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The Power of Adversity: How External Challenges Drove the European Fiscal Integration

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"The structure of the United States of Europe will be such as to make the material strength of a single State less important. Small nations will count as much as large ones and gain their honour by a contribution to the common cause [...] But I must give you warning, time may be short. At present there is a breathing space. The cannons have ceased firing. The fighting has stopped. But the dangers have not stopped. If we are to form a United States of Europe, or whatever name it may take, we must begin now. In these present days we dwell strangely and precariously under the shield, and I even say protection, of the atomic bomb. The atomic bomb is still only in the hands of a nation which, we know, will never use it except in the cause of right and freedom, but it may well be that in a few years this awful agency of destruction will be widespread and that the catastrophe following from its use by several warring nations will not only bring to an end all that we call civilisation but may possibly disintegrate the globe itself. [...] . If at first all the States of Europe are not willing or able to join a union we must nevertheless proceed to assemble and combine those who will and who can. The salvation of the common people of every race and every land from war and servitude must be established on solid foundations and must be created by the readiness of all men and women to die rather than to submit to tyranny. In this urgent work France and Germany must take the lead together. Great Britain, the British Commonwealth of Nations, mighty America - and, I trust, Soviet Russia, for then indeed all would be well - must be the friends and sponsors of the new Europe and must champion its right to live. Therefore I say to you "Let Europe arise!".

-Winston Churchill, speech delivered at the University of Zurich, 19 September 1946.

Introduction

On September 1946, at the Zurich University, Winston Churchill used for the first time the term "United States of Europe", highlighting the importance of creating a union of nations based on economic and political cooperation able to assure security and prosperity. At that time the priority was to construct a feeling of self-identification with the European family in order to avoid the spectrum of new wars. Today, after almost 80 years, a lot has changed. The European Union is an international organization that counts 27 members States (28 before Churchill's home-country left) which has experienced almost 70 years of peace since its foundation while the meaning of "United States of Europe" has changed. The new objective promoted by some European leaders and contested by others is called "Federalism" and implies the complete integration of the national economies in addition to the already done monetary union.

According to the former head of the ECB and former Italian Prime Minister Mario Draghi, the European citizens nowadays are more prepared for a major integration compared to 20 years ago[1]. The ultimate objective to achieve should be a common financial policy within the eurozone which would assure more independence to the Union. The result of the last two decades of economic, health and geopolitical crisis is the acknowledgement that the external dependance for security, manufacturing products and energy has become insufficient and unreliable[2]. The EU's framework requires several transitions and changes which are unsustainable by the single Member States themselves asking a common orientation towards the same priorities to be pursued with communitarian instruments and resources. However, this is not the first time that the European Union is encouraged towards more integrations by external factors. We could say that the same birth of the European Community in 1957 was generated by the necessity of creating a free economic market which would simplify the movement of people and goods for the Europe's reconstruction after war. Then, at the end of the 80s, the European Union decided to implement the European Common Market by unifying the monetary system. Today there are 20 countries out of 27 within the euro-area whose monetary policy is decided at the Communitarian level by the European Central Bank (ECB). However, the management of the fiscal policies is left at the national level whose coordination, until the 2011, was assured only by the convergence towards the Maastricht criteria established in 1992 and then by the Stability and Growth Pact (SGP), signed in June 1997. The surveillance mechanism has been implemented after the economic crisis by strengthening the preventive and corrective arm

[1] Cantarini, Simone. "Per Draghi è Necessaria Una Revisione Dei Trattati UE E l'Avvio Di Un "Genuino" Processo Politico." *Euractiv.it*, EURACTIV
[2] Draghi, M. (2023) *Mario Draghi on the path to fiscal union in the Euro Zone*, *The Economist*.

with the institution of the “Six-Pack” and “Two-Pack” legislative measures. Furthermore, in order to sustain the economic architecture of the most affected Member States, it has been established the European Stability Mechanism (ESM), which is considered the first attempt to provide instruments for the common management of fiscal policies. Nonetheless, the fiscal situation of the EU is still fragmented, this results in different responses to same external threats, underlining a heterogeneity of economic soundness. This issue has generated great internal division when two important crises erupted, the Pandemic crisis in 2020 and the energy crisis in 2022. The first one highlighted conflicts of interest between the so-called “frugal states” of Northern Europe and the Southern European ones. This division, which will be analyzed below, is caused by different types of national economies which leads to a different management of the public finances and so, different reactions. However, in 2020, as for the Debt crisis in 2011, the spillover effect transformed the economic and mainly health issue of one Member State into a Common issue. Also, in that case the solution has been found at the EU’s level, with a common purchase of vaccines and most important the establishment of a common fund, the Next Generation EU worth 750 billions of euros and financed through the emission of public debt. The energy crisis, generated after the outbreak of the war in Ukraine, represented for the European Union a further black swan[3] demanding for efficient common responses and highlighting the problem of having 27 different scale of economic priorities under the same economic union. The last twenty years have been characterized by financial, economic and geopolitical crisis that have strongly involved the European sphere highlighting the insufficiency of a lone monetary union. The aim of this study is to evaluate the process of fiscal integration adopted by the EU and demonstrate how the external challenges to the economic and political stability of the EU functioned as boosting factors.
The first chapter will deliver a description of the current EU’s fiscal framework and the toolbox available to control and assure minimum level of compliance of the nationals’ financial behavior. Beside the public budget’s rules and the surveillance mechanisms, adopted during the sovereign debt crisis, the European taxation policy has gone through an interesting evolution since the establishment of the free trade area and represents one of the main topics of discussion when talking about federalism due to its political implications. The first part compares the different taxation rules within the member states and the instruments used to harmonize them. With the second chapter, which represents the core part of the thesis, it will be discussed the shift from a de-centralized fiscal union to a centralized one, in particular by studying the cause-effect relation among the three main European crises of the 21st century (Sovereign Debt, Pandemic and Energetic), and their outcomes on the Union’s fiscal framework. Then, it will be drawn up a comparison between the EU and three other

[3] Black swan: A black swan is an unpredictable event that is beyond what is normally expected of a situation and has potentially severe consequences.

federalism systems: the U.S., Germany and Spain. The third and final chapter delivers an explanation of the reforms adopted in 2024 regarding the Stability and Growth Pact and their consequences. Furthermore, it will be assessed what the European Member States would gain and lose from an implementation of the fiscal integration[4].

Previous studies on European Federalism

Even if the discussions about a further European economic integration, that would involve the fiscal systems, started to gain relevance especially after the sovereign debt crisis, the idea of making the EU a federal system emerged at the end of the 70s with the MacDougall Report[5]. A relevant document was published in 1977 by a group of experts appointed by the Commission of the European Communities whose chairman, Donald MacDougall, presents the first volume of its report discussing the role of public finance in European integration. After making previsions on the changes in the Community's expenditures, the authors considered three hypothetical degrees of integration:

- Pre-federal integration
- Federation with a small public sector at the Community level
- Federation with a large public sector at the Community level

More than 40 years later we can say that the EU is completing the process towards a Federation with a small public sector. This stage includes a common market, a common monetary system and the establishment of rules for the expenditures of European funds.

The persecution of a complete Federalism has been discussed by several experts. It has been considered that a Fiscal Union should be addressed to the failure of some coordination policies

[4]Draghi, M. (2023) *Mario Draghi on the path to fiscal union in the Euro Zone*, *The Economist*.
[5] Wilson, T. and MacDougal, D. (1978) 'Report of the Study Group on the role of Public Finance in European integration. volume I. General Report.', *The Economic Journal*, 88(352), p. 858. doi:10.2307/2231994.

reputed “Idiosyncratic” meaning national policies incompatible with the EU economic system that caused the debt and financial crisis. According to the economist Carlo Cottarelli, a fiscal union that meets the needs of the euro could be built on three pillars[6]:

- Stronger constraints relating to Member State deficits and debt, which would reduce the risk of idiosyncratic fiscal policy shocks;
- A larger central budget, as this would both provide the tools for risk sharing and contribute to reducing some key economic differences across countries;
- Increasing the harmonization of nonfiscal policy, starting with the priority of setting up a banking union with an appropriate fiscal backstop.

While some of these suggestions have been implemented in the last ten years, the EU still lacks a harmonization of the national fiscal systems. The European rules, that compose part of the literature and will be deeply analyzed, establish a coordination of the national public economies rather than an integration requiring the adoption of ad-hoc solutions when a crisis comes up. According to the former head of the ECB, Mario Draghi, the motivations behind the necessity of a Fiscal Union have changed. Back from a period of weaknesses and instability, the EU needs a fiscal integration because *“There is a serious risk that Europe underdelivers on its climate goals, fails to provide the security its citizens demand and loses its industrial base to regions that impose fewer constraints on themselves”*[7].

To deliver a clear and broad explanation of the current fiscal framework I will exploit academic and analytic papers published by study centers and experts. Important research have been made about the functioning of new coordination mechanisms, as the ESM, and how to integrate them with the fiscal supervision and the joint guarantees related[8]. Other studies are more focused on the technical functioning of a hypothetical Fiscal Union and the steps required for its achievement[9]. This paper will provide a broad analysis of the case, explaining the promoting reasons for a fiscal union and the details of the adoption process, considering the current situation and the existing fiscal rules.

[6] Cottarelli, C. (2013) ‘European Fiscal Union: A vision for the long run’, *Swiss Journal of Economics and Statistics*, 149(2), pp. 167–174. doi:10.1007/bf03399387.
[7] Draghi M. (2023)
[8] Fuest, Clemens; Peichl, Andreas (2012) : European Fiscal Union: What Is It? Does It work? And Are There Really 'No Alternatives'?, CESifo Forum, ISSN 2190-717X, ifo Institut - Leibniz-Institut für Wirtschaftsforschung an der Universität München, München, Vol. 13, Iss. 1, pp. 3-9
[9] Thirion, G. (2017) ‘European Fiscal Union: Economic rationale and design challenges’

Methodology

The proposed research aims to analyze the evolution of the European Fiscal integration process linking the adoption of several important measures to the incurrence of external threats. In order to do so it could be useful to look at the European Union as a political and economic body that works in a competitive environment. The 27 Member States, and particularly the 20 ones of the Euro-area, compose a set of different fiscal and macroeconomic systems which are supposed to share the same faith. However, despite the continuous attempts to strength the political cohesion, the priorities are often heterogenous causing interest conflicts and slowing down the integration process. These obstacles belong to the difficulty of looking at the EU as a unique common actor instead of 27 different regimes. In the private business sector, an essential instrument for the stability of a company's strategic position and its efficiency is the S.W.O.T. analysis. The S.W.O.T. analysis, which stands for Strength, Weaknesses, Opportunities and Threats, uses a matrix composed by these 4 elements which are examined and discussed. Subject the EU, treated as an economic actor which produces goods and services to be preserved, to this type of analysis could represent an interest way to exploit its potential, defend its stability and make it stronger in a complex geopolitical framework. In particular the analysis will be applied to the economic governance of the Union which presents both strength and weak points, has already exploited and might exploit opportunities of development and is exposed to external threats. These four aspects will be discussed in the following order.

The first step will be the description of the current fiscal framework of the European Union which is object of discussions, especially in the last years, due to its broad heterogeneity. This study will remark the measures adopted so far and the evaluation of their impact on the EU economic stability. The strengthening process of the European financial structure has evolved a lot after the establishment of the common market in 1992, responding to the necessity of rules and harmonization of the national behaviors. In order to evaluate the impact of these adopted measures It will be used a quantitative approach that considers economic indicators as the *spread*[10] or the ECB interest rates. On the other side, a qualitative approach based on the annual official relation published by the EU Institutions represents a useful method as well to understand if the results obtained by certain measures satisfied the expectations.

The second phase of the research will consist in presenting a costs-benefits analysis of a stronger fiscal integration. The analysis will be made up by using the winners and losers approach based on past and recent fiscal constraining measures. The EU had often transformed external challenges into

[10] Index based on the difference between the rates of return of different government bonds.

opportunities of evolution for the economic cohesion. However, there have always been Member States more in favor than others, creating an internal division between the so-called "Frugal Countries" and the Southern-European ones. A Fiscal Union is seen by the first group as a threat to the privileges of their economies. At the same time the increased control on the national fiscal policies has been required by the bad financial management of the Mediterranean states. This section will evidence the opportunities for both the groups deriving from a greater integration.

The third and last part will describe the role of the external threats in the integration process. After the recent geopolitical and energy crisis, implementing the economic integration of the EU has become a matter of European security. The establishment of a European Common Defense would be financed by joint resources available only through the creation of a common budget law. The current criteria resulted to be insufficient as it is highlighted by the creation of ad-hoc solutions when a crisis occurs. This last section will describe the effect that the three main crisis of the last decades had on the fiscal integration process and will analyze if and how more integration would mean more protection.

1. Current EU's fiscal framework

1.1 One monetary policy and 20 fiscal policies

The 90s have represented for the European Union a decade of transition and convergence towards an Economic and Monetary Union. The publication of Delors' "White Paper" in 1985 established the path for the completion of the internal market. The process was divided into three different steps to be reached in separate defined periods. The first one, achieved between 1990 and 1993, included the abolishment of exchange controls and the liberalization of capital movements within the community. The milestone of these years was the signing of the Maastricht Treaty, in 1992, that established the completion of the European Monetary Union (EMU) as a formal objective and sets a number of economic convergence criteria, concerning also the public finances. The second stage covered the years from 1994 to 1998 and saw the birth of the name "Euro" related to the common currency, the adoption of the Stability and Growth Pact, as an instrument to ensure budgetary discipline and the institution of the European Central Bank (ECB), in 1998, with the task to manage the monetary policy. The third and last stage started in 1999 and implies the adoption of the Euro as common currency after a three-years transition period; in 2002 the euro notes and coins have been introduced. After 25 years the member states belonging to the euro-area are 20 out of 27 and are likely to become 21 in 2025 with the joining of Bulgaria.

The management of the monetary policy is up to the ECB, based in Frankfurt. The institution pursues the target inflation of 2% by controlling the interest rates and the supply of money. These two activities belong to the set of the "standard instruments" available for the monetary policy including the determination of three interest rates at which commercial banks can borrow from or deposit with the ECB[11]:

1. The **main refinancing operations (MRO)** rate: paid by the banks when they borrow money for one week and requires collateral to guarantee the repayment currently at (currently at 3.65%);
2. The **deposit facility rate**: set by the ECB every six weeks and used to make overnight deposits (currently at 3.50%);
3. **The marginal lending facility rate**: an interest rate on overnight credits to banks against broad collateral (currently at 3.90%).

However, since the subprime crisis, the ECB started to adopt some so-called "non-standard instruments" which allow the institution to conduct asset purchase programs on the private markets having direct and indirect fiscal consequences for governments. While, before the crisis, the fiscal consequences of ECB policy was underrated and with an higher degree of de-regulation, since the crisis started, they gained huge attention[12]. The reason is that it has been understood the complexity and the issues related to having one common monetary union and 27 different fiscal policies.

