Public goods in a federal Europe
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Executive Summary

Europe should become stronger and more sovereign through the provision of more and better European Public Goods (EPGs). The European Union (EU) should take on more of the tasks to which it can lay claim by virtue of its size and function. Europe should become more European. In order to make good this claim, the Union more than likely will have to assume more of the features of a cooperative federal state.

Putting the concept of European common goods into practice requires one to spell out more clearly the way forward and to know how these EPGs can then be set to work. The present paper addresses the following issues: first, the appropriate institutional framework for the introduction and provision of European public goods; second, how best to phase in that provision within the European multi-level system of governance. For this purpose, it uses two analogies.

With the first analogy, we ask whether the EU as a sui generis political entity would not be better understood by being explicitly viewed as a co-existence of federal state and confederation. The federal-state-like supranational model provides a democratically and fiscally appropriate governance framework for the provision of new European public goods but places significant obstacles in the way of their introduction. The opposite is true for the confederation-like intergovernmental model: this is poorly suited for the provision of new European public goods but offers greater prospects for their successful introduction. Such considerations might suggest that additional EPGs are faced with their own “federal paradox”. This paradox is not insurmountable but must always be kept in mind.

The second analogy compares the EU – especially its federal component – with the German model of cooperative federalism or “administrative federalism”. This comparison brings to the fore the issues and tasks that providing for EPGs involves when the legislative, administrative and financing competences may well be and are allocated to different levels of government. It thus helps to understand that many EPGs should not be provided by the EU alone.

If one were to consider only the US-American-style federal state model for European federalism, few European common goods could be designed. In vertically cooperative federal states, on the other hand, the legislative, administrative and financing competences for certain public services are not always entrusted to the same level of government. This may entail connectivity problems. Nevertheless, an efficient allocation of tasks is created precisely for the many instances in which there are no EU administrative bodies locally and none should be contemplated. We develop a criteria matrix that serves as a guide for the tailor-made fiscal-federal design of a wide variety of EPGs.

The most important prototypes of the vertical allocation of competences are presented by means of four illustrative scenarios. In fine-tuning such a design, we pay particular attention to the central financing of those European common goods which are administered locally by the Member States. This promising model is still quite fresh – and innovative – in federal practice.

With a view to the resurgent debate on the future financing of the EU, we also discuss the long-standing and contentious issue of juste retour. This issue symbolically and factually embodies one of the central hurdles that still distinguishes the supranational system of the EU from the "normal" top tier of a federal state. It will therefore only be solved consistently if key revenue instruments politically assigned to the EU are used to finance services with a visible European added value – i.e. genuine European common goods. The innovations in terms of EU taxes and common debt occasioned by NextGenerationEU and the EU Recovery Fund open up additional possibilities here that would hardly have arisen without the great coronavirus crisis acting as an unwished-for catalyst for European progress.
A. Introduction

Europe should become stronger and more sovereign through the provision of more and better European public goods (EPGs). The European Union (EU) – that’s the premise of the project “Vision Europe” – should take on more of the tasks to which it can lay claim by virtue of its size and function. Today more than ever, it is important that each level of government in Europe focuses on the public tasks for which it is best suited. In the EU’s case, this means placing less emphasis on regional or even local public goods, which currently dominate the scene with cohesion and agricultural policies, and taking on more genuinely European and global responsibilities. The need for such a reallocation of duties, in particular the stronger “Europeisation of the EU” through policies with recognisable European added value vis-à-vis national measures, has become all the more apparent during and after the coronavirus pandemic.¹

The paradigm of European public goods can become an important driver for further European integration. However, this will only succeed if the concept of “public goods” derived from economic theory is measured against European realities in several steps. The present paper takes up a central aspect that has received little attention in the discussion so far: clarifying how the realisation of European tasks can be realistically approached within the EU’s multi-level framework and which governance issues this raises. The doctrine of public goods, applied to the allocation of tasks within the European “multi-level state”, implicitly envisages a clear division of tasks among different levels of government: each of these regulates its own tasks, finances them from its own resources and then proceeds to carry them out itself. This design, which corresponds to a US-American understanding of “dual federalism”, may well offer the most efficient solution for some European common goods. But that is likely to be true only for a minority of the new common goods of interest.

