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research paper

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FUNDING THE WAR IN UKRAINE: THE EUROPEAN PEACE FACILITY, THE MACRO-FINANCIAL ASSISTANCE INSTRUMENT AND THE SLOW RISE OF AN EU FISCAL CAPACITY

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ABSTRACT

The war in Ukraine represented a major geopolitical shock for the European Union (EU). In the face of an illegal Russian aggression EU institutions and member states rallied to support Ukraine. Nevertheless, the war in Ukraine also exposed the limited fiscal capacity of the EU. As a result, EU institutions and member states had to come up with creative ways to financially back Ukraine's military and civilian efforts. This paper examines the two key tools deployed by the EU to fund Ukraine in its war against Russia, namely the European Peace Facility (EPF) and the Macro-Financial Assistance (MFA+) Instrument. The paper details the legal features of these tools, evaluates their intergovernmental vs supranational nature, and reflects on their significance for the consolidation of an EU fiscal capacity. As the paper argues, the war in Ukraine quickly prompted the EU to replicate some of the novelties it used to respond to the Covid-19 pandemic, namely the use of common borrowing and spending. Nevertheless, structural fiscal and governance weaknesses still limit the ability of the EU to mobilize resources and leverage power on the international stage.

Keywords: War in Ukraine, EU budget, debt, European Peace Facility, Macro-Financial Assistance

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1. Introduction • 2. The European Peace Facility • 3. The Macro-Financial Assistance Instrument • 4. Exogenous threats and path dependency: the consolidation of an EU fiscal capacity • 5. Governance problems and constitutional constraints: challenges towards fiscal integration • 6. Conclusion

1. Introduction

The war in Ukraine, which began on 24 February 2022, when Russia illegally invaded the sovereign territory of an independent nation, posed an unprecedented challenged for the European Union (EU). The return of war on the European continent shattered illusions of a perpetual peace, and forced the EU to confront the demands of hard power at its Eastern borders. In this context, a pressing need for the EU institutions and member states has been to support Ukraine financially in its efforts to defend itself against the Russian aggression. The Russian military invasion of Ukraine, in fact, caused a dramatic death toll, with probable cases of war crimes, massive displacement of refugees and widespread damage to critical infrastructures. Reacting to these horrific facts, and to such a blatant breach of international law, the EU mobilized resources to both assist the Ukrainian military in purchasing defense weapons and the Ukrainian civilian authorities in funding operational government expenses and rebuilding, to the extent possible, critical infrastructures.

The purpose of this article is to examine from an EU law and policy perspective the two key instruments that the EU deployed in 2022 to finance Ukraine in the war against Russia's aggression, namely the European Peace Facility (EPF),[1] and the Macro-Financial Assistance Instrument for Ukraine (MFA+).[2] The article endeavors to detail the legal features of these tools, to evaluate their intergovernmental vs supranational nature, and to reflect on their significance for the consolidation of a fiscal capacity in the EU. As the article points out, at the beginning of the war in Ukraine, the EU resorted to the EPF, a novel funding instrument dedicated to foreign policy objectives, worth 5.6bn€, which is fully funded by member states' transfers and subjected to their unanimous intergovernmental decision-making in Council. Subsequently however, as the war in Ukraine continued, the EU crafted the MFA+, a larger 18bn€ financing tool approved jointly by the European Parliament (EP) and Council, which enables the Commission to issue common debt, backed-up by states' guarantees, and to transfer these own resources to Ukraine.

As the article argues, the war in Ukraine quickly prompted the EU to replicate some of the novelties it used to respond to the Covid-19 pandemic. As it is well known, to address the devastating socio-economic consequences of the pandemic, the EU agreed in 2020 to establish ground-breaking instruments such a 100bn€ unemployment re-insurance system called SURE,[3]

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[1] Council Decision (CFSP) 2021/509 of 22 March 2021 establishing a European Peace Facility and repealing Decision (CFSP) 2015/528, OJ 2021 L 102/14 [hereinafter EPF Decision]

[2] Regulation (EU) 2022/2463 of the European Parliament and the Council of 14 December 2022 establishing an instrument for providing support to Ukraine for 2023 (macro-financial assistance +), OJ 2022 L 322/1 [hereinafter MFA+ regulation]

[3] Council Regulation (EU) 2020/672 of 19 May 2020 on the establishment of a European instrument for temporary support to mitigate unemployment risks in an emergency (SURE) following the Covid-19 outbreak, OJ 2020 L 159/1 [hereinafter SURE regulation]

and a 750bn€ Recovery Fund, known as Next Generation EU (NGEU).[4] The latter, in particular, endowed the EU with a fiscal capacity by empowering the Commission to raise funds by issuing common debt on the financial markets, to transfer these amounts to the member states as grants and loans, and long term to levy new taxes to repay capital and interests on the debt.[5] Formally speaking, the financial tools rolled out to address Covid-19 were designed to be temporary. Yet, NGEU, and SURE, provided a model that the EU promptly re-used when facing the war in Ukraine. In particular, the MFA+ entails once again common borrowing and spending, which suggests a trend towards consolidating a centralized fiscal capacity at the EU level of government.

