A Euro area budget: another seedling?

by Marijn van der Sluis
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Abstract:
The negotiations for a new budgetary instrument for the euro area are progressing. Whilst the original plans called for a more ambitious euro area budget than what is on the table at the time of writing (October 2019), the scaled down plans nevertheless raise several legal issues. This working paper first briefly discusses the several proposals leading to the current plan for the Budgetary Instrument for Convergence & Competitiveness (BICC), before commenting on several legal aspects of the plans. These include the legal basis, the connection between the purpose of the budget and differentiated integration, the requirements of the EU budget and lastly the no-bailout clause. This working paper suggests that the main added-value of the BICC is found in its potential for growth, rather than in its immediate contribution to the functioning of the euro.

Keywords:
Euro, Eurozone budget, BICC, convergence, structural reform, differentiated integration, cohesion, Eurogroup, asymmetric shocks, stabilization function.

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1. Introduction

This working paper examines the recent proposals for a euro area budget as part of the ongoing efforts to reform the euro.\(^1\) In June 2019, the Eurogroup reached consensus on a ‘term sheet’ regarding a new budgetary instrument, the *Budgetary Instrument for Competitiveness and Convergence* (BICC), whose immediate history can be traced back to the 2015 report by the five Presidents of the EU (European Commission, European Council, Eurogroup, European Central Bank (ECB), European Parliament (EP)).\(^2\) That report set the agenda for the reforms for the post-crisis era and included several small reform proposals, such as the creation of a system of national competitiveness authorities and a European Fiscal Board, as well as several larger proposals, such as a ‘macroeconomic stabilization function for the euro area’. This would be due in the ‘stage 2’ outlined in the report, i.e. between June 2017 and 2025.

The stabilization function for the euro area would (partly) fulfill a long-standing desire to ‘complete’ the euro. The original ‘imbalance’ of the Economic and Monetary Union (EMU), with a strongly developed monetary union and a weakly developed economic union, is seen by many as a lead cause of the euro crisis. By elevating monetary policy to the European level and keeping fiscal and economic policy largely decentralized, the Member States (MS) lost their tools to combat so-called asymmetric shocks, i.e. an economic downturn that affects only a group of MS. Even though the euro-crisis led to an overhaul of EMU, most of the measures taken during the euro-crisis have been targeted at crisis fighting, rather than crisis prevention. A European stabilization function would offer targeted support to MS to help them overcome an economic downturn and prevent small economic problems from turning into European catastrophes.

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Whether the euro area budget will indeed fulfil the role of stabilizer is, however, not a foregone conclusion. The Four Presidents’ Report from 2012 suggested another objective for a euro area budget, namely to promote structural reforms in the Member States. Financial support by the EU could facilitate the transition to new economic policies on the national level. Offering incentives for structural reforms would be complementary to another aspect of euro-crisis law, namely the extension of economic governance through the Six Pack and Two Pack. The purpose of the new budgetary tool subsequently became the focal point of the discussions. Whereas the support of structural reforms would imply the need for a budget of a very modest size, a stabilizing function would require a considerably larger budget. Folded into the discussion over the purpose are therefore the debates over how the budget is implemented and the size of the budget. Moreover, the function of the budget is also of relevance for the participation of non-euro area MS, or rather, for the ability of the euro area MS to exclude the non-euro area MS. Whilst there is clear wish for a specific budgetary instrument for the euro area, there are currently few legal arguments to exclude the non-euro area MS.

During the euro-crisis, one point of controversy was the prominent role of the MS in shaping the future of the euro, and an academic debate ensued over the new institutional balance in the EU. The negotiations for the new budgetary instrument can shed new light on these discussions in two ways; first, in showing where the center of gravity lies in negotiations over the future of the euro outside the crisis, and second, by creating new possibilities for EU institutions to grow their role in the management of the euro.

The ideas for the new budgetary function came together through a variety of sources. The Four and Five Presidents Reports set the agenda, followed by a set of initiatives from the Commission, including several proposals for legislation. The EP submitted its own ideas in 2017. The political debate was launched by the Meseberg Declaration by French President Macron and German Chancellor Merkel from June 2018. Opposition to an ambitious new budgetary function was organized through a loose alliance of several fiscally conservative (northern) MS, informally dubbed the New Hanseatic League. The resulting compromise for the BICC shows the balance of forces in the post-crisis euro era.

As should be clear from this introduction, the debates over a euro area budget touch upon many different aspects of E(M)U constitutional law. This working paper first outlines several proposals that have appeared in recent years: the EP’s resolution, the Commission proposals, the Franco-German Meseberg Declaration and the recent Eurogroup agreement. The comments will then focus on four constitutional aspects of the proposals: the legal basis, differentiation and purpose, the relation with the EU budget and the relation with the non-

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3 Herman Van Rompuy, ‘Towards a Genuine Economic and Monetary Union’, (December 2012).
bailout clause. As will become clear in the following sections, the current proposals envision a new budgetary function with limited ambition (and thus of limited size). However, the history of EMU shows that where initiatives for reform are initially restricted due to political disagreement, there is a tendency for them to grow during a crisis. One question central to this working paper is whether the characteristics of the new BICC are such that they could enable the mechanism to quickly expand under different political circumstances, i.e. whether the BICC is a seedling that could grow into a full-blown Euro area budget.