[11] https://www.europarl.europa.eu/erpl-app-public/factsheets/pdf-chapter/en/en-chapter-2.pdf
[12] Orphanides, A. (2020) 'The fiscal–monetary policy mix in the euro area: Challenges at the zero lower bound', *Economic Policy*, 35(103), pp. 461–517. doi:10.1093/epolic/eiaa017.

The fact is that, unlike other federations as the US or Japan, in the euro area the fiscal policy can be exploited as an area-wide stabilization tool only through a coordination of national (country-specific) fiscal policies[13]. This means that the European Institutions, in particular the ECB, has no right to impose a specific behavior in fiscal matters as public spending, taxation or public debt emission but can only try to encourage some common limits. The explanation behind this separation of powers can be found in the will of the national governments to keep sovereignty on fiscal policy so to exploit it as a political leverage. In addition, given the different political behaviors within the EU, many citizens would define unpopular a common taxation. Even if the public debt has to be kept within the limit of 60%, weighted for GDP, several states do not comply with it, resulting in differences between "reliable" and "unreliable" countries within the EU; this was the key problem of the 2012 Euro-crisis[14]. As established by the article 123 of the TFEU[15], the ECB could not buy national public debt on the primary market. In the specific case of Greece, the Debt/GDP ratio reached 170% in 2012, 110 points above the limit imposed by the Maastricht criteria. The risk of default was tangible as it was the hypothesis of a "Grexit" to avoid a contagious effect in the whole euro area. Since the poor economic conditions of Greece and of other affected Member States (Italy, Spain, Portugal and Cyprus) were the consequences of incautious fiscal conducts, it was evident the necessity of a tighter fiscal coordination at the communitarian level.

1.1.1 Taxation policies in the EU

Within the EU's fiscal framework, some financial instruments have already been integrated, creating a distinction between shared and individual powers. The adoption of such measures was required by the establishment of a common market and free trade, concerning mainly the taxation policy. Until the 70s in fact, each EU country had their own individual system for taxing the production and consumption of goods and services, making difficult doing business across borders. This is why, in 1977, the Member States agreed on a common set of tax rules for goods and services and a general framework of rates establishing the bases for the **EU Value Added Taxation (VAT)** system. The European VAT is a consumption tax charged on most goods and services and paid to the government

[13] Alloza, M. et al. "Fiscal Policies in the Euro Area: Revisiting the Size of Spillovers." *Journal of Macroeconomics*, vol. 61, Sept. 2019, p. 103132, https://doi.org/10.1016/j.jmacro.2019.103132. Accessed 2 July 2020.
[14] Regling, K. "EU Fiscal Rules: A Look Back and the Way Forward." *Intereconomics*, vol. 57, no. 1, Jan. 2022, pp. 8–10, https://doi.org/10.1007/s10272-022-1020-2. Accessed 23 Mar. 2022.
[15] Treaty on the functioning of the European Union

where the consumer is located. "*Under the European VAT system, only the end consumer is ultimately taxed on the goods or services. Businesses involved in the supply chain are, in most cases, required to apply VAT when selling on to the next customer in the chain*"[16]. Then there are the **Excise duties** which are indirect taxes on alcoholic beverages, tobacco and energy products. The directive on the common excise duties aimed to reduce the scope for distortions among the national excises after the abolishment of tax controls at the borders in 1993. The legislation establishes the minimum rates that the EU countries must apply, the scope for possible exemptions and the general rules for producing, storing and moving these goods around the EU.

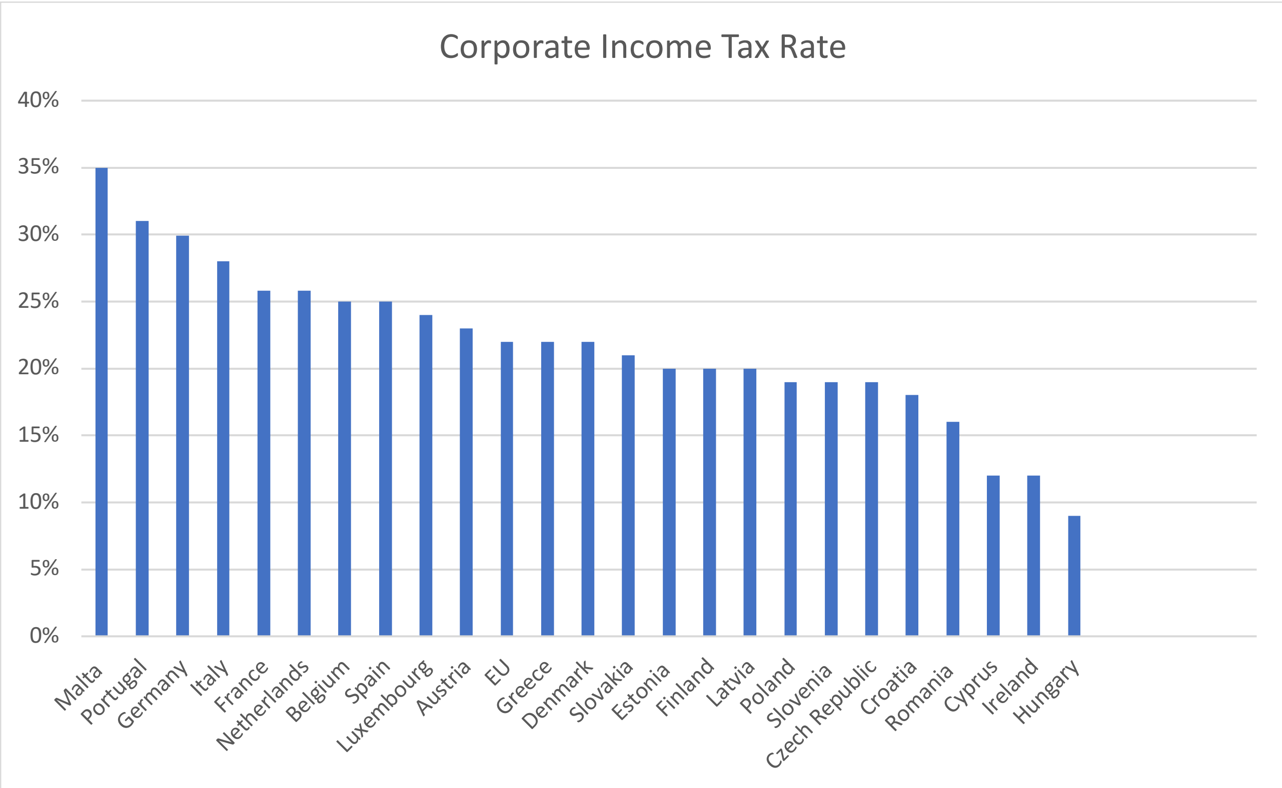
With the growth of global economic competition and of the easiness with which industries started to move their capitals, the EU has introduced rules and directive aiming to fight the tax avoidance of privates and companies with the *Directive 2016/1164*. The directive lays down anti-tax-avoidance rules in 4 specific fields to combat Base Erosion and Profit Shifting:

- ***Interest limitation rules:*** *where multinational companies artificially erode their tax base by paying inflated interest payments to affiliated companies in low-tax jurisdictions. The directive aims to dissuade companies from this practice by limiting the amount of interest that a taxpayer has the right to deduct in a tax period. The maximum amount of deductible interest is set at a maximum of 30% of the taxpayer's earnings before interest, tax, depreciation (a measure of how much of an asset's value has been used up at a given point in time) and amortization (spreading payments over multiple periods).*
- ***Exit taxation rules:*** *where taxpayers try to reduce their tax liability by transferring its tax residence and/or its assets to a low-tax jurisdiction, solely for the purposes for aggressive tax planning. Exit taxation rules aims to prevent the erosion of the tax base in the EU country of origin when high-value assets are transferred with ownership unchanged, outside the tax jurisdiction of that country. The directive gives taxpayers the option of deferring the payment of the amount of tax over 5 years and settling through staggered payments, but only if the transfer takes place within the EU.*
- ***General anti-abuse rule:*** *this rule aims to cover gaps that may exist in a country's specific anti-abuse rules against tax avoidance and allows tax authorities the power to deny taxpayers the benefit of abusive tax arrangements.*
- ***Controlled foreign company (CFC) rules:*** *in order to reduce their overall tax liability, corporate groups are able to shift profits to controlled subsidiaries in low-tax jurisdictions.*

[16] https://taxation-customs.ec.europa.eu/taxation/vat_en

CFC rules reattribute the income of a low-taxed controlled foreign subsidiary to its more highly taxed parent company. As a result of this, the parent company is charged to tax on this income in its country of residence.

However, most of the taxation policies, such as the personal, financial and company taxation, are decided by the national governments and are subjected to the limits of mere recommendations and attempts to harmonization. One of the most discussed topics concerns the possibility for some countries to apply an advantageous companies' taxation policy which attracts investments to the detriment of other Member States.



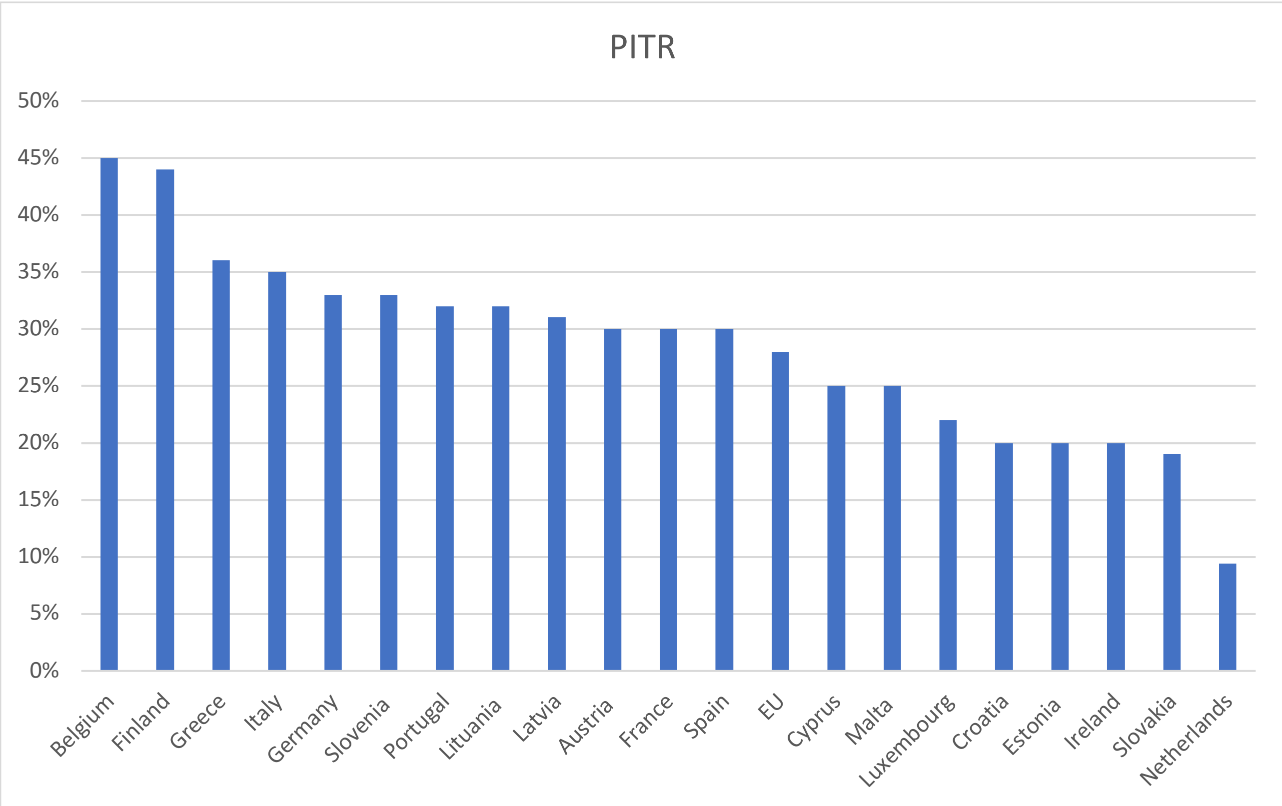
Fonte: Tax Foundation

Countries as Luxembourg and Netherlands, despite a CIT above the EU average, still represent an attractive destination for big societies due to the possibility of tax optimization. The authors of OpenLux (a research paper on Luxembourg's status as a tax haven published in 2021) claim that the effective rate, given possible optimizations, could be as low as 1% or 2%[17]. In 2015 the European Commission, after a corruption investigation, asked the termination of the optimization agreements between societies and government. However, Luxembourg has not eliminated this practice but has undertaken to inform the European Commission on the progress of agreements with multinationals.

[17] https://luxtoday.lu/en/knowledge/luxembourg-a-tax-haven-in-the-center-of-europe

This led to the phenomenon of the so-called "Tax Havens", member states where the corporate and property taxation is slightly below the European average or easily avoidable. In 2018, Italy experienced a profit shifting of 24 billion euros and lost 19% of fiscal revenues due to fiscal havens as Luxembourg, Ireland and Netherlands[18]. For this reason, in January 2024, the European Commission established that every Member States have to set a minimum CIT at 15%. This historic act accomplishes EU commitment to be among the first to implement OECD tax reform to tackle fiscal disparities and aggressive fiscal regime.

However, what still lacks a homologation that would allow a fairer European labor market is the personal income tax. Within the European Union and the Eurozone, the differences among the Personal Income Taxation Rates are incredible, this contributes to divide Europe in job-attractive countries and brain draining countries[19]. If we consider that the average European GAP is 36.000 euros, the tax rates relating to this salary are the following:



Fonte: PwC-tax summaries

[18] Tørsløv, Thomas R, et al. *The Missing Profits of Nations*. NATIONAL BUREAU OF ECONOMIC RESEARCH, 2018.
[19] Oxfam International (2015) 'Pulling the plug: How to stop corporate tax dodging in Europe and beyond', *Human Rights Documents Online* [Preprint]. doi:10.1163/2210-7975_hrd-9824-2015007.

Nevertheless, it is important to remark that some of the member states are considered fiscal advantaged due to remarkable differences on high incomes taxation such as Luxembourg, Cyprus and Ireland. The adoption of such regimes represents for some member states an important component of their national economies as for Ireland and Cyprus. A unification of the fiscal policies would find the opposition of these member states that would face a severe downfall of their competitiveness but, at the same time, it would allow a fairer market, decreasing the "profit shifting" phenomenon. In addition it would allow a smoother process of tax controls at the European level. One of the crucial obstacles to rapid progress on tax in Europe is the unanimity requirement established with the Lisbon Treaty, meaning that even if political will is there, 27 Member States unanimously need to agree on a common text, which allows just one or two of them to block a reform for years. Furthermore, unlike other important issues like competition or internal market, taxation is seen as a sovereign competence of the 27 Member States, which means the European Commission can only make proposals and the European Parliament provides non-binding opinions. This is why without political will – or massive tax scandals such as Luxleaks – some files can take a very long time before arriving to a unanimous agreement[20]. These factors enable the Haven Tax Member States to promote their own interest over greater European progress in the fight against corporate tax avoidance.

