CENTRO STUDI SUL FEDERALISMO

THE FINANCIAL TRANSACTION TAX:
LEGAL AND POLITICAL CHALLENGES
TOWARDS A EURO-ZONE FISCAL CAPACITY

Federico Fabbrini

October 2013

Research Paper

ISSN: 2038-0623
ISBN 9788896871454

ABSTRACT

The paper examines the recent high-level policy proposals to establish a fiscal capacity for the Euro-zone and discusses the relationship between taxing and spending in the Economic and Monetary Union (EMU) by examining the need and possibility to levy taxes at the supranational level to sustain this new fiscal capacity. To this end, the paper focuses on the pending legislation for the introduction of a Financial Transaction Tax (FTT) and considers the legality of resort to enhanced cooperation to adopt a FTT among a sub-group of Euro-zone countries. While the use of enhanced cooperation in the area of FTT has been the object of recent challenges, the paper discards these concerns and argues that the adoption of a FTT through enhanced cooperation is consistent with the constitutional function of this instrument, complies with the principles of the internal market and does not affect the rights of non-participating member states – so it is legal. However, the paper suggests that the use of enhanced cooperation to enact a FTT meets several political challenges, precisely because of the connection between taxing and spending in the Euro-zone. Since only eleven member states have agreed to levy an FTT, it appears difficult to appropriate the revenues of the FTT for the benefit of a common Euro-zone budget. In the end, the establishment of a fiscal capacity for the Euro-zone requires further institutional reforms in the architecture of the EMU aimed at ensuring a more effective and legitimate decision-making process in fiscal affairs.

Federico Fabbrini is Assistant Professor of European & Comparative Constitutional Law, Tilburg Law School (NL)
E-mail: F.Fabbrini@tilburguniversity.edu

This text was delivered at the Workshop "What Form of Government for the Political Union of the Euro-zone?" held at the Scuola Superiore Sant'Anna, Pisa (Italy), on 27 September 2013.

1. *Introduction*

Since the outburst of the Euro-crisis, the member states and the institutions of the European Union (EU) have reacted by introducing important changes to the constitutional architecture of the Economic and Monetary Union (EMU). Most of the legal measures adopted so far have attempted to *reduce the risks* stemming from EMU, by strengthening fiscal discipline and budgetary constraints at the national and supranational level. Increasingly, however, calls have been made for new legal instrument at the EU level that would allow the member states to *share the risks* associated with EMU. In particular, several high-level policy documents – the report of the President of the European Council 'Towards a Genuine EMU,'[1] and the blueprint of the European Commission 'For a Deep and Genuine EMU'[2] – have recently proposed the introduction of a fiscal capacity for the EMU, that is a budget for the Euro-zone finalized to assuage the asymmetric shocks occurring within the EMU and to carry out those counter-cyclical policies no-longer possible at the national level. The proposals to introduce a fiscal capacity for the Euro-zone, however, inevitably raise the question of how to levy the necessary resources to sustain an EMU budget.

The aim of this paper is to explore the interconnection between taxing and spending in the Euro-zone, focusing on the case of the Financial Transaction Tax (FTT). Originally conceived by the Commission as a way to make the financial sector contribute to the costs of the crisis, and at the same time to endow the EU with an authentic own resource for its fiscal policy,[3] the proposal to introduce a FTT did not muster the unanimous support of all the EU member states, and was therefore brought forward only be eleven Euro-zone countries through the mechanism of enhanced cooperation.[4] The use of enhanced cooperation to introduce the FTT, however, has been the object of legal and political challenges. In April 2013, the United Kingdom (UK) lodged proceedings before the EU Court of Justice (CJEU) claiming that the Council authorization to use enhanced cooperation for the introduction of the FTT unlawfully affected its right as a non-participating member state.[5] In September 2013, moreover, the Legal Service of the Council leaked a confidential opinion in which it expressed concerns about the legality of the scope of

---

[1] President of the European Council, Final Report 'Towards a Genuine EMU', 5 December 2012
[2] Commission Communication, 'A Blueprint for a Deep and Genuine EMU: Launching a European Debate', 28 November 2012, COM(2012)777 final
[3] Commission Proposal for a Council Directive 'On a Common System of FTT', 28 November 2011, COM(2011)594 final
[4] Commission Proposal for a Council Directive 'Implementing Enhanced Cooperation in the Area of a FTT', 14 February 2013, COM(2013)71 final
[5] Case C-209/13, *United Kingdom v. Council*, Application lodged on 18 April 2013

application *ratione personae* of the FTT as proposed in the draft legislative text of the Commission.[6]

By examining the use of enhanced cooperation in the area of FTT in light of the Treaty rules and the jurisprudence of the CJEU – notably: the April 2013 Grand Chamber judgment in *Spain and Italy v. Council of the EU*,[7] dealing with the legality of enhanced cooperation for the creation of an EU unitary patent regime – the paper argues that in this case resort by a vanguard group of EU member states to the mechanism of enhanced cooperation passes all legal tests. Contrary to the view of the UK and the Council Legal Service, the adoption of a FTT through enhanced cooperation is consistent with the constitutional function of this instrument, complies with the principles of the internal market and does not affect the rights of non-participating member states. However, the paper suggests that the use of enhanced cooperation to enact a FTT generates several political difficulties, precisely because of the inter-linkages between taxing and spending in the EU and the Euro-zone. Whereas the initial proposal to introduce a FTT were finalized to raise a new EU revenue, the fact that only several member states participate to the venture raises hurdles to the ability to use the revenues of the FTT to create a true fiscal capacity.

In other words, while the paper claims that the adoption of the FTT through enhanced cooperation is legal and sets aside any opinion to the contrary, it suggests that the use of enhanced cooperation is a politically inadequate tool towards the establishment of a Euro-zone fiscal capacity. In the EU, as in any constitutional system, spending and taxing constitute two sides of the same coin. On the one hand, the proposals for a new fiscal capacity require authentic EU or Euro-zone taxes. On the other hand, taxes must be levied uniformly throughout the EU or the Euro-zone if they are going to be used for common budgetary purposes. However, as long as unanimity remains the prescribed requirement for the adoption of tax legislation at the EU level, the chances to reach consensus in this field appear limited. In prospect, therefore, the proposals to endow the Euro-zone with a fiscal capacity must be associated with a reform of the EMU decision-making process in fiscal affairs, which allows a more efficient and legitimate framework of governance based on qualified majority voting (QMV) and the full involvement of the EU Parliament. It is only in a Union that binds anew taxing and spending at the supranational level, in fact, that the EU citizens and member states can regain the power to control those activities that now escape any form of fiscal regulation at the national level – as is the case of the FTT.[8]

A preliminary warning is in order: This paper examines the introduction of a FTT from a legal point of view. The paper does not consider the FTT from an economic perspective. Unsurprisingly, economists disagree about the virtues and vices of this tax, as of any other. The aim of the paper is to discuss whether the instrument of enhanced cooperation provides an adequate tool to introduce the FTT for a number of EU member states. Whether this is sound policy or economic suicide is ultimately for the political process to decide, in the Union and the states. The paper however explores the political challenges of the use of enhanced cooperation for the introduction of a FTT, emphasizing the link between taxing and spending in the Euro-zone. The

[6] Council of the EU, Opinion of the Legal Service, JUR 448, 6 September 2013 (Confidential Document Interinstitutional File: 2013/0045 (CNS))
[7] Joined Cases C-274/11 and C-295/11, *Spain & Italy v. Council*, Judgment of 16 April 2013, nyr
[8] See also M Maduro, 'A New Governance for the European Union and the Euro: Democracy and Justice', Report commissioned by the European Parliament Constitutional Affairs Committee, PE 462.484 (2012)

paper is structured as follows. Section 2 surveys the recent proposals to create an EMU fiscal capacity. Section 3 discusses the problem of raising revenues at the EU level to sustain a fiscal capacity and explains why EU taxes – and not inter-state transfers – must be the basis of a new EMU budget. Section 4 examines the legislative history and the content of the Commission proposal to introduce the FTT through enhanced cooperation. Section 5 considers the legal challenges against the use of enhanced cooperation to adopt the FTT and discards them. Section 6 instead considers the political challenges. Section 7, finally, concludes by outlining several prospects for future reform.