Given that the EU has no own administration of substantial latitude at work across its entire territory, many European common goods are likely to be provided in cooperation with the Member States or their sub-state entities, as now. This means that the legislative competence, the administrative competence and the financing competence will not all rest with the same level of government. Such a model of decentralised administration is more akin to the cooperative “administrative federalism” practised – in different forms – in Germany and Austria. While the cooperative model allows for realising far more European common goods than that of dual federalism, it also poses a number of political, administrative and financial challenges that need to be tackled through forward-looking policy design.

The most important coordination and governance questions that need to be answered in the context of cooperative federalism revolve around the “principle of connectivity”. Its two – quite opposite – expressions are also used here to examine the European provision of more common goods. If, in a multi-level system, public tasks are legislatively regulated at the central government level, but enacted at the decentralised level, “execution connectivity” argues in favour of placing the financing obligation at the lower level. The basic idea is that the executive authority manages “its own money” more efficiently.

¹ See earlier papers published within the framework of the “Vision Europe” project: Thöne and Kreuter (2020a); Thöne and Kreuter (2020b); Gnath et al. (2020); Callies (2021).
"Causal connectivity", on the other hand, requires in such constellations that the financing obligation be put in the hands of central government. The motto "who orders, pays" is intended to prevent legislation being passed with the decentralised level of government bearing the costs. Both sides of the principle must be considered when European common goods are provided cooperatively.

This paper analyses the EU in the light of the theory of fiscal federalism and real experience within the federal multi-level state. To this end, we use two analogies. Neither of them is an exact match, as is the nature of analogies. Nevertheless – or perhaps even because of this – we believe that both are very instructive for the further development of the Union.

With the first analogy, we ask whether the EU as a *sui generis* political entity – featuring *sui generis* obstacles to development – might better be understood as a combination of federal state and confederation. To this end, we shed light on the co-existence of the supranational and intergovernmental systems in the EU and take a look at the current innovations that may emerge with the coronavirus recovery fund NextGenerationEU.

The second analogy, which follows on from the first, compares the EU – especially its federal component – with the German model of cooperative federalism or “administrative federalism”. Such a comparison highlights the issues and tasks that arise in connection with the provision of EPGs when the legislative, administrative and financing competences cannot or should not – all three – rest at European level.

With the help of these two analogies, we explore the ways in which more and better European common goods can be introduced and provided in federal Europe. Specifically, the first analogy helps one to better understand the problem associated with establishing such EPGs. Here, we come across a – not insurmountable – “federal paradox”: the characterisation of the supranational system as a federal state and that of the intergovernmental system as a confederation of states suggests that new European common goods can, by their very nature, be better provided within the supranational system, but more realistically introduced within the intergovernmental system.

The second analogy turns to the question of separate or cooperative realisation of tasks within the multi-layered governance system. This perspective helps one to understand why many EPGs should not be provided by the EU alone. If one were to consider only the US-American-style federal state model for European federalism, few European common goods could be designed. In vertically cooperative federal states, on the other hand, the legislative, administrative and financing competences for certain services are not always allocated to the same level of government. This raises connectivity issues. At the same time, however, it can ensure an efficient allocation of tasks, especially in the frequent cases where the EU has no administrative bodies of its own locally and should refrain from even contemplating them. On the basis of extensive experience with German administrative federalism, we develop a criteria matrix that serves as a guide for the tailor-made fiscal-federal design of a wide variety of EPGs. The most important prototypes are presented in four illustrative scenarios. In "fine-tuning" such a design, we
pay particular attention to the central financing of European common goods administered by the Member States. This promising model is still quite fresh – and innovative – in federal practice.