With the institution of the common currency, the goal of the EU became the coordination of the fiscal policies, pursued by establishing fiscal rules and directives which are analyzed in the following paragraph.

1.2 European fiscal rules

This part will describe and discuss the fiscal framework of the European Union which is composed by coordinative rules, stabilization and surveillance mechanisms and convergence criteria. This set of elements has witnessed an implementation and strengthening during the past twenty-years after having experienced crisis and "idiosyncratic" policies[21]. It was clear since the establishment of a single monetary system that a harmonization of the fiscal policies was required; however, too much tight rules would have brought arguments about the loss of national sovereignty. The scope of the

[20] OXFAM INTERNATIONAL "How to stop corporate tax dodging in Europe and beyond briefing note march 2015", 2015.
[21] Cottarelli, C. (2013) 'European Fiscal Union: A vision for the long run', *Swiss Journal of Economics and Statistics*, 149(2), pp. 167–174. doi:10.1007/bf03399387.

rules is to ensure sound government finances, preserve debt sustainability, maintain trust between the member states and strengthening the confidence of citizens and financial markets in the euro.[22]

1.2.1 What came with the Monetary Union

The first step was the establishment of the **Maastricht Criteria** in 1992. In order to join the European economic and monetary union the Member States have to comply with two fundamental parameters: the annual ratio Deficit/GDP has to be below 3% and the ratio Debt/GDP below 60%. The aim of these two limits is to avoid spillover effects and unsustainable public finances. The deficit represents in fact the difference between the incomes and the spending of a state and establishing a defined proportionality to maintain means encouraging a similar behavior in managing public finances. At the same time, the debt parameter represents a way to avoid imbalances in terms of interest rates, preserving the financial stability. In order to assure the respect of these parameters, in 1997 it has been adopted the **Stability and Growth Pact (SGP)**. The SGP, which has been reformed in 2011 after the Debt Crisis, is regulated by article 121 and 126 of the TFEU and comprehend the existence of a "preventive arm" and a "corrective arm". The first one aims to assure the balance of public finances through multilateral surveillance and the establishment of a Medium Term budgetary Objectives (MTOs). The MTOs are set to ensure sound fiscal health and are updated every 3 years; in case of significant deviation the Commission shall recommend the Council to open a so-called Significant Deviation Procedure which, if not corrected, could evolve in an Excessive Deficit Procedure under the corrective arm of the Stability and Growth Pact. The Excessive Deficit Procedure begins with a Member State being in risk of breaching the deficit threshold of 3% of GDP or having violated the debt rule by having a government debt level above 60% of GDP. This means that the gap between a country's debt level and the 60% reference needs to be reduced by 1/20th annually[23].

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[22] Regling, K. "EU Fiscal Rules: A Look Back and the Way Forward." *Intereconomics*, vol. 57, no. 1, Jan. 2022, pp. 8–10, https://doi.org/10.1007/s10272-022-1020-2. Accessed 23 Mar. 2022.
[23] https://www.europarl.europa.eu/factsheets/it/sheet/89/il-quadro-ue-per-le-politiche-fiscali

1.2.2 What came with the Debt Crisis

After being acknowledged of the weaknesses in the economic governance during the 2011 financial crisis, the EU took a wide range of measures to enhance policy coordination and strengthen the Stability and Growth Pact. The first measure was the establishment of the **European Semester** which ensures that Member States discuss their economic, social and budgetary plans with their EU partners at specific times in the first half of the year[24]. This interaction provides a multilateral confrontation on each other's fiscal plan, taking better account of common challenges. The cycle of the European Semester starts in autumn with the publication, by the Commission, of the Annual Sustainable Growth Survey (ASGS) which sets the general economic and social priorities for the EU and provides Member States with policy guidance for the following year. Then, the Alert Mechanism Report (AMR) highlights the beginning of Macroeconomic Imbalance Procedure (MIP) that aims to identify potential risks early on, prevent the emergence of harmful macroeconomic imbalances and correct the imbalances that have already materialized. In February, the Council adopts the euro area recommendations and then in March the EU leaders consider the ASGS and the AMR. In April the Members States subjected to MIP present their national reform programs and their stability or convergence programs, receiving the feedback of the Commission one month after[25].

As it may be understandable, the Commission plays an important role in assessing the national budgetary plans of the Member States and making recommendations. This is also thanks to another measure undertaken during the Crisis framework which is the **Six-Pack.** The Six-Pack is made of five regulations and one directive proposed by the Commission and approved by the Parliament in October 2011. This new instrument implements the preventive arm of the SGP, establishing new minimum requirements for national budgetary frameworks and the corrective arm as well by regulating a new macroeconomic imbalance procedure and a stronger enforcement mechanism through new financial sanctions. According to the new rules a Member State that does not take adequate action to comply with the specific recommendations of the Council to correct their excessive deficit, will occur in financial sanctions. In addition, if the 60% for the debt/GDP ratio is not respected the Member State concerned will be put in excessive deficit procedure, even if the deficit is below 3%. An important rule introduced with the Six-pack is the **Debt rule** which requires that the debt-to-

[24] Darvas, Zsolt M.; Leandro, Álvaro (2015) : The limitations of policy coordination in the euro area under the European Semester, Bruegel Policy Contribution, No. 2015/19, Bruegel, Brussels.
[25] ibidem

GDP ratio should fall by an average of one-twentieth of the excess between the actual debt ratio and 60 per cent of GDP; so if the ratio is 130%, the gap is 70 points and has to be reduced of 3.5 percentage points every year. In May 2013 enters into force the **Two-Pack** measure. It enables the MS of the euro area to strengthen the coordination and surveillance of budgetary policies and is composed by two regulations. The first one applies to those in the corrective arm of the SGP while the second sets out clear and simplified rules for enhanced surveillance for Member States facing severe difficulties regarding their financial stability. The last important implementation of the fiscal rules is the **Fiscal Compact**. The fiscal compact is officially considered a a step towards a true "fiscal stability union". It has been signed by the Heads of Governments of every EU country with the exception of UK, Czech Republic and Croatia. Within this agreement there is a distinction between a cyclical deficit and a structural deficit[26], with particular consideration of the latter which cannot exceed the 0.5% of the GDP (1% in case of compliance with the Debt/GDP ratio of 60%). In addition, the MS must pursue the structural equilibrium of public balances incorporating it into the national legal system[27].

1.2.3 Data

In order to assess the impact of these new rules on the national economies we have to consider two kinds of indicators. A first type has to describe the financial health of a Member State before and after the adoption of the fiscal rules while the second one has to relate the changes expressed by the first index to the fiscal rules' efficiency. For the first variable it is possible to use a monetary policy index which is the long-term interest rate on the Government Bond Yields. The interest rates on the public debt are a measure of the investors' confidence in a national economy, if it is too high it means that the investment is considered risky with low trust on the country's capacity to pay back. As the graphs below show, between 2011 and 2012, the interest rates on the Italian, Greek and Spanish debt were extremely high compared to others as the German and French.

[26] A *structural deficit* occurs when a government's expenditures exceed its revenues even at full employment, reflecting underlying fiscal policy issues. It represents long-term fiscal imbalance. A *cyclical deficit* arises during economic downturns, when tax revenues fall and welfare spending rises due to lower economic activity. It is temporary and linked to the business cycle.
[27] Gocaj, Ledina, and Sophie Meunier. "Time Will Tell: The EFSF, the ESM, and the Euro Crisis." *Journal of European Integration*, vol. 35, no. 3, Apr. 2013, pp. 239–253,

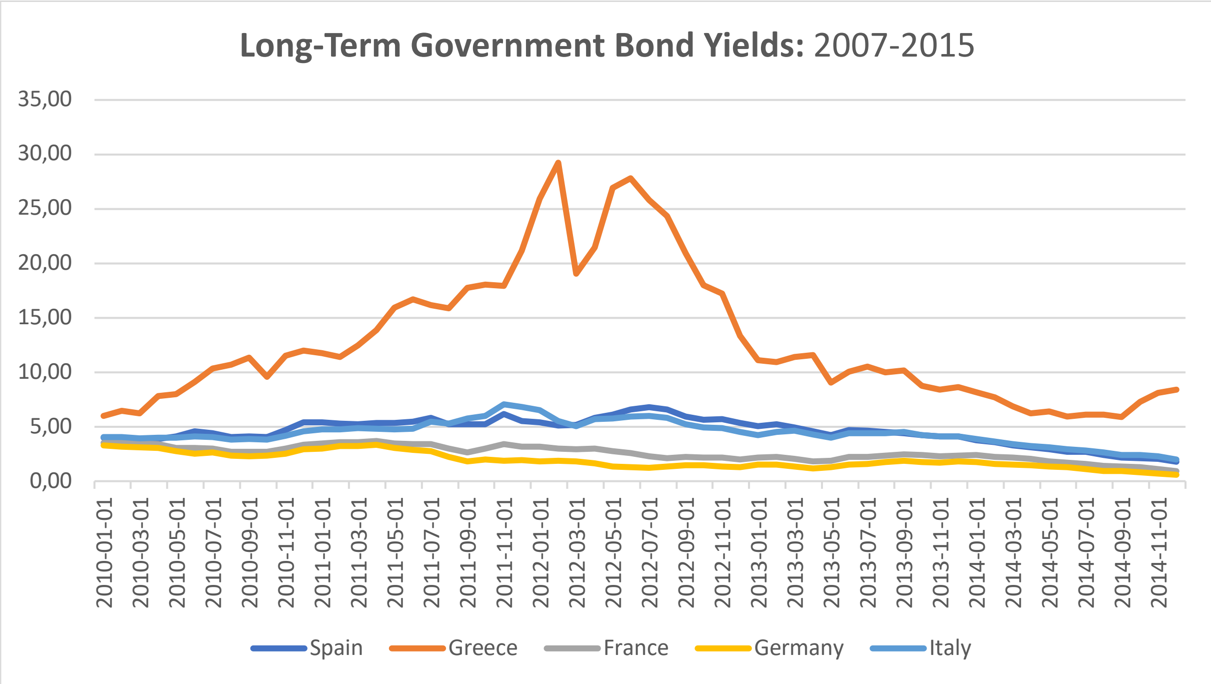


Figure 1 Data source: Federal Reserve

The gap (*spread)* between the interest rates is an index of different soundness of the European public finances at that time. The fact that, after 2013, they started to converge, could be explained by different factors. First of all, the recession started, causing a deflation which has been fought by the ECB by decreasing the interest rates in order to stimulate the consumptions. The national banks of the risky countries could manage to tackle this policy also thanks to unconventional monetary instruments adopted by the ECB that will be discussed below. However, the process of recovery was subjected to the respect of the new-born fiscal rules previously discussed. The EU's objective was to maintain the financial stability within the Euro area and the aim of the rules was and currently is to assure it and avoid spillover effects. To evaluate the strength of the fiscal rules within the Euro-area, the Directorate General for Economic and Financial Affairs constructed a model of Fiscal Rules Index (FRI) which considers: expenditure rules, balanced budget rules, revenue rules and debt rules. The Figure 2 shows the development over time, 1990–2012, of average fiscal rule strength for all EU countries and the separate developments for euro area (EA) members and non-EA members.

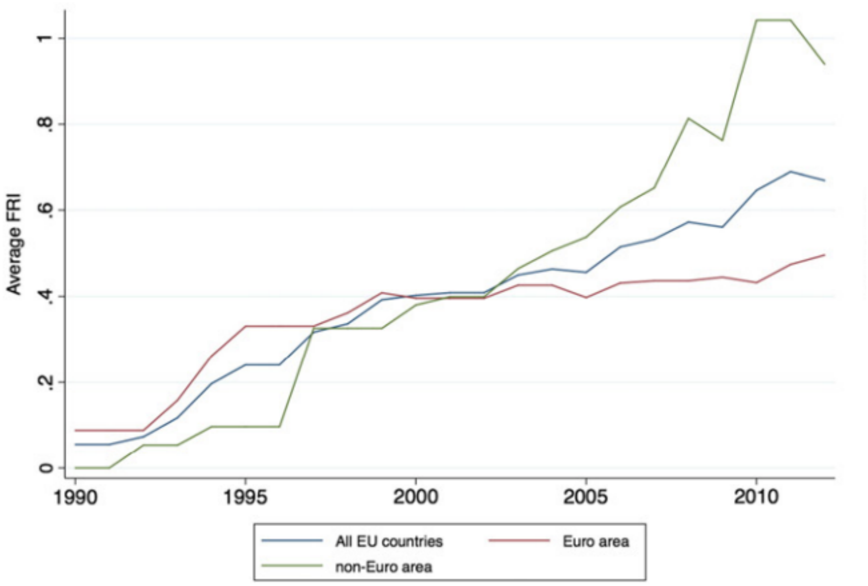


Figure 2: U.M. Bergman et al. / European Journal of Political Economy 44 (2016) 1–19

It emerged that non-Euro countries had stronger fiscal rules than Euro countries by 2012. However, the strength index of the Euro area grew between 2010 and 2012, when the Debt Crisis hit. To complete the analysis, it is important to understand which kind of rules is more effective in improving the primary balance performance. According to the regression model constructed by Bergman, the most effective instruments to increase the primary balance are the balanced budget rules (BBR) and debt rules (DR), with both coefficients significantly positive at the 10% level of confidence. The fiscal rules adopted by the EU in the second decade of the 2000s regard mainly these two policy fields, imposing criteria and sanctions. On the other side, the expenditures and revenue managing do not have clear limits and are subjected just to an approvement of the Commission.

However, it has been clearly stated by high economic commissioners as Pierre Moscovici that, beside fiscal implementations at the communitarian level, the countries must undertake structural reforms and step-up investments in order to preserve the jobs market and growth. The recommendation was referred to the issue illustrated below where it is possible to notice the gap of the unemployment rate between countries within the Euro-area as the Spanish one which was five times the Austrian one. This highlights the importance of adopting policies which are not only controlled and accepted by the Commission but also addressed to the same priorities in order to avoid social and economic disparities.