Nevertheless, the consolidation of a fiscal capacity in the EU continues to be hampered by structural weaknesses. In particular, as the article highlights, the MFA+ is exclusively designed to fund Ukraine in 2023 – for a 12-month period. Moreover, tactical opposition by a single member state – Hungary, which vetoed the measures for several months – almost derailed the effort to pass the MFA+. In fact, the need to modify the general EU budget act – the Multi-Annual Financial Framework (MFF)[6] – in order to enable to Commission to issue common debt proved so daunting that the MFA+ was adopted by resorting to member states' financial guarantees, which will only in time be replaced by a single guarantee from the EU budget, when the MFF is amended. This confirms that several constitutional and governance shortcomings still limit the EU's ability to mobilize resources and leverage power on the international stage. While certainly the war in Ukraine proved correct the insight from historians, political scientists and sociologists that war is a powerful driver of state building and institutional change,[7] at the moment the effort to establish a permanent fiscal capacity in the EU remains a process still in the making.

As such, this article is structured as follows. Sections 2 and 3 analyzes respectively the EPF and the MFA+, highlighting their main legal features, legal bases, funding mechanisms, and governance arrangements – thus highlighting their intergovernmental vs supranational features (or their variation). Section 4 contextualizes the EPF and MFA+ in light of the legal and institutional innovations created by the EU and its member states to respond to Covid-19; it points out that the war in Ukraine increased the need for the EU to reproduce funding mechanisms based on common debt akin to those rolled out during the pandemic; and it reflects on how the war in Ukraine contributed to the slow consolidation of a fiscal capacity in the EU. Section 5, however, underlines how this trend is slowed by governance shortcomings and constitutional constraints, which make it difficult for the EU to decide, and to upscale its financial firepower. Finally, section 6 concludes.

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[4] Council Regulation (EU) 2020/2094, of 14 December 2020, establishing a European Union Recovery Instrument to support the recovery in the aftermath of the COVID-19 crisis, OJ 2020, L 433 I/23; and Regulation (EU) 2021/241 of the European Parliament and of the Council of 12 February 2021 establishing the Recovery and Resilience Facility, GUUE 2021 L 57/17 [hereinafter RFF]

[5] See Federico Fabbrini, *EU Fiscal Capacity: Legal Integration after Covid-19 and the War in Ukraine* (Oxford University Press 2022)

[6] Council Regulation (EU, Euratom) 2020/2093 of 17 December 2020 laying down the multiannual financial framework for the years 2021 to 2027, OJ 2020, L 433 I/11.

[7] See Miguel Centeno & Elaine Enriquez, *War & Society* (Polity 2016), Margareth McMillan, *War: How Conflict Shaped Us* (Profile Books 2020), and famously Charles Tilly (ed), *The Formation of National States in Western Europe* (Princeton University Press 1975).

2. *The European Peace Facility*

The EPF is novel funding mechanism that the EU created in 2021 as part of the financial package for 2021-2027, which is centered on the MFF and also includes (in response to Covid-19) the NGEU Recovery Fund. Its name notwithstanding, the EPF is specifically established as a 5.6bn€ special fund to finance the common costs of military operations by EU member states under the EU Common Security and Defence Policy (CSDP), as well as actions to improve the military and defence capabilities of third states and partner international organizations. The EPF – which is adopted in the form of a Council decision – is based on Articles 28(1), 41(2), 42(4) and 30(1) TEU, which respectively allow the EU to act when the international situation so requires, to pool resources to this end, and to adopt initiatives unanimously in the Council, also at the request of the High Representative for Foreign Affairs and Security Policy (HR).[8] The EPF is built as an off-budget fund, outside the MFF, because Article 41(2) TEU explicitly prohibits charging to the EU budget "expenditure arising from operations having military or defense implications".