2. Plans for a Euro (Area) budget

2.1. The Four and Five Presidents’ reports

The Four Presidents’ report from 2012 envisioned a fiscal capacity for EMU that would first offer financial incentives for Member States to adopt structural reforms on the basis of contractual arrangements. In a later stage, this would develop in a fiscal capacity that could facilitate adjustment to economic shocks through an insurance-mechanism.6

The Five Presidents’ report from 2015 focused on the latter function, calling it a stabilization function for the euro area that would operate automatically. It expressly left the design of this function to an expert group, but defined its task in a negative sense. The stabilization function should not lead to permanent transfers, should not undermine the incentives for sound fiscal policy making and should not be an instrument for crisis management.

2.2. The European Parliament Resolution

In February 2017, the European Parliament adopted a resolution on budgetary capacity for the euro area.7 Beyond the tasks of incentivizing structural reforms and addressing asymmetric shocks, the EP also envisioned the new capacity to address symmetric shocks that affect the euro area as a whole.

Instead of contractual arrangements for the encouragement of structural reforms, the resolution laid out a new ‘convergence code’, which would function beside the Stability and Growth Pact, and which would offer an ‘investment strategy’. It would focus on new convergence criteria, such as taxation, the labour market, social cohesion and good governance. Compliance with the convergence code would be a requirement for participation in the fiscal capacity.

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6 Herman Van Rompuy, ‘Towards a Genuine Economic and Monetary Union, (December 2012), 9-12.
Funding for the budgetary capacity would first come from the Member States as external assigned revenue and later through an amendment of the system of own resources.

2.3. The Commission proposals (2018)

The Five Presidents’ report had tasked the Commission with assessing progress and outlining further steps, which it did first with a Reflection Paper on the Deepening of EMU in 2017. This was followed by a set of legislative proposals in December 2017, on amongst others the integration of the European Stability Mechanism in the EU legal order and on a European Finance Minister. A communication on new budgetary instruments for the euro area was also included in this package. In May 2018, the Commission submitted two more legislative proposals on a reform support program and a European Investment Stabilization Function (EISF, not to be confused with the European Fund for Strategic Investment, EFSI, also known as the Juncker Fund, or the European Structural and Investment Funds, ESIF). The two legislative proposals from May 2018 are discussed below.

2.3.1. Reform Support Program

The proposal for a Reform Support Program consists of three parts, of which one aspect clearly builds on earlier steps by the Commission in this area, namely the Structural Reform Support Service that was introduced in 2015. This service offers technical expertise to MS that want to implement structural reforms. The second element of the proposal is a new reform delivery tool, which would offer MS financial incentives to reach the targets of structural reforms, as outlined in a ‘reform commitment’ entered into by a MS with the Commission. Another new aspect of the proposal was to include a convergence facility, that would prepare non-euro area MS to join the Eurozone.

The legal basis of the proposal is article 175(3) Treaty on the Functioning of the EU (TFEU) on economic, social and territorial cohesion and article 197(2) TFEU on administrative capacity building. The Reform Support Program would be part of the EU budget. It would be included in the Multianual Financial Framework 2021-2027 and would be allocated 25bn euro, of which 22bn euro for the reform delivery tool.

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In parallel to this, the Commission has sought to test the reform delivery tool, submitting a proposal to amend the current Common Provisions Regulation. The European Parliament rejected the proposal.

2.3.2. European Investment Stabilization Function
The second leg of the Commission’s proposal for a euro area budget within the EU budget was the European Investment Stabilization Function. The Reflection Paper from 2017 had considered three options for a stabilization function, namely investment protection, unemployment reinsurance and a “rainy day” fund. The December 2017 Communication on New Budgetary Instruments prioritized the investment protection as it “would allow for a swifter roll-out in comparison to the two other options”. In May 2018, the Commission produced a draft regulation for this stabilization function, based on article 175(3) TFEU on economic, social and territorial cohesion.

Support under the EISF would come in two forms: first, a MS experiencing a large asymmetric shock would receive a loan in order to invest in support of objectives as defined under the Common Provisions Regulation and to maintain public investment. Whether a country is experiencing an asymmetric shock would be determined by the level of unemployment in a MS, compared to the previous year and to the average of the previous five years. Upon repayment of the loan or when the interest over the loan is due, the MS could receive a second form of support, namely an interest rate subsidy, covering 100% of the interest rate costs.

The size of the loan a MS could receive would be determined by a formula that weighs the eligible public investment and size of the asymmetric shock. The maximum of loans to the MS would be set at 30bn euro. Neither the loans, nor the interest rate subsidy, would directly impact the EU budget, as the Commission would be authorized to borrow the required amounts for the loans and a Stabilization Support Fund would provide the interest rate subsidy. That fund would be established on the basis of an intergovernmental agreement.

2.4. The Meseberg Declaration & the New Hanseatic League

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15 European Commission, supra note 8, 15.
Adopted in June 2018, after the start of a new term for Chancellor Merkel and the election of President Macron, the Franco-German Meseberg Declaration set forth a vision for deeper integration, with considerable attention for issues of EMU. The creation of a euro area budget, it stated, would promote competitiveness, convergence and stabilization. However, the explicit purpose of the budget would be competitiveness and convergence. An unemployment stabilization fund would be examined later.

