ESM.⁷⁶ According to the European Parliament, the fiscal capacity for the euro area should pursue three main functions, namely: 1) to foster economic and social convergence, including by supporting structural reforms; 2) to smooth the differences in the business cycles of the member states, by tackling asymmetric shocks; and 3) to increase the resilience of the Eurozone addressing symmetric shocks.⁷⁷

Calls by the European Parliament for the establishment of a fiscal capacity interact also with ongoing work on the next MFF. Hence, in its March 2018 resolution on the preparation for the 2021-2027 MFF the European Parliament expressed its expectation that the new MFF will integrate a specific euro area budgetary capacity, which “should be part of the Union budget, counted over and above the ceilings of the multiannual financial framework, without prejudice to the other MFF programmes, and should be financed by euro-area and other participating members via a source of revenue to be agreed

⁶⁷ European Parliament, Resolution of 20 November 2012 with recommendations to the Commission on the report of the Presidents of the European Council, the European Commission, the European Central Bank and the Eurogroup, Towards a genuine Economic and Monetary Union, ([2012/2151\(INI\)](#)).

⁶⁸ Ibid, para CR.

⁶⁹ Ibid, para 11.

⁷⁰ European Parliament, Resolution of 23 May 2013 on future legislative proposals on EMU: response to the Commission communications ([2013/2609\(RSP\)](#)), para 22.

⁷¹ Ibid, para 26.

⁷² European Parliament, Resolution of 12 December 2013 on the constitutional problems of multi-tier governance in the European Union, ([2012/2078\(INI\)](#)), para 2.

⁷³ European Parliament, Resolution of 24 June 2015 review of economic Governance framework: Stocktaking and challenges ([2014/2145\(INI\)](#)), para 57(c).

⁷⁴ European Parliament, Resolution of 16 February 2017 on budgetary capacity for the euro area, ([2015/2344\(INI\)](#)).

⁷⁵ See European Parliament, resolution of 16 February 2017 on improving the functioning of the European Union building on the potential of the Lisbon Treaty, ([2014/2249\(INI\)](#)), and European Parliament, resolution of 16 February 2017 on possible evolutions of and adjustments to the current institutional set-up of the European Union, ([2014/2248\(INI\)](#)).

⁷⁶ See note 74, para 1.

⁷⁷ Ibid.

between participating Member States and considered to be assigned revenue and guarantees; considers that the fiscal capacity could be financed, once in a steady state, through genuine own resources."⁷⁸ At the same time, the European Parliament efforts to set up a fiscal capacity also overlapped with initiatives to strengthen the legitimacy and accountability of the EU generally, and the Eurozone specifically. In this regard, the European Parliament affirmed in February 2017 that "the establishment of a European fiscal capacity and the European Monetary Fund may be steps in the process of creating a European Treasury, which should be accountable to the European Parliament."⁷⁹

3.4. The member states

The proposals in favor of a stabilization function at EU level have increasingly gained the support of the EU member states, either severally or acting through intergovernmental institutions. Traditionally, since 2013 the main proponents of a Eurozone fiscal capacity have been France,⁸⁰ and Italy,⁸¹ with member states such as Spain,⁸² and Belgium,⁸³ also expressing their support for this instrument, while Germany maintained a more skeptical view. Yet, following the election of President Emmanuel Macron in May 2017, and his grand plan to relaunch the EU,⁸⁴ including by creating a Eurozone Minister of Finance,⁸⁵ greater convergence between France and Germany has been achieved also on this point. In fact, in the Meseberg Declaration of 19 June 2018, France and Germany agreed to propose jointly the establishment of "a Eurozone budget within the framework of the European Union to promote competitiveness, convergence and stabilization in the euro area, starting in 2021,"⁸⁶ and in a document published on 16 November 2018 the Ministers of Finance of France and Germany outlined a possible structure for such an instrument.⁸⁷ On the basis of this proposal the Eurozone budget would be part of the overall EU budget and linked to the MFF, but focused on the Eurozone only and subject to specific governance under the leadership of the Euro Summit. Moreover, while the Eurozone budget would be based on existing legal bases under the EU treaties, its funding would derive from "external assigned revenues,"⁸⁸ including allocation of EU tax revenues as well "regular contributions by Eurozone Member States, collected and transferred to the EU budget on the basis of an intergovernmental agreement."⁸⁹

Needless to say, while the Franco-German proposal for a Eurozone budget marks a major step forward in building political consensus in favor of an EMU fiscal capacity, resistance towards new supranational mechanisms of fiscal stabilization and convergence remain strong in some quarters. In

⁷⁸ European Parliament, resolution of 14 March 2018 on the next MFF: Preparing the Parliament's position on the MFF post-2020, (2017/2052(INI)), para 12.

⁷⁹ See note 74, para 70.

⁸⁰ See French President Francois Hollande, Intervention liminaire de lors de la conférence de presse, Paris, 16 May 2013, 7 (speaking in favour of 'une nouvelle étape d'intégration avec une capacité budgétaire qui serait attribuée à la zone euro'; and French President François Hollande, 'Entretien à l'occasion du 14 juillet', Paris, 14 July 2015 (speaking for "un budget de la zone euro, pour pouvoir agir en termes d'investissements, y compris pour les pays qui sont le plus en retard").

⁸¹ See Italian Prime Minister Enrico Letta, Keynote Speech at Annual Dinner Brugel, 9 September 2013, 5 (arguing that "there is room to reflect on a fiscal capacity for the euro area.") and Italian Minister of Finance Pier Carlo Padoan, Speech at the Camera dei Deputati, Rome, 29 July 2015 (stating that "L'Unione monetaria deve essere affiancata da [...] una autentica unione economica e fiscale, dove al rispetto delle regole si accompagna una altrettanto necessaria condivisione del rischio, necessaria e sostenuta da una adeguata mutualizzazione delle risorse. Il Governo italiano si sta impegnando per portare avanti questa linea").

⁸² See Government of Spain, 'Better Economic Governance in the Euroarea: Spanish Contribution', May 2015, 7 (expressing support in favor of "the creation of a limited common fiscal capacity within the EMU").

⁸³ See Government of Belgium, Report on Preparing for Next Steps in Better Economic Governance in the Euroarea, 27 April 2015, 3 (stating that "a fiscal capacity and a treasury function for the euroarea could be envisaged").

⁸⁴ See French President Emmanuel Macron, speech, Université La Sorbonne, 26 September 2017.

⁸⁵ See also Emmanuel Macron, *Revolution* (XO 2016).