Examining vertical cooperation and related connectivity issues brings one to the conclusion that for many EPGs the primary legislative and financing competence should rest with the EU, while administrative competence should go to the Member States. Except for the financing competence, this pattern is quite similar to the division of competences that already characterises EU provision of many European public goods. We put up for discussion the question of how to prevent the European spirit, due to be strengthened by providing new European common goods, from being diminished by the external impression of “more of the same”.

B. The current federal structure of the EU

In order to address the issue of an appropriate vertical organisation for the provision of (new) European public goods within the multi-level system, it is first useful to recapitulate the actual federal structure of the EU. Simplifying, we view here Europe as a co-existence of the “supranational governance model” (B.1) and the “intergovernmental governance model” (B.2). If one abstracts from institutional subtleties and existing overlaps, this constellation reflects a co-existence of federal state and confederation of states (Section C) – that’s the first analogy of the present paper. We use this perspective to gain a clearer understanding of the challenges involved in the introduction and – quite differently – in the provision of European common goods.

The possibility for the EU to act is limited by the principle of conferral. According to Article 5 of the Treaty on European Union (TEU) “the Union shall act only within the limits of the competences conferred upon it by the Member States in the Treaties to attain the objectives set out therein”. Within this framework, the Treaty of Lisbon (2009) institutionalised two fundamental and different governance models: the supranational model and the intergovernmental model.²

B.1. Supranational governance model

The supranational governance model – also often referred to as the “Community method” – evolved continuously from the foundation of the European Economic Community to the creation of the European internal market. In the process, an institutional setup emerged within which integration is promoted through legal acts.

The right of initiative rests solely with the European Commission, which consists of one Commissioner per Member State. Proposals for EU legislation must always be approved by the Council of the European Union (also known as the “Council of Ministers”), which is composed of specialised government ministers from each Member State, and by the

² We follow here the representation of Fabbrini (2019).
European Parliament, which is directly elected by the citizens of all Member States: the Council of Ministers generally votes by qualified majority, in exceptional cases by unanimity; the European Parliament generally votes by simple majority, in exceptional cases by absolute majority. The European Commission is then responsible for implementing the decisions taken, and the European Court of Justice ensures a uniform interpretation of EU law. The European Council, which is made up of the Heads of State or Government, mainly defines the general political guidelines and acts as an umpire of last resort.

Thus, horizontally at EU level, the supranational governance model provides for the – albeit imperfect\(^3\) – separation of powers à la Montesquieu (legislative, executive and judicial) and guarantees inter-institutional checks and balances. It should be noted here, however, that the Council of Ministers and the European Council, as they comprise members of national governments, are inevitably always also representatives of national interests – or at least are perceived as such. Moreover, it should be noted that the ministers of the Member States perform legislative functions at the European level, while they are part of the executive at the national level.

On the other hand, vertically, the supranational governance model provides for the explicit participation of the lower level of government, i.e. the Member States. Regulation of most policy areas falls is shared between the EU and the Member States (Art. 4 TFEU). An essential consequence of shared competence is that the exercise of the Member States’ original competences is limited by action on the part of the Union – in accordance with the principle of subsidiarity. This, however, does not apply to an entire policy area, but only where the Union has enacted concrete legal acts. Accordingly, national regulations and European standards often co-exist within a given policy field. This co-existence can take the form of a hierarchical relationship between European framework setting and national enactment. But it may also be the case that, alongside issues regulated at European level, there are others which are not regulated centrally and thus only by the Member States.

Furthermore, and this is of great importance in the context of our analysis, the EU has only limited powers and capacities to execute its own law. "Direct administration" can be found, e.g. in the area of EU civil service and labour law as well as in the area of anti-trust and competition law. In most fields of action, however, the EU is dependent upon "indirect administration" by the Member States (Art. 4 TEU, Art. 197 TFEU, Art. 291 TFEU).