2. Proposals for a Euro-zone fiscal capacity

The proposals to endow the EMU with a fiscal capacity are extremely recent. The October 2010 report of the task force chaired by the President of the European Council, 'Strengthening Economic Governance in Europe', which served as the basis for most of the reforms in the architecture of the EMU adopted to respond to the Euro-crisis, did not contain any hint about this idea.[9] In fact, the first time the term fiscal capacity is used in an EU official document is in the October 2012 interim report of the President of the European Council, 'Towards a Genuine EMU.'[10] Although already in its June 2012 inaugural report[11] the President of the European Council had 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,'[12] it is in the October 2012 report that one finds a first articulate presentation of the idea of fiscal capacity and its form. 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 President of the European Council 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.'[13]

According to the President's 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.'[14] At the same time, '[a]nother important function of such a fiscal capacity would be to facilitate structural reforms that improve competitiveness and growth.'[15] These ideas were later developed by the President of the European Council in the December 2012 final report,[16] where the establishment

---

[9] See Report of the Task Force of the European Council, 'Strengthening Economic Governance in the EU', 21 October 2010 (identifying 5 pillars for reform, namely: 1. Greater fiscal discipline, 2. Broader economic surveillance, 3. Deeper economic coordination via the European Semester, 4. More robust framework for crisis management, 5. Stronger institutions for more effective economic governance).
[10] President of the European Council, Interim Report 'Towards a Genuine EMU', 12 October 2012
[11] President of the European Council, Report 'Towards a Genuine EMU', 25 June 2012
[12] Ibid., 5
[13] President Interim Report (n 10), 4
[14] Ibid., 5
[15] Ibid.
[16] President Final Report (n 1)

of a fiscal capacity was clearly linked to the creation of a 'shock-absorption function' to improve the resilience of EMU.[17] As the President's final report underlined, in fact, '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.'[18] 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.[19] Because of its 'insurance-type' nature, at the same time, the President's report suggested alternative macro or micro economic approaches to set-up a fiscal capacity,[20] and emphasized that its design would still have to avoid 'the risk of moral hazard inherent in any insurance system.'[21]

In the vision outlined in the President's final report, therefore, the fiscal capacity of the EMU would largely operate as a sort of 'rainy day fund' – that is, like a savings fund to which member states contribute in times of economic upswing and from which they would be able to draw in times of economic downswing, to cushion the effects of a recession.[22] In fact, although the final report leaves open the possibility that the fiscal capacity may be funded by own financial resources, including a capacity to borrow via the establishment of an EU Treasury,[23] the acknowledgement that 'the financial implications for national budget would depend on the [fiscal capacity's] precise design and parameters'[24] suggests that state contributions would be, at least in the short term, the main sources of its funding. In terms of timing, moreover, the President's final report suggested the possibility to achieve a fiscal capacity in stages. In a first phase, 'limited, temporary, flexible and targeted financial incentives'[25] would be developed to support structural reforms in those member states in fiscal difficulties that are willing to enter into contractual arrangements with the EU institutions, while in the long run a more stable instrument to provide 'fiscal solidarity […] over economic cycles' would have to be put in place.[26]

Analogous ideas for the establishment of a fiscal capacity were also advanced by the European Commission. The November 2012 blueprint 'For a Deep and Genuine EMU'[27] endorsed the idea of a fiscal capacity to underpin structural reforms at the national level and provide a stabilization tool at EMU level to support adjustment to asymmetric shocks. Moreover, also the Commission suggested to distinguish between a short term, in which 'the economic governance framework should be strengthened further by creating a "convergence and competitiveness instrument" [(CCI)] within the EU budget to support the timely implementation of structural reforms, on the condition that "contractual arrangements" are concluded between Member States and the

[17] Ibid., 5
[18] Ibid., 9
[19] Ibid., 10
[20] 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).
[21] Ibid., 10
[22] On the 'rainy day' fund mechanism in the US system of fiscal federalism see R Inman & D Rubinfeld, 'Fiscal Federalism in Europe: Lessons from the United States Experience', (1992) 36 *European Economic Review* 654, 655
[23] President Final Report (n 1), 12
[24] Ibid., 11
[25] Ibid., 9
[26] Ibid.
[27] Commission Communication (n 2)

Commission,'[28] 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 a Communication for the introduction of CCI, emphasizing the link between structural reform and financial support to be provided by member states.[29]

These proposals for the creation of a fiscal capacity have found a mild endorsement by the EU Heads of States and Governments congressed in the European Council. Tellingly, while the Conclusions of the December 2012 European Council largely endorsed the President's report and followed in its footsteps to outline the process of future reforms of the EMU, no reference is made to the term fiscal capacity.[30] More modestly, the Conclusions refer to 'solidarity mechanisms'[31] aimed at supporting member states who agree through contractual arrangements to undertake structural reforms, as suggested both by the President's report and the Commission's blueprint. However, the proposal to endow the Euro-zone with an autonomous budget has received the individual support of prominent institutional players within the European Council. While German Chancellor Merkel had already embraced the idea in a speech before the European Parliament in November 2012,[32] recently also French President Hollande and Italian Prime Minister Letta indicated their support for it. [33]

Moreover, the idea of a fiscal capacity has found increasing backing in the European Parliament. In its November 2012 resolution 'Towards a Genuine EMU',[34] the Parliament had 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'[35] 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.'[36] In its recent May 2013 resolution 'On Future Legislative Proposals on EMU',[37] then, the Parliament clarified that it considered the CCI proposed by the Commission as 'building blocks towards a genuine fiscal capacity.'[38] 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

---

[28] Commission Memo, 'A Blueprint for a Deep and Genuine EMU', 28 November 2012, MEMO/12/909, 2
[29] Commission Communication, 'The Introduction of CCI', 20 March 2013, COM(2013)165 final
[30] European Council Conclusions, 13-14 December 2012, EUCO 205/12
[31] Ibid., 5
[32] See European Parliament, Communique de Presse, 'Angela Merkel donne sa vision d'une UE renouvelée', 7 November 2012
[33] See F Holland, President of France, 'Intervention liminaire de lors de la conférence de presse', 16 May 2013, 7 (speaking in favour of a 'une nouvelle étape d'intégration avec une capacité budgétaire qui serait attribuée à la zone euro.'). See E Letta, Prime Minister of Italy, 'Keynote Speech at Annual Dinner Bruegel', 9 September 2013, 5 (arguing that 'there is room to reflect on a fiscal capacity for the euro area.')
[34] European Parliament Resolution 'Towards a Genuine EMU', 20 November 2012, P7_TA(2012)0430
[35] Ibid., par CR
[36] Ibid., par 11
[37] European Parliament Resolution 'On Future Legislative Proposals on EMU', 23 May 2013, P7_TA(2013)0222
[38] Ibid., par 22

EU budget, but outside the MFF ceiling, so as to ensure that the European Parliament is fully involved as a legislative and budgetary authority.'[39]

Overall, therefore, there seems to be a slow but growing institutional consensus within the EU toward the idea of complementing the constitutional architecture of EMU with a form of fiscal capacity. As the fiscal discipline side of EMU is made ever more secure by being entrenched in constitutional norms at EU and state level,[40] the awareness becomes greater on the necessity to create new supranational instruments to support fiscal adjustments in the EMU.