⁸⁶ Franco-German Declaration, Meseberg, 19 June 2018.

⁸⁷ Franco-German Proposal on the Architecture of a Eurozone Budget within the Framework of the European Union, 16 November 2018.

⁸⁸ Ibid.

⁸⁹ Ibid.

fact, a coalition of Northern EU countries led by the Netherlands which includes both Eurozone and non-Eurozone member states, informally known as the new Hanseatic League, has expressed its reservation against such initiatives. In a letter published on 6 March 2018, the Finance Minister of Denmark, Estonia, Finland, Ireland, Latvia, Lithuania, the Netherlands and Sweden, affirmed that deepening EMU should not result in “far-reaching transfer of competences to the European level”⁹⁰ and pleaded for reaching consensus on reforms which were needed, as opposed to reforms which were “nice to have.”⁹¹ Moreover, in a document released on 1 November 2018, the group – which was joined this time also by Slovakia and the Czech Republic – stressed its preference to ground the reform of EMU in a stronger role for the ESM, and did not make any reference to fiscal capacity as a priority.⁹²

Nevertheless, the proposal for a Eurozone budgetary capacity has recently entered into a package deal of reforms endorsed at the level of the Euro Summit. Following preparatory work undertaken by the President of the Eurogroup Mario Centeno,⁹³ the Minister of Finance of the Eurozone member states, debating in an inclusive format with their non-Eurozone counterparts, presented in December 2018 a report on deepening EMU to the heads of state and government, which included, besides agreement to complete Banking Union and to enhance the ESM, also a “possible budgetary instrument for the euro area.”⁹⁴ While the Eurogroup admitted that a common view did not yet exist among member states on the establishment of a tool designed to increase competitiveness, convergence and stabilization in the EMU,⁹⁵ the Euro Summit on 14 December 2018 decided to give its endorsement to the plan, and mandated the Eurogroup to undertake further “work on the design, modalities of implementation and timing of a budgetary instrument for convergence and competitiveness for the euro area.”⁹⁶ Although the Euro Summit exclusively referred to an instrument for convergence and competitiveness, without mentioning its stabilization function, it clarified that “the features of the budgetary instrument will be agreed in June 2019,”⁹⁷ thus indicating the prospect of an entry into force in conjunction with the new MFF.

In conclusion, since 2012 increasing attention has been dedicated at the highest institutional level to reflect on a fiscal capacity for the Eurozone: in fact, there seems to be growing awareness among the EU institutions and member states on the need for such an instrument – although divergences remain on the functions, forms and funding of this new dedicated euro area budget.

⁹⁰ Shared views from the Finance Minister of Denmark, Estonia, Finland, Ireland, Latvia, Lithuania, the Netherlands and Sweden, 6 March 2018.

⁹¹ *Ibid.*

⁹² Shared views of the from the Finance Minister of the Czech Republic, Denmark, Estonia, Finland, Ireland, Latvia, Lithuania, the Netherlands, Slovakia and Sweden, 1 November 2018.

⁹³ Eurogroup President Mario Centeno, Letter to Euro Summit President Donald Tusk, 25 June 2018.

⁹⁴ Eurogroup report to Leaders on EMU Deepening, 4 December 2018, PRESS 738/18.

⁹⁵ *Ibid.*

⁹⁶ Euro Summit statement, 14 December 2018, PRESS 790/18.

⁹⁷ *Ibid.*

4. COMPARATIVE OUTLOOK

The need to endow the Eurozone with a fiscal capacity is confirmed by comparative analysis. As the Four Presidents final report underlined, “while the degree of centralization of budgetary instruments and the arrangements for fiscal solidarity against adverse shocks differ, all other currency unions are endowed with a central fiscal capacity.”⁹⁸ In particular, federal unions with a single monetary policy offer an important model for the EMU. In fact, as argued by the IMF in a report making the case for the creation of a fiscal capacity in the Eurozone, “[w]hile the euro area is not a federal state itself and legal arrangements differ significantly from existing federations, the degree of economic and financial integration between member states is of the same order of magnitude as that of the different regions of many federal states. This suggests that, on economic grounds, federal states offer the closest benchmark for the euro area.”⁹⁹

This section, therefore examines in comparative perspective how other federal systems have endowed themselves with mechanisms to manage structural imbalances or asymmetric shocks.¹⁰⁰ However, in order to follow a methodologically sound logic of case selection,¹⁰¹ the analysis focuses here exclusively on two examples: the US and Switzerland. As explained by scholars of comparative law¹⁰² and comparative politics,¹⁰³ in fact, federal systems can be distinguished between ‘holding together federations’ – where federalism is introduced top down in a previously unitary state e.g. to manage devolutionary pressures, such as in Belgium, or Canada – from ‘coming together federations’ – where instead federal principles are introduced to integrate more closely previously separated states. Conventionally, the US and Switzerland are the two examples of federal unions aggregating states,¹⁰⁴ and thus their experience offers important lessons for EMU. In fact, both the case of the US and Switzerland show that coming together federations have created a fiscal capacity at the central level of government, albeit through long and incremental historical process driven by crises and legal and institutional responses.

4.1. United States of America

The US Constitution of 1787 marked a major step forward in forming a fiscal union in America compared to the Articles of Confederation, the basic law which had governed the US from the time it declared its independence from the UK.¹⁰⁵ While the Articles of Confederation had created a weak central government, deprived of an executive branch, and dependent on the fiscal transfer of the 13 separate colonies to fund its activities, the US Constitution vested the executive powers in the President of the US,¹⁰⁶ and endowed the federal Congress with the power to levy and collect taxes.¹⁰⁷ In fact, under the leadership of the first secretary of the Treasury, Alexander Hamilton, an ardent federalist,¹⁰⁸ the nascent US government took crucial steps in affirming its fiscal role, including by assuming the states’ debt incurred during the Revolutionary War, and chartering the first central bank of the US.¹⁰⁹ Nevertheless, it would be “a profound mistake to assume that America’s early ‘Hamiltonian moment’ of establishing a common federalized government debt instrument heralded the creation of a fully-

⁹⁸ Four Presidents, report Towards a Genuine Economic and Monetary Union, page 9, 5 december 2012.

⁹⁹ IMF Staff Discussion Note, Toward a Fiscal Union for the Euro Area, October 2013, note 5, page 15.

¹⁰⁰ George Anderson, *Fiscal Federalism: A Comparative Introduction* (OUP 2009).