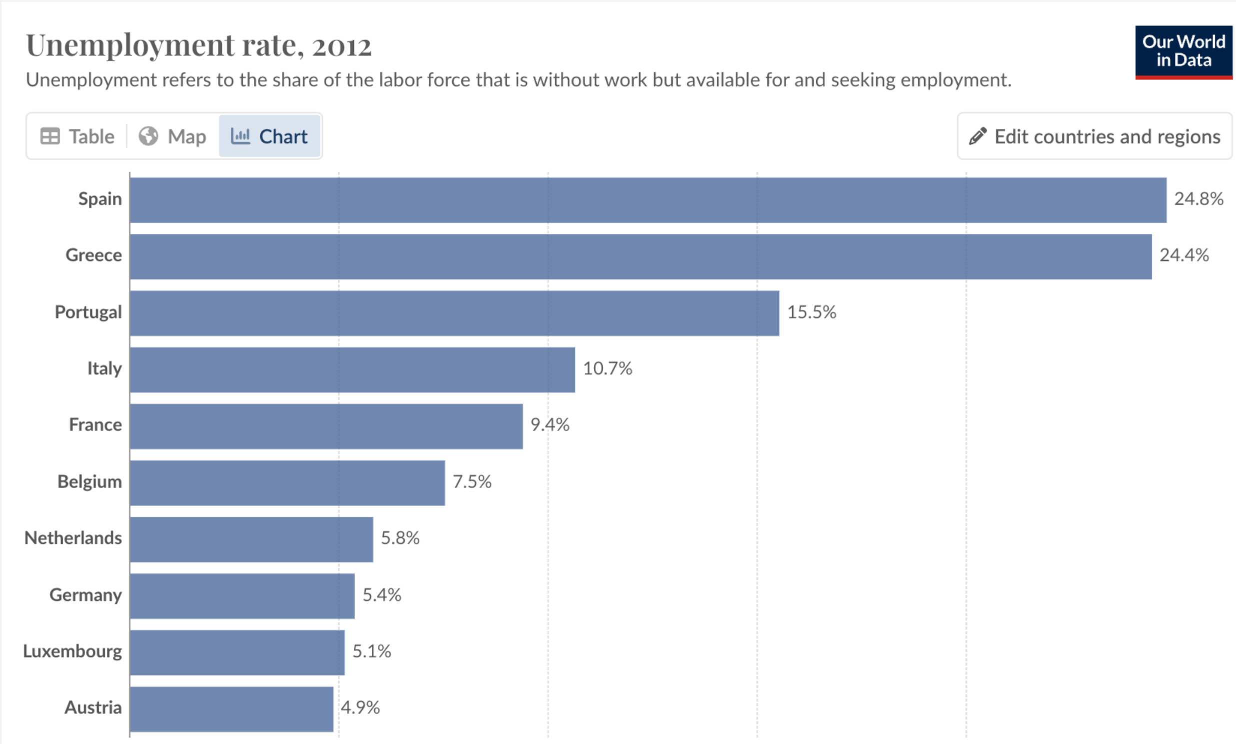


Figure 3: Our World in Data

2. From a fiscal coordination to a fiscal integration

At this juncture, it is crucial to assess the level of fiscal harmonization achieved by EU Member States, identify the gaps that remain, and understand the implications of achieving a complete Fiscal Union. In 2013, the need for a Fiscal Union was strongly advocated by academics, such as Professor Carlo Cottarelli, primarily to stabilize the already fragile economic and financial system. However, the priorities of the EU have since evolved. Mario Draghi, former Head of the ECB and Italian Prime Minister, emphasized that economic integration is now essential not only for economic stability but also to address broader challenges. Draghi highlighted that without deeper economic integration, the EU risks failing to meet its climate goals, provide the security its citizens demand, and maintain its industrial base in the face of competition from regions with fewer constraints. Therefore, the current priority is to reestablish the EU's strategic fiscal and geopolitical importance. This objective begins with completing financial integration as a foundational step. Achieving full fiscal harmonization would involve aligning fiscal policies, budgetary frameworks, and tax regulations across all Member States. It would mean establishing unified fiscal rules, centralizing certain fiscal powers at the EU level, and creating mechanisms for mutual fiscal support and risk-sharing among Member States. This integration would not only enhance the EU's ability to respond to economic shocks but also bolster its global economic and political standing. Despite significant progress, several gaps remain. Differences in tax policies, budgetary practices, and compliance with fiscal rules continue to pose challenges. Moreover, political resistance to ceding fiscal sovereignty and the requirement for unanimous agreement on fiscal matters impede rapid progress. Addressing these issues will require sustained political will, comprehensive reforms, and perhaps a re-evaluation of the existing treaties governing fiscal policy in the EU.

2.1 Definition and limits of a Fiscal Union

Even though the term "Fiscal Union" has been used to describe the ultimate stage of an ongoing process, it is essential to define what this term entails. According to M. Dabrowski (2015), a fiscal union can be broadly defined as *"the transfer of part of fiscal resources and competences in the area of fiscal policy and fiscal management from the national to supranational level"*[28]. This can involve various elements such as the harmonization of taxation, the development of European revenue sources for the EU budget, and the creation of institutions with fiscal authority at the supranational level.

[28] Marek Dabrowski. *Monetary Union and Fiscal and Macroeconomic Governance*. Brussels European Commission, Directorate-General For Economic And Financial Affairs, 2015.

Achieving this model would represent a step towards European Federalism, a regime favored by proponents of the “United States of Europe.” In summary, a fiscal union would necessitate the establishment of a supranational institution tasked with managing fiscal resources, adopting a federal debt system, and centralizing spending (Draghi, 2023).

In 1977, when the MacDougall Report first proposed the idea of a fiscal union, the EU comprised nine Member States, which expanded to 12 with the accession of Greece, Spain, and Portugal a few years later. This initial expansion highlighted the need for an instrument to reduce disparities among European regions, leading to the creation of the European Regional Development Fund (ERDF). The ERDF facilitated the transfer of resources from wealthier to poorer regions, marking an early attempt to strengthen the European economy through a common budget. Although this initiative did not imply fiscal or monetary integration, the MacDougall Report emphasized the effort required to transition from “pre-federal integration” to a “federation with a large public sector at the Community level.” The report highlighted the importance of gaining more bargaining power vis-à-vis third countries, achieving “economies of scale,” and generating positive spillover effects. Despite significant progress since then, the process remains incomplete due to several challenges[29].

The first obstacle to achieving European Federalism lies in the institutional structure of the EU, which is not conducive to this transition. There is no common strategy for integrating public spending at the European level, nor is there a proposal for a permanent federal instrument to address common external threats. The Next Generation EU, which will be discussed later, represents a temporary fund with no long-term substitute once it expires. Many believe that the EU’s long-term budget, representing just 1% of the EU’s GDP, is insufficient to ensure a countercyclical insurance mechanism[30]. Such a mechanism would create common buffers during prosperous times to mitigate adverse conditions during economic downturns[31]. The reluctance of national governments to relinquish their financial autonomy for political maneuvering further hinders fiscal integration. Centralizing the management of spending and revenues would require Member States to sacrifice a significant portion of their fiscal sovereignty, a challenging prospect given the current high level of distrust towards technocrats and European institutions. The Eurozone's inability to integrate its 20 different fiscal policies stems from the varying economic behaviors of the "frugal" Northern states and the Southern European states.

[29] Saurugger, Sabine. *The European Union and Federalism: Possibilities and Limits*. No. 218, 1 Jan. 2018, pp. 173–200.
[30] Marek Dabrowski. *Monetary Union and Fiscal and Macroeconomic Governance*. Brussels European Commission, Directorate-General For Economic And Financial Affairs, 2015.
[31] Thirion, G. ‘European Fiscal Union: Economic rationale and design challenges’, 2017.

These differences are rooted in the distinct industrial relations systems in Western Europe: the North is characterized by "coordinated market economies," while the South is defined by "mixed market economies." This disparity affects wage-setting systems and has resulted in increased external competitiveness for the North and decreased competitiveness for the South since the advent of the monetary union[32].
In conclusion, the limitations to integrating fiscal policies are primarily due to the EU's institutional structure, which lacks effective strategic instruments, and the diverse national economic systems that appear more competitive than coordinated. Addressing these issues will require substantial reforms and a shift towards a more unified and strategic approach to fiscal management within the EU.

2.1.1 A good time for federalism

During the past 30 years of EU's life and mainly in the last 10, a lot has been done to assure a fiscal convergence which seems heading towards more integration. After the breakout of the Russia-Ukraine conflict pressures for a European Common Defense has been exerted by some European leaders, first by the French President Macron and the former President of the ECB, Mario Draghi. While the first encourages the institution of a common army, the second sustains more the need of a common foreign policy for the political economy, which, nowadays, represents a powerful instrument for geopolitical threats. The European Member States have appeared too weak when asked to face external challenges alone, as in the case of Covid-19. That same event could be taken as an example of how the response is stronger if adopted at the communitarian level, referring to the purchase of vaccines. It can be also considered the generational factor. The outbreak of these three main crises (Debt crisis, Covid-19 and the war in Ukraine) has created a perception, among the new generations, of a Europe subjected to continuous stress but at the same time present and able to deliver a prompt response. While the fiscal integration could still sound far away, the institution of the ESM and the creation of the NextGenEU are two demonstrations that the solution for the biggest external challenges has been found in supporting mechanisms of common finance instead of allowing more fiscal autonomy. From this perspective we can say that external threats functioned as accelerating factors for the fiscal integration by creating ad-hoc solution, an approach that cannot last forever.

However, there is still something missing. The main difference between the EU fiscal institutions and those of other federal states is the dimension of the budget which, in the case of the EU, is smaller

[32] Carrera, Andrea, et al. *Southern Europe and the Frugal Four: Structural External Over-Indebtedness?* 1 Jan. 2023, https://doi.org/10.2139/ssrn.4441999. Accessed 4 Apr. 2024.

(1% of EU GDP). Professor Cottarelli (2016) described the costs deriving from such a limited budget that emerged during the 2011 crisis such as the insufficient convergence of factor and product markets, the development of unsustainable fiscal positions, difficulties in implementing fiscal policies that consider the needs of the whole area and the inability of the euro to function as a reserve of value. The resizing of the budget would allow a more efficient harmonization of the fiscal policies and better reaction to external crisis. Along with the need of a larger budget, the Debt crisis suggested the possibility of centralizing the spending and revenue policies such as the corporate income tax, the unemployment subsidies and the pension system. The centralization of these “automatic stabilizers” would assure a coherent and effective countercyclical policy across the whole area.

2.2 Step towards the Fiscal Union: the crisis’ effect

According to the OECD economist Gilles Thirion (2017) the process towards a Fiscal Union is made up by 5 steps:

1. Rules and coordination
2. Crisis management mechanism
3. Banking Union (with common deposit insurance and/or fiscal backstop)
4. Fiscal Insurance and risk sharing
5. Joint debt issuance

In Chapter 1 it has been analyzed and discussed the EU fiscal framework by describing the coordination of the national fiscal policies assured by common rules which confirms the achievement of the first point. With the sovereign debt crisis, the EU developed a crisis management mechanism based on common response in order to avoid the risk of spill-over effect and creating ad-hoc tools.
The third point, the Banking Union, is again the result of the Sovereign Debt Crisis which evidenced the need of more control on the national banks. The European Banking Union is based on two pillars which are the Single Supervisory Mechanism (SSM) and the Single Resolution Mechanism (SRM). These two pillars represent the foundation of the single rulebook which is a set of rules provides legal and administrative standards to regulate, supervise and govern the financial sector in all EU countries more efficiently. The SSM establishes that the ECB, as an independent body of the EU, together with the national supervisory authorities, ensure an effective and consistent supervision of the European banking system by conducting inspections, setting higher capital requirements (buffers) and ensuring compliance with EU prudential rules. The SRM, on the other side, applies when a bank is failing or likely to fail and allows bank resolution to be managed effectively through a single resolution board and a single resolution fund, financed by the banking sector. However, this third point can be considered uncompleted. The third pillar expected, which was the European Deposit Insurance

Scheme (EDIS), is still lacking a Communitarian formulation undermining the investors position and the national banks' anti-crisis response. The last two points are those that would complete the fiscal integration and can be considered present at the embryo status within the EU. Both of them would imply the same risk-exposition of all the Member States and means the unification of the capital markets.

2.2.1 The Economic Crisis' Effect: The European Stability Mechanism

The European Stability Mechanism is an intergovernmental organization established by member states of the euro area in 2012 based in Luxemburg. It replaced the European Financial Stability Facility (EFSF), a temporary institution created in 2010 to support the financial integrity of the member states most hit by the debt crisis. To provide financial assistance the ESM raises funds through the sale of bonds and bills to investors and uses them by granting loans in sustain of macroeconomic programs, as in the case of Cyprus and Greece, or to recapitalize banks, as done for Spain. In general, the ESM loans are subjected to some so-called "conditionalities", such as economic reforms and macro-economic adjustments, that the ESM member State involved has to take in order to receive the tranches. Then the Member State has to repay its loans starting by a specific maturity date according to an interest rate that includes the cost of borrowing money from financial markets (base rate), a service fee (covering the ESM's operational costs), margin, and commitment fee. In 2020 the ESM has been implemented with the Pandemic Crisis support arm, a special fund targeted at euro area member states' healthcare costs related to the pandemic. The birth of the ESM was the solution to please the request of some Member States to increase the lending capacity of the EFSF and lowering its interest rates. Other countries, like Germany, was adamantly opposed to expanding the EFSF's powers but supported a treaty change to set up a permanent rescue mechanism that would allow a method for orderly default. When the ESM has been established it had a lending capacity of €500bn and the interest rates were 100 basis points lower than the EFSF, in addition, the ESM could buy debt bonds on primary and secondary market to sustain bail-out programs. The main characteristics of the ESM that differentiate it from the previous EFSF is its permanent nature that assures a containment of the risk of "moral hazard", its largest lending capacity that allows biggest structural reforms and the structure pf its governance and shareholders. Each ESM Member contributes to the ESM authorized capital based on each country's respective share of the EU total population and gross domestic product. The institution's lending measure has been used for 5 different countries: Greece, Ireland, Cyprus, Portugal and Spain. In the first four cases the loans were addressed to the implementation of macroeconomic adjustment programs of those countries which had lost the access to the markets and presented unsustainable public finances. In the case of Spain the loans' objective was to preserve the financial stability of the euro area by addressing those cases where the financial sector is primarily at the root of a crisis[33]. This category of supports belongs to the loans for indirect banking recapitalization. The Spanish crisis in fact, unlike the Greek one, was caused by a crack of the banking system, highlighting the need of the banking union, previously discussed, based on the three pillars. These two types of crisis however, had the same result of pushing the EU to take measures against the uncontrolled policies of the private and public sector by strengthening the fiscal and economic rules and, at the same time, to provide an efficient, permanent instrument of financial sustain, the ESM. Since the ESM raises funds through the sale of bonds and bills to investors it started to be used the term "Eurobond" referring to communitarian obligations issued to support the euro-area[34].