Indirect administration can take two forms. If Union law is directly applicable (regulations and decisions), national authorities are only required to implement and enforce it. In doing so, they must follow specific rules; in particular, they have to comply with the principles of effectiveness and equivalence.\(^4\) If, on the other hand, Union law is not directly

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3 The European Commission is formally the executive, but it also has the monopoly on legislative initiative and, to some extent, the power to sanction infringements. The President of the European Commission is elected by the European Parliament following nomination by the European Council, although in 2014 the nomination itself was influenced by the European Parliament via the Spitzenkandidat process.

4 **Principle of effectiveness**: The application of national law must not lead to the effectiveness of Union law being rendered practically impossible or excessively difficult. **Principle of equivalence**: The application of national law must not lead to a discrimination between matters relating to Union law and matters that are purely national in nature.
applicable (via directives), Member States must first transpose it into national law to give it full legal effect, before they can implement and enforce it. Although EU directives are binding as to the result to be achieved and, in practice, often contain detailed provisions for their transposition, they leave some discretion in the choice of form and methods, thus allowing Member States to take account of specific national circumstances.

In addition to the classic categories of direct and indirect administration, certain forms of co-administration or shared administration are also becoming increasingly apparent. These include, among others, the so-called “staged indirect administration” (such as in the context of state aid control or in the area of drug approval), cross-border networks of authorities (e.g., the network of authorities in the field of cartel law) and transnational administrative acts (such as the issuing of driving licences).

The transfer of administrative competences to the Member States allows the EU to externalise the associated costs as well. However, national authorities can act both as instruments for achieving EU goals and as a permanent threat to their uniform realisation. Indeed, infringements of Community law are only accompanied by sanctions, which are often criticised as weak. A striking example of this is the EU’s hesitant action against judicial reform in Poland, a reform that is incompatible with fundamental European values. Although the EU Commission had already initiated proceedings under Article 7 of the EU Treaty in December 2017, it became apparent at the end of 2020 that the intended suspension of Poland’s voting rights in the Council of Ministers would be deferred. Such a measure would require the consent of all other EU states (except Poland). In this case, the current governments of Poland and Hungary engaged in classic “logrolling”, trying to protect each other from sanctions threatened by the European Community of values. The sanction can be further weakened by an “intervention paradox” (Schlipphak and Treib, 2019): governments willing to impose sanctions shy away from this step because they fear it will strengthen populist tendencies in the sanctioned Member States. With a view to the Polish and Hungarian violations of European rule of law principles, only the important, but narrow compromise reached in the dispute over the Multiannual Financial Framework at the end of 2020 opened up a (provisional) way out.

The EU is also highly dependent on the decisions taken by the Member States when it comes to financing Community tasks. The multiannual financial framework (MFF), which must be adopted unanimously by the Council of Ministers, sets the maximum annual amounts that the EU can spend in each policy area over a period of at least five (usually seven) years. While this long-term definition of the scope for action facilitates budget planning and ensures balanced budgets, it also reduces budget flexibility and the ability to take on new European tasks and realise them by prioritising budget resources. Within the MFF ceilings, the European Commission presents an annual draft budget, which must always be formally balanced. At around 148 billion euro (appropriations for payments), in 2019 it accounted for about 2 percent of total public spending in all EU countries.

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5 See Stelkens (2019) on the three phases of implementation (sensu lato) of Union law by the Member States.