¹⁰¹ Ran Hirschl, ‘The Question of Case Selection in Comparative Constitutional Law’ (2005) 53 *American Journal of Comparative Law* 125.

¹⁰² Koen Lenaerts, ‘Constitutionalism and the Many Faces of Federalism’ (1990) 38 *American Journal of Comparative Law* 205.

¹⁰³ Alfred Stepan, ‘Federalism and Democracy: Beyond the US Model’ (1999) 10 *Journal of Democracy* 19.

¹⁰⁴ Sergio Fabbrini, *Compound Democracies* (OUP 2010).

¹⁰⁵ Michael Klarman, *The Framers’ Coup: the Making of the United States Constitution* (OUP 2016).

¹⁰⁶ US Const Art II.

¹⁰⁷ US Const Art I, sec. 8, cl. 1.

¹⁰⁸ Ron Chernow, *Alexander Hamilton* (Penguin 2004).

¹⁰⁹ Jonathan A. Rodden, *Hamilton’s Paradox: The Promise and Peril of Fiscal Discipline* (CUP 2006).

fledged fiscal union. Instead, the present day fiscal union and the scale of the federal government in the United States emerged gradually, accelerating only after the US participation in World War I.”¹¹⁰

In fact, the original US constitutional settlement included a number of constraints on federal action, and for many decades the American political culture worked against a strong role for the central government. Hence, while Congress enjoyed taxing power, the Constitution indicated that direct taxes had to be apportioned among the several states, according to population¹¹¹ – a provision which effectively prohibited federal income taxation¹¹² – and with the victory of the Jeffersonian and Jacksonian Democrats in the first half of the 19th century, the early efforts at centralizing monetary policy were laid to rest, as evidenced by the decision not to re-authorize the Second central Bank of the US.¹¹³ As a result – with the exception of the Civil War between 1861 and 1865, which saw a temporary rise of the federal government’s fiscal role – it is only with the turn of the 20th century that the US experienced a more sustained involvement of the central government in economic and monetary affairs.¹¹⁴ In particular, during the so-called Progressive Era, the XVI Amendment (1913) to the US Constitution empowered the US to levy income taxes,¹¹⁵ the XVII Amendment (1916) introduced direct election for US senators,¹¹⁶ and the Federal Reserve Act created a real central bank for the US, tasked to manage the supply of currency for the all union.¹¹⁷

While these legal and institutional reforms altered the constitutional landscape of fiscal federalism in the US, it was exogenous factors – notably the Great Depression and then particularly the need to participate to two world wars – that fundamentally changed the power-relation between the states and the federation in the fiscal domain.¹¹⁸ While the New Deal led to the creation of a swath of new federal agencies and programs such as the Federal Emergency Relief Administration, the Social Security Act, and the Federal Deposit Insurance Corporation, all driven by a Keynesian understanding on the need for the central government to undertake counter-cyclical economic policy,¹¹⁹ the projection of the US as a leader on the world stage resulted in a steady expansion of the US federal budget. As a result, after a bi-centennial evolution, the federal government has acquired fiscal dominance in the US, running a budget which since the 1950s is well over 5% of gdp (and close to 20% if one includes also military expenditures).¹²⁰ Hence, while US states remain subject to balanced budget constitutional amendments, and there is a political norm that bans federal bail-outs of failing states,¹²¹ the US federal government has a federal budget, backed up by own resources, that can be effectively employed to smooth asymmetric shocks and the negative effects of the business cycle.¹²²

¹¹⁰ Jacob Funk Kirkegaard, ‘A More Perfect Fiscal Union’, in Jacob Funk Kirkegaard and Adam Posen (eds), *Lessons for EU Integration from US History* (European Commission 2018), page 18.

¹¹¹ US Const Art I, sec. 2, cl. 3.

¹¹² Erik Jensen, ‘Taxation and the Constitution: How to Read the Direct Tax Clause’ (1999) 15 *Journal of Law & Policy* 687.

¹¹³ See *McCulloch v. Maryland*, 17 U.S. (4 Wheat.) 316 (1819) (US Supreme Court holding that the federal Congress has the power to create a central bank under the necessary and proper clause of the Constitution) with President Andrew Jackson, Veto Message, July 1832 (vetoing the congressional bill establishing the Second Bank of the US).

¹¹⁴ Ajay Mehrotra, *Making the Modern American Fiscal State: Law, Politics and the Rise of Progressive Taxation 1877-1929* (CUP 2014).

¹¹⁵ The XVI Amendment overruled the US Supreme Court decision *Pollock v. Farmers’ Loan & Trust Co.*, 175 U.S. 429 (1895) (declaring a 1894 federal income tax law unconstitutional).

¹¹⁶ According to the original US constitutional design, US senators were appointed by state legislatures, hence the introduction of direct elections significantly contributed to enhancing their democratic and federal role.

¹¹⁷ See *Federal Reserve Act (1913)*, Public Law 63-43, 63d Congress (US).

¹¹⁸ Bruce Ackerman, *We The People. Volume II: Transformations* (Harvard UP 1998).

¹¹⁹ David A. Super, ‘Rethinking Fiscal Federalism’ (2005), 118 *Harvard Law Review* 2544, 2575.

¹²⁰ See Congressional Budget Office, ‘The U.S. Federal Budget’, available at: <http://www.cbo.gov/sites/default/files/budgetinfographic.pdf> (last visited 28 May 2015).

¹²¹ Peter Conti-Brown and David Skeel Jr. (eds.), *When States Go Broke: The Origins, Context and Solutions for the American States in Fiscal Crisis* (CUP 2012).

¹²² Randall Henning and Martin Kessler, ‘Fiscal Federalism: US History for Architects of Europe’s Fiscal Union’, Bruegel Essay and Lecture Series 2012, 5–6.