2.2.2 The Pandemic Crisis' Effect: The NextGenerationEU

In May 2020 the situation of the European health system became unsustainable due to the aggressive impact of the Covid-19 pandemic which paralyzed the national economies. The so-called "frugal states" (Germany, Austria, Netherlands, Denmark and Sweden), which until that moment were reluctant to finance measures by issuing common debt, got convinced of the necessity to undertake emergency economic plan. In July the European Commission approved the temporary fund "Next Generation EU" (NGEU) worth 723 bn euros, financed through the emission of Euro-debt and accessible after the approvement of an investment plan proposed by the Member states called "Recovery Plan". The plan has been defined by the Commission's President Von Der Leyen as "The largest recovery project in Europe since the Marshall Plan" and it does effectively present some similarities. From the objective point of view, it aims to allow an economic recovery from the pandemic shut down, encouraging investments and covering the economic loss caused by the shock as the Marshall plan was addressed to reconstruct the European economies brought to their knees by the war. However, unlike the Marshall Plan, the NGEU pursue the goal of an EU more sustainable, digital and resilient. If in fact, in 1946 the priority was to assure security and reconstruction by liberalizing the trade of raw materials as coal and steel, the post-pandemic period has been seen as an opportunity to restart a process which encourages the development of green policies, fighting the

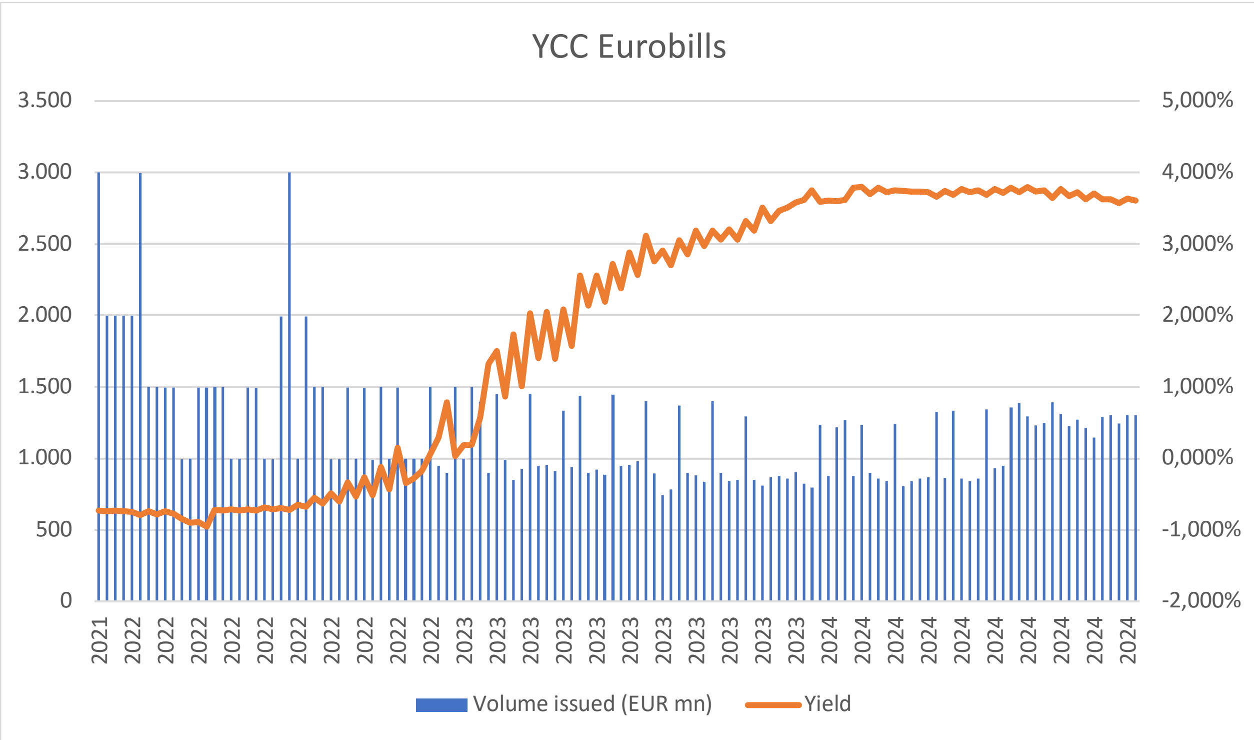
[33] https://www.esm.europa.eu/financial-assistance/lending-toolkit
[34] External Audit Services Audit of the financial statements of the European Stability Mechanism for the financial years 2023 – 2025 (2022)

climate changes and implement common traditional policies as the Common Agricultural Policy (CAP).
It is possible to compare the Recovery Fund proposed by the NGEU to the ESM fund of 2012, which has been expanded with the Pandemic Crisis Support Arm in 2020. Both the two programs have been created as a response to a common emergency and present some similarities. From the point of view of the instruments' financing sources in 2020 as in 2012 the EU has decided to operate on the financial market as a single and unique actor by issuing common debt addressed to the same finality: providing temporary support to member states with economic difficulties. However, understanding the core differences between the two tools is essential to comprehend why the NGEU is considered a successful case of fiscal integration while the ESM remains a controversial topic. First of all, the institution established in 2012 is financed by and applies only to the Euro-area member states while the NGEU provides resources to all the EU countries. The presence of a permanent institution addressed to the rescue of countries united by the same currency highlights the fragility of a monetary union that lacks sound coordination at the base. If a member state is called to ask for the help of the ESM the consequences are a decrease of trust in both the euro system and in the economic management of the single member state which loses credibility in front of its investors. The NGEU on the other hand applies to all the member states without distinction of currencies and demonstrates the capacity of the Union to preserve the economic integrity by auto-financing common investments[35].

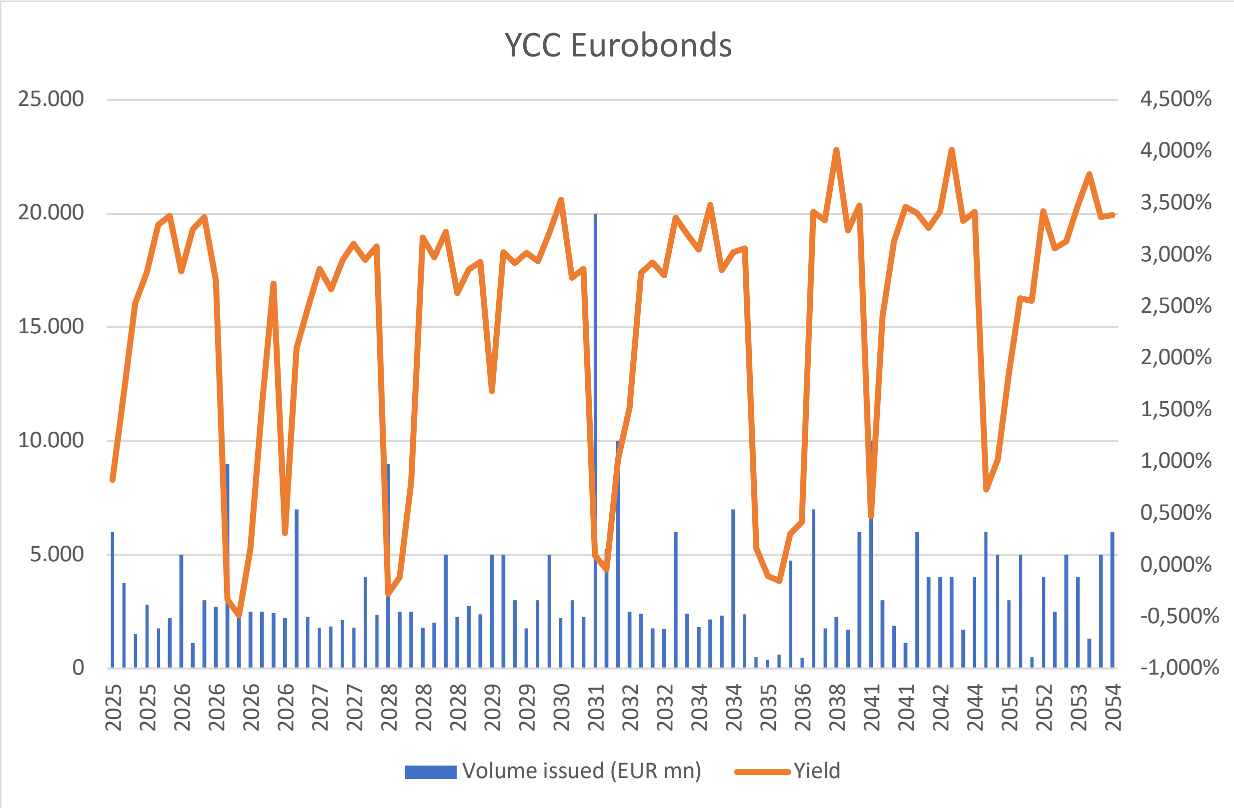
The mechanism of the Next Generation EU is more complex and structured than the ESM's one and represents something totally new for the EU. The Member States in fact gain access to the NGEU funds by presenting national plans of investment and reforms called "Recovery and Resilience Plans" (RRP). The approvement of the RRP leads to the transfer of the "Recovery and Resilience Facility" (RRF) an instrument that offers grants and loans to support reforms and investments in the EU Member States financed by grants and loans. Under the RRF, up to €338 billion of grants will be financed through borrowing operations. Member States will also receive additional RRF grants of €17.3 billion financed under the Emissions Trading System (ETS) and €1.6 billion under the Brexit Adjustment Reserve (BAR). Borrowing operations will also finance RRF loans. Of the total available RRF loan envelope of €385 billion, close to €291 billion has been committed by end 2023, following Member States' requests. In addition, up to €83.1 billion of NextGenerationEU funds are being used

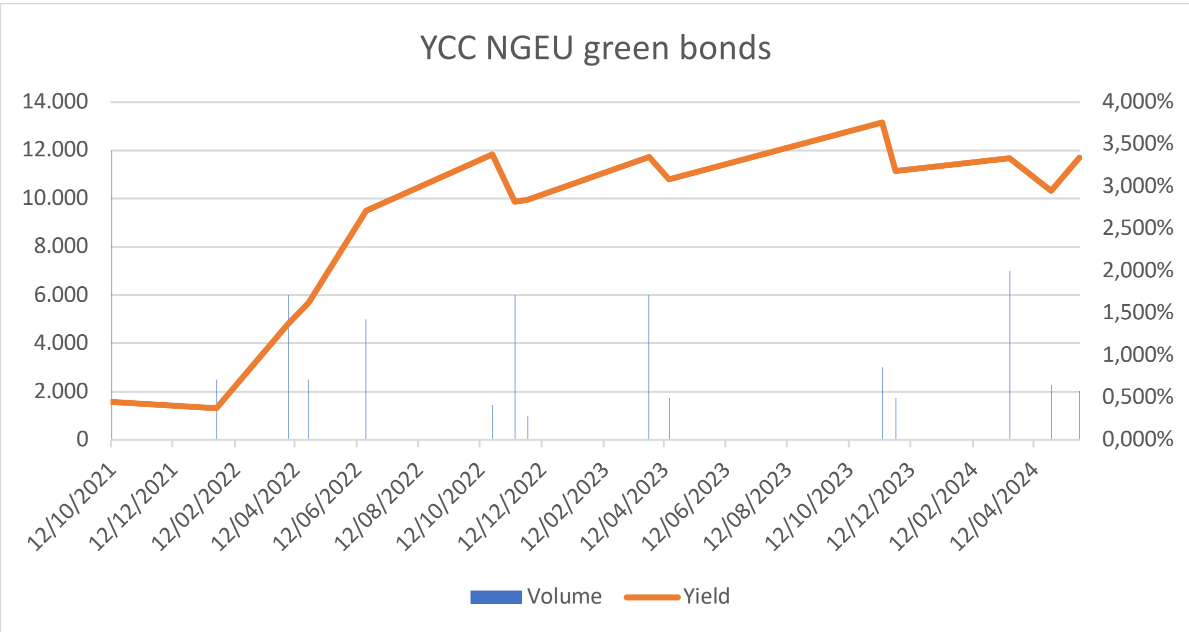
[35] Schramm, L. and Terranova, C. (2024) 'From NGEU to repowereu: Policy Steering and budgetary innovation in the EU', *Journal of European Integration*, pp. 1–19. doi:10.1080/07036337.2024.2353791.

to reinforce several existing EU programs[36]. Although, the Commission will finance up to 30% of NextGenerationEU by issuing some so-called “Green Bonds”, making the Commission the largest green bonds issuer in the world. The first “NextGenerationEU Green Bond” has been issued in October 2021 and through this 15-year bond, the Commission raised €12 billion, making it the world's largest green bond transaction to date. Since then, the Commission has continued to be active in the market with new green lines and taps.



[36] https://commission.europa.eu/strategy-and-policy/eu-budget/eu-borrower-investor-relations/nextgenerationeu_en?prefLang=ro


YCC Eurobonds
25.000
20.000
15.000
10.000
5.000
0
4,500%
4,000%
3,500%
3,000%
2,500%
2,000%
1,500%
1,000%
0,500%
0,000%
-0,500%
-1,000%
Volume issued (EUR mn)
Yield


YCC NGEU green bonds
14.000
12.000
10.000
8.000
6.000
4.000
2.000
0
4,000%
3,500%
3,000%
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12/10/2021
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12/04/2024
Volume
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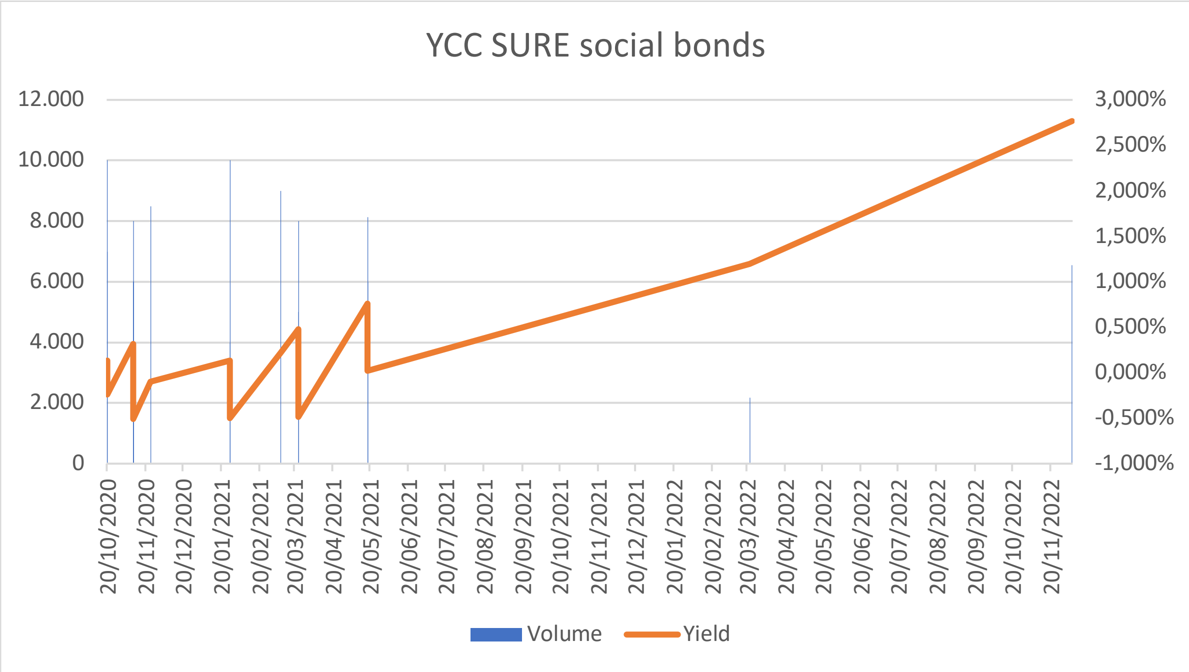


The graphs above show four different Yield curves for the four different instruments issued by the EU on the financial markets: Eurobills, Eurobonds, Next Generation EU green bonds and the SURE social bonds. This last instrument is the EU program to finance short-term employment schemes across the EU and keep people in jobs during the coronavirus pandemic. On 7th December 2022, the EU issued its last bond under SURE, raising €6.55 billion through a 15-year social bond. The transaction brought the total funding raised under the program to €98.4 billion, out of a maximum funding envelope of €100 billion (available only until the end of 2022). The Commission's unified funding approach is an extension of the diversified funding strategy originally put in place for borrowing under the NextGenerationEU program. The repayment of EU borrowing allocated to NextGenerationEU will start in 2028 and will take place over a 30 years horizon – until 2058. The loans will be repaid by the borrowing Member States while the grants will be repaid by the EU budget.