The EPF, as a tool of EU Common Foreign & Security Policy (CFSP) and CSDP, is exhibit A of intergovernmentalism in the EU. The Council Decision establishing the EPF is extremely long – 76 articles and 5 annexes – and over-complicated. The EPF, as clarified in Article 9, should be used to achieve "the strategic priorities set by the European Council and the Council", and must be consistent with the CFSP goals of the EU.[9] Importantly, according to Article 36 "assistance measures can be implemented through grants". Yet, from a governance viewpoint the EPF is managed by a Facility Committee (FC), composed by representatives from all 27 member states, which must take decisions by unanimity.[10] A large administrative bureaucracy operates under the direction of the FC.[11] Moreover, as a further guarantee to member states, the Decision establishes a direct link between participation in decisions on, and contribution to the financing of, operation and assistance measures: in particular, pursuant to Article 5, "a member state which has abstained in a vote on a Council Decision [...] is not obliged to contribute to the funding of that operation."

From a financing viewpoint, as mentioned, the EPF is entirely resourced through member states' transfers. According to Article 18(7)(a) of the Council Decision, the EPF revenues consist primarily of "contributions payable by the contributing member states". As clarified in Article 26, member states' contributions are determined on the basis of the Gross National Income (GNI), and are requisitioned by the FC annually.[12] Nevertheless, as a further guarantee to member states' discretion – and yet another confirmation of the intergovernmental nature of the EPF – Article 27 states that "[a] Member State which has indicated its intention to abstain from the adoption of an assistance measure [...] may identify other assistance measures to which it will make an additional contribution". This means that while the EPF is a common financial pot, each member state still maintains full control on where its share of the funding is directed. Furthermore, numerous reporting and accounting obligations are connected to the EPF, including a duty by

[8] See Joris Larik, *Foreign Policy Objectives in EU Constitutional Law* (Oxford University Press 2016).
[9] EPF Decision, Article 8
[10] Ibid., Article 11(14)
[11] See Ibid., Articles 12, 13, and 15
[12] Ibid., Article 29

administrators to report to the FC on expenditures every 3 months,[13] and a right for the Council to review the Decision whenever a member state so requires, and at least every 3 years.[14]

At the explosion of the war in Ukraine, the EU quickly decided to mobilize the EPF to provide financial support to the Ukrainian military, including funding for the purchase of lethal weapons – a step which was hailed as historic (not least given that some EU member states still abide by a policy of military neutrality). In particular, in February 2022 the Council approved a Decision on assistance measure for the supply to the Ukrainian armed forces of military equipment.[15] The Decision empowered the HR to implement the measure,[16] making arrangements with the beneficiary, including ensuring compliance with international human rights law and humanitarian law,[17] and foresaw a disbursement of 450mn€.[18] This amount was subsequently doubled in March 2022,[19] and tripled in April 2022 to a total of 1.5bn€.[20] Subsequently, EPF funding to support to the Ukrainian military were further tapped in May 2022,[21] and July 2022,[22] bringing the total size of support to 3.1bn€. This, combined with other EPF expenditures towards other third countries carried out in 2022, largely depleted in a single year a budget that had been designed for a seven-year time-frame. As a result, the Council decided in December 2022 for a 2bn€ increase in the EPF for 2023.[23]

3. The Macro-Financial Assistance Instrument

Given the limited resources available under the EPF, and as the war in Ukraine worsened, in Fall 2022 the European Commission proposed to establish the MFA+ in the form of a regulation of the EP and Council.[24] Going beyond the piecemeal support that the EU had given to the Ukrainian

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[13] Ibid., Article 38
[14] Ibid., Article 75
[15] See Council Decision (CFSP) 2022/338 of 28 February 2022 on an assistance measure under the European Peace Facility for the supply to the Ukrainian Armed Forces of military equipment and platforms designed to deliver lethal force, OJ 2022 L 60/1.
[16] Ibid., Article 4
[17] Ibid., Article 3
[18] Ibid., Article 2
[19] See Council Decision (CFSP) 2022/471 of 23 March 2022 amending Decision (CFSP) 2022/338 of an assistance measure under the European Peace Facility for the supply to the Ukrainian Armed Forces of military equipment and platforms designed to deliver lethal force, OJ 2022 L 96/43.
[20] See Council Decision (CFSP) 2022/636 of 13 April 2022 amending Decision (CFSP) 2022/338 on an assistance measure under the European Peace Facility for the supply to the Ukrainian Armed Forces of military equipment, and platforms, designed to deliver lethal force, OJ 2022 L 117/34
[21] See Council Decision (CFSP) 2022/809 of 23 May 2022 amending Decision (CFSP) 2022/338 on an assistance measure under the European Peace Facility for the supply to the Ukrainian Armed Forces of military equipment, and platforms, designed to deliver lethal force, OJ 2022 L 145/40
[22] See Council Decision (CFSP) 2022/1285 of 21 July 2022 amending Decision (CFSP) 2022/338 on an assistance measure under the European Peace Facility for the supply to the Ukrainian Armed Forces of military equipment, and platforms, designed to deliver lethal force, OJ 2022 L 195/93
[23] Council of the EU press release, 'European Peace Facility: Council agrees €2 billion increase of the financial ceiling in 2023', 12 December 2022.
[24] See European Commission proposal for a Regulation of the European Parliament and the Council establishing an Instrument for providing support to Ukraine for 2023 (macro-financial assistance+), 9 November 2022, COM(2022)597 final.