3. Problems of raising revenues for a fiscal capacity

The proposals in favor of endowing the Euro-zone with a fiscal capacity inevitably raise the question of where from to draw the resources needed to feed an EMU budget. As the previous Section underlined, the reports of the President of the European Council and the blueprint of the Commission appear ambiguous in this regard, hinting that the fiscal resources necessary for a Euro-zone fiscal capacity may be based – at least initially – on direct contributions from the member states, but leaving open the possibility that they may derive – in the mid-long term – from a real EU revenue power. The European Parliament, on the contrary, has been adamant in claiming that a Euro-zone fiscal capacity must be immediately based on authentic EU own resources. This implies an EU power to tax, and to borrow money. In its November 2012 resolution 'Towards a Genuine EMU', the Parliament recommended to the Commission to 'return to the spirit and letter of the [Treaties]'[41] and develop a budgetary capacity *funded by own resources*. In its resolution the Parliament emphasized especially the economic advantages of this move: at a time of budget consolidation at the national level, the existence of EU own resources would free the member states from the duty to increase their contributions to finance a fiscal capacity of the EMU. Nevertheless, the Parliament's proposal would also have a clear political advantage. This becomes apparent in light of the deep asymmetry which characterizes the member states of the EU.

As it is well known, in the EU, member states differ in size, wealth and economic performances. This asymmetry has over-time come to play a heavy influence on the decision-making process about the EU budget – the MFF. The EU budget, in fact, is nowadays made up for the most part of contributions by the member states. As a result, the decision-making process about the EU budget has been captured by endless negotiation among the member states about the precise costs and benefits that each member states would incur. Because no member state its willing to transfer *its* money to the EU budget for the benefit of *other* member states, the discussion about the MFF have 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. The latest evidence of this are the recent events relating to the MFF for 2014-2020, where the European Council was first unable to reach a compromise on the EU budget, and then found a minimum

---

39 Ibid., par 26

40 See F Fabbrini, 'The Fiscal Compact, the "Golden Rule" and the Paradox of European Federalism', (2013) 38 *Boston College Int'l & C. L. Rev.* 1

41 European Parliament Resolution (n 34), Recommendation 2.4

level convergence which, by reducing the size of the overall budget, was voted down by the European Parliament.[42]

The asymmetry between the member states in size, wealth and economic performances, and the implication of this state of affairs on EU fiscal policy, however, has been magnified by the Euro-crisis. The intergovernmental method by which the Euro-crisis has been handled, and the wide recourse that member states have made to international agreements outside the EU legal order, have deepened the differences between the member states exacerbating the cleavage between creditor countries – states which have been net contributors to the newly created mechanisms of stabilization of the EMU – and debtor countries – states which have largely benefitted from financial transfer to address their fiscal troubles.[43] As it has been argued, the Euro-crisis and the responses to it have weakened the balance between member states and favored their polarization.[44] Member states which were net contributors to the rescue of the EMU have become increasingly impatient towards debtor states and as a result have demanded harsh programs of economic adjustments to assisted countries as a condition for further help. At the same time, member states which were net benefiters of rescue measures have become increasingly impatient toward creditor states and have perceived the austerity measures conditioning rescue packages as forms of hegemonic rule.

Yet, a system of fiscal governance which is unable to neutralize the challenge of asymmetry presents shortcomings, which threaten its capacity to endure in the long run. 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.'[45] 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.'[46] The unsustainability of a fiscal union based on financial transfers between member states has been acknowledged by multiple quarters. Expressing the concerns of creditor states, German Chancellor Merkel made clear in February 2012 that further steps toward closer economic ties in the EMU should not open the door toward a 'Transfer Union', with permanent payments from richer to poor states.[47] At the same time, among debtor states, discomfort has grown bigger for the harsh conditionality that has accompanied financial aids.[48] It is in light of this problem that calls have been made to disentangle the EMU fiscal capacity from the contributions of the member states and to connect

[42] European Parliament Resolution 'On the MFF', 13 March 2013, P7_TA(2013)0078, par 1
[43] See S Fabbrini, 'Intergovernmentalism and its Limits: Assessing the European Union's Answer to the Euro Crisis', (2013) 20 *Comparative Political Studies* 1
[44] See E Chiti & PG Teixeira, 'The Constitutional Implications of the European Responses to the Financial and Public Debt Crisis', (2013) 50 *CMLRev* 683
[45] Maduro (n 8), 18
[46] Ibid.
[47] See T Czuczka, 'Merkely Says Euro-Area Fiscal Union won't be "Transfer Union"', *Bloomb. News*, 7 February 2012
[48] See A Higgins, 'Europe Pressed to Reconsider Cuts as Cure', *The New York Times*, 27 April 2013

it, instead, with the wealth that the Union generates (e.g. through the functioning of the internal market).[49]

By breaking the wrong equation between fiscal capacity and inter-state transfers, the introduction of authentic EU taxes to feed a Euro-zone fiscal capacity would neutralize the challenge of asymmetries that exist in the EMU, while simultaneously contributing to a clearer justification of the project of European integration by pointing out to the European citizens what the EU does.[50] If a system of own resources independent from the financial contributions of the member states were in place, the Euro-zone fiscal capacity would avoid the difficulties that as of now characterize the debate about fiscal policy in the EU. From a strictly legal point of view, otherwise, it appears that the EU Treaties offer room for the introduction of EU taxes. A first acknowledgement of the competences of the EU in tax affairs is made in Article 113 TFEU which empowers the Council, acting unanimously and after consulting the European Parliament, to 'adopt provisions for the harmonisation of legislation concerning turnover taxes, excise duties and other forms of indirect taxation to the extent that such harmonisation is necessary to ensure the establishment and the functioning of the internal market and to avoid distortion of competition.' Yet, this clause, which is located in the TFEU's Title on Common rules on competition, taxation and the approximation of laws, is not directly finalized to the introduction of a new European tax, but rather to the harmonization of tax rates across the member states.

However, Article 311 TFEU states that '[t]he Union shall provide itself with the means necessary to attain its objectives and carry through its policies.' And although this clause, which is located in the TFEU's Tile on Financial Provisions, does not mention explicitly a taxing power for the EU, it affirms that '[w]ithout prejudice to other revenue, the budget shall be financed wholly from own resources.' Moreover, whereas the old text of Article 269 TCE only allowed the Council to lay down provisions relating to the system of own resources of the Community, which it shall recommend to the Member States for adoption in accordance with their respective constitutional requirements, the Lisbon Treaty has now modified Article 311 TFEU, enlarging the power of the Council to shape the own resources of the EU. Pursuant to Article 311(3) TFEU, in fact, 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. That decision shall not enter into force until it is approved by the Member States in accordance with their respective constitutional requirements.'