Beside the different financing and functioning structure of the ESM and NGEU, it is important however to remark on the diverse typology of the two crises that led to the creation of the instruments. While the first one was characterized by an aggressive speculation of national bonds on the financial markets that has worsened the already misconducted economic condition of the Southern European countries, the second one involved the collapse of the health system with spillover effects on the real global economy, in particular of the European ones. At the first stage the undertaken measures were decided at the local levels, such as social distancing, total or partial lockdowns and other kinds of limitations. Then the response has been made at the communitarian level with the purchase of vaccines by the EU Commission, the imposition of a Green Pass and finally the establishment of a Recovery Fund within the NGEU initiative. Even if both the two crises had the same consequence of strengthening the European integration evidencing how the European national economic systems are so interconnected, the solutions adopted are addressed to deal with two different issues. One is asked to repair structural fiscal problems reflected on the monetary system of target countries while the second had to restart the paralyzed economy of the whole area.

2.2.3 The Geopolitical Crisis' Effect: REPowerEU

In February 2022 the Russian invasion of Ukraine caused the disruption of a geopolitical crisis that hit Europe hardly. The European Union felt challenged at the security and energetic levels and was demanded once again to provide fast response to preserve the safeness of its citizens. Within this context the implementation of measures aiming to strengthen integration at the European level functioned as a shield against an external geopolitical threat that, however, has not been totally averted. The first issue to deal with was the severe increase of the energy price which, in particular gas, rose up to 559%[37] for some European countries.

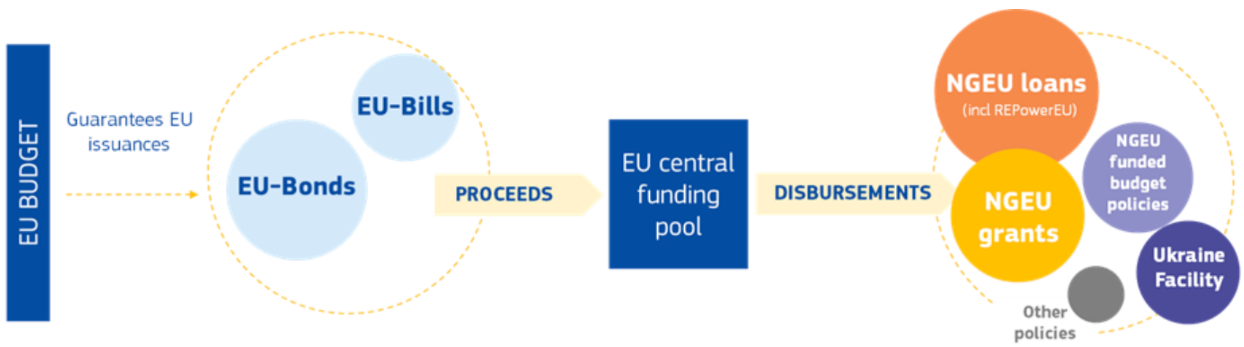
Suddenly, the objective of the Union became the energetic independence from Russia which used the gas furniture as a blackmail against the EU's sanctions. Again, the Union had to deal with the difficulties of finding compliance within a heterogeneous framework of countries with different energetic sources. The plan launched by the Commission to pursue its aims has been called "REPowerEU" based on the 3 main actions:

- Save energy
- Produce green energy
- Diversify the energetic sources

The first important measure has been proposing common European procurements for the gas which means a common purchase of energy avoiding internal competition and decreasing the prices. Then the Member States agreed on changing the energetic directives in order to save energy by establishing the percentage of plant-stock filling of 80%. Another agreement has been found in decreasing gas consumption by up to 15% at the national level. Furthermore, according to the European Commission, the production of wind and solar energy in 2023 exceeded the gas one and ensuring that 39% the electric energy came from renewable sources. The reason why the REPower EU plan, implied in the European Energetic Strategy, represents a valuable example for the purpose of this thesis is the way

[37] https://www.greenmatch.co.uk/blog/energy-prices-europe

it is financed and its scope. The investments realized with the plan required huge reforms and resources. The EU institutions, in particular the Commission and the European Investment Bank, mobilized almost 300 bn of euros whose 72 in grants and 225 in loans. Of course, the Resilience and Recovery Plan represents a key tool of the financing mechanism. The rapidity that characterized the adoption of this measure was required by the necessity of dealing with an abnormal inflation that hit the whole EU. While the ECB tried to preserve the currency's power by increasing the interest rates (monetary policy), the Commission's priority was to contain the energy's price, in particular of gas and carbon fuel, to protect the Member States and their purchase power. This collective effort not only harmonizes regulatory frameworks and investment strategies but also facilitates the pooling of resources and expertise, leading to greater efficiency and cost-effectiveness in the transition to clean energy. The REPowerEU has been inserted within the NGEU plan 2021-2026 and so implemented in the national recovery plans. Unlike the solution adopted to deal with the sovereign debt crisis, the measures implemented during the 20s show a shift towards using financing rather than rulemaking to influence how European Member States work[38]. However, the budgetary capacity of the Union is thus limited and constrained by the overall ceiling of EU expenditure, determined every seven years in the MFF depending on the priorities demanded by the external and internal context.



2.2.4 Changing in the EU's budgetary policy

When talking about fiscal integration we have to make a distinction between two instruments: fiscal regulation and fiscal capacity. The first one, that comprises rules regulating the EU's and Member State's revenues and expenditures, has been analyzed in the first chapter and is still subjected to an on-going process of harmonization and integration. The fiscal capacity on the other side, which

[38] Weber, Ruth. *The Financial Constitution of European Integration*. Hart Publishing, 2023.

represents the object of the regulation, composed by expenditures and revenues policies, has experienced a great integration only recently and mainly for its first component, the expenditures. With the NextGenerationEU program and the REPowerEU one, the Union started a massive plan of common expenditures financed by the emission of European debt. These expenditures will be repaid not by national or European public revenues as taxes but by three different ways proposed by the Commission: the first based on revenues from emissions trading (ETS), the second drawing on the resources generated by the proposed EU carbon border adjustment mechanism, and the third based on the share of residual profits from multinationals that will be re-allocated to EU Member States under the recent OECD/G20 agreement on a re-allocation of taxing rights[39]. The incorporation of these new own resources in the EU budget is made up by two parts. First, the Commission proposes to amend the Own Resources Decision to add the three proposed new resources to the existing ones. Secondly, the Commission puts forward a targeted amendment of the regulation on the current long-term EU budget 2021-2027, also known as the Multiannual Financial Framework (MFF Regulation). This amendment offers the legal possibility to start repaying the borrowing for NextGenerationEU already during the current MFF (European Commission, 2021). When the EU's supranational institutions (Commission and Parliament) are involved in the fiscal capacity and fiscal regulation decision-making process, the two components can be conceived as "autonomous". On the contrary, the two instruments of fiscal integration are dependent on the MSs if the intergovernmental institutions (the Council and the European Council) are the key decision-makers[40]. The European Union is currently experiencing a transitional period where an autonomous expenditure which, however, has a temporal effectiveness (2021-2027) and targets only particular investments, is financed by differentiated revenues excluding an autonomous taxation talking about a "budgetary dependency". Nonetheless, the Pandemic crisis blurred part of the fiscal sovereignty's boundaries between the EU and the MSs. However, before conceiving the NextGenEU program, some MS have considered the possibility of an intervention made up by the European Stability Mechanism, the institution created in 2012, that would have led to a distinction between needing member states and apparently "stronger" ones. The adoption of the NGEU in 2020 and of the REPowerEU in 2022, reshaped the EU budgetary policymaking. A previous example of fiscal policy born to protect the interest of the European economies as a redistributive instrument that became then the core of European economic integration is the Common Agricultural Policy (CAP). Unlike the CAP, the

[39] Newsroom. "Coronavirus: EU Strengthens Action to Tackle Disinformation." *Modern Diplomacy*, 11 June 2020, moderndiplomacy.eu/2020/06/11/coronavirus-eu-strengthens-action-to-tackle-disinformation/. Accessed 19 Sept. 2024.
[40] Woźniakowski, Tomasz P, et al. "Comparative Fiscal Federalism and the Post-Covid EU: Between Debt Rules and Borrowing Power." *Politics and Governance*, vol. 11, no. 4, 27 Oct. 2023, pp. 1–5, https://doi.org/10.17645/pag.v11i4.7653. Accessed 19 Apr. 2024.

NGEU and the REPowerEU have been thought as crisis's resolution mechanisms, created in times of urgency as happened with the ESM during the eurozone crisis. At the same time, these new budgetary instruments do not rely on intergovernmental treaties but operate within the Union's legal structures and apply to all EU member states. Both these two new instruments are also characterized by three important features that confer to the European budgetary governance an advanced function[41]. First, they establish a more direct link between fiscal policies and political objectives. While agricultural and cohesion funds are treaty-based programs legally defined and addressed to the structural functioning and harmonization of the European economies, the NGEU and REPowerEU involve political priorities such as the green transition which, in the REPowerEU context, is explicitly linked to an overcoming of the European dependency on the Russian fossil fuel. The second feature is the room for maneuver left by the two instruments to the national authorities for the designation and implementation of their plans. Although the transposition of the RFF resources is subjected to an approvement by the Commission of the national plans, the new budgetary policy promote the principle of national ownership and collaboration among national and supernational levels rather than a subordination. This represents an important changing compared to the measures implemented in previous crisis. The last characteristic that allows a successful interaction between EU institutions and member states, based on a "soft" conditionality imposed by the former on the latter for the development of the Union's economy, is the obligation to promote investments and reforms. It links financial assistance to the definition and implementation of national plans following the country-specific recommendations of the European Semester. This performance-based approach again differs from the supranational constraints to national spending as part of the austerity measures adopted in response to the Eurozone crisis.

To conclude, we can say that the new budgetary policy of the EU is composed by a public spending financed through the emission of a temporary public debt which leaves almost the same degree of maneuver to the national fiscal authorities in terms of taxation. However, this program is supposed to terminate in 2027 (deadline of the NGEU), on the other side an hypothetic permanent adoption of this new European fiscal mechanism would require a revision of its functioning in order to understand whether the sustainability of this model, that avoid a European direct taxation, is possible. Recalling the Ricardian theory, which affirms that issuing more public debt today means an higher tax burden for the future generation, the involvement of the national fiscal regimes seems to be a natural evolution of the new European policy. A mandatory step to be achieve in order to obtain the last

[41] Schramm, L. and Terranova, C. (2024) 'From NGEU to repowereu: Policy Steering and budgetary innovation in the EU', *Journal of European Integration*, pp. 1–19. doi:10.1080/07036337.2024.2353791.

tranche of the NGEU is in fact a reform of the national fiscal system. At this point a useful instrument to understand the potential framework of a European federalism is to analyze and compare already established fiscal integrated models.

2.3 The EU and other federalism systems

According to what has been discussed so far it emerges that the European Union is experiencing a shifting process from its "regulatory state" nature[42] to a fiscal policy-maker actor. Nonetheless it still relies a lot on the regulation policy tool which allows the EU to be so influential with so few staff and such relatively small resources. Until the NGEU program, the EU Commission has been mainly market-oriented. The priority since the birth of the Union was the preservation of the internal market functioning which has been broadly regulated at the central level but left an important aspect of the EU's economic system deregulated and remitted to the discretion of the member states. Given this premises the first question arising when comparing the EU to other political-economic systems is whether the Union is or not assimilable to a federation. In order to answer we can compare it with pre-established federalism models external and internal the EU. In general, a federalism system is characterized by centralized and local functions. Within the first group usually the most important are: defense, external relations, commerce, labor law and public health. However, the powers division differs by country, here are analyzed three different models: U.S, Germany and Spain.

2.3.1 Federalism in the U.S.

The federalist model of the United States of America has experienced a gradual evolution through the years since the independence in 1776. At first the model was conceived as a Confederation which would have allowed an high degree of sovereignty to the States. However, in 1787 the new

[42] Scott L. Greer (2021), "Health, federalism and the European Union: lessons from comparative federalism about the European Union".