A follow-up statement in December 2018 developed further the Franco-German vision of a euro area budget. Here, the aim of the budget is convergence and reform, achieved through the co-financing of investment. The new budget could thereby also fulfill a stabilizing function, it is mentioned, because economic downturns put pressure on public investments.

The ‘fiscal rules’ of the Eurozone would set negative eligibility criteria, but the budget would not explicitly be oriented towards the fulfillment of the goals of economic policy as formulated through the European Semester, nor of the European Structural and Investments Funds. Instead, the Euro Summit would provide ‘strategic guidance’ for the budget, which the Eurogroup would operationalize. MS would submit proposals to implement the budget, reflecting the funding priorities, which the Commission would approve.

Opposition to an ambitious Euro area budget came from the newly created Hanseatic League, a loose alliance of several Northern MS. One of its first joint statements concerned the architecture of EMU. Regarding the new Multiannual Financial Framework (MFF), it noted that the EU budget could be better aligned to implement structural reforms. Targeted investments by the EU, under the cap of the MFF, could be complementary. After the agreement in the Eurogroup in December 2018 (see below), a statement of ‘joint language’ further discussed the views of the members on a budgetary instrument. Notable elements of the letter are that the budget is envisioned to fall under the expenditure and own resources ceilings of the EU and that access to funds is conditional upon respect for the rule of law. The


envisioned size of the new instrument would moreover be significantly below what the Commission had envisioned for its reform delivery tool (i.e. below 22bn euro).

2.5. The Eurogroup agreements on the BICC

The Eurogroup reached a tentative agreement on a Eurozone budget in December 2018.\(^{20}\) The two main conclusions of the Eurogroup, supported by the Euro Summit, were that no conclusion could be reached on the stabilization function of the new budget and that the proposal by France and Germany would be the starting point of the further discussions.

In June 2019, the Eurogroup then reached agreement on a ‘term sheet’ for the Budgetary Instrument for Convergence and Competitiveness (BICC).\(^ {21}\) Its name indicates its limited ambition, but the instrument would not only incentivize reform, but also public investment.

The priorities of the budget would be reviewed yearly by the Euro summit and the Eurogroup through strategic guidance. MS should then submit their proposals for reform and investment on the basis of the strategic guidance. The Commission, in cooperation with the Eurogroup, would assess the proposals, on the basis of transparent criteria. One set of eligibility criteria would come from the Common Provisions Regulation, as its macroeconomic conditionality applies. This means that a MS would not be able to receive funds if it is subject to certain decisions under the Stability and Growth Pact and the Imbalances procedures.

For the governance framework ‘an additional act’ is envisioned, next to a legislative act based on the Treaties and a Commission proposal. The size of the instrument will be determined “in the context of the MFF”. The Euro area MS would participate in the new budgetary instrument, as well as any MS participating in the Exchange Rate Mechanism II that wishes to do so. For other non-euro area MS, appropriate arrangements should be defined, when the financial aspects of the BICC are arranged. That also highlights the lack of agreement on the method of funding in the Term Sheet. No decision was made as to whether to finance the BICC through EU own resources or through external assigned revenue.

2.6. The Commission proposal (2019)

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In July 2019, the European Commission submitted a legislative proposal to the European Parliament and the Council for (a part of) the governance framework of the BICC.\textsuperscript{22} It is based on articles 136(1)(b) and 121(6) TFEU.

The proposal lays out one aspect of the governance of the BICC, namely the formulation of the strategic orientations for reform and investment for the euro area (as a whole) and of country specific guidance. These two aspects are directly linked to the European Semester, as the strategic orientations shall be part of the euro area recommendation and the country specific guidance shall be in conformity with the country specific recommendations. The country specific guidance shall then be used by the Member States for their reform and investment packages (to be regulated under another Regulation), that shall form the basis for the actual funding decisions.

Although the BICC is not primarily concerned with stabilization, the proposal by the Commission provides for the “modulation of national co-financing rates”, in case the Commission and the Council find that a MS is experiencing a severe economic downturn.

2.7. The Eurogroup’s October Term Sheet

In October 2019, the Eurogroup reached agreement on another Term Sheet.\textsuperscript{23} It provided some guidance on the use of the own resources for funding the BICC and the allocation key, but left open the key issue of using external assigned revenue. For the own resources, the starting point for the negotiations in the MFF is the original proposal by the Commission for the euro area share of the financial envelope of the Reform Delivery Tool, i.e. around 17bn euro. At least 70% of what the MS contribute to the instrument, they will receive back from the instrument. In total, at least 80% of the BICC will be allocated according to the allocation key, based on population and inverse of GDP per capita and up to 20% can be distributed flexibly, reacting to country specific challenges and ambitious reform and investment plans.

The use of external assigned revenue will remain a possibility by including an enabling clause into the regulation that is still to be negotiated. Discussions on an intergovernmental agreement are continuing.

On the issue of governance, the October Term Sheet largely supports the Commission proposal from July 2019, with the main difference being that in the view of the Eurogroup the


Eurosummit and the Eurogroup ‘kick-start’ the discussion on the priorities in the BICC. In the Commission proposal, that discussion is started by a Commission proposal.