government in the initial months of the war,[25] the MFA+, worth 18bn€, was designed to provide predictable, continuous, orderly and timely financial relief to Ukraine in 2023, thus supporting its rehabilitation and reconstruction and prospectively its preparation for EU membership.[26] The Commission's proposal, which was based on Article 212 TFEU – the treaty provision dealing with economic, financial and technical cooperation with third countries[27] – was endorsed by the EP and the member states in the Council. Hungary however vetoed it, mostly as a bargaining chip to obtain concession from the Commission on an unrelated measure: To tackle the problem of rule of law backsliding at play in Hungary, in fact, the Commission had suspended the transfer of NGEU funds to Hungary,[28] which was thus eager to use every available card to overcome the application of the rule of law conditionality regulation,[29] and obtain much needed additional EU funds.

In the end, in order to circumvent Hungary's veto, in December 2022 the Council decided to amend slightly the Commission proposal, and passed it with the EP approval.[30] Specifically, the Council changed the original funding scheme proposed by the Commission, which envisaged guaranteeing the issuance of 18bn€ of common debt through the EU budget. Since that required an amendment to the MFF – a change on which Hungary had a right to veto[31] – the Council rather opted to back-up the 18bn€ of new common debt of the MFA+ through member states' guarantees, provided by 26 member states pro-quota.[32] (In what is certainly not a coincidence, though, two days before the Council also approved the Hungarian National Recovery and Resilience Plan (NRRP),[33] thus ensuring that Hungary could access in the future NGEU money, if the Commission were to de-block them pursuant to the rule of law conditionality regulation.) Admittedly the MFA+ still foresees that were an amendment to the MFF to be approved, then the EU budget would replace member states' guarantees – but as the MFA+ only operates in 2023, it is unclear if that will actually occur.

The MFA+ presents more supranational features than the EPF. The EP and Council regulation establishing the MFA+ is only 21 articles long, and fairly linear. As clarified in Article 2, the objective of the instrument is to provide "short-term financial relief to Ukraine [...] and initial support towards post-war reconstruction", and the MFA+' areas of support include financing of Ukraine's funding need, restoring critical infrastructure as well as alignment with the EU regulatory

[25] See e.g. Decision (EU) 2022/1201 of the European Parliament and the Council of 12 July 2022 providing exceptional macro-financial assistance to Ukraine OJ 2022 L 186/1 (providing 1bn€ of emergency funds)
[26] European Council conclusions 23-24 June 2022, EUCO 24/22, para. 11(granting candidate status to Ukraine)
[27] See Erlbacher, 'Article 212 TFEU' in M. Kellerbauer et al (eds), *The EU Treaties and the Charter of Fundamental Rights (OUP 2019).*
[28] *European Commission press release, "EU budget*: Commission proposes measures to the Council under the conditionality regulation", 18 September 2022, IP/22/5623.
[29] Regulation (EU, Euratom) 2020/2092 of the European Parliament and of the Council of 16 December 2020 on a general regime of conditionality for the protection of the Union budget, OJ 2020 L I 433/1
[30] European Parliament legislative resolution of 14 December 2022 on the Council position at first reading with a view to the adoption of a regulation of the European Parliament and of the Council establishing an instrument for providing support to Ukraine for 2023, P9_TA(2022)0439.
[31] See Article 312 TFEU
[32] European Parliament press release, "Parliament agrees to adapted €18 billion loan to Ukraine", 14 December 2022.
[33] Council of the EU press release, "NextGenerationEU: Member States Approve National Plan of Hungary", 12 December 2022

framework.[34] Based on Article 4 of its regulation, the MFA+ provides support in the form of loans, although additional amounts can be contributed by member states as grants. From a governance viewpoint, the MFA+ regulation vests the key decision-making power in the European Commission. Pursuant to Article 11, "the support under the Instrument shall be made available by the Commission in installments". The regulation however introduces a number of pre-condition for the support under the MFA+, including "that Ukraine continue[s] to uphold and respect effective democratic mechanisms [...] and the rule of law."[35] The Commission signs the memorandum of understanding (MoU) with Ukraine setting out priority actions;[36] reviews compliance with the ex ante conditionality;[37] and can reduce, suspend or cancel support under the MFA+.[38]