The exact interpretation of these provisions is a matter of debate among tax lawyers.[51] In principle, the Treaties could be construed restrictively, arguing that the own resources clause is intended simply to prohibit the member states from refusing to contribute to the budget of the Union. The Commission however has construed Article 311 TFEU in a more constructive manner and argued that, and, if combined with Article 133 TFEU, it could be read as granting to the EU the power to adopt new taxes for the benefit of the EU budget. In its June 2011 proposal for a Council

---

[49] See eg I Pernice et al, 'Challenges of Multi-Tier Governance in the European Union', Report commissioned by the European Parliament Constitutional Affairs Committee, PE 474.438 (2013)
[50] Ibid.
[51] See E Traversa & A Maitrot de la Motte, 'Le fédéralisme économique et la fiscalité dans l'Union européenne', paper presented at the Conference 'L'Union européenne et le fédéralisme économique', Paris, 21 June 2013

decision 'On the system of own resources of the EU,'[52] in fact, the Commission proposed to the Council to introduce as a new category of own resources under Article 311 TFEU a FTT, to be collected by the member states and transferred to the EU budget in lieu of other contributions currently in place. And in its subsequent proposal for a Council directive on a FTT,[53] 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 with the aim to feed the EU budget.

Nevertheless, it is clear that Articles 113 and 311 TFEU raise a new constitutional challenge on the road toward the establishment of a Euro-zone fiscal capacity. Pursuant to Article 113 TFEU, in fact, the adoption of any legal measure for the harmonization of tax laws must be taken by the Council *unanimously*. At the same time, under Article 311 TFEU the establishment of new own resources for the EU requires a *unanimous* decision by the Council – to be approved moreover by every member state in accordance with its constitutional requirement. The existence of a unanimity rule in the field of taxation places a formidable burden on the ability of the EU to make steps ahead in the process of European integration. Joseph Weiler famously emphasized how the 'shadow of the veto' shaped policy-making in the EU before the introduction of QMV.[54] As it has been stated, '[u]nder the prevailing unanimity rule in fiscal matters, an individual Member State can adamantly oppose to any surrender of tax sovereignty to the EU level.'[55] States opposition to EU taxation may be due to political reasons – such as the 'often visceral rejection of anything that suggests a federal state of affairs'[56] – but also on economic reasons, namely the preservation of state's interest in protecting the fiscal status quo.

In sum, the proposals in favor of a fiscal capacity for the Euro-zone inevitably pose the question of how to raise resources for an EMU budget. Because of the asymmetry of the EMU, it appears that a Euro-zone fiscal capacity could only be sustained by authentic EU revenues. But the taxing power of the EU is currently subject to a unanimity requirement, which renders the exercise of this revenue-raising authority virtually impossible. It is in this context that resort to enhanced cooperation emerged as an option to get out of the EU conundrum in taxing affairs. The case of the FTT provides the emblematic example in this regard.

4. Enhanced cooperation for the introduction of a FTT

The debate about the introduction of a FTT – originally proposed by US economist James Tobin in the 1970s – saw a rise in popularity in the aftermath of the financial crisis of 2008.[57] The International Monetary Fund (IMF) discussed the option of a FTT in a 2010 report,[58] and the

[52] Commission Proposal for a Council Decision 'On the System of Own Resources of the EU', 29 June 2011, COM(2011)510 final
[53] Commission Proposal (n 3)
[54] See JHH Weiler, 'The Transformations of Europe', (1991) 100 *Yale LJ* 2423
[55] S Plasschaert, 'Towards an Own Resource for the European Union? Why? How? And When?', [2004] *European Taxation* 470, 476
[56] Ibid.
[57] See A Seely, 'The Tobin Tax: Recent Developments', House of Commons Library, SN6184, 11 September 2013
[58] IMF, 'A Fair and Substantial Contribution by the Financial Sector: Interim Report for the G20', April 2010

theme was raised by member states of the Group of 20 (G20) the following year.[59] While the debate at the international level did not lead to any concrete step toward the introduction of a global FTT, a number of EU member states unilaterally decided to enact FTT at the national level.[60] It is in this context that in September 2011 the Commission tabled a proposal for a Council directive on a common system of FTT to be applied throughout the EU.[61] The Commission proposal was based on Article 113 TFEU and, bearing in mind the increasing number of uncoordinated national tax measures being put in place, sought the harmonization of FTT across the EU with the aim to avoid fragmentation in the internal market for financial services.[62]

The Commission proposal, however, was the object of prolonged discussion in the Council and met the fierce opposition by several member states wary of introducing legislation which would affect their financial markets.[63] Eventually, in June 2012 the European Council had to acknowledge that the differences between the member states were unbridgeable and that 'the proposal for a FTT will not be adopted by the Council within a reasonable time.'[64] Given the impossibility to reach consensus in the Council on the introduction of a FTT, in September 2012 eleven member states – Belgium, Germany, Estonia, Greece, Spain, France, Italy, Austria, Portugal, Slovenia and Slovakia – requested to make use of the enhanced cooperation procedure to introduce a FTT among themselves. The enhanced cooperation procedure is a tool, originally introduced by the Amsterdam Treaty and subsequently revised by the Lisbon Treaty, which allows a vanguard group of at least nine member states to embark upon a project of differentiated integration in fields which are not yet ripe for common action by all EU member states.[65] Pursuant to the EU treaties, the activation of an enhanced cooperation requires a number of procedural steps which involve all the main EU institutions. In October 2012, the Commission proposed a Council decision authorizing enhanced cooperation.[66] The European Parliament consented to this in December 2012,[67] and the Council authorized the cooperation by QMV in January 2013.[68]

On the basis of this, in February 2012 the Commission published a proposal for a Council directive implementing enhanced cooperation in the area of FTT.[69] The February 2012 Commission proposal for the introduction of a FTT largely mirrors the original proposal of September 2011 and, according to the Explanatory Memorandum, would lead to expected revenues of roughly 31 billion Euros annually for the eleven member states that are party to enhanced cooperation.[70] As the first recital to the draft directive makes clear, the proposal for the introduction of a FTT springs from the ongoing debate 'at all levels on additional taxation of the financial sector. [It…]

[59] G20, Cannes Summit Final Declaration, 4 November 2011, par 82
[60] See e.g., France : Art. 5, Loi n° 2012-354, J.O.R.F. n° 64 du 15 mars 2012, 4690. See now also Italy: Art. 1(491), Legge n. 228 del 24 dicembre 2012, G.U.R.I. n. 302 del 29 dicembre 2012.
[61] Commission Proposal (n 3)
[62] Ibid.
[63] See 'Europe's Financial Transaction Tax: Oops', *The Economist*, 27 April 2013
[64] European Council Conclusions, 28 June 2012, EUCO 76/12, 13
[65] See also D Thym, 'The Political Character of Supranational Differentiation', (2006) 31 *ELRev* 781
[66] Commission Proposal for a Council Decision 'Authorizing Enhanced Cooperation in the Area of FTT', 25 October 2012, COM(2012)631 final/2
[67] European Parliament Legislative Resolution, 'On the Proposal for a Council Decision Authorizing Enhanced Cooperation in the Area of the Creation of a FTT', 12 December 2012, P7_TA(2012)0498
[68] Council Decision 2013/52/EU, [2013] OJ L 22/11
[69] Commission Proposal (n 4)
[70] Ibid., 14

originates from the desire to ensure that the financial sector fairly and substantially contributes to the costs of the crisis and that it is taxed in a fair way vis-à-vis other sectors for the future, to dis-incentivise excessively risky activities by financial institutions, to complement regulatory measures aimed at avoiding future crises and to generate additional revenue for general budgets or specific policy purposes.'