The October Terms Sheet has a 25% national co-financing rate. This rate can be modulated i.e. reduced. The trigger for the modulation is ‘related to severe economic circumstances, as defined in the SGP’. In the July 2019 Commission proposal, the trigger was not connected to the definition of severe circumstances as found in the SGP.

The negotiations are expected to be finalized by the end of the year, together with the EU budget negotiations.

3. Legal aspects of the BICC

The following paragraphs highlight several legal aspects of the BICC. As the current plan is an amalgam of conclusions, informal agreements and proposals, my comments are tentative and will consider the overall direction in which the plans have developed.

3.1. The legal basis

The first issue concerns the legal basis for the budgetary instrument. The proposal submitted in July 2019 by the Commission is based on article 136 TFEU and article 121(6) TFEU but only concerns a part of the governance framework of the BICC. Another legislative proposal is expected that would create the BICC, based on article 175(3) TFEU, using the ordinary legislative procedure. The Commission proposals for the investment stabilization and the Reform Support Programme, as well as the Franco-German proposal opted for article 175 paragraph 3 TFEU as legal basis, with the latter suggesting articles 182 (research and technological development), 173 (industry competitiveness) and 136 TFEU as possible supportive bases.

The Commission proposal for investment stabilization from 2018 provided a clear link between the objective of stabilization and the objective described by its legal basis, namely cohesion. Article 175(3) TFEU allows the Council and the EP to adopt measures to fulfill the goals of article 174 TFEU that cannot be achieved through the Structural Funds. These goals are territorial, economic and social cohesion, to the benefit of the harmonious development of the Union.

24 The October Term Sheet only mentions article 136 TFEU in this regard. The difference is that on the basis of article 136 and 121(6) TFEU, the ordinary legislative procedure applies, whilst if only article 136 TFEU is used, the Council can adopt a measure by itself.
25 The reference here is to the third paragraph of article 175 TFEU.
26 These legal bases concern industrial policy, research and technological development and the euro.
27 Measures based on article 175(3) TFEU may aim at a specific form of cohesion. Repasi, “Legal Options and Limits for the Establishment of a European Unemployment Benefit Scheme,” 21.
Regulation. As the Commission proposal connected the spending priorities of the new budgetary instrument for investment stabilization to the objectives as formulated through the Common Provisions Regulation, it is clear that the new instrument would be geared towards the same objectives as the existing funds. As the objective of stabilization cannot be achieved through the existing funds, it is also clear that a new mechanism is needed, thus satisfying the two requirements of Article 175(3) TFEU.

The Commission proposal for the Reform Support Programme was also based on article 175(3) TFEU, in combination with 197(2) TFEU, but here the connection with the legal basis is more tenuous. Rather than connecting it directly to the CPR Regulation, the proposal sees cohesion as a result of “improving the national economies ... and social structures in the Member States”. The Reform Delivery Tool is primarily oriented towards the objectives of the European Semester; cohesion is only a secondary objective. Hence, the suitability of article 175(3) TFEU as a legal basis is questionable. Using article 175(3) as the legal basis for the BICC is problematic for the same reason.

The main issue is whether convergence and competitiveness can be seen as stimulating a form of territorial, social or economic cohesion. One argument against equating convergence and cohesion is that the former arises from a legal field that has traditionally promoted market-based solutions for achieving Union goals, whilst the latter is more closely associated with public interventions to achieve those goals. Rather than use cohesion policies to mitigate negative effects from market integration and the single currency, cohesion policies would now be defined in terms of market integration and monetary stability. National experiences with reforms associated with membership of the Eurozone are often defended in terms of economic necessity and efficiency, rather than cohesion. Perhaps the promotion of public investments is what brings the BICC closer to the original purpose of cohesion policies, but then the question is why the existing funds are insufficient to achieve this goal.

3.2. Differentiation and the purpose of the BICC

One of the points of discussion on the BICC is the relation between the Members of the Euro area and non-euro area MS. Naturally, the idea of a specific budget for the euro area would be contradicted by the inclusion of non-euro area MS. However, the debate over differentiation does not appear to be primarily concerned with the participation of non-euro

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28 Article 4(a) of the proposal. It is furthermore noted in article 6 that the objectives shall refer to policy areas related to, amongst others, cohesion, competitiveness and productivity.
29 It should be noted that the proposal for a new Common Provisions Regulation also aims to align the ESI-Funds with the goals of the European Semester. European Commission, Proposal for a Regulation of the European Parliament and of the Council laying down common provisions on the European Regional Development Fund, the European Social Fund Plus, the Cohesion Fund, and the European Maritime and Fisheries Fund and financial rules for those and for the Asylum and Migration Fund, the Internal Security Fund and the Border Management and Visa Instrument, COM(2018) 375 final. See e.g. articles 8(a), 9(1) and 14(1) of the Commission proposal.
area MS in the budget. Rather, the debate over differentiation appears to be a proxy for several other issues, such as governance, purpose, and funding.