From a financing viewpoint, the MFA+ instrument is based on the issuance of common EU debt, rather than member states' transfers. Specifically, Article 16 of the MFA+ regulation states that "in order to finance the support under the Instrument in the form of loans, the Commission shall be empowered, on behalf of the Union, to borrow the necessary funds on the capital markets or from financial institutions". Loans to Ukraine, which are set at a very favorable term, "shall have a maximum duration of 35 years"[39] and the EU can offer an interest rate subsidy to Ukraine.[40] The supranational dimension of EU common debt, though, is counter-balanced by the intergovernmental left-over of member states' guarantees. As already mentioned, in fact, given the impossibility to amend the MFF and raise the EU budget ceiling, Article 5(2) of the MFA+ regulation states that member states contribute to guarantee the debt "in the form of irrevocable, unconditional and on-demand guarantees through a guarantee agreement to be concluded with the Commission." Such national guarantees are determined pro quota on the basis of each member state's GNI,[41] but "shall cease to be callable as of the date of application of an amendment to [the MFF Regulation]."[42] The usual annual reporting obligation is imposed by the regulation on the Commission,[43] which must also constantly keep the EP and Council informed on disbursement operations.[44]

4. Exogenous threats and path dependency: the consolidation of an EU fiscal capacity

The EU financial response to the war in Ukraine during 2022 reveals a trend towards the consolidation of a fiscal capacity in the EU.[45] The unprecedented geo-political threat posed by the Russian military aggression at Europe's Eastern borders forced the EU institutions and member states to resort to funding mechanisms analogous to those rolled out in response to

[34] MFA+ regulation, Article 3
[35] Ibid., Article 8
[36] Ibid., Article 9
[37] Ibid., Article 12
[38] Ibid., Article 13
[39] Ibid., Article 16(2)
[40] Ibid., Article 17
[41] Ibid., Article 5(3)
[42] Ibid., Article 6(f)
[43] Ibid., Article 20
[44] Ibid., Article 15
[45] See Fabbrini (n 5)

the Covid-19 pandemic. As pointed out in the prior sections, at the start of the war in Ukraine the EU member states deployed for the first time the EPF – a new tool designed to back up the EU voice in foreign affairs. Nevertheless, the limited size of the EPF – and arguably its complicated governance arrangements – quickly led the European Commission to propose an alternative funding instrument, in the form of the MFA+. Grounded on a different Treaty legal basis – and justified also in light of the EU grant of candidate status to Ukraine – the MFA+ enabled the Commission to raise 18bn€ on the financial markets on behalf of the EU, and to transfer these to the Ukrainian government in 2023 as concessionary loans subject to standard conditionality.

While the EPF presents features which resemble the traditional EU budget, the MFA+ rather tracks the solution that the EU adopted to tackle the Covid-19 pandemic. As is well known, despite the letter and the spirit of the EU treaties, The EU budget – the MFF – is mostly funded by member states' transfers (based on GNI);[46] and as pointed out above, the same is true for the EPF. On the contrary, in response to the Covid-19 pandemic the EU experimented with novel financial instruments, legally engineering a constitutional transformation in the EU architecture of economic governance.[47] To address the devastating socio-economic damages caused by the pandemic, in particular, the EU set up SURE mechanism, worth 100bn€, and subsequently the NGEU Recovery Fund, worth 750bn€. Under SURE, the European Commission was empowered to raise 100bn€ on the financial markets by issuing common debt on behalf of the EU, subject to 25bn€ of member states' guarantees.[48] In the case of NGEU, instead, the Commission was empowered to raise 750bn€ by issuing common debt on behalf of the EU, with the general EU budget serving as a back-up through an increase of the EU Own Resources Decision (ORD)'s ceiling.[49]

From this point of view, the MFA+ follows in the footsteps of SURE and NGEU. In particular, the MFA+ scheme tracks SURE, to the extent that both mechanisms rely on member states' guarantees to empower the Commission to issue EU common debt. Moreover, like SURE the MFA+ provides loans, rather than grants. At the same time, the MFA+ also draws from the example of NGEU – and specifically the Recovery and Resilience Facility (RRF), the main program funded under the Recovery Fund and designed to support member states. The RRF requires member states to design NRRPs, with specific targets, milestones and objectives to be achieved in order to receive NGEU funds, and empowers the Commission to assess them. At the same time, the rule of law conditionality regulation subjects disbursement of funding to the respect of basic rule of law principle, which again the Commission is empowered to evaluate. Along the same lines, as mentioned, the MFA+ regulation foresees that Ukraine and the Commission will enter into a MoU outlining the specific objectives to be achieved with EU funding, and empowers the Commission to evaluate compliance as a condition for the payment of installments. At the same time, while the EPF conditions funding to continuing respect of international human rights law