4.2. Switzerland

Like the US, also Switzerland emerged as a loose confederation of pre-existing states – known as cantons – aggregating for the purpose of external collective self-defense and of internal reciprocal trade.¹²³ During the 19th century a more stable framework of cooperation was established with the adoption of the 1848 and 1874 Constitutions.¹²⁴ Nevertheless, these federal documents created an institutionally weak central government, based on a consociational logic, with very limited fiscal resources.¹²⁵ In fact, the cantons maintained full sovereignty in levying and collecting taxes, and the federal budget mostly resulted from custom duties and cantonal contributions.¹²⁶ Moreover, multiple religious, linguistic and socio-economic cleavages, combined with the strong tradition of local participatory democracy reflected in the peculiar Swiss institution of the referendum,¹²⁷ restrained for long the ability of the federal government to expand its fiscal capacity.¹²⁸ As such, in another interesting historical analogy with the US, “[i]t is only from the end of World War I that this situation progressively improved. New federal taxes on tobacco, beer, income and capital, as well as the predecessor of the value added tax (VAT) regime were introduced.”¹²⁹ And only in the aftermath of World War II, with the expansion of the welfare state, a constitutional amendment provided the federal government with the power to equalize fiscal disparities among cantons.¹³⁰

The new Swiss Constitution of 1999, which entirely replaced the prior constitution, and entered into force in 2000, has confirmed many conventional features of Swiss federalism.¹³¹ The federation, which enjoys only the competences specifically delegated to it, controls monetary policy,¹³² and shall take measures to achieve balanced economic development, in particular preventing and combatting unemployment and inflation.¹³³ Moreover, the federation can levy direct taxes,¹³⁴ and a system of federal-cantonal equalization is in place with the aim to reduce cantonal disparities based on their fiscal capacity.¹³⁵ Nevertheless, federal direct taxes are limited in time, and require periodic renewal by the people and the cantons through referenda.¹³⁶ Furthermore, because Switzerland, a country of only 7 million people, plays a very limited international role,¹³⁷ the Swiss federal budget has remained small – particularly if compared with the US budget. Yet, the Swiss federal government has the fiscal capacity to intervene in the economic domain, including by supporting cantons facing an economic recession.

In conclusion, a comparative analysis of the US and Switzerland offers important lessons for the EU and the Eurozone: although in both these federal unions the central government initially enjoyed limited fiscal power – and notwithstanding the fact that in both systems the lower levels of governments (the cantons, in Switzerland; and the states, in the US) retain significant budgetary autonomy – over-time major constitutional changes, often driven by crises, created the pressure to develop instruments at the central level to smooth the effects of asymmetric shocks.¹³⁸

¹²³ Daniel Elazar, *Exploring Federalism* (Alabama UP 1987).

¹²⁴ Hans Conrad Peyer, *Verfassungsgeschichte der alten Schweiz*, (Schulthess Polygraphischer Verlag 1978).

¹²⁵ Arendt Lijphart, *Patterns of Democracy* (Yale UP 1999).

¹²⁶ Edmondo Mostacci, ‘Federalismo fiscale e autonomia finanziaria degli enti territoriali nella Repubblica elvetica’ in Giuseppe Franco Ferrari (ed), *Federalismo, sistema fiscale, autonomia* (Donzelli 2010) 107.

¹²⁷ Max Frenkel, ‘The Communal Basis of Swiss Liberty’ (1993) 23 *Publius* 61.

¹²⁸ Bernard Dafflon, ‘Le fédéralisme fiscal en Suisse: un relevé des enjeux constitutionnels, des responsabilités budgétaires et de la péréquation’, rapport pour la Commission sur les déséquilibre fiscal (2002).

¹²⁹ Hanspeter Kriesi and Alexander Trechsel, *The Politics of Switzerland* (CUP 2008) 35-36.

¹³⁰ Bernard Dafflon and Steve Perritaz, ‘Federal Cantonal Equalisation in Switzerland’, Forum of Federation paper, 2002, page 12.

¹³¹ Thomas Fleiner, ‘Recent Developments of Swiss Federalism’ (2002) 32 *Publius* 97.

¹³² Art. 99 Const Switz.

¹³³ Art. 100 Const Switz.

¹³⁴ Art. 128 Const Switz.

¹³⁵ Loi fédérale sur la péréquation financière et la compensation des charges du 3 Octobre 2003.

¹³⁶ See note 128, page 36.

¹³⁷ Georges-André Chevallaz, *The Challenge of Neutrality: Diplomacy and the Defense of Switzerland* (Lexington Books 2001).

¹³⁸ Daniel Kelemen, ‘Building the New European State? Federalism, Core State Powers, and European Integration’, in Philipp Genschel and Markus Jachtenfuchs (eds) *Beyond the Regulatory Polity? The European Integration of Core State Powers* (OUP 2013), 211.

5. FISCAL FEDERALISM WITHOUT A POLITICAL FEDERATION IN THE EU

If the comparative outlook confirms the importance of completing EMU with a fiscal capacity, it is necessary to consider how such a tool could be established within the EU constitutional system. This section therefore will consider the possible legal bases, funding mechanisms and governance and accountability rules of such a fiscal capacity as well as the window of opportunity to set it up at this critical time in the history of European integration.

5.1. Legal bases

Extensive discussion has taken place among scholars and policy-makers on whether the EU would have the competence under the current treaties to develop a fiscal capacity.¹³⁹ The Lisbon Treaty sought to introduce a distinction between types of EU competences in Articles 2 to 6 TFEU. In this context, a new provision with specific regard to EMU has been inserted, Article 5 TFEU, which states that: “the Member States shall coordinate their economic policies within the Union. To this end, the Council shall adopt measures, in particular broad guidelines for these policies.” In light of this, one could conclude that the only power of the EU in the field of economic policy is a coordinating one, and thus that there is no way for the EU institutions to undertake a real macro-economic policy. Nevertheless, the meaning of Article 5 TFEU must be appreciated within the broader constitutional fabric of the Treaty. On the one hand, Article 2(3) TFEU states that “The Member States shall coordinate their economic and employment policies within arrangements as determined by this Treaty, which the Union shall have competence to provide” – thus suggesting that the EU has a competence to provide arrangements in the field of economic policy, which goes beyond mere coordination.¹⁴⁰ On the other hand, Article 2(6) TFEU affirms that “the scope of and arrangements for exercising the Union’s competences shall be determined by the provisions of the Treaties relating to each area” – hence clarifying that the real powers of the EU are defined in the specific legal bases existing in the substantive chapters of the Treaties.¹⁴¹

If one considers the entirety of the legal bases existing in the TFEU it actually emerges that the EU has significant powers to take legislative action in the field of economic policy, broadly intended here to refer to macro-economic governance.¹⁴² First, the EU treaties grant to the EU institutions extensive power to intervene in the functioning of the internal market.¹⁴³ In fact, the importance of the internal market competence of the EU in the field of economic policy is explicitly enshrined in Article 119 TFEU stating that “the economic activities of the Member States and the Union shall include, as provided in the Treaties, the adoption of *an economic policy which is based on the coordination of the Member States’ economic policies, on the internal market, and on the definition of common objectives.*”¹⁴⁴ Second, the EU treaties grant to the EU institutions the power to legislate in specific fields which have relevant connection to macro-economic policy, including trans-European networks,¹⁴⁵ research and technological development,¹⁴⁶ and industry.¹⁴⁷ In fact, the Lisbon Treaty has arguably extended EU competences which also have an impact on macro-economic policy, including in the field

¹³⁹ Federico Fabbrini, ‘Economic Policy in the EU After the Crisis: Using the Treaties to Overcome the Asymmetry of EMU’ (2016) 20 *Diritto dell’Unione europea* 529.