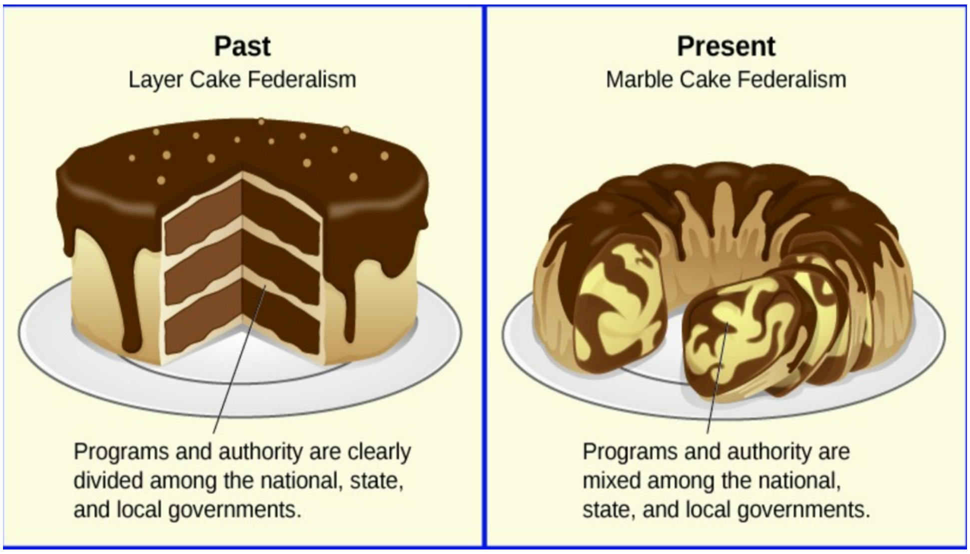
Constitution established the adoption of a federal system thus strengthening the prerogatives of the central power. The new state that born in 1776 and was then reshaped by the Federal Constitution was an extraordinary exception to the dominant models in Europe. It was in fact - also because of the peculiar form assumed from the beginning by the British colonies in America - a State without noble hierarchies and class, based on the idea of a substantial equality of citizens' rights, on political and religious freedom, the separation of Church and State, and a strong tradition of self-government. With the defeat of the Confederate States after the Civil War in 1865 the balance of power between the states and the central government experienced an important impact in two different ways[43]. First, the Union victory put an end to the right of states to secede and to challenge legitimate national laws. Second, Congress imposed several conditions for readmitting former Confederate states into the Union. This was the beginning of what is considered a "**Dual federalism**". Under this model the states and national government exercise exclusive authority in distinctly delineated spheres of jurisdiction. Like the layers of a cake, the levels of government do not blend with one another but rather are clearly defined. The federal government and state governments were co-equal entities. Article I, Section 8 of the United States Constitution listed a few things that the federal government was empowered to do. The federal government could: tax, declare war, establish foreign policy, regulate interstate commerce, make copyright and patent laws, establish post offices, and coin money[44]. On the other side the Member States had an high degree of maneuver in civil and criminal law, conduct elections, education, public health and amend U.S. Constitution. The model started to appear weak at the end of the 1920s when the economic depression hit the industrialized world. With the collapse of the economic system and a growing social crisis, the U.S. central government started to collaborate with the states in shared subjects in order to find better solutions. **Cooperative federalism** also referred to as "marble-cake" federalism, emerged during the New Deal, where the federal and state governments developed a flexible relationship with overlapping and shared power in cooperation to address specific issues or implement programs. Examples include: (1) **grants-in-aid**, where the federal government allocates funds to states to use for a specific purpose or a broader policy; and (2) **regulated federalism**, where the federal government sets mandated regulations and rules for states to follow, with or without federal funding.

We could say that the European Union is currently experiencing that same shifting from a dual federalism to a cooperative federalism after experiencing an economic crisis considering the NextGenerationEu as a European "New Deal". However, one of the most important powers of the U.S. central government which is that of collecting taxes still remains out from the EU Commission's

[43]https://oertx.highered.texas.gov/courseware/lesson/1173/overview#:~:text=In%20the%20era%20of%20dual,previously%20handled%20by%20the%20states.

[44] https://usgovtpoli.commons.gc.cuny.edu/chapter-five-federalism-american-style/

competence. However, there are some so-called “tax heavens” within the U.S. as well. Every states has in fact some own fiscal policy instruments that may favorite the inflow of capitals, one example is Delaware. An important difference between the EU fiscal system and the U.S. one is the budget available which represents the 20% of the GDP for the United States and just the 1% for the EU.



Fonte: OER Commons

2.3.2 Federalism in Germany

As established by Article 70 of German Constitution, all the lawmaking power rests in the hands of the 16 states or *Länders* that compose Germany. The historical roots behind this administrative division is totally different from the North American one. It comes from political arrangements born during the middle age when the current German territory was made up by principalities and royal houses with their own customs and culture that decided to sign agreements for allegiances in foreign policy. After being abolished under the Nazi government, the *Länders'* administration has been restored in the 40s following a division scheme designed by the allies' occupation of 1945. In 1949 it has been established the *Bundesrat,* an institution addressed to representing the *Länders* in front of the Federal Government and the European Union. Thanks to *Bundesrat* the individual federal state governments participate directly in the decisions taken by the national state. For this reason the *Bundesrat* is the element that mainly differentiate the German federalism from others competing in three main functions[45]:

- It defends the interests of the *Länder* vis-à-vis the Federation and, indirectly, vis-à-vis the European Union.

[45] https://www.bundesrat.de/EN/funktionen-en/funktion-en/funktion-en-node.html

- It ensures that the political and administrative experience of the *Länder* is incorporated in the Federation's legislation and administration and in European Union affairs.
- Like the other constitutional organs of the Federation, the *Bundesrat* also bears its share of overall responsibility for the Federal Republic of Germany.

The *Bundesrat* can be considered a both top-down, bottom-up functioning institution which allows the participation of the *Länders* within the framework laid out in the constitution, formulating the political objectives of the national state as a whole and at the same time it enables the Federation to extend the impact of policy measures to the territories of the federal states. This is done through bills, ordinances and general administrative provisions, as well as indirectly through European Union legislation.

For what regard the policymaking division between the Federal government and the *Länders* the first body has exclusive legislative power for foreign policy issues, defense, citizenship and unity of customs. On the other side the *Länders* have a high degree of legislative power for what concern public health, education and welfare system. Germany has one of the highest levels of fiscal decentralization in the EU. Due to the considerable responsibilities of the sub-national governments, 50% of the government expenditures were managed by the *Länders* (31%) and municipalities (19%) in 2018. The German system seeks to ensure that funding distribution and the executive responsibilities are clearly defined[46]. The taxation system differs from other federalism system because of its “shared regime”. Corporation tax and income tax are shared equally between the Federal government and the *Länders* and additionally, 75% of VAT revenues are redistributed across the *Länders* to ensure a uniform standard of living across the country. This last measure is part of the fiscal equalization mechanism of Germany which is considered one of the strongest in Europe. It is developed on three levels: primary horizontal equalization between the *Länders*, secondary horizontal equalization within the *Länders*, and finally vertical equalization by supplementary federal grants. For what regard the first level, a maximum of 25% of Länder’s share of VAT goes to the Länders characterized by tax revenues below the average. The secondary level implements the equalization of *Länders'* fiscal capacity and in the third step supplementary grants are provided by the Federation to those Länder with subpar fiscal capacity. This resources’ transfer mechanism is not currently appliable in Europe since it would require a political agreement on common spending of tax revenues from a Member States to another. However, such a measure would strengthen already existing

[46] https://portal.cor.europa.eu/divisionpowers/Pages/Germany-Fiscal-Powers.aspx#:~:text=Germany%20has%20one%20of%20the,municipalities%20(19%25)%20in%202018.

mechanism as the Regional Development Fund that aims to ensure an equal economic development of the whole European territory.

2.3.3 Federalism in Spain

Unlike the previous models the Spanish one in not an official federalism since the Constitution of 1978 established the nature of “Constitutional Monarchy” and declares “inadmissible” the creation of a federation. Although, the territory of Spain is composed by 17 *Comunidades Autonomas,* local administrative units with a high degree of autonomy concerning fiscal policy, public health and education. The taxation system differs according to the region, today, almost all the taxation policies in the Spanish fiscal system are assigned to the *Comunidades Autonomas*, the only major taxes that remains at the central government’s level are a component of the IRES (personal incomes), corporate income tax, non-resident tax, social security contributions[47]. There are two different regimes, a classic one and the “*charter regime”* one applied to two Communities: Basque Countries and Navarra. In general, the *Comunidades* collect the local taxes and transfer them to the central government which then calculate the amount of share to be re-allocate among the regions. The *charter regime* works on the other way. The Basque Countries and Navarra collect the local taxes and transfer part of the money to the Central Government. However, when the central government allocates the revenues among the regions, the first element considered is the calculation of each region’s expenditure needs. This relates to the level of expenditure a region needs to provide the same level of services in a particular area of its competency as other regions. In the charter regime, there is no calculation of expenditure needs to guide revenue allocation as in the case of the common regime. The two regions concerned are financed exclusively from the taxes accruing in their territory, which are referred to as “agreed taxes”. Another peculiarity of the Spanish financial regime is the possibility of the regions to issue own public debt within the limit established by the Maastricht Criteria. Nevertheless, the central government represents the main debt holder for most of the regions with the exception of the Basque Countries and Navarra.

[47] López-Laborda, Julio. “The Assignment of Revenue to Spain’s Autonomous Regions.” *SEFO -Spanish Economic and Financial Outlook*, vol. 1, no. 4, 2012, www.funcas.es/wp-content/uploads/Migracion/Articulos/FUNCAS_SEFO/004art08.pdf.

<< 2022	Deuda: Comparativa CCAA 2023			
CCAA	Deuda total (M.€)	Deuda (%PIB)	Deuda Per Cápita	Deuda con el Estado (M.€)
Cataluña [+]	85.986	31,00%	10.720 €	74.087
Comunidad Valenciana [+]	57.993	42,20%	10.908 €	50.083
Andalucía [+]	38.649	19,80%	4.484 €	25.337
Comunidad de Madrid [+]	35.875	12,60%	5.125 €	0
Castilla-La Mancha [+]	16.156	31,90%	7.691 €	12.635
Castilla y León [+]	13.865	19,90%	5.801 €	1.966
Galicia [+]	12.170	16,10%	4.498 €	2.538
Región de Murcia [+]	12.139	31,20%	7.736 €	11.274
País Vasco [+]	10.661	12,40%	4.786 €	0
Aragón [+]	9.186	20,30%	6.810 €	5.695
Islas Baleares [+]	8.579	22,30%	6.967 €	5.178
Canarias [+]	6.518	12,20%	2.915 €	1.288
Extremadura [+]	5.322	21,80%	5.052 €	3.167
Asturias [+]	4.243	15,10%	4.206 €	722
Cantabria [+]	3.316	19,90%	5.609 €	3.075
Navarra [+]	2.951	12,00%	4.351 €	0
La Rioja [+]	1.625	15,70%	5.011 €	922
Total	**325.234**			**197.968**

Fonte: Expansion/Datosmacro.com

The Spanish model might represent the near-future evolution of the EU's federalism: a system made up by local administrative entities (the Member States), with own taxation policies and debt-issuance capacity, under a central government (the Commission) that manages the allocation of revenues and the emission of communitarian debt. However, there are some important elements missing when comparing the EU to the model of unitary State that characterizes Spain. First and foremost, the presence of a central political unitary government with a higher degree of connection with the local authorities and their administrations. The European Union incorporates member states with far more differences among them compared to those among the Spanish *Comunidades* in terms of culture, politics and economic priorities. This implies greater difficulties in finding common policy guidelines and even greater in establishing a unique political and economic system. The second issue is the absence of common corporate taxation policy within the EU. As previously discussed, the different Corporate Income Taxation rates of the Member States is one of the main causes of economic inequalities within the EU. Establishing a common rate following the Spanish example, would assure a better competitiveness of the private market and more transparency.

3. Consequences and perspectives

3.1 Reform Proposals

Through 15 years of economic, health and geopolitical crisis the EU has undertaken important changes to its fiscal regime. Those already implemented have been widely analyzed in the previous chapter but there is still an on-going process of reform mainly concerning the Stability and Growth Pact. After one year of negotiations, on December 2023, the European Council agreed on a new proposal of the SGP presented to the legislative bodies on April 2024 which includes:

- A regulation for the institution of a new preventive arm;
- A regulation for the modification of the existing corrective arm;
- A directive for the new national budget requirements.

The aim of the reform is to ensure sound and sustainable public finances, while promoting sustainable and inclusive growth in all member states through reforms and investment.
The announced objective is to reduce debt ratios and deficits in a gradual and growth-friendly manner, protecting reforms and investments in strategic areas such as digital, green or defense. At the same time, the new framework will provide appropriate room for counter-cyclical policies and help address existing macroeconomic imbalances[48].

3.1.1 Reform of the Preventive Arm

The new regulation 2024/1263 repeals the old regulation 1466/1997 by strengthening the Preventive Arm of the Stability and Growth Pact. With this reform the EU Commission aims to encourage structural reforms and public investments. Under the new rules, the member states have to deliver national medium-term fiscal structural plan that spans over 4-5 years where they explain how it is meant to respond to the main challenges identified in the context of the European Semester, in particular in the country-specific recommendations. In addition, the member state has to incorporate in the structural plan the recommendations of the Commission for a net expenditure path regarding those countries with macroeconomic and deficit imbalances. This recommendation called "reference trajectory" contains two safeguards[49]:

- **debt sustainability safeguard**, to ensure a minimum decrease in public debt levels;

[48] https://www.consilium.europa.eu/en/press/press-releases/2024/04/29/economic-governance-review-council-adopts-reform-of-fiscal-rules/
[49] https://eur-lex.europa.eu/legal-content/IT/TXT/?uri=OJ:L_202401263

- **deficit resilience safeguard**, to provide a safety margin below the Treaty public deficit reference value of 3% of GDP, in order to create fiscal buffers.

The fiscal structural plan will be then subjected to the Council to be approved and then controlled in order to record hypothetical deviations from the net expenditure path. Member states will be allowed to ask for an extension of the plan to a maximum of seven years, if they commit to a set of certain reforms and investments such as fair, green and digital transition, ensuring energy security, strengthening social and economic resilience and, where necessary, the build-up of defense capabilities. This last incentive highlights the impact of the recent crisis on the EU's priorities that make the difference between the new and the old SGP's objective.

3.1.2 Reform of the Corrective Arm

For what concerns the reform of the Corrective Arm, composed by the deficit-based and debt-based excessive procedure, regarding the second component it has been decided to consider the operation of the new multi-annual framework and adopt a dynamic vision of the member state's economic performance. In particular the Commission starts a debt-based excessive procedure in three cases described by the regulation 2024/1264 which modifies the reg. 1467/1997[50].

- the ratio of the government debt to GDP exceeds the reference value
- the budgetary position is not close to balance or in surplus
- the deviations recorded in the control account of the member state either exceed 0.3 percentage points of GDP annually, or 0.6 percentage points of GDP cumulatively.

On the other side the deficit procedure is not appliable if the exceedance is considered to be temporary or exceptional. The excessive deficit shall be considered as temporary if the budgetary projections drawn up by the Commission indicate that the deficit will decrease below the reference value after the serious downturn has ceased, this is the case of Spain which, despite being above the limit value for the deficit, has been assessed able to reduce it within the 2025 and so it has not been subjected to an Excessive Deficit Procedure.

3.1.3 Reform of the National Budget Requirements

The Directive 2024/1265 modifies the old dir. 2011/85/UE concerning the requirements for the Member State's budget. This directive aims to strengthen and improve public accounting practices

[50] https://eur-lex.europa.eu/legal-content/IT/TXT/?uri=OJ:L_202401264

and the quality of fiscal statistics, ensuring greater reliability and comparability of data among Member States. The main changes of the new directive are represented by the following points[51]:

- **Strengthening public accounting practices**: the directive encourages Member States to maintain comprehensive and reliable public accounting practices across all subsectors of public administration. This is crucial for producing high-quality statistics and ensuring the proper functioning of the EU's fiscal surveillance framework.
- **Quarterly data on deficit and debt**: member States and the Commission are required to publish quarterly data on public deficit and debt. This measure allows for closer supervision and improves the quality of budgetary forecasts.
- **Macroeconomic and budgetary forecasts**: member States must compare their macroeconomic and budgetary forecasts with those of the European Commission and other independent bodies. These forecasts should undergo periodic evaluations to improve their accuracy.
- **Independence of fiscal institutions**: the directive reinforces the role of independent fiscal institutions responsible for overseeing public finances. These institutions must ensure the preparation, evaluation, or endorsement of macroeconomic forecasts.