[46] Ubaldo Villani-Lubelli and L Zamparini (eds), *Features and Challenges of the EU Budget* (Elgar 2019).
[47] Bruno de Witte, 'The European Union's Covid-19 Recovery Plan: The Legal Engineering of an Economic Policy Shift' (2021) 58 *Common Market Law Review* 635.
[48] SURE regulation, Articles 11 and 12
[49] Council Decision (EU, Euratom) 2020/2053, of 14 December 2020, on the system of own resources of the European Union and repealing Decision 2014/335/EU, Euratom, OJ 2020 L 424/1, Article 5(1)

and humanitarian law, the MFA+ requires Ukraine to abide by democratic and rule of law principles to receive cash, effectively replicating – albeit arguably in a lighter form – the EU rule of law conditionality rules.

The adoption of the MFA+, therefore, reveals the importance of path dependency in the functioning of the EU. As political science literature on historical institutionalism,[50] and legal scholarship research on emergency legislation[51] have both pointed out, once norms are adopted in time of emergency and become entrenched, they set a precedent for future action. Interestingly, all measures enacted by the EU to address the Covid-19 pandemic had a sunset. The SURE regulation foresaw that its funding "shall end on 31 December 2022" unless the Council on a proposal of the Commission agrees to extend it further, each time for an additional period of six months.[52] Similarly, the NGEU Recovery Fund was designed to be a one-off, exceptional tool: as stated by the European Council "the powers granted to the Commission to borrow are clearly limited in size, duration and scope"[53] with the RRF designed to run "until 31 August 2026."[54] Yet, SURE and NGEU offered the policy template and legal technique which the EU could resort to in order to address a new crisis arising even before the Covid-19 pandemic dissipated.

The explosion of the war in Ukraine, at the same time, suggests that external threats are one of the strongest drivers of fiscal integration in federal unions of states. Indeed, a comparison with the United States (US) highlights the point. According to Tomasz Wozniakowski internal threats, notably the Shay's Rebellion, explain the groundbreaking decision by the US federal government to assume the state Revolutionary war debt in 1781[55] – the Hamiltonian moment *par excellence* in US history. Nevertheless, as I have explained elsewhere,[56] the real emergence of a centralized fiscal capacity in the US only occurred much later in time, through a slow process, and mostly in response to external challenges. Indeed, building on the institutional transformations of the Progressive Era and the New Deal in the early 20th century, it was particularly World War II and the rise of the US as a global super-power during the Cold War that led to a massive increase of the US federal budget, making the US federal government the key player in US economic governance.[57] To some extent, the war in Ukraine has served a similar purpose in the EU, requiring it to upscale its fiscal resources to face an unprecedented geopolitical threat at its doorsteps.

[50] See Kurt Dopfer, 'Toward a Theory of Economic Institutions: Synergies and Path Dependency' (1991) 25 *Journal of Economic Issues* 535

[51] See Oren Gross & Fionnuala Ní Aoláin, *Law in Times of Crises: Emergency Powers in Theory and Practice* (CUP 2006).

[52] SURE regulation, Article 12(3)

[53] European Council Conclusions, 17-18-19-20-21 July 2020, EUCO 10/20, para. A4.

[54] RRF Regulation, Article 18(4)(f)

[55] Tomasz Woźniakowski, *Fiscal Unions: Economic Integration in Europe and the United States* (Oxford University Press 2022).

[56] Fabbrini (n 5) 92-8

[57] See Ira Katznelson and Martin Scheffer (eds), *Shaped by War and Trade: International Influences on American Politics Development* (Princeton University Press 2002).

5. Governance problems and constitutional constraints: challenges towards fiscal integration

Nevertheless, the road towards the consolidation of a fiscal capacity in the EU remains fraught with difficulties and uncertainties. Indeed, as also the approval of the MFA+ highlights, the EU is hampered by governance problems and constitutional constraints which severely undermine its capacity to raise a fiscal capacity and rise to the geopolitical challenges it is facing. A rough comparison between the EU and the US funding to Ukraine in the first year of the war drives home the point. The 3.1bn€ of EPF funding combined with additional smaller EU grants and the 18bn€ of MFA+ support (which however applies to 2023) pale in comparison to the 54bn$ of spending the US provided to Ukraine in just three months, between March and May 2022,[58] which were further increased by an additional 44bn$ in December 2022 as part of a stunning 858bn$ military bill for 2023.[59] Even accounting for the additional spending that EU member states provided on their own, how can we make sense of this embarrassing imbalance?