6 This compromise cannot be seen as a real breakthrough in the application of rule of law principles. The rather narrowly defined anti-corruption clause against the waste of EU funds is often criticised as very weak.
The outbreak of the coronavirus crisis in 2020 has highlighted the limits of the budget instrument. It quickly became clear, and hardly a bone of contention, that the EU as such must take comprehensive measures on its own to contain the pandemic and cushion its macroeconomic consequences on top of those undertaken by Member States. But the I EU budget itself is in play here. In fact, in 2020, after approval by the European Parliament, the European Council adopted an MFF for 2021 to 2027 that deflated the many expectations of renewal, as it remains tied to the Union’s past budgetary policy. Thus, no significant increase in the volume of the regular budget is on the cards in the coming years either; there is virtually no room for European common goods. For the major task of combating the pandemic and its economic consequences, a temporary ancillary budget has instead been created through the NextGenerationEU (NGEU) recovery fund. This gives the EU a makeshift stabilisation mechanism. However, it is only available for expenditure over the period from 2021 to 2024. Accordingly, from 2025 onwards, the EU’s financial policy will again remain exclusively in the narrow and rather backward-looking corset of the MFF. This “backsliding” will probably become striking after the NGEU years. Greater flexibility in the regular budget of the Union and correspondingly in the MFF would be desirable here so as to render the Union permanently quasi-immune to crisis and enable it to set current and forward-looking priorities and implement them promptly over a prolonged period.

The low degree of flexibility on the expenditure side of the European budget is mirrored by equally scant flexibility on the revenue side. This becomes particularly evident when looking at the composition of revenues. In addition to customs duties and value-added tax shares, the EU is financed to the tune of around 70 percent from own resources calculated on the basis of the Member States’ respective gross national income (GNI). Basically, these GNI-based own resources are very good instruments for financing the Union via contributions on a basis that is fair and geared to the economic performance of Member States. In perspective, GNI-based own resources could also prove to be an adaptable source of funding for proceeding with multi-speed integration or for a variety of more or less deeply integrated European “clubs”.

At present, however, financing through GNI-based own resources heightens the sense that Europe is financed by the Member States – not by its citizens and businesses, the actual taxpayers.

One consequence of the state-dependent financing mode is the oft-lamented juste retour logic. This principle of an appropriate return of funds for payments made – which has a fundamentally positive connotation in finance – has long been perceived as a major problem as regards the EU budget: the “monster juste retour” (Richter, 2008). Member States and EU parliamentarians can be marked by regarding the Union and its

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7 If there were clubs of EU Member States that in certain policy areas are more deeply integrated than the EU-27 as a whole, the associated additional costs would have to be financed by the club members alone (who would then, however, have lower national expenditure in the relevant policy areas). Since GNI is indeed an objective indicator of the economic strength of each member state, proportional (or even progressive) financing contributions – which are collected only from the respective club members – can well be linked to it. This does not preclude the possibility of choosing other indicators as a basis for the calculation of such “membership contributions”, which would then be financed out of national budgets or – as own resources – at the expense of national tax revenues. On the other hand, financing additional European common goods through specific levies or taxes, which as such would only be imposed in the club Member States, is likely to be considerably more difficult. Indeed, the range of possible EU taxes that would also be good levies from a fiscal policy and systematic point of view is very limited anyway. An exception could be levies that follow directly from the club's stated purpose and are policy instruments that promote this purpose (e.g. climate protection levies in a “decarbonisation club”). On the club idea – without these considerations about revenue instruments - see Demertzis et al. 2018. For possible EU levies, see HLGOR (2016), Büttner and Thiöne (2016), Fuest and Pisany-Ferry (2020).
budget primarily as a source of the largest possible financial flows back to individual countries, their regions and constituencies. The visibly national own resources contributions on the one hand and the (for the main) easily localisable EU expenditures on the other hand make terms like "net contributor" and "net recipient" possible in the first place. From the perspective of individual Member states, the comparison turns out simple: what a country "pays in" and what it "gets back". Yet this approach ignores the fact that important EU tasks cannot be localised, or can only be localised with great difficulty, as they are genuine European common goods. For example, the economic benefits of the Common Market and of the four fundamental freedoms are hard to allocate to individual Member States. The most important common goods for Europe do not automatically have to entail the highest budgetary spending. However, the established budget is dominated by funds for agricultural policy and cohesion policy, both EU tasks that primarily generate regional and local benefits and, thus, are very easy to localise.\(^8\)

A distinction must be made here: if it were the declared task of the supranational system and the EU budget to provide for a kind of European financial equalisation through a combination of contributions based on economic strength and grants distributed according to needs, little could be said against the focus on net balances and juste retour. All financial equalisation schemes in federal systems must be able to meet this criterion. And indeed: although, as already mentioned, the image of financial turntable falls far too short for the EU and, although the EU budget functions at best only partially as a de facto fiscal equalisation system (Thöne, 2017), most Member States act in the budget negotiations rather prototypically as "recipients" or "payers" of fiscal equalisation transfers.\(^9\) In such a constellation, the financial interests of the individual Member States dominate, and they behave (in a selfish sense) as perfectly rational actors.