¹⁴⁰ See also Jean-Victor Louis, ‘Economic Policy Under the Lisbon Treaty’, in Stefan Griller and Jacques Ziller (eds), *The Lisbon Treaty: EU Constitutionalism Without a Constitutional Treaty?* (Springer 2008), 285.

¹⁴¹ Monica Claes and Bruno De Witte, ‘Competences’, in Steven Blockmans and Adam Lazowski (eds), *Research Handbook of EU Institutional Law* (Elgar 2016).

¹⁴² Roland Bieber, ‘The Allocation of Economic Policy Competences in the European Union’, in Loïc Azoulay (ed), *The Question of Competence in the European Union* (OUP 2015), 86.

¹⁴³ Art. 114 TFEU.

¹⁴⁴ Emphasis added.

¹⁴⁵ Art. 170 TFEU.

¹⁴⁶ Art. 179 TFEU.

¹⁴⁷ Art. 173 TFEU.

of services of general interest,¹⁴⁸ space,¹⁴⁹ and energy.¹⁵⁰ Moreover, the Lisbon Treaty has also introduced a new provision, Article 136 TFEU, which allows the adoption of “measures specific to those Member States whose currency is the euro.”

Therefore, a comprehensive and systematic constitutional reading of the treaties suggests that the EU is empowered to act in the field of economic policy including by establishing a budgetary instrument to improve the functioning of EMU. The European Commission May 2018 proposal for the establishment of the European Investment Stabilization Function identified Article 175 TFEU as a sufficient legal basis to endow EMU with a counter-cyclical fiscal tool; and the Franco-German proposal for a Eurozone budget of November 2018 affirmed that the “legal bases for such an instrument could be Article 175 (3) TFEU (specific actions outside Structural Funds), possibly in conjunction with Article 182 TFEU (research and technological development) and Article 173 TFEU (competitiveness of the industry) depending on the concrete design in conjunction with Art 136 (provisions specific to euro area Member States).”¹⁵¹ This, after all, tracks the experience of the adoption of the European Fund for Strategic Investments established in 2015,¹⁵² which as far as its legal basis was concerned, was grounded on Articles 172, 173, 175(5) and 182(1) TFEU, concerning respectively the Treaty chapters dealing with trans-European networks, industry, economic, social and territorial cohesion, and research and technological development.

5.2. Funding

If the EU is endowed with the competences to develop a fiscal capacity, a separate but crucial question concerns how to fund such a budgetary instrument. In this regard, alternative views have emerged. The Commission proposal for a European Investment Stabilization Function would allow the Commission to borrow on the financial markets, up to a maximum of 30bn€, to provide loans, while a special new Stabilization Support Fund resourced by the member states would subsidize the loans' interest rates.¹⁵³ The Franco-German proposal for a Eurozone budget instead, conceives this tool as fund being primarily “financed by external assigned revenues, possibly including the allocation of tax revenues (such as an FTT according to the French model) and European resources (such as the proposed reform delivery tool).”¹⁵⁴ While this is more consistent with the federal logic, where the central government supports states via grants (rather than loans), the Franco-German blueprint, drawing on the experience of the Single Resolution Fund for failing banks¹⁵⁵ – which is funded through national contributions transferred on the basis of an intergovernmental agreement¹⁵⁶ – indicates that “the assigned revenues would consist of regular contributions by Eurozone Member States, collected and transferred to the EU budget on the basis of an intergovernmental agreement.”¹⁵⁷ This differs from the proposal of the Monti report, which had envisioned financing the Euro area budget through real own resources, including some specifically connected to the functioning of EMU.¹⁵⁸

Yet, the issue of funding is anything but technical. In fact, designing a proper financing of the fiscal capacity is essential to tackle the challenge that has long affected EU budget-making.¹⁵⁹ As is

¹⁴⁸ Art. 14 TFEU.

¹⁴⁹ Art. 189 TFEU.

¹⁵⁰ Art. 194 TFEU.

¹⁵¹ See note 87.

¹⁵² See Regulation EU 2015/1017 of the European Parliament and the Council of 25 June 2015 on the European Fund for Strategic Investments, the European Investment Advisory Hub, and the European Investment Project Portal and amending Regulations (EU) No 1291/2013 and (EU) No 1316/2013, OJ 2015 L 169/1.

¹⁵³ See note 62.

¹⁵⁴ See note 87.

¹⁵⁵ See Agreement on the transfer and mutualisation of contributions to the Single Resolution Fund [hereinafter SRF Agreement], 14 May 2014 available at: <http://register.consilium.europa.eu/doc/srv?l=EN&f=ST%208457%202014%20INIT>

¹⁵⁶ For a critical view see Federico Fabbrini, ‘On Banks, Courts and International Law: the International Agreement on the Single Resolution Fund in Context’ (2014) 21 *Maastricht Journal of European & Comparative Law* 444.

¹⁵⁷ See note 87, page 1.

¹⁵⁸ See note 47, page 67.

¹⁵⁹ Federico Fabbrini, ‘Taxing and Spending in the Eurozone’ (2014) 39 *European Law Review* 155.

well-known, because today the EU budget is for the most part financed by national contributions, the decision-making process about EU revenues and expenditures has been captured by endless negotiation among the member states about the precise costs and benefits that each member state would incur. Although formally speaking, once the system has been ratified, own resources are automatically due to the EU without the need for further decision at member state level, and states' delays in making available own resources are unlawful,¹⁶⁰ EU member states have mostly regarded the contributions they make to the EU budget as *their* money,¹⁶¹ and have aggressively measured the difference between their contributions to, and their receipts from, the EU budget. Because no member state is willing to transfer *its* money to the EU budget for the benefit of *other* member states, the discussion about the MFF has become increasingly costly and decreasingly effective – every member state having a veto power on how much resources the EU should raise and how it should spend. All this has been further aggravated by the euro-crisis, which has pitted debtor creditor countries against debtor countries,¹⁶² and entrenched dynamics of domination between larger, economically wealthier states and the others.