To begin with, there are a number of constitutional constraints on the ability of the EU to raise fiscal resources. At the time of the approval of NGEU a debate occurred on whether EU efforts to establish a fiscal capacity where limited by national or EU constitutional rules.[60] In the end, legal concerns were largely overcome – including in the most reluctant member state: Germany. In particular, in an important ruling delivered in early December 2022, the German Federal Constitutional Court (*Bundesverfassungsgericht*) rejected the legal challenges that had been raised against the NGEU and ORD.[61] As the Court clarified in a 7-1 judgment, the establishment of NGEU and the empowerment of the European Commission to issue 750bn€ of common debt violated neither the EU Treaties nor the German Basic Law. According to the Court, the Recovery Fund was compatible with Articles 122, 125, and 311 TFEU, and did not constitute an ultra vires action by the EU, thus complying with the integration agenda foreseen in the Basic Law, particularly as the size of NGEU funded by raising common debt was inferior to the size of the MFF, resourced via states' transfers. As a result, albeit with caveats that may come to haunt it later, the German Constitutional Court endorsed the path towards common debt.

Yet, other EU constitutional rules weaken the EU's ability to mobilize resources at need. On the one hand, as pointed out in section 2, Article 41(2) TEU explicitly prohibits charging to the EU budget "expenditure arising from operations having military or defense implications" – which means that CSDP expenses have to be covered by separate funds, like the EPF, set up outside the MFF. On the other hand, Title II of Part VI of the TFEU, which sets the "Financial Provisions" of the EU, lays out daunting rules. In particular, according to Article 310(1) TFEU, the revenues and expenditures of the EU budget "shall be in balance". Moreover, Article 312 TFEU states that the MFF, which is to be approved by the Council unanimously with the consent of the EP, must set "the amounts of the annual ceilings on commitments appropriations by category of expenditures

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[58] See Bianca Pallaro & Alicia Parlapiano, 'Four Ways to Understand the $54 Billion in U.S. Spending on Ukraine', *The New York Times*, 20 May 2022.

[59] See Catie Edmonson, 'Congress Passed an $858 Billion Military Bill. Here is what's in it', *The New York Times*, 16 December 2022.

[60] Brady Gordon, *The Constitutional Boundaries of European Fiscal Federalism* (Cambridge University Press 2022).

[61] BVerfG, 2 BvR 547/21, 2 BvR 798/21, Final Judgment of 6 December 2022.

and of the annual ceilings on payment appropriations". Finally, Article 311 TFEU requires the EU budget to "be finance wholly from own resources" – to be approved by the Council unanimously, and ratified by each member state in accordance with its constitutional requirements. The combined effect of the abovementioned provisions is therefore to require a cumbersome amendment to the MFF and ORD every time the EU wants to increase spending, and borrow money. This is why in the MFA+ case, national guarantees had to be used to empower the issuance of 18bn€ of EU debt.

A second main structural obstacle towards the development of a permanent fiscal capacity in the EU – admittedly also flowing from the EU Treaties – is the governance problem. As scholars have emphasized, CFSP and CSDP are by design fully intergovernmental policies. According to the EU Treaties supranational institutions like the EP and the Commission have hardly a role – and decision-making power is fully vested in the member states in Council and European Council. These arrangements however constantly subject EU actions to member states' vetoes, and as a result the EU has so far punched well below its weight in foreign relations.[62] In fact, the institutional features of the EPF, detailed above, reflect this state of affairs. As mentioned, the EPF has a highly cumbersome governance structure, with a 27-member FC at the helm, and member states still have multiple prerogatives, including the right to opt-out of funding operations they dislike. While in the end member states unanimously agreed to deploy the EPF to support Ukraine in 2022, it is clear that this is not congenial to fast and vigorous decision-making.

Otherwise, intergovernmental governance also afflicts the core decision-making procedures about EU public finances. As noted previously, member states' governments must unanimously approve the MFF, or amendments thereof, and the ORD – which must also be ratified by each member state in accordance with its constitutional requirements (usually parliamentary procedure). This again means that a single member state can veto efforts by the others to enable further EU borrowing and spending – even for unrelated, idiosyncratic reason. This is exactly what happened in the case of the MFA+: as explained above, Hungary vetoed an amendment to the MFF, which was needed to raise the EU budget ceiling required to issue 18bn€ of new common debt, seeking to leverage its vote in order to obtain the Council endorsement of its NRRP overcoming the Commission's rule of law concerns.[63] The shrewd blackmail by the Hungarian government forced the other member states to resort to member states' guarantees (and ultimately payed off, as before the approval of the MFA+ the Council also gave its conditioned green light to the Hungarian NRRP). Clearly however, the dependence on the consent of 27 member states for any financial operation is bound to continuously create challenges for the EU in the long term.