Pursuant to Article 2(2) of the proposal, a financial transaction is to be intended as any purchase and sale of a financial instrument before netting or settlement; transfer between entities of a group of the right to dispose of a financial instrument as owner and any equivalent operation implying the transfer of the risk associated with the financial instrument; conclusion of derivatives contracts before netting or settlement; exchange of financial instruments; repurchase agreement, reverse repurchase agreement, securities lending and borrowing agreement. The institutions subject to the payment of the FTT include, according to Article 2(8) of the Commission proposal, investment firms, regulated markets, credit institutions, insurance undertakings, pension funds, alternative investment funds, securitization vehicles and special purpose vehicles. Moreover the tax applies to any undertaking, institution, body or person trading with respect to any financial instrument, acquiring holdings in undertakings and participating or issuing financial instruments, provided the average value of the financial transactions constitute more than 50% of its overall average net annual turnover.

Articles 3 and 4 constitute the central provisions of the Commission proposal, outlining the scope of application of the directive. According to Article 3(1) '[t]his Directive shall apply to all financial transactions, on the condition that at least one party to the transaction is established in the territory of a participating Member State and that a financial institution established in the territory of a participating Member State is party to the transaction, acting either for its own account or for the account of another person, or is acting in the name of a party to the transaction.' With the aim to prevent the FTT from negatively affecting either 'the refinancing possibilities of financial institutions and states, []or monetary policies in general or public debt management,'[71] Article 3(4) excludes from the scope of the directive transactions on the primary market, with the ECB or the central banks of the member states, with the EU, the EFSF, the ESM, the EIB, and other international organizations and bodies. Pursuant to Article 4, 'a financial institution shall be deemed to be established in the territory of a participating Member State where any of the following conditions is fulfilled: (a) it has been authorised by the authorities of that Member State to act as such, in respect of transactions covered by that authorisation; (b) it is authorised or otherwise entitled to operate, from abroad, as financial institution in regard to the territory of that Member State [...]; (c) it has its registered seat within that Member State; (d) its permanent address or [...] its usual residence is located in that Member State; (e) it has a branch within that Member State [...]; (f) it is party, acting either for its own account or for the account of another person, or is acting in the name of a party to the transaction, to a financial transaction with another financial institution established in that Member State pursuant to points (a), (b), (c), (d) or (e) [...] ; (g) it is party [...] to a financial transaction in a structured product [...] issued within the territory of that Member State [...].'

---

[71] Ibid., 9

As indicated in Article 5, '[t]he FTT shall become chargeable for each financial transaction at the moment it occurs.' The Commission proposal, instead, differentiates the FTT rates to be applied in the case of transactions related to derivative contracts (Article 7) and transactions other than those related to derivative contracts (Article 6): according to Article 9(2), the rates shall be no lower than '0.1% in respect of the financial transactions referred to in Article 6; [and] 0.01% in respect of financial transactions referred to in Article 7.' Member states remain free to enact tax rates higher than the EU minima. Pursuant to Article 15, however, '[t]he participating Member States shall not maintain or introduce taxes on financial transactions other than the FTT object of this Directive.' The Commission proposal then includes a set of provisions aimed at minimizing tax evasion, avoidance and abuse. As indicated in Article 10(1), the 'FTT shall be payable to the tax authorities of the participating Member State in the territory of which the financial institution is deemed to be established.' Article 11(5) then prescribes that the FTT shall be paid to the participating member state 'at the moment when the tax becomes chargeable in case the transaction is carried out electronically; [and] within three working days from the moment the tax becomes chargeable in all other cases.' Articles 12 and 13 call the states to adopt measure to prevent tax fraud or arrangements that defeat 'the object, spirit and purpose' of the FTT. Article 19, finally, introduces a review clause asking the Commission to examine in three years 'the impact of the FTT on the proper functioning of the internal market, the financial markets and the real economy.'

While Article 20 of the Commission proposal ambitiously planned the entry into force of the FTT in January 2014 for the eleven states participating to the enhanced cooperation, it is unlikely this target will be reached. The Commission proposal received in July 2013 the endorsement of the EU Parliament – which however has only a consultative role in the procedure.[72] Yet, as mentioned, in April 2013 the UK brought legal proceedings in front of the CJEU against the decision of the Council to authorize the use of enhanced cooperation for the introduction of a FTT.[73] Moreover, in September 2013, the Legal Service of the Council of the EU leaked a confidential opinion questioning the legality of the scope of application of the Commission proposal.[74] Both these event raise important questions about the use of enhanced cooperation for the adoption of a FTT, which need now to be addressed.

5. Enhanced cooperation for the introduction of a FTT: legal questions

The use of enhanced cooperation for the introduction of a FTT raises a number of critical legal questions. Besides setting a plurality of procedural rules, the EU Treaties foresee resort to enhanced cooperation subject to several substantive requirements.[75] Furthermore, in the recent

[72] European Parliament Legislative Resolution, 'On the Proposal for a Council Directive Implementing Enhanced Cooperation in the Area of FTT', 3 July 2013, P7_TA(2013)0312. See also European Economic and Social Committee Opinion, 'On the Proposal for a Council Directive Implementing Enhanced Cooperation in the Area of FTT', 19 September 2013, 2013/0045(CNS) ('welcom[ing] the proposal put forward by the Commission.')
[73] Application (n 5)
[74] Opinion of the Legal Service (n 6)
[75] Ed. Comments, 'Enhanced Cooperation: A Union *à taille réduite* or *à porte tournante*?', (2011) 48 *CMLRev* 317

April 2013 Grand Chamber decision in *Spain & Italy v. Council of the EU*,[76] dealing with enhanced cooperation in the field of unitary patent, the CJEU provided new insights to evaluate the legality of the use of enhanced cooperation in the framework of EU law. In what follows, I will focus on the substantive constraints that surround resort to enhanced cooperation and I will suggest that three main tests must be met for a decision on enhanced cooperation to pass muster. For labeling purposes, I will call the first: the 'constitutional test', the second: the 'internal market test'; and the third 'the non-affectation test'. As I will argue, the use of enhanced cooperation for the introduction of the FTT easily meets the first and second tests. At the same time, I will claim that – contrary to the opinion of the UK and the Council Legal Service – both the Council decision authorizing enhanced cooperation and the Commission draft directive implementing enhanced cooperation comply with the third test.