Therefore, in designing a fiscal capacity for EMU policy-makers should break the wrong equation between fiscal capacity and inter-state transfers. As Miguel Maduro has argued, in terms of effectiveness, such a system leaves the governance of the euro “dependent on a permanent ‘negotiation’ with national democracies [boosting] the uncertainty as to the extent of financial and political support underlying the common currency.”¹⁶³ At the same time, in terms of legitimacy, this system fosters mistrusts between states: “States paying will think they are carrying other states on their shoulders and rewarding moral hazard. [States] being “disciplined” will take as being governed by those loaning the money.”¹⁶⁴ This state of affairs can only be addressed if resources for a fiscal capacity are not drawn from state contributions but rather from own resources that the EMU levies *as a Union*. In fact, “[i]t is essential that the Union is seen as redistributing the Union wealth and not the wealth of some states”¹⁶⁵ and therefore that the revenues of the EU budgetary instrument are disentangled from national contributions. From this point of view, the European Parliament has perfectly grasped with the source of the problem when it recommended to the Commission to “return to the spirit and letter of the [Treaties]”¹⁶⁶ and develop a budgetary capacity *funded by own resources*.¹⁶⁷

This indicates the importance of making progress in introducing new own resources for the EU and the Eurozone – a call further supported by the Monti recommendations.¹⁶⁸ Pursuant to Article 311 TFEU the Council, acting unanimously and after consulting the European Parliament shall “adopt a decision laying down the provisions relating to the system of own resources of the Union. In this context it may establish new categories of own resources or abolish an existing category” – and the Commission has interpreted this provision in a constructive manner. In fact, in its proposal for a Council directive on a Financial Transaction Tax (FTT),¹⁶⁹ the Commission indicated that its draft legislative text would be based on Article 133 TFEU, thus the harmonization clause in the TFEU, but that the revenues of the tax would be appropriated by the EU under Article 311 TFEU, with the aim to feed the EU budget and free the member states from parts of their current contributions.¹⁷⁰ Nevertheless, the difficulties in reaching consensus on the FTT – which ultimately prompted 11 EU member states to proceed with the

¹⁶⁰ See Case 93/85 *Commission v. United Kingdom* [1986] ECR 4011.

¹⁶¹ See also Jorgen Mortensen et al, ‘How do Member States handle contributions to the EU budget in National Budget’, study commissioned by the European Parliament Policy Department for Budgetary Affairs, July 2014.

¹⁶² Kenneth Dyson, *States, Debt & Power: ‘Saints’ and ‘Sinners’ in European History & Integration* (OUP 2014).

¹⁶³ Miguel Maduro, ‘A New Governance for the European Union and the Euro: Democracy and Justice’, study commissioned by the European Parliament Policy Department for Citizens’ Rights and Constitutional Affairs, September 2012, 18.

¹⁶⁴ *Ibid.*

¹⁶⁵ *Ibid.* 21.

¹⁶⁶ See note 67, Recommendation 2.4.

¹⁶⁷ See also European Parliament resolution of 14 March 2018 on reform of the EU’ system of own resources, ([2017/2053\(INI\)](#)).

¹⁶⁸ See note 47.

¹⁶⁹ Commission Proposal for a Council Directive On a Common System of FTT, 28 November 2011, COM(2011)594 final.

¹⁷⁰ *Ibid.*

discussion through enhanced cooperation in January 2013¹⁷¹ – reveal the challenges that still surround tax policy in the EU given the need to obtain the unanimous consent of the member states.¹⁷² In this context, the recent Commission proposal to move beyond unanimity in the field of taxation is to be very welcome as a step to introduce a more democratic and efficient system for decisions on the EU revenues.¹⁷³

5.3. Executive governance and parliamentary accountability

If a sustainable fiscal capacity demands own resources to be levied through EU taxes, another challenge that has to be addressed concerns the governance of such a new budgetary instrument, and its accountability. On the governance side, while the Commission proposal of the EISF would vest the management of this new stabilization tool in the Commission itself, the Franco-German proposal for a Eurozone budget affirms that this new instrument “would operate with the strategic guidance of the Euro summit, which would be operationalized by the Eurogroup on a yearly basis”¹⁷⁴ – a point further endorsed by the Euro Summit, which indicated that this new budget would work under the “strategic guidance from the euro area Member States.”¹⁷⁵ Nevertheless, the Commission communication on a European Minister of Economy and Finance,¹⁷⁶ which interplays with the call by French President Emmanuel Macron in favor of establishing a Eurozone government in charge of the specific euro area budget,¹⁷⁷ suggests that institutional developments may mature toward the creation of a real Eurozone Treasury, as in the US and Swiss systems of fiscal federalism.

Be that as it may, the strengthening of executive authority must go hand in hand with the reform of legislative accountability. In fact, parliamentary representation – as the way to endow governmental decisions with democratic legitimacy – is the foundation of governmental authority, also in the fiscal domain. After all, it is an everlasting principle of constitutionalism, from the Magna Charta of 1215, through the revolutionary experiences of 17th and 18th century England, America and France, up to contemporary models of constitutional government, that the power of taxation must be legitimized and controlled by adequate democratic representation.¹⁷⁸ Pursuant to this constitutionalist tradition, no governmental authority in fiscal affairs can be justified unless it is at the origin authorized by the people through their representatives. Now, in the current institutional system of the EU, the principle of representation is only partially accomplished:¹⁷⁹ the European Parliament has only a consultative role in the field of taxation, because decisions on tax harmonization under Article 113 TFEU or on the creation of new tax-based EU own resources under Article 311 TFEU are taken exclusively (and unanimously) by the Council. Therefore, ensuring the involvement of the European Parliament in decisions about EU taxation appears from a normative point of view a necessary development towards a more democratic EMU.

The European Parliament has been rightly explicit in calling for such a change, stating that “a substantial improvement of the democratic legitimacy and accountability at Union level of the EMU governance by an increased role of Parliament [i]s an absolute necessity,”¹⁸⁰ and repeating that

¹⁷¹ Council Decision of 22 January 2013 authorising enhanced cooperation in the area of financial transaction tax 2013/52/EU, [2013] OJ L 22/11.

¹⁷² Sylvain Plasschaert, ‘Towards an Own Resource for the European Union? Why? How? And When?’ (2004) *European Taxation* 470.

¹⁷³ European Commission, communication Towards a More Efficient and Democratic Decision Making in EU Tax Policy, COM(2019)8 final, 15 January 2019.

¹⁷⁴ See note 87 page 1.

¹⁷⁵ See note 96.

¹⁷⁶ See note 63.