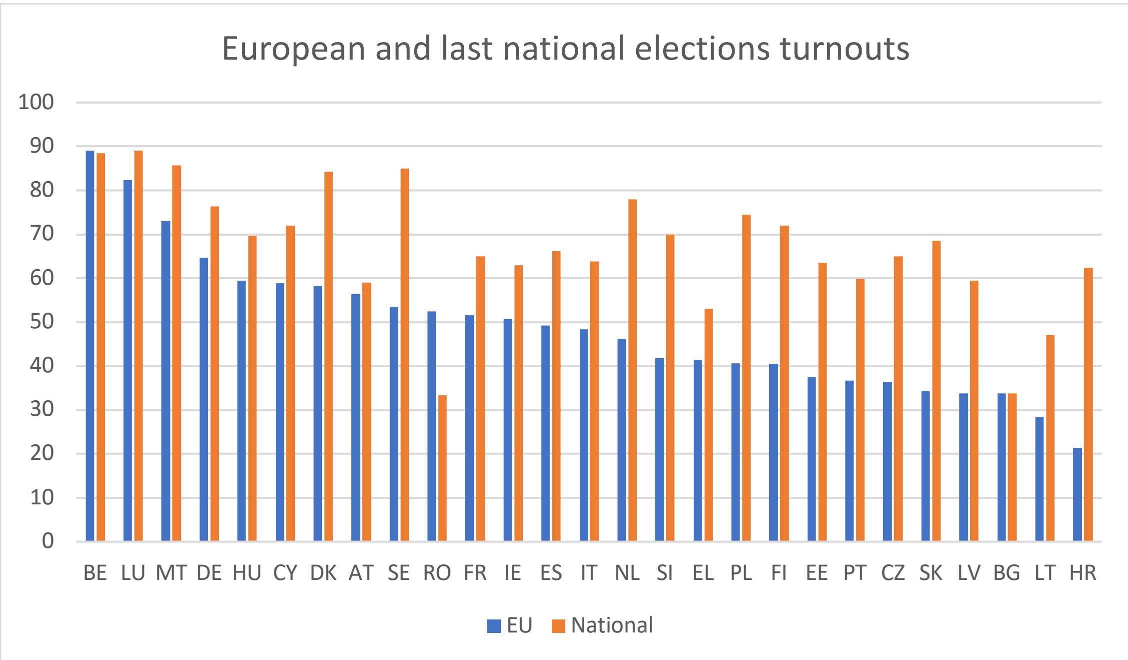
The four components of the new Stability and Growth Pact aim to implement fiscal harmonization and coherence among the member states and ensure more transparency of the national and communitarian financial policies.

The reasons behind the adoption of such reform are multiple. First of all, there was the need to deliver better fiscal surveys and analysis improving the quality of fiscal policy recording in order to provide an higher fiscal surveillance. In addition, the SGP adopted in 2011 was still lacking some elements and needed to be updated to comply with the new international economic practices. An important actor of this reform has been the European Court of Auditors which suggested in 2019 a revision of the budget requirements in order to implement the surveillance and the harmonization. The last reason is the necessity of providing reliable macroeconomic analysis and compare the Commission's one and the national ones evaluating them ex-post.

[51] https://eur-lex.europa.eu/legal-content/IT/TXT/?uri=OJ:L_202401265

3.2 Winners and losers

The European crisis had a dual effect on EU's political framework. First, citizens blamed both the European integration and their own governments for their perceived difficulties. The increased degree of politization led to a major polarization of opinions and to a reconsideration of the European policy mechanisms. The growth of populist parties and Euroscepticism reach the peak in 2016 with the Brexit referendum which caused the fear for a European disintegration. At the same time the EU undertook a reinforcement of the integration process in several policy areas as analyzed in the previous paragraphs. Thus, the reforms adopted and the new initiatives have brought the European Union further to the path towards an 'Ever Closer Union'[52]. By strengthening the fiscal surveillance and the socioeconomic governance on indebt member states, the EU politics has become more coercive leading to a new demand of political power by the states. What is clear is that citizens are still looking at their own national governments as an instrument to gain political advantages in Europe instead of considering the EU a comprehensive body. If we look at the European elections it is clear that the member states' turnouts are always lower than those for the election of the national government (with the exception of Belgium and Romania) and most of time by far.



Fonte: EU Parliament

[52] Saurugger, Sabine. *The European Union and Federalism: Possibilities and Limits*. No. 218, 1 Jan. 2018, pp. 173–200.

This demonstrates a concerning low level of European identity among the citizens reflected by a lack of communitarian solidarity which emerged during the first phase of the Covid crisis. When the economic crisis resulted by the pandemic seemed to be limited to Italy, the skepticism for resources-sharing of northern European countries highlighted the divergence between the so-called frugal countries and the southern European ones. A similar situation happened in 2011 when many Germans were worried whether the European crisis would lead the German economy to redistribute its wealth to its southern neighbors[53]. Angela Merkel severely criticized the idea that Germany was going to pay for countries such as Greece or Portugal which were blamed for their fiscal imprudence, an idea shared also by the Finnish and Dutch governments[54]. Like the Spanish model, discussed above, there are some member states claiming to contribute more than what they receive from EU in financial terms accusing the European redistribution mechanism of unfairness, especially in crisis 'times. This has been one of the main accuse of the pro-Brexit campaign in UK. If we classify the MS based on their net contributions (Contributions-Returns), Germany occupies the first place, putting in 25.6 billion euros more than it gets out, then France follows with net contributions of 12.4 billion euros. The UK, previously came in second place in the ranking, is now third with roughly 10 billion euros of net contributions in 2018[55]. Poland, on the other side, has been the highest beneficiary in 2021 with a net income of 11.9 billion euros (almost all the contribution of France). However, this distinction is not necessarily correlated with the level of European support expressed by the citizens. In Germany, for example, support for the EU is high despite the budget contributions might outweigh direct financial benefits for the country. The impact on the national economy in fact has been real, according to a study by the Bertelsmann foundation[56] the single EU market increased the average incomes of Germans by over 1000 euros, above the EU average increase of 840 euros. In addition, Germany had already experienced resources transfer mechanism after the fall of the Berlin wall when there was the necessity to encourage the development of the eastern regions. The reason behind this economic rivalry among the European member states are mainly linked to cultural differences and a market historical competition. Furthermore, a complete fiscal integration would imply an economic system that relies upon different fiscal behaviors under a same regime. The idea of a common taxation policy is considered almost impossible to realize due to the high political protection especially in the "Tax

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[53] Saurugger, Sabine. *The European Union and Federalism: Possibilities and Limits*. No. 218, 1 Jan. 2018, pp. 173–200. Accessed 8 July 2024.

[54] Saurugger, Sabine. "Sociological Approaches to the European Union in Times of Turmoil." *JCMS: Journal of Common Market Studies*"

[55] Buchholz K. "Which Countries are EU Contributors and Beneficiaries? (2023)

[56] Gnath, Katharina. "Study - EU Single Market Boosts per Capita Incomes by Almost 1,000 Euros a Year." *Www.bertelsmann-Stiftung.de*, 2019, www.bertelsmann-stiftung.de/en/topics/latest-news/2019/may/eu-single-market-boosts-per-capita-incomes-by-almost-1000-euros-a-year.

Heavens" countries. If we imagine a hybrid model, similar to the Spanish one, as a way to gradually transform the model "Multi-speed Europe" towards a federalism, we'll realize that some countries will pay an higher cost than others in terms of contributions/revenues ratio as it happens now. However, what would really make the difference would be the establishment of a common corporate tax on incomes that would ensure a fairer job market and encourage the development of "brain draining" member states. To make this hypothetical scenery work, it should be implemented the private fiscal surveillance instead of the public one. Corporates and citizens of all the EU area are supposed to adopt the same practices in compliance with the common rules. Recalling the three pillars explained by Professor Cottarelli[57] for a fiscal integration: stronger constrains on the fiscal policies, a larger central budget and the harmonization of non-fiscal policy, every member state will be affected in a different way and will be asked to consider gains and losses of this "transformation". The stronger constrains on fiscal policies, that are usually strongly supported by the so-called "frugal states", as the last implementation of the Stability and Growth Pact are, on the other side, contested and accused of excessive technocracy by the Southern European Member states. However, the latter group will benefit from a larger central budget which will be financed more by the first ones following a proportionary mechanism. For what regard the third pillar, the harmonization of non-fiscal policy, such as the defense policy, will encounter several challenges in dealing with politically non-aligned European governments, first of all the V4[58] ones.

3.3 Perspectives: Draghi's Report on European Competitiveness

The importance of the arguments discussed so far is strengthened by the Draghi's Report "The Future of the European Competitiveness" published on September 2024[59]. The paper addressed three main issues of the EU considered responsible of a severe fall in its economic competitiveness compared to two main actors: the U.S. and China. The first cause is represented by an excessive *innovation gap* between Europe and its competitors which slows down the production pipeline of the first actor's industrial system. The EU position on the global rank of advanced technologies' producers is notably weak and this risks to discourage investors and capital inflows paralyzing markets and trades. Another obstacle to the European economic development is the energy landscape which has been negatively influenced since February 2022, leading to electricity prices

[57] Cottarelli, C. (2013) 'European Fiscal Union: A vision for the long run', *Swiss Journal of Economics and Statistics*, 149(2), pp. 167–174. doi:10.1007/bf03399387.
[58] The Visegrád countries: Hungary, Czechia, Slovakia and Poland. The V4 are often unaligned with the European political trajectory, especially for what concerns the migration policy.
[59] Draghi, M., 2024. *Il futuro della competitività europea: raccomandazioni e strategie per un'Europa più forte*. Bruxelles: Commissione Europea. Disponibile su: https://www.eunews.it [Accesso 17 Settembre 2024]

that are 2-3 times those in the US and even higher gas prices. The energy transition with the dismission of fossil fuels represents a priority to achieve as soon as possible, especially if we look at the speed with which China, the biggest competitor in this sector, is undertaking the same process. The third and last issue highlighted by the former ECB's president is the EU's poor geopolitical relevance on the global equilibrium due to its high degree of dependance in key sectors as raw materials, defense and technology. The report suggests then accurate possible solutions that include some of the objectives described in this thesis. The core part of the strategy involves the full implementation of the Single Market in order to: enable an integrated multimodal transport market; negotiating preferential trade deals and building more resilient supply chains; mobilizing greater volumes of private finance; and as a result, for unlocking higher domestic demand and investment. Then, it is remarked to importance to invest in industrial and trade policy at the European level and considered as a part of an overall strategy which includes also a larger EU budget for investments which now remains around 1% of EU GDP. The final consideration is about the EU's governance which, according to Draghi, needs a reform which increases the cross-national coordination and reduces the regulatory burden. The progressive steps suggested have to be undertaken with coherence and smoothness avoiding bureaucratic process as Treaty's reform. The economic and financial integration is seen as a key tool to increase the efficiency of the European market and its stability.

Conclusion

The completion of the European fiscal integration represents a topic that has been discussed for decades at different stages. During the second half of the 20th century, the centralization of the European economy was considered an instrument to relaunch the continental market, sharing materials and important resources as energy, coal and steel. In the 70s it was clear that such centralized system was generating disparities among the peripheric regions with a slower index of development. For this reason, it was created the European Regional and Development Fund, a set of resources addressed to assure a homogenous economic growth of the whole EU area. The real game changer set of rules arrive in the 90s, following the instructions set by the "White Paper" of Delors' Commission in 1985. The creation of a well-established internal market was to be accomplished in three steps: the abolishment of exchange controls and the liberalization of capital movements within the community; the adoption of fiscal rules (SGP) and the creation of a monetary policy-making authority (ECB) to assure budgetary discipline; the adoption of the Euro as a common currency. Then the Union has been enlarged towards East, embracing some of the ex-soviet countries, from this point the economic nature that represented the core essence of the EU was replaced by a political one. With the Lisbon Treaty of 2009, which established the figure of the European Commissioner for the External Relations, it was clear that the EU adopted a significant political sense strengthening its institutional powers and temporarily underestimating its economic weaknesses. When the financial crisis broke out in 2011, the political internal divisions contributed to worsen the economic situation of the Southern-European countries and discussions about the failure of the EU project and "Grexit" exposed the whole Euro-area to an unprecedent risk of default. The immediate solution has been political rather than economic. The announcement of the adoption of the so-called "out-right monetary transactions" by the ECB helped to cool down the crisis and assured the European cohesion. However, the Union understood the importance of strengthening the economic and financial system along with the political one, resulting in the institution of the ESM, which saved Greece, Spain and Cyprus from the default, the unification of the banking system and the establishment of new fiscal rules within the Six Pack, the Two Pack and the Fiscal Compact. The implementation of the fiscal surveillance has guaranteed more economic stability but then the EU had to deal with two new black swans: health and energetic crisis. The first one, which has been faced with more compactness compared to the financial crisis, led to the launch of the biggest resources-allocation plan since the Marshall Plan, the NextGenerationEU. This initiative has been realized through the emission of common debt bonds (Eurobonds), a measure widely discussed which had often encountered the opposition of the "frugal states". The energy crisis, on the other side, was more related to a larger context of geopolitical crisis that asked for a stronger effort of the EU Commission in finding a solution able to comply with three objectives: energetic independence, green transition and security. With the REPowerEU initiative it has been drawn the path to achieve the first two points while the last one represents a crucial object of discussion. The institution of a Common Defense body at the European level would have a huge impact on both the political and economic level. It would require a continuous resources contribution financeable through common expense. If, as we have seen, each external threat involving the EU resulted in implementing the Union's economic, political and fiscal system, in this case a threat to the common security might have a dual consequence: the implementation of common defense and the enlargement of the EU's budget, a measure achievable likely with common taxation. The pros and cons of this policy can be easily deducted, and this is why it represents such an objected topic. However, if we look at other federal systems, we could imagine a fair alternative to the "Multi-speed Europe" model which creates much competitiveness among member states rather than among single economic actors, slowing down development and weakening our political cohesion. A European federalism would represent the final stage of the European Union project born after the second world war but speculating on its efficiency and consequences is complex given the different historical, economic and political background that the member states have and from which they will hardly detach unless there is a serious threat to their security. The past should have taught us that prevention is better than correction not only for what regards the single national fiscal behaviors but for the common political-economic one as well. If the EU continues to find itself suddenly exposed to disruptive events of different nature it will always react firstly with failing national measures instead of efficient communitarian ones. To invert the process, it will be needed standard political measures, greater central budget and equal fiscal rules that would assure similar national priorities and interests. The last 10 years have witnessed an important effort generated by the EU policy-making actors that now has to be completed by structural changes addressed to an economic enforcement of the Union.

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