The first substantive test that enhanced cooperation must meet is the 'constitutional test'. Although the EU Treaties give only a very sketchy explanation of the constitutional function of enhanced cooperation – Article 20 TEU stating that enhanced cooperation 'shall aim to further the objectives of the Union, protect its interests and reinforce its integration process' – I have argued elsewhere that the history of the introduction of this mechanism in the EU Treaties and a systematic interpretation of the provisions regulating its use, suggest that enhanced cooperation aims to create a pathway through which a 'vanguard group' of states can move ahead in achieving an 'ever closer Union' in new policy areas.[77] Because enhanced cooperation is not simply a tool to ensure flexibility and differentiation in an enlarging EU, but is actually designed to achieve a specific goal, namely greater *integration* among a group of EU Member States, I suggested that Member States can activate an enhanced cooperation when they disagree *whether* to act jointly at the EU level. On the contrary, the procedure cannot be used when Member States agree on the opportunity of expanding integration into a new legal field but disagree on *how* to act at the EU level.[78]

In its first decision dealing with the legality of the use of enhanced cooperation the CJEU embraced a broader understanding of the function of enhanced cooperation. Rejecting the plea raised by Spain and Italy that the use of enhanced cooperation for the introduction of a unitary EU patent constituted misuse of power, the CJEU held that the use of enhanced cooperation was not restricted only to cases where 'at least one Member State declares that it is not yet ready to take part in a legislative action of the Union in its entirety.'[79] On the contrary, according to the CJEU, 'the situation that may lawfully lead to enhanced cooperation is that in which "the objectives of such cooperation cannot be attained within a reasonable period by the Union as a whole". The impossibility referred to in that provision may be due to various causes, for example, lack of interest on the part of one or more Member States or the inability of the Member States,

[76] Judgment (n 7)
[77] F Fabbrini, 'Enhanced Cooperation Under Scrutiny: Revisiting the Law and Practice of Multi-Speed Integration in Light of the First Involvement of the EU Judiciary', (2013) 40 *Legal Issues Economic Integration* 197
[78] Ibid 208
[79] Judgment (n 7), par 36

who have all shown themselves interested in the adoption of an arrangement at Union level, to reach agreement on the content of that arrangement.'[80]

With this reasoning the CJEU *de facto* gave up on its task to scrutinize the reasons why states decide to resort to enhanced cooperation – a conclusion that I have criticized for failing to protect the integrity of the EU legal order and prevent circumvention of EU Treaty rules.[81] Whatever one's view of the appropriateness of the CJEU's approach, however, it seems undisputed that the use of enhanced cooperation in the case of the FTT is compatible with the 'constitutional test' that allows member states to use enhanced cooperation when a 'vanguard group' of Member States wants to move forward in the project of EU integration while others consciously decided to step back. The UK and several other EU member states had indicated clearly their opposition *tout court* toward the adoption of EU rules in the area of FTT.[82] Contrary to the case of enhanced cooperation for the establishment of a EU patent – where Italy and Spain did not disagree with the other member states on the opportunity to introduce a EU patent protection system, but rather disagreed with the other member states on how do so (namely: what languages to use) – in the case of the FTT the opposition of the UK goes to the very heart of the proposal to enact harmonizing measures at the EU level to introduce a common system of FTT.[83] In this state of affairs, the use of enhanced cooperation by eleven member states is legitimate.

The second test that the use of enhanced cooperation must meet is the 'internal market test'. Pursuant to Article 326 TFEU, in fact, 'enhanced cooperation shall comply with the Treaties and Union law. Such cooperation shall not undermine the internal market or economic, social and territorial cohesion. It shall not constitute a barrier to or discrimination in trade between Member States, nor shall it distort competition between them.' In its judgment in *Spain & Italy v. Council of the EU*, the CJEU did not dwell at length on the meaning of Article 327 TFEU, rejecting the plea of the applicant state on the argument that 'it cannot validly be maintained that, by having it in view to create a unitary patent applicable in the participating Member States and not in the Union, the contested decision damages the internal market or the economic, social and territorial cohesion of the Union.'[84] The matter was however addressed in greater depth by Advocate General (AG) Bot in his opinion of December 2012.[85] There the AG stated that there was no evidence that the decision authorizing the use of enhanced cooperation in the field of unitary patent would undermine the internal market or economic, social and territorial cohesion. In fact, according to the AG, 'it would do precisely the opposite'.[86] Citing the impact assessment of the Commission, the AG emphasized how 'a mechanism intended to create a unitary patent entailing uniform protection on the territory of several Member States contribute[d] to the harmonious

[80] Ibid
[81] Fabbrini (n 77) 220
[82] See Council of the EU, PRESSE 23, 22 January 2013 (indicating that the decision authorizing enhanced cooperation for the introduction of a financial transaction tax was adopted by qualified majority, with the abstention of the UK, the Czech Republic, Luxembourg and Malta, all of which declared their opposition to the adoption of common EU rules in the field)
[83] See also HC Debate, 16 October 2012, cc11-12 WS (UK Chancellor of the Exchequer G Osborn stating in the House of Commons that 'the UK would not be joining' enhanced cooperation for a FTT)
[84] Judgment (n 7), par 75
[85] Joined Cases C-274/11 and C-295/11, *Spain & Italy v. Council*, Opinion of 11 December 2012
[86] Ibid., par 143

development of the Union as a whole, since it ha[d] the consequence of reducing the existing disparities between those Member States'.[87]

The opinion of the AG suggests that the EU judiciary is employing a comparative test to evaluate whether the use of enhanced cooperation violates the provision of Article 326 TFEU. Under this test, an enhanced cooperation is regarded as legitimate when it *does not worsen* the (already existing) fragmentation of the internal market. On the contrary, enhanced cooperation would not be authorized if it *worsened* the status quo, e.g. by introducing new obstacles to the functioning of the EU internal market. In the case of the enhanced cooperation for a unitary patent, the AG underlined how, until then, twenty-seven different national patent systems coexisted within the EU, fragmenting the internal market,[88] and how, instead, enhanced cooperation 'relating to the creation of a unitary patent producing uniform effects on the territory of […] 25 Member States, necessarily help[ed] to improve the functioning of the internal market and to reduce barriers to trade and also the distortion of competition between the Member States.'[89] Applying *mutatis mutandis* this reasoning to the case of FTT, it appears that also in this context the use of enhanced cooperation meets the 'internal market test'. As of today, EU member states are free to adopt national FTT – and some of them have.[90] This has an impact on the functioning of the internal market. By introducing a common system for the member states that participate to the enhanced cooperation, the proposal for a FTT reduces the differences in the regulatory regimes in place across the EU member states. As such, while the use of enhanced cooperation does not resolve the problem of the fragmentation of the internal market, it certainly does not worsen it either. Rather, it creates a more consistent regulatory framework at least for all those states which are party to the cooperation. Hence, the proposal for a FTT via enhanced cooperation meets also the 'internal market test'.

The third core substantive test that the use of enhanced cooperation must pass is then the 'non-affectation test'. Pursuant to Article 327 TFEU 'enhanced cooperation shall respect the competences, rights and obligations of those Member States which do not participate in it.' Surprisingly, the 'non-affectation test' seems to be at the heart of the proceedings brought by the UK in front of the CJEU with regard to the legality of the Council decision authorizing enhanced cooperation in the area of FTT.[91] Nevertheless, the question whether enhanced cooperation affects in an impermissible manner the competences, rights and obligations of those member states which do not participate to it, hardly arises in the decision of the Council which *simply* authorizes enhanced cooperation. Rather, the question will only arise once the member states which are party to enhanced cooperation exercise their power within this framework: it is in fact the legal act adopted by the EU member states participating to enhanced cooperation that might adversely affect non-participating member states. This point emerges plainly from the judgment of *Spain & Italy v. Council of the EU*, where the CJEU, following in AG Bot's footsteps, discarded as

---

[87] Ibid., par 151
[88] Ibid., par 144
[89] Ibid., par 149
[90] See supra n 60
[91] Council of the EU, Information Note of the Legal Service, JUR 264, 24 May 2013, par 2 (Council Legal Service reporting that the grounds of the challenge of the UK before the CJEU are that 'the Authorizing Decision is unlawful because it authorises the adoption of a [FTT] with extraterritorial effects which is contrary to Article 327 TFEU [...].')

inadmissible at that stage the plea raised by the applicant states which concerned the substance of the future measures to be adopted in the framework of enhanced cooperation.[92]