¹⁷⁷ See French President Emmanuel Macron, Interview, *Les Temps* (June 21, 2017) (saying that “il faut avoir une intégration plus forte au sein de la zone euro. D’où l’idée, que je défends avec vigueur, d’un budget de la zone euro, doté d’une gouvernance démocratique”).

¹⁷⁸ See eg Bruce Ackerman, ‘Taxation and the Constitution’ (1999) 99 *Columbia Law Review* 1.

¹⁷⁹ Giacinto Della Cananea, ‘No Representation without Taxation: the European Union’, in Lina Papadopoulou, Ingolf Pernice and Joseph Weiler (eds), *Legitimacy Issues of the European Union in the Face of the Crisis* (Nomos, 2017), 95.

¹⁸⁰ See note 67, para 9.

“parliamentary input on economic [issues] is an important aspect of any democratic system.”¹⁸¹ Yet, tellingly, even top EU decision-makers seem to have taken notice of this need, as questions of legitimacy and accountability feature in both the Four Presidents report,¹⁸² and the Five Presidents report.¹⁸³ Ensuring the full involvement of the European Parliament in decisions on the revenue-side of a Eurozone budget raises important issues on the internal organization of this institution.¹⁸⁴ In fact, because the European Parliament includes MEPs elected in member states which are outside the Eurozone, entrusting the assembly with the responsibility to oversee the use of a Eurozone-specific tool raises a well-known problem of possible over-representation.¹⁸⁵ Nevertheless, it is uncertain to what extent this will remain an issue following Brexit, since at that stage only one EU member state will have an opt-out from the euro, with the other 7 non-Eurozone states being pre-ins.¹⁸⁶ In any case, there could be ways for the European Parliament to deal with this situation, for instance, by establishing a Eurozone committee.

Yet, leaving the abovementioned organizational issue for future in depth analysis, there is no doubt that to address the current state of affairs, which sees the European Parliament’s powers in the field of taxation limited compared to those of the Council, legal changes are necessary too. The current treaty framework already allows for a short-term solution: In particular, pursuant to Article 333 TFEU it is possible to resort to a “*passerelle* clause” shifting to the co-decision procedure the competences which would otherwise be reserved to the exclusive purview of the Council.¹⁸⁷ This is precisely what the European Parliament asked in its resolution authorizing the use of enhanced cooperation for the introduction of the FTT, to enhance its role in decision-making related to taxation.¹⁸⁸ Nevertheless, it seems clear that more structural, long-term solutions should be pursued through treaty changes – as had been suggested at the time of the European Constitutional Convention¹⁸⁹ – to strengthen the role of the European Parliament in this field.¹⁹⁰

5.4. Brexit as a window of opportunity

The creation of a fiscal capacity may appear an ambitious task at a time when euro-skepticism is on the rise. A Eurozone budget done right would imply an empowerment of the EU institutions, which may seem at odds with the increasing hostility toward the EU emerged in a number of recent national elections.¹⁹¹ Nevertheless, in my view the dissatisfaction of European citizens and states should not be interpreted as an opposition to European integration as such. Rather, discontent vis-à-vis the EU should be seen as the product of an unsatisfactory settlement in the EU constitutional architecture.¹⁹² In fact, the asymmetry of EMU is itself at the root of the euro-crisis, which has been a major challenge to the

¹⁸¹ See note 73, para 50.

¹⁸² See note 30.

¹⁸³ Ibid.

¹⁸⁴ Federcio Fabbrini, ‘Representation in the European Parliament: of False Problems and Real Challenges’ (2015) 75 *Zeitschrift für Ausländisches öffentliches Recht und Völkerrecht* 823.

¹⁸⁵ Deirdre Curtin and Cristina Fasone, ‘Differentiated Representation: Is a Flexible European Parliament Desirable?’ in Bruno De Witte et al (eds), *Between Flexibility and Disintegration: The State of EU Law Today* (Elgar 2015).

¹⁸⁶ Pawel Tokarski and Serafina Funk, ‘Non-euro countries in the EU after Brexit’, SWP Comment 2019/C 03.

¹⁸⁷ On the potential of the ‘*passerelle* clauses’ to induce reforms within the framework of the existing Treaties, see Giuliano Amato, ‘Future Prospects for a European Constitution’, in Giuliano Amato et al (eds), *Genesis and Destiny of the European Constitution* (Bruylant 2007), 1271, 1272.

¹⁸⁸ European Parliament, Legislative Resolution of 12 December 2012 on the proposal for a Council decision authorizing enhanced cooperation in the area of the creation of a FTT, P7_TA(2012)0498, para 2.

¹⁸⁹ European Convention, Working Group VI on Economic Governance, Final Report, 21 October 2002, CONV 357/02, WG VI 17.

¹⁹⁰ See also Cinzia Alcidi et al, ‘Enhancing the Legitimacy of EMU Governance’ study commissioned by the European Parliament Policy Department on Scientific and Economic Policy, December 2014.

¹⁹¹ Catherine De Vries, *Euroskepticism and the Future of European Integration* (OUP 2018).

¹⁹² See also Jürgen Habermas, ‘Democracy in Europe: Why the Development of the EU into a Transnational Democracy is Necessary and How is it Possible’ (2015) 21 *European Law Journal* 546.

legitimacy and effectiveness of the EU.¹⁹³ Hence, reforming the European architecture of economic governance in a way that addresses this problem is not a passing fancy: it is a necessity to restore the foundations of EMU and ensure its long term success. Moreover, political momentum seems to be growing for action in this direction, as reflected in the statement of the Euro Summit of December 2018, where the leaders in an inclusive format mandated “the Eurogroup to work on the design, modalities of implementation and timing of a budgetary instrument” in the context of the next MFF with a view to agree its features by June 2019.¹⁹⁴

At the same time, while this deadline may be ambitious given the forthcoming European Parliament elections in May 2019, there is an important collateral development that opens a relevant window of opportunity toward the establishment of a fiscal capacity: the UK withdrawal from the EU. In fact, while many uncertainties still surround the ratification of the withdrawal agreement and framework for future EU-UK relation – with the risk of a ‘hard Brexit’ still on the table¹⁹⁵ – there is no doubt that Brexit has important constitutional implications on the EU itself. Following Brexit, the EU constitutional system has to be re-adapted to the reality of a Union at 27 and this requires changes, on the one hand, to the EU institutions, and, on the other, to the EU financial provisions. In fact, several institutional changes have already been brought to bearing in the EU – including most notably by re-allocating seats in the European Parliament.¹⁹⁶ With regard to the financial provisions, instead, Brexit has important consequences on the ongoing negotiations for the future MFF 2021-2027, changing the stakes in the negotiations in favor of those institutional actors seeking reforms of the EU financing system.¹⁹⁷