In terms of their economic performance, the five largest net contributors to the European budget in 2019 were Germany (0.41 per cent/GDP), the Netherlands (0.36 per cent), Denmark (0.32 per cent), Austria (0.31 per cent) and Sweden (0.29 per cent).\(^10\) Except for Germany, these were the so-called "frugal four" that during the July 2020 European Council summit pushed for annual spending cuts in the 2021-27 MFF as well as for significant changes to the recovery fund.\(^11\) However, the extensive lump-sum rebates for the above-mentioned top five net contributors, also agreed for the new MFF, benefit Germany, by virtue of its size, the most — at 3.7 billion euros annually. At the centre of this struggle for a net balance favourable to one’s own country are small net contributors such as Italy. Although it is a net contributor, the question of the best negotiating tactic finds no clear answer. Often, putting the brakes on EU revenues is a less effective tactic compared to obtaining and fostering additional EU spending in those policy areas that tend to favour one’s own country and one’s own net balance. The more opportunities a Member State offers for traditional EU spending, the more this is the case, i.e. the stronger the agricultural sector is and/or the more economically deprived regions there are. For the net recipients of the EU budget, this is clearly the superior strategy. In terms

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\(^8\) See Thöne and Kreuter (2020b).
\(^9\) This is somewhat ironic insofar as, precisely from the point of view of many net contributors, the concept of a "transfer union" — i.e. a fiscal equalisation union — is treated as one of the major taboos in European policy.
\(^10\) Source: Bankenverband based on European Commission data (https://bankenverband.de/blog/eu-nettozahler-und-netzahmenfanger/).
\(^11\) At the time, Germany held the EU Council Presidency and acted „more neutrally“ in this role.
of economic performance, the small Baltic states often top the net beneficiary Member States’ ranking; in absolute terms, Poland and Hungary, of all countries, were the largest net recipients in 2019. This financial position, which has hardly changed in the MFF 2021-27, may help to explain the willingness of those two states to compromise in the aforementioned dispute over the so-called rule of law mechanism.

A way to alleviate the *juste retour* problem, at least on the revenue side of European finances, is emerging now, of all times, – and thus unexpectedly – with the NGEU recovery fund. It works as follows: first, an overall amount of 750 billion euros (in 2018 prices) will be raised on the capital market as EU own debt. The capital raised will only be available for the period from 2021 to 2024. Of that, 360 billion euros will be passed on to weaker Member States in the form of repayable loans. The somewhat larger NGEU share of 390 billion euros, on the other hand, is to be provided in the form of grants. About 80 percent of these grants will be allocated to the Member States within the framework of the “Recovery and Resilience Facility” (RRF) – through which NGEU loans will also be processed. Almost 20 percent will be used under the REACT-EU heading to increase funding for by and large current programmes. As far as the loans component is concerned, the *juste retour* symmetry of receiving and paying is automatically ensured through the granting and repayment of loans. Only the interest advantages over individual new debt of the beneficiary Member States convey intended, but also clearly attributable net benefits. The *juste retour* logic remains intact here.