In this context, it appears therefore a number of institutional reforms are clearly needed to increase the EU capacity to act – as pointed out by the EP.[64] In particular, as I have argued

[62] Sergio Fabbrini, "Intergovernmentalism and its Limits" (2013) 46 *Comparative Political Studies* 1003

[63] See Kim Lane Scheppele, "The Treaties Without a Guardian: The European Commission and the Rule of Law" (2023 forthcoming) *Columbia Journal of European Law*.

[64] European Parliament resolution of 19 May 2022 on the social and economic consequences for the EU of the Russian war in Ukraine – reinforcing the EU's capacity to act, P9_TA(2022)0219.

elsewhere,[65] if the EU wants to make its fiscal capacity permanent it must remove the balance budget obligation enshrined in Article 310 TFEU, overcome unanimity requirements on decisions about borrowing and spending, and endow the EU with the power to levy direct taxes – a much needed development, particularly as the EU step-by-step increases the amount of common debt it will have to repay. At the same time, enhanced EU powers in the fiscal domain require constitutional adjustments to make sure that the EP – the sole EU institutions directly elected by European citizens – gains an equal voice to the Council on revenues, in line with the old adage 'no taxation without representation.' Some of these constitutional changes can be achieved through the use of *passerelle* clauses,[66] while others require an outright treaty amendment. Be that as it may, support for such steps has increased not only among EU institutions[67] and leading national policy-makers,[68] but also in the European citizenry at large: the Conference on the Future of Europe – a bottom-up participatory process to reflect on the prospects of European integration, which came to an end on 9 May 2022 – listed these reforms in a package of recommendations for future action.[69] It remains to be seen though if the war in Ukraine will provide the spur to achieve these constitutional reforms.[70]

6. Conclusion

The war in Ukraine has posed yet another unprecedented challenge for the EU. The Russian military aggression of a sovereign country at the EU's Eastern borders shattered European illusions of a perpetual peace and forced the EU to face the reality of hard power. In response to the illegal Russian invasion, the EU mobilized to support Ukraine. In particular, the EU deployed for the first time the EPF – funding the purchase of weapons for the Ukrainian military; and it then established the MFA+ – devising a scheme to predictably fund the Ukrainian government in 2023. As this article claimed, the EU efforts to support Ukraine increased over time – through the use of funding mechanisms which track the model employed to address the Covid-19 pandemic. In particular, while the EPF is a new mechanism of common EU spending, the MFA+ also relies on the issuance of common EU debt. As such, the war in Ukraine reveals a trend towards the consolidation of a fiscal capacity in the EU – suggesting that indeed wars and external security threats remain the most powerful engine of fiscal centralization in federal unions of states.

Nevertheless, the process of fiscal union in the EU remains very much in the making. Indeed, as the article explained, constitutional constraints and governance problems hamper the ability of the EU to raise resources and rise to the geopolitical challenges it faces. While the EPF is a purely intergovernmental arrangement, an idiosyncratic veto by Hungary forced the EU to set up the

[65] Fabbrini (n 5) 141-4
[66] Article 48 TEU
[67] See e.g. European Parliament resolution of 9 June 2022 on the call for a Convention for the revision of the Treaties, P9_TA(2022)0244; and European Parliament resolution of 15 December 2022 on upscaling the 2021-2027 multiannual financial framework: a resilient EU budget fit for new challenges, P9_TA(2022)0450
[68] See e.g. French President Emmanuel Macron, Speech, Strasbourg, 9 May 2022; and German Chancellor Olaf Scholz, Speech, Prague 29 August 2022
[69] Conference on the Future of Europe, Report on the Final Outcome, 9 May 2022.
[70] See also Federico Fabbrini, *Brexit and the Future of the European Union: the Case for Constitutional Reforms* (Oxford University Press 2020)

MFA+ through member states' guarantees – rather than the single guarantee provided by the EU budget. Otherwise, the EU Treaties currently prevent the use of EU resources for CSDP purposes, and severely constrain the ability of the EU to borrow money and spend. In this context, the EU is likely to struggle in its efforts to financially support a neighbor – and now candidate member state – like Ukraine. Longer term, therefore, a number of constitutional reforms appear inevitable if the EU wants to endow itself with the means to act autonomously on the international stage. While the final outcome of the war in Ukraine will determine the destiny of the Ukrainian people, the continuation of the war will likely influence whether the EU moves towards a fiscal union or not.

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