Although the UK enjoys a famous rebate (obtained in 1984, and preserved ever since) which allows it to pay less than it should, it still remains one of the major contributors to the EU budget – the 4th total net payer into the EU coffers (after Germany, France and Italy).¹⁹⁸ Hence, when the UK leaves the EU the question will arise of how to handle the loss of UK contributions to the EU budget. In principle, the EU could reduce expenditures in proportion to the UK quota – but it seems unlikely that states which are net beneficiaries of EU spending would endorse such an outcome. Alternatively, the states which are net contributors to the EU budget could increase their contributions to wind-up the shortfall – but again it seems unlikely that countries which are already paying into the EU budget more than what they get in return would endorse this option. In this context, therefore, Brexit may create a window of opportunity for a more significant constitutional rethinking of the EU financing system, including through the creation of a euro area budget funded by new, genuinely supranational, own resources. Although until now member state governments have been lukewarm at initiatives to endow the EU with adequate taxing and spending powers – independent from member states’ financial transfers – in the aftermath of Brexit these ideas may acquire a new attractiveness as a way to tackle the budget shortfall created by the UK withdrawal, and in a context of broader constitutional reorganization of the EU.¹⁹⁹

¹⁹³ Joseph H.H. Weiler, ‘Europa: “Nous Coalisons des Etats, Nous N’Unissons pas des Hommes”’, in Marta Cartabia and Andrea Simoncini (eds), *La sostenibilità della democrazia nel XXI secolo* (Il Mulino 2009), 51, 62

¹⁹⁴ See note 96.

¹⁹⁵ Federico Fabbrini, ‘The Institutional Consequences of a “Hard Brexit”’, in-depth analysis commissioned by the European Parliament Policy Department for Citizens’ Rights and Constitutional Affairs, May 2018.

¹⁹⁶ See European Council Decision (EU) 2018/937 of 28 June 2018 establishing the composition of the European Parliament, *OJ L 165I*, 2.7.2018, page 1–3.

¹⁹⁷ Federico Fabbrini, ‘Brexit and EU Treaty Reform: A Window of Opportunity for Constitutional Change?’, in Federico Fabbrini (ed), *The Law & Politics of Brexit* (OUP 2017) 267.

¹⁹⁸ See European Commission, EU Expenditure and Revenue 2014-2020, interactive chart available at http://ec.europa.eu/budget/figures/interactive/index_en.cfm

¹⁹⁹ See note 198.

6. CONCLUSION

As this in-depth analysis pointed out the Eurozone remains incomplete, as the responses to the euro-crisis have not fixed the original asymmetry of EMU. Yet, while economists have emphasized the need for a centralized budget to counter asymmetrical shocks, a comparative analysis of other federal unions by aggregation such as the US and Switzerland shows that proper mechanisms have been created over time there to manage the negative effect of a recession through a centralized budget. In fact, growing awareness seems to exist at the highest institutional level in the EU on the need to endow the Eurozone with a fiscal capacity and a number of proposals from the European Parliament, the European Commission and the French and German Governments are currently on the table to achieve this goal in the near future – as requested recently also by the Euro Summit.

This in-depth analysis has examined the establishment of a fiscal capacity for the Eurozone from a constitutional perspective. As this contribution claimed, the EU treaties already provide sufficient legal bases to set up such a budgetary instrument, and – paradoxically – Brexit may represent a window of opportunity to reach this objective, as the withdrawal of the UK creates a shortfall in the EU budget that will need to be compensated through new resources. Nevertheless, as this paper explained, it is crucial that the design of a possible fiscal capacity for the Eurozone anticipates potential challenges, including the sources of funding and the governance and accountability of this new tool. In this regard, in particular, it was explained that the revenues for the new euro area budget must be new, genuine own resources – rather than state financial transfers – and that the functioning of this instrument be legitimated by appropriate parliamentary representation.

Specifically, the in-depth analysis maintained that a fiscal capacity can be established *à traité constant*, on the basis of a multiplicity of treaty provisions – including Articles 172, 173, 175(5) and 182(1) TFEU, if need be combined with Article 136 TFEU. However, contrary to several proposals by the Commission and national governments, the in-depth analysis emphasized that the revenues to support a fiscal capacity should not consist of state transfers: rather, drawing from the comparison with the US and Swiss federal system, the in-depth analysis argued that a federal spending power should be backed by a federal taxing power, with real supranational revenues collected by the EU – as repeatedly affirmed also by the European Parliament. Finally, the in-depth analysis emphasized that while the management of a fiscal capacity requires an executive governance – ideally in the form of a federal treasury, as in the US and Switzerland – it also necessitates adequate mechanisms of parliamentary accountability: in particular, the European Parliament should be given full authority to authorize taxing and oversee spending in order to guarantee that the principle of ‘no taxation without representation’ is respected in the EU institutional system too.

In conclusion, endowing the Eurozone with a fiscal capacity entails continuing the process of federalization of the EU. Yet, as ECB President Mario Draghi said in front of the European Parliament on the occasion of the celebrations for the 20th anniversary of the euro, “Today, our duty is to complete what we started two decades ago” when the euro was introduced as a tangible instrument of political union in Europe.²⁰⁰

²⁰⁰ ECB President Mario Draghi, Speech at the session of the plenary of the European Parliament to mark the 20th anniversary of the euro, Strasbourg, 15 January 2019.

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This in-depth analysis, commissioned by the European Parliament's Policy Department for Citizens' Rights and Constitutional Affairs at the request of the AFCO Committee, considers from a constitutional perspective the introduction of a fiscal capacity for the Eurozone. After explaining the constitutional asymmetry of Economic & Monetary Union, and surveying several recent proposals to establish a fiscal capacity, the in-depth analysis explains in comparative perspective how other federal unions by aggregation such as the United States and Switzerland are endowed with centralized fiscal stabilization tools and discusses how such a fiscal capacity could be established in the Eurozone, considering issues of legal bases, governance and accountability, as well as possible windows of opportunities to introduce it post-Brexit.

PE 608.862

Print ISBN 978-92-846-4621-0 | doi: 10.2861/705606 | QA-03-19-118-EN-C
PDF ISBN 978-92-846-4622-7 | doi: 10.2861/844702 | QA-03-19-118-EN-N