Both the Commission proposal for investment stabilization and the Franco-German proposal refer to the need for an objective justification for the exclusion of non-euro area MS from the application of the budget. The economic rationale for a specific euro area budget would be that Eurozone MS have lost some of their tools to absorb or counteract certain economic phenomena, such as asymmetric shocks. In an asymmetric shock, a single MS or a group of MS of the Eurozone experiences a sudden economic downturn. Since these MS are part of the Eurozone, they cannot use their monetary policy tools, including the exchange rate, to stimulate their economies. Monetary policy is instead defined by the ECB for the Eurozone as a whole and the exchange rate also follows the economic conditions of the Eurozone as a whole. Hence the need for a tool on the European level that responds quickly and targets a subset of MS.

None of the proposals, however, neatly follows this narrative. The Commission proposal for investment stabilization would be available only for euro area MS and those participating in ERMII. However, its activation requirements solely see to the economic situation in a specific MS. It is therefore possible that all Eurozone MS would qualify at the same time for support. The mechanism is thus not specifically addressed to asymmetric shocks, but also to symmetric shocks. It follows in this regard the resolution of the European Parliament, which explicitly called for the budgetary instrument to also target symmetric shocks.

An economic justification for such a tool is certainly available, but it would touch upon a broader set of beliefs about the functioning of EMU as a whole, and hence be more controversial. Whereas a symmetric shock affects all MS, it does not (necessarily) affect the relative economic strength of the Eurozone Member States in relation to each other. Hence, the ECB can adjust monetary conditions for the Eurozone as a whole, and the exchange rate would also respond to the economic situation of the Eurozone as a whole. Reasons to Europeanize the response to a symmetric shock would be the insufficiency of current monetary tools and the high levels of public debt in certain Member States, which might stand in the way of significant stimulus packages on the national level. Those who consider

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30 Another issue with the proposal by the Commission is that the form in which support is offered is inconsequential for euro area MS who have easy access to the financial markets and who currently borrow at negative or very low interest rates. The proposal would therefore be most beneficial for MS who are experiencing economic difficulties and who are losing trust from financial markets.


that the origins of these two problems lie with some MS’ specific current economic policies would thus oppose the Europeanization of the solution.

The Franco-German Proposal and the envisaged BICC also do not correspond to the economic justification for the exclusion of non-euro area MS, because stabilization would not be the primary objective. Rather, both seek to promote competitiveness and convergence through structural reforms and investments. Hence, the economic justification for the BICC that MS have lost the tools to counter asymmetric shocks does not apply. The loss of monetary policy tools does not inhibit Eurozone MS from adopting structural reforms and making investments.\(^{34}\)

The necessity of the BICC can certainly be defended on other grounds, but none of these grounds justify the exclusion of non-euro area MS. It should be noted that the necessity of the BICC for the euro does not, by itself, justify the exclusion of non-euro area MS. This is because the euro is a policy of the Union, not just of the Eurozone. This is best illustrated by the need for convergence. Convergence has been at the heart of the debates on the process of monetary integration.\(^{35}\) Whereas some saw monetary integration as a means for European economies to converge, others saw convergence as a requirement for monetary integration. The Maastricht Treaty set several convergence criteria, including on levels of inflation and government deficits. It is therefore clear that convergence is a crucial aspect of EMU. It is, however, not exclusively applicable to the Eurozone MS, as most non-euro area MS are under a legal obligation to try to join the Eurozone. Non-euro area MS can therefore have an interest in a budgetary mechanism that might help them fulfill the convergence criteria.

This interest of non-euro area MS in the new budgetary instrument is not negated by the unwillingness of some of them to try to join the Eurozone.\(^{36}\) Non-euro area MS are subject to many aspects of economic governance and might even face adverse consequences of ignoring

\(^{34}\)There is a (new) economic perspective, Modern Monetary Theory, that advocates the use of monetary policy for a broad range of economic and social goals. From this perspective, the Europeanization and strict mandate of monetary policy are obviously a restriction on the ability of national and European policy makers to invest in a broad range of economic policies.

\(^{35}\)As regards the objective of competitiveness, the case for restricting participation is even weaker. Competitiveness is connected to various areas of EU law, with no indication that it should apply only to a subsection of MS. For example, according to article 3 TEU, the aim of the EU is to establish an internal market that promotes a highly competitive social market economy.

\(^{36}\)The Commission proposal for the Reform Support Programme has an interesting feature in this regard. Access to the Convergence Facility, which is only open to non-euro area MS, would be conditional on the MS taking “demonstrable steps towards joining the single currency within a given time-frame”. This includes “a formal letter from the government of the Member State concerned to the Commission stating its clear commitment to join the euro area within a reasonable and defined timeframe”. If adopted, this would be further evidence of the reversal of the membership policy of the Eurozone, whereby the legal obligation to join the Eurozone is no longer the primary tool to promote monetary integration. See Thomas Beukers and Marijn Van der Sluis, “The Variable Geometry of the Euro-Crisis: A Look at the Non-Euro Area Member States,” EUI Working Paper Law 2015/33 (2015).
the prescriptions it produces. Although the imposition of fines *within* the procedures of economic governance is excluded for non-euro area MS, this does not mean that economic governance cannot have financial consequences. For example, when in 2012 the Council found that Hungary (a non-euro area MS) had not taken sufficient action to remedy its excessive deficit, this led to a suspension of commitments from the Cohesion Fund for Hungary.\(^{37}\) Given that structural reforms and public investments can help a MS fulfill its obligations under the procedures of economic governance, it would be contrary to the goals of EMU to restrict the application of the BICC to euro area MS only.