In light of the above, it would seem inevitable to conclude that the UK challenge before the CJEU is bound to meet an inadmissibility decision, because it concerns a question that has nothing to do with the Council decision *authorizing* enhanced cooperation in the area of the FTT, but rather concerns the substance of the Commission proposal for a Council directive *implementing* enhanced cooperation in the area of the FTT. However, because the question whether the FTT designed by the Commission is liable to infringe the 'non-affectation test' was at the core of the leaked opinion of the Council Legal Service, it is appropriate to consider here already whether the worries raised by the UK and the legal experts of the Council have any foundation. In its leaked document, the Legal Service of the Council took issue especially with Article 4(1) point f) of the Commission proposal, which introduces a so-called 'counter-party' principle which makes subject to the FTT also financial institutions established outside the FTT-zone which transact with financial institutions established within the FTT-zone.[93] As was mentioned in the previous Section, Article 4(1) of the Commission proposal sets a number of connecting factors to regulate the scope of application of the FTT: the FTT is chargeable to any financial institution which is either resident in the FTT-zone (residence principle: Article 4(1), points a) to d)), or is party to a financial transaction in structured products issued within the FTT-zone (issuance principle: Article 4(1) point g)), or to transacts with an institution of the FTT-zone (Article 4(1) point f)).

According to the Council Legal Service, by deeming established within the FTT-zone a financial institution resident outside the member states party to the cooperation when it interacts with a financial institution resident within the member states of the cooperation, Article 4(1) point f) of the Commission draft violates a number of legal tenets – which ultimately concern the 'non affectation test'. In the Legal Service's view: First, Article 4(1) point f) raises issues of 'extraterritorial exercise of jurisdiction'[94], since it would impose tax obligations 'over entities located outside the geographical area concerned by the legislation adopted under the enhanced cooperation.'[95] Second, it threatens different treatment of resident and non-resident financial institutions as to the connecting factors applied, by discriminating against financial institutions that are not resident in the participating state.[96] Third, it infringes the right of the non-participating member states by limiting their capacity 'to maintain or adopt their own tax system.'[97] Fourth, it distorts competition between the member states.[98] And fifth, it would hinder free movement of capital, by producing 'an effect equivalent to that of a duty imposed in return of the possibility to enter into a transaction with an institution located in a participating Member State.'[99]

The criticisms of the Council Legal Service do not appear convincing. First, the concern that the 'counter-party' principle results in an extra-territorial application of tax jurisdiction, fails to notice

[92] Judgment (n 7), par 76
[93] Opinion of the Legal Service (n 6)
[94] Ibid., par 17
[95] Ibid., par 18
[96] Ibid., par 26
[97] Ibid., par 35
[98] Ibid., par 39
[99] Ibid., par 40

that Article 4(1) point f) of the Commission proposal valorizes a clear connecting factor: once a financial institution resident outside the FTT-zone transacts with a financial institution resident within the FTT-zone, *it shall pay the FTT*. This customarily occurs in tax legislation. To put it with an example: if a British citizen purchases wine from an Italian producer, he/she will be subject to Italian VAT – regardless of where he is resident, of course. Why would rules have to be different where a transaction involved financial institutions and concern financial instruments? The nature of the economic operation is diverse, but the underlying logic is the same: once someone does business with the FTT-zone, it can be taxed by it. Second, the Council Legal Service argues that Article 4(1) point f) has a discriminatory effect between transactions involving financial institutions which are resident in the FTT-zone, and institutions which are not. In fact, however, the very opposite is true. The end result of the rule designed in the Commission proposal is that *every financial institution transacting within the FTT will be taxed*. Discrimination would instead emerge if the Commission were to exempt from the FTT financial institutions resident outside the FTT-zone, but transacting within it – as the Council Legal Service suggests. In this case, institutions established outside the FTT could do business within the FTT without having to bear the tax costs that apply to institutions resident within the FTT. Third, the Council Legal Service contends that Article 4(1) point f) interferes with the tax jurisdiction of non-participating member states. This is untrue: financial institutions established outside the FTT-zone and which do not do business with the FTT-zone, are not subject to the FTT. Non-participating member states are free to regulate and tax operations occurring outside the FTT-zone as they see fit, and it is only the autonomous choice of economic actors outside the FTT-zone to transact with financial institutions within the FTT-zone that brings them under the scope of application of the FTT. Which leads us to the last points raised by the Council Legal Service: namely, that Article 4(1) point f) distorts competition and hinders free movement of capital. However, bluntly put: this argument is not a legal one. Chicago School economists have developed economic arguments to claim that taxes are costs that burden the functioning of the financial markets – but no legal principle prevents sovereign states to introduce (even stupid) taxes if they democratically decide so. Every tax may affect the functioning of the market, and the FTT is no exception. However, this does not prohibit states from introducing an FTT, either severally or jointly through the form of enhanced cooperation.

All in all, therefore, it seems that the legal questions raised about the legality of resort to enhanced cooperation for the introduction of a FTT can be set aside. The Council decision authorizing the use of enhanced cooperation in the area of FTT, as well as the follow-up draft Commission proposal for a Council directive implementing enhanced cooperation in the area of FTT, meet the 'constitutional test', the 'internal market test' and the 'non-affectation test'. In particular, the concerns that animate the legal challenges of the UK before the CJEU and the leaked opinion of the Council Legal Service do not withstand attentive legal scrutiny. Yet, the legality of enhanced cooperation in the area of FTT tells us nothing about the political challenges that this option faces, due to the interaction between taxing and spending in the EMU. I shall now turn to this question.

6. Enhanced cooperation for the introduction of a FTT: political questions

Whereas the use of enhanced cooperation to introduce a FTT withstands legal scrutiny, the adoption of the FTT by a limited number of EU member states raises several political questions. These become evident if we return to the starting point of the analysis: namely, the relationship between taxing and spending in the Euro-zone. Since the beginning, the proposals to endow the EMU with a fiscal capacity and those to introduce authentic EU taxes were linked. As explained in Section 3, raising revenues at the EU level was seen as the necessary step to establish a real budgetary power in the Euro-zone and liberate the EMU fiscal policy from the recriminations that to these days characterize fiscal transfers between the member states. As argued by Miguel Maduro, the introduction of EU taxes – be it the FTT, or alternatively, a carbon emission tax or an EU corporate tax – 'will not only provide [the EU] with the funds necessary to support [a] budget increase but will contribute to a clearer justification of the project of European integration. [...] It is essential that the Union is seen as redistributing the Union wealth and not the wealth of some states.'[100] However, the introduction of a FTT by only *some* member states – eleven out of seventeen of the Euro-zone – makes it politically difficult to direct the revenues levied through the FTT into common spending for *all* the EMU.

This state of affairs is reflected in the changing destination envisioned for the FTT by the Commission. While the original November 2011 Commission proposal for a Council directive on the FTT clearly linked the introduction of the FTT to the creation of 'a new own resource to be entered into the budget of the EU,'[101] the new February 2013 proposal, taking stock of the fact that only a few member states will introduce the FTT via enhanced cooperation, proposes less ambitiously that 'part of the receipts generated by the FTT shall constitute an own resource' reducing the direct contribution by these member states.[102] As explained in the Legislative Financial Statement annexed to the proposal, the Commission envisioned that 'levying FTT would facilitate efforts of budgetary consolidation in the participating member states.'[103] Yet, the FTT could at best replace other forms of direct contribution that the member states currently make to the EU budget, with 'their GNI-based national contributions [being] reduced.'[104] Hence, although the European Council had noted in February 2013 the use of enhanced cooperation for the introduction of the FTT and invited the participating member states to examine if the FTT could become the basis for a new own resource for the EU budget, without impacting non-participating member states,[105] the Commission proposal retreated to a position in which the FTT will accrue the member states' budget and used at best to replace other forms of national contributions to the EU budget.