The weak rationale for differentiation also translates into a legal problem. The application of rules of secondary law to a subset of MS must be based on primary law, with EMU as the leading example. Where the Treaties do not foresee differentiated integration, a group of MS can make use of enhanced cooperation (article 20 and articles 326-334 TFEU). In some cases, secondary legislation that is not directly based on a rule of primary law that envisions differentiated integration builds on a distinction introduced elsewhere in primary law. The Single Resolution Mechanism Regulation, for example, is based on article 114 TFEU (internal market), but applies only to Eurozone MS and MS where close cooperation has been established. Notwithstanding some other difficulties with this setup, the legality of the differentiation as such is not in doubt, given the many direct connections between the Single Resolution Mechanism and the ECB, whose acts do not apply to non-euro area MS (article 139(2)(e) TFEU).\(^{38}\)

The question is therefore whether the likely legal basis for the BICC, article 175(3) TFEU, tolerates (or provides for) differentiated integration in this case. The text of article 175(3) TFEU is silent on this issue, but the measure must promote the goals as found in article 174 TFEU. This means that the cohesion must benefit the harmonious development of the Union. This does not mean that targeted measures are prohibited as such. In *Parliament v. Council*, the CJEU allowed a measure specific to the situation in Ireland and Northern-Ireland.\(^{39}\) Measures contributing to economic cohesion in Ireland and Northern-Ireland were found to contribute to the peace process and thus to the overall development of the Union as a whole.

As no economic rationale requires the exclusion of non-euro area MS, it is doubtful that the BICC can be seen as promoting the cohesion for the harmonious benefit *of the Union*. Many of the Eurozone MS are amongst the most prosperous in the Union and many of those outside the Eurozone are amongst the most economically disadvantaged. An instrument that seeks to promote the competitiveness and convergence of Eurozone MS, to the exclusion of non-

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euro area MS, can therefore not be seen as promoting the economic or social cohesion (of the Union).\textsuperscript{40}

The issue of differentiated integration is presented in the Term Sheet and in the complimentary letter from Eurogroup President Centeno to Euro summit President Tusk primarily as a financial issue.\textsuperscript{41} Since the BICC will be financed through EU own resources, non-euro area MS are contributing to the BICC through their contribution to the EU budget. This aspect is discussed in the next section, but it is relevant to note here that solving the issue of non-euro area MS liability for the BICC, as Centeno calls it, does not solve the legal problem of the lack of a proper justification for the exclusion of non-euro area MS from the BICC.

As noted elsewhere\textsuperscript{42}, the relation between the Eurozone’s in’s and out’s has been inverted over time. Whilst first the emphasis lay on the euro as the currency of the Union, with specific exceptions for those temporarily on the outside, now the Eurozone is seen as requiring a special place within the Union. The introduction of article 136 TFEU in the Lisbon Treaty was the most obvious symbol of this transformation, as it allows the Euro area MS to adopt measures, rather than exclude non-euro area MS from participation. The transformation is incomplete, however, as the status of ‘MS with a derogation’ still dominates the overall setup of the euro. The problems for the BICC in terms of differentiation are thus the result of an incomplete transformation in the legal thinking on the place of the euro in the EU.

\textbf{3.3. The BICC as part of the EU budget}

According to the Term Sheets, the BICC will be part of the EU budget. This means, amongst other things, that the Commission has the (primary) responsibility for the execution of the budget (article 17 TEU) and that the Court of Auditors scrutinizes its implementation. For the governance of the BICC, i.e. the expenditure side, the Term Sheet from June envisioned an ‘additional act’, for which the Commission has already submitted a legislative proposal and which the October Term Sheet largely supports. For the funding of the BICC, the June Term Sheet already noted that it would make use of the EU own resources, possibly complemented by external assigned revenue, based on an intergovernmental agreement. Each method of funding comes with its own problems.

\textsuperscript{40} If the BICC cannot be adopted under article 175(3) TFEU on the ground that it does not foster cohesion, it would then also follow that the BICC cannot be adopted through enhanced cooperation (article. 20 TEU and article. 326-334 TFEU), as one of the conditions of enhanced cooperation is that it would not undermine cohesion.

\textsuperscript{41} Eurogroup President Centeno, Letter to Euro summit President Tusk, 10 October 2019, available at: https://www.consilium.europa.eu/media/41008/091019_eurogroup-president-letter.pdf.

\textsuperscript{42} Beukers and Van der Sluis, “The Variable Geometry of the Euro-Crisis: A Look at the Non-Euro Area Member States.”
As noted above, the use of EU own resources for the BICC has the effect that non-euro area MS contribute to the new instrument through their contributions to the EU budget. Hence, they want to be compensated. According to the October Term Sheet, this can be either in the form of a dedicated instrument, or through another financial arrangement. The October Term Sheet furthermore suggests that Sweden and Denmark are expected to choose the latter option. The dedicated instrument could come in the form of a replacement of the Commissions convergence facility, as the Finnish Council Presidency has apparently been working on a Convergence and Reform Instrument (CRI). It would aim at “supporting convergence of non-euro area MS towards the euro area, by providing financial support for structural reforms”. At least in its purpose and setup, the CRI strongly resembles the BICC, confirming the artificiality of the divide between euro and non-euro area MS.

The October Term Sheet keeps open the possibility of using external assigned revenue, raised on the basis of an intergovernmental agreement (IGA), to increase the size of the BICC. The Eurogroup working group continues the discussions on this topic, but even if no agreement is reached before the launch of the BICC, an IGA can be adopted later, as an enabling clause to that effect is to be adopted in the regulation that establishes the BICC.

The use of external assigned revenue avoids some complications, while raising others. External assigned revenue is used to finance specific items of expenditure and enables contributions to the EU budget from non-EU sources.\(^\text{43}\) The funding would thus not come from an own resource of the EU, but from the MS as organized through a separate international agreement. First, this avoids the involvement of non-euro area MS in the funding of the BICC. The second benefit is that the BICC could grow quickly in size, as it is not capped by the MFF. In a next crisis, the Eurozone MS could easily increase their contributions.

One problem with using external assigned revenue is the reliance on an international agreement for the organization of MS contributions.\(^\text{44}\) It counters recent attempts by the Commission to ‘repatriate’ the ESM Treaty and the Fiscal Compact in the EU legal order. Although the downside of the use of international treaties outside the Union legal order is easily exaggerated, a long-term view on the development of the euro should favor a single integrated legal framework for reasons of simplicity and clarity.


Another complication is that the use of external assigned revenue deepens the reliance on national contributions for the functioning of EMU. Rather than develop a budgetary instrument that provides for a European value, based on a source of funding derived from European activities, the use of external assigned revenue reinforces the position of the MS as the interlocutors for EU policies.\textsuperscript{45} Currently, also the EU budget relies heavily on national contributions, although plans circulate to overhaul the financing of the EU budget.\textsuperscript{46} In any case, it will be difficult to expand the BICC, as long as the MS remain the primary vehicles through which the BICC is funded and executed. The reason is that it makes MS net beneficiaries and net contributors. If the BICC would lead to significant re-distribution amongst MS, this would be criticized on the grounds that the new instrument should not be geared towards redistribution. The Five Presidents’ Report was very clear in this regard. If the BICC would not lead to significant re-distribution and the MS would receive back what they put into the BICC, the question arises as to the added value of the BICC. MS would then provide funding to the BICC, to receive it back with conditions. Only when the BICC would be funded through truly European own resources, derived from European activities and without national labels, can this problem be solved.

The allocation key suggested by the Term Sheet provides that MS at least receive back 70% from their contribution to the BICC. Combined with the envisioned size for the BICC, this leads to the conclusion that the new instrument would not contribute in a significant way to the functioning of EMU.

For the implementation of the BICC, the term sheet suggests a complicated interaction between the Euro summit, the Eurogroup, the preparatory committees of the Eurogroup and the Commission. This part of the proposal is thus also premised on the exclusion of non-euro area MS. The Commission Proposal for the governance of the BICC only regulates the easy part of this difficult process, namely the formulation of objectives for the euro area as a whole and for individual MS. More problematic will be the decision making on the actual allocation of funding.

According to the term sheet, the guidance from the Euro Summit and the Eurogroup should result in ‘transparent criteria’, on the basis of which the Commission can assess the national plans for investment and reform. Whilst the responsibility for the implementation of the expenditure of the BICC will formally rest with the Commission, the preparatory committees of the Eurogroup and the Eurogroup itself are also involved. It will be challenging to translate


this construction into a legal proposal that respects the constitutional responsibility of the Commission for implementing the Union’s budget.\footnote{Since the Lisbon Treaty, the Commission is responsible for the implementation of the budget “in cooperation with the Member States”. This reflected the fact that most Union funds are ultimately distributed by the Member States.}

The involvement of the Eurogroup in this stage of the process also risks ongoing political bickering over the BICC; where the Council is not able to agree on ‘transparent criteria’ or a clear strategy for the whole Euro area, MS may attempt to steer the use of the BICC also in the last stage. The continuous involvement of the MS thus takes away the incentive to formulate clear criteria. A clearer separation of responsibilities in the implementation of the BICC would be more likely to lead to clear priorities.

Notably absent from these arrangements is the EP. Whereas in part this logically follows from the close connection of the BICC to the European Semester, where it is also the Council that takes center stage, it goes against the movement to strengthen the democratic legitimacy of EMU through the involvement of the EP. Although the Commission’s proposal for the governance of the BICC calls for an extension of the economic dialogue, where the President of the Council, the Commission and the President of the Eurogroup can be invited for discussion, it is doubtful this would lead to meaningful influence of the EP over the implementation of the BICC.\footnote{Commission proposal on the governance framework.} As budgetary matters are often seen as a core task of parliaments, it is unclear what justifies the exclusion of the EP in the formulation of priorities under the BICC.\footnote{One contentious aspect of the involvement of the European Parliament in matters of EMU is the contribution of members elected in non-euro area MS.}

\textbf{3.4. The no-bailout clause}

In other commentaries on euro-area reform, and also with regard to a euro area budget, article 125 TFEU (the so-called no-bailout clause) is sometimes discussed as a possible legal obstacle.\footnote{Lionello, “Establishing a Budgetary Capacity in the Eurozone. Recent Proposals and Legal Challenges,” 833.} Article 125 TFEU is then seen as reflecting a principle of EU law with broad application.\footnote{Repasi, “Legal Options and Limits for the Establishment of a European Unemployment Benefit Scheme,” 44.} It is argued here that this approach is mistaken.