This seems an inevitable choice, as acknowledged also by the EU Parliament in its legislative resolution of July 2013.[106] Commenting in its consultative role the February 2013 Commission proposal for the implementation of enhanced cooperation in the area of FTT, the Parliament

[100] Maduro (n 8), 21
[101] Commission Proposal (n 3), 3
[102] Commission Proposal (n 4), 4
[103] Ibid., 33
[104] Ibid.
[105] European Council Conclusions, 8 February 2013, EUCO 37/13, para 115
[106] European Parliament Legislative Resolution (n 72)

underlined how '[t]he use of FTT revenue as Union own resources is possible under the enhanced cooperation procedure only if national contributions of participating Member States to the Union budget could be reduced by the same amount and would avoid the disproportionate contribution by participating Member States compared to non-participating Member States.'[107] At the same time, the Parliament expressed its wish that things could change in the long-term, holding that '[o]nce FTT is implemented at Union level, all or part of the amount of the own resources originating from FTT should be added to the national contributions of the Member States in order to gather new funding sources for European investment without a reduction of the national contributions of the participating Member States to the Union budget.'[108]

Of course, if at least all the member states of the Euro-zone were participating to the enhanced cooperation, the resources raised with a FTT could be set aside in a special Euro-zone fund, functioning as the bulk of the fiscal capacity proposed in the high-level policy documents discussed in Section 2. However, the refusal to join an enhanced cooperation in the area of FTT did not come only from the UK, or other member states outside the Euro-zone: Cyprus, Finland, Ireland, Luxembourg, Malta and the Netherlands – countries within the Euro-zone which embrace a lighter taxing and regulatory framework toward the banking sector, or simply oppose further EU integration in the fiscal arena – refused to be involved in raising the FTT.[109] It would therefore be politically difficult to justify the use of resources gathered within the FTT-zone to address, say, risks of bank failures in Cyprus of high unemployment rates in Ireland (two hypotheses which are far from imaginary). At the same time, while proposals have been made to create a special fund among the eleven member states of the FTT-zone to be used for the common benefits of the members only,[110] it is clear that such a step would require a political agreement – which is hardly likely to take place given the eagerness of the participating member states to use the income of the FTT to fill up their depleted coffers.[111]

In conclusion, if the use of enhanced cooperation to adopt a FTT appears legally sound, it makes it politically difficult to establish an EMU fiscal capacity endowed with own resources. Although, as it has been stated, '[t]he political difficulties in the way of a genuine EU tax [...] could, in principle, be overcome if a substantial number of Member States were to muster the political will to move ahead, conceivably within the "enhanced cooperation" framework, thus sidestepping the unanimity rule which remains staunchly defended by a few member states,'[112] the relationship between taxing and spending undermines the ability of enhanced cooperation in the area of FTT to provide the financial resources needed for a Euro-zone fiscal capacity. From this point of view, it looks that, after more than ten years, the recommendations of the European Convention Working Group VI on Economic Governance remain viable: 'some changes should be made to the

107 Ibid., Amendment 2
108 Ibid.
109 See C Grant, 'Britain Could Reshape Europe, if it Only Tried', *The Financial Times*, 14 May 2013 (outlining arguments for opposition to the FTT in several Euro-zone member states)
110 See A Majocchi, 'A European Fund for Growth and Development', *The New Federalist*, 30 June 2013
111 See D Pesole, 'Ora Roma teme riflessi sul debito', *Il Sole 24 Ore*, 14 February 2013 (explaining that the Italian government has already committed the income of the FTT to its domestic budget)
112 Plasschaert (n 55) 479

existing decision-making procedures in order to facilitate progress in the area of fiscal policy' through the use of QMV.[113]

At the same time, another political difficulty has to do with the role of the EU Parliament. As things stand, the institution directly representing the EU citizens has only a consultative role in tax matters. In its resolution authorizing the use of enhanced cooperation for the introduction of the FTT, the Parliament complained of this state of affairs and called the Council to enhance the role of the Parliament in decision-making related to taxation through the use of the '*passerelle* clause'. As the Parliament emphasized, on the basis of Article 333(2) TFEU '[w]here a provision of the Treaties which may be applied in the context of enhanced cooperation stipulates that the Council shall adopt acts under a special legislative procedure, the Council, acting unanimously […] may adopt a decision stipulating that it will act under the ordinary legislative procedure.' Hence, the Parliament 'call[ed] on the Council to adopt a decision pursuant to Article 333(2) TFEU, stipulating that when it comes to the proposal for a Council Directive implementing enhanced cooperation in the area of FTT pursuant to Article 113 TFEU, it will act under the ordinary legislative procedure.'[114] Yet, resort to the '*passerelle* clause' depends on a political decision of the member states in the Council. Once again, therefore, political challenges lie on the way toward a fiscal capacity which is not only grounded on common resources, but also consistent with constitutional principles of 'no taxation without representation'.[115]

7. Conclusion

The paper examined the recent proposals to endow the Euro-zone with a fiscal capacity and explained how this requires raising new EU own resources. It analyzed the draft legislation on the FTT and discussed its introduction by eleven Euro-zone countries through the use of enhanced cooperation given the absence of consensus among all the EU member states. Resort to enhanced cooperation in the area of FTT has been the object of legal challenges but this paper set them aside. Enhanced cooperation for the introduction of the FTT is compatible with the constitutional function of this instrument, does not unlawfully interfere with the functioning of the internal market and leaves unaffected the rights and privileges of the non-participating member states – so it is legal. However, the paper noticed that resort to enhanced cooperation for the adoption of the FTT complicates the possibility to use the revenues of the FTT for common EMU spending. Because taxing and spending are two sides of the same coin, levying the FTT in eleven countries of the Euro-zone undermines the possibility to appropriate the FTT revenues for the benefit of a common Euro-zone budget. The proposals to create a fiscal capacity outlined in the report of the European Council President and in the blueprint of the Commission are part of a broader road-map of reforms of the EMU. In the end, this paper suggests that a fiscal capacity – a much needed improvement to manage the interdependences that exist in the Euro-zone – cannot be severed from an enhanced EMU governance framework in fiscal affairs. Common spending requires the capacity to levy taxes, but also QMV and 'no taxation without representation'.

---

[113] European Convention, Working Group VI on Economic Governance, Final Report, 21 October 2002, CONV 357/02, WG VI 17, 6

[114] European Parliament Legislative Resolution (n 67), par 2

[115] See also B Ackerman, 'Taxation and the Constitution', (1999) 99 *Columbia LRev* 1

Ultimately Fiscal Union demands Political Union. While so far resort to enhanced cooperation to adopt a FTT is wholly acceptable from a legal point of view, further institutional reforms are needed in political terms to re-unite taxing and spending at the supranational level and establish a deeper and more genuine EMU.

CENTRE FOR STUDIES ON FEDERALISM
Via Real Collegio 30, 10024 Moncalieri (TO) - Italy
Tel. +39 011 670 5024 Fax. +39 011 670 5081
www.csfederalismo.it info@csfederalismo.it