Naturally, the interpretation by the CJEU of this provision in the \textit{Pringle} case must be leading in any discussion on article 125 TFEU.\footnote{CJEU Case C-370/12, \textit{Pringle}, EU:C:2012:756.} In \textit{Pringle}, the Court set three requirements for the legality of financial assistance under article 125 TFEU: “1) Member States must remain responsible for their commitments to creditors, 2) the activation of financial assistance must be subject to strict conditionality and 3) this activation must be indispensable for the
safeguarding of financial stability of the euro area as a whole.” The discussion has focused so far on the three requirements and less on the trigger for these requirements: the provision of financial assistance.

The Court itself does not define what constitutes financial assistance, as there was very little reason to do so in the Pringle case. The ESM Treaty itself defines its support as financial assistance (article 3), and article 136(3) TFEU states that the granting of “any required financial assistance under the mechanism will be made subject to strict conditionality.” EU primary law furthermore speaks of financial assistance in article 122 TFEU, regarding EU support to a MS who is in difficulties or threatened with severe difficulties. Article 144 TFEU allows for mutual assistance, which is developed in Council Regulation 332/2002, creating a facility for medium term financial assistance. In these three instances, there is a direct connection between financial assistance and the existence of a crisis or difficulties in a MS. Hence, EU (primary) law offers no indication that financial assistance must be understood in a broad sense, but only covers emergency measures targeted at a single or a small group of Member States.

A restricted interpretation of financial assistance is also in line with the original purpose of article 125 TFEU, as it can be found in the proposals submitted by the MS in the negotiations leading up to the Maastricht Treaty. In their proposals, the MS put forward different versions of a no bailout clause, including a ‘no automatic bailout clause’ and a ‘no unconditional bailout clause’. The economic logic for a ‘no bailout clause’, which gained momentum throughout the negotiations, was that the growing interconnectedness between MS made them vulnerable to coercion by a MS in severe troubles. A single MS has leverage over its economic partners to demand economic support during a crisis, because an economic meltdown in one MS would spill-over into other MS. In ordinary times, when there is no immediate crisis, MS do not have this type of leverage over each other, leaving them free to decide together on projects that deepen integration or even promote outright solidarity on other grounds. In other words, what the no bailout clause sought to prevent was a form of forced solidarity in moments of crisis. Since the BICC is not designed to assist MS in times of crisis and is available to all euro area MS, it must be concluded that the new budgetary instrument should, in its current form, not be considered to offer financial assistance. The requirements of article 125 TFEU are therefore not applicable.

A narrow approach to what constitutes financial assistance might also enable a strict interpretation of the requirements as formulated by the Court in Pringle. As the legality of many different proposal for further euro-reform are currently tested against article 125 TFEU,
there is continuous pressure to interpret the three *Pringle*-requirements very narrowly, in order not to frustrate deepening integration. That pressure dissipates with a strict reading of ‘financial assistance’.

4. Conclusion

The negotiations over the BICC have been relatively straightforward, with a clear connection between the primary issue and the secondary issues. The primary issue is the overall purpose of the BICC, connected to that are the size, the method of funding, the governance structure and differentiated nature of the budget. The resulting compromise appears, so far, to be leaning towards those who favor a budget aimed at supporting reforms and national investments, implying a relatively small budget. The new budgetary instrument would be closely aligned with the objectives of the European Semester and part of the EU budget, but perhaps also funded through external assigned revenue.

In the upcoming negotiations for the legal framework of the BICC and perhaps also in the implementation of the BICC, the debate will be over the balance between supporting reforms and stimulating public investment. Whereas the former is closely aligned with the needs of the European Semester, the latter invites the formulation of other European economic objectives and would thereby open the door to the further development of the BICC.

Both the process of negotiations and the substance of the agreements so far have centered on the MS. The agreements in the Eurogroup discarded the initiatives of the Commission in favor of an outline proposed by two Member States. The influence of the EP so far seems negligible; the question is to what extent it will be able to demand changes to a finalized political compromise between the MS. Or perhaps the EP blocks the BICC in the hope that a new initiative would lead to a more ambitious euro area budget.

What has been remarkable in the negotiations amongst the MS so far was the two-step process through which the ambitious plans of the French have been scaled down. The first step was the negotiations with the Germany, in which the stabilization function was already demoted to a secondary objective. It then appears that the German negotiators allowed the members of the New Hanseatic League to challenge their joint declaration in the second step of the negotiations.

In the setup of the BICC, the MS again loom large. In the setup as currently envisioned, the MS set the priorities through the Euro summit/Eurogroup, maintain their presence at the stage of the assessment of national plans and perhaps solely decide the size of the external assigned revenue. One effect of the predominance of the MS in the setup and functioning of the BICC is that it would allow for a rapid expansion of the instrument under the right political circumstances. At the same time, it is doubtful whether in the long-term the reliance on the
MS for the functioning of EMU is sustainable, in lieu of relying on strong, democratic institutions on the European level.