However, the *juste retour* logic could be overcome gradually in connection with the repayment of NGEU grants. The repayment of NGEU grants is scheduled to take place between 2028 and 2058. In principle, traditional own resources can be used for this purpose. The regular own resources ceiling will be increased from 1.22 to 1.40 per cent of EU GNI as of the 2021-2027 MFF; additional own resources of up to 0.6 per cent of EU GNI can also be called upon from the Member States up to 2058. This extra margin would serve to ensure the repayment of NGEU grants. In fact, it already covers more than what is needed to pay off the NGEU grants (Heinemann, 2020). But the increase in the regular own resources ceiling to 1.4 per cent of EU GNI could easily be used for other purposes as well. Moreover, the additional 0.6-margin is intended only as reinsurance if the repayment financing does not go through as planned. After all, as a matter of priority, new own resources in the form of taxes or tax-like revenues are to be introduced for the repayment of the NGEU grants. This sets out a path to combat the *juste retour* problem by reducing national imputability of European revenues. According to the Council decision of July 2020, the first step will be a levy on non-recycled plastic packaging waste, which is supposed to partially replace the existing GNI-based own resources as early as 2021. This "plastic tax" will then be followed by other concrete models in (by EU standards) rapid succession. The Commission has been tasked to put forward by June 2021 proposals for new own resources along the lines of a CO\textsubscript{2} border adjustment mechanism, a digital levy and the EU Emissions Trading Scheme. By June 2024, the Commission also plans to propose further new sources of revenue, such as a financial transaction tax, a financial contribution linked to the corporate sector and a common consolidated corporate tax base.

These decisions of summer 2020 go far beyond the vague recommendations to review the own resources system that have been routinely adopted with every Own Resources Decision since 1988 (Cipriani, 2016, footnote 12). That, after all, *fiscal* innovations could
indeed mark a promising path for the further development of the EU’s supranational system had become less likely in recent years. True, the “High Level Group on Own Resources” – the so-called Monti Group, set up in February 2014 after the previous Own Resources Decision – presented a forward-looking report on parafiscal own resources at the end of 2016 (HLGOR 2016). But, as is so often the case in a period between Own Resources Decisions (i.e. without external pressure to act), these recommendations remained without practical European policy consequences.

At the same time, assessing the juste retour problem shifted from European revenues towards EU expenditures. The basic idea here is very plausible (see e.g. Schäuble, 2016): If the Member States – and thus also their citizens – are no longer to view the EU budget primarily as a collective money pot from which each country seeks to extract on a net basis the most it can get for itself, then more goods with European added value would have to be provided at the Community level. As outlined above, this idea underlies the concept of European public goods. Such common goods, such as climate protection and external security, are services provided by an upper federal level that cannot be allocated territorially or at best very imprecisely.

Ultimately, the juste retour problem is so relevant because it occurs on both the expenditure side and the revenue side. It can therefore only be solved consistently if key revenue instruments politically assigned to the EU are used to finance public goods with a visible European added value12 – i.e., genuine European common goods. Only by adopting this twofold perspective does it becomes clear why juste retour as a point of conflict is always so politically charged. Far from being a special problem of financial policy, it symbolically and at the same time factually embodies a core hurdle that still distinguishes the EU’s supranational system from the “normal” upper level of a federal state.

The signs of innovation on the revenue side go hand in hand – within the framework of the NGEU recovery fund – with additional European impulses on the expenditure side. These impulses, however, largely flow into the financing of national measures; hardly any reach original EU projects as such. The great haste due to the crisis and the desire to avoid the emergency measures, despite the inevitable delay in their implementation, having too pro-cyclical an effect on economic recovery, left little alternative to a European spending mode strongly tied to the status quo and easily assembled.

This is even truer for the regular expenditures of the EU budget and the MFF. Here, the juste retour problem is not only exacerbated because, with structural and agricultural policy, regional and local public goods dominate the scene (Thöne and Kreuter, 2020b). The fact that European projects are primarily carried out through nationally co-financed grants and subsidies also facilitates and reinforces the juste retour approach. At the same time, this political entanglement binds the EU and the Member States together in a way that makes clear governance difficult and can blur political responsibilities. Indeed, the national budgets of the Member States must contribute to the financing of many individual Community tasks: among others, projects financed by the European Social Fund or the European Regional Development Fund require national co-financing as

12 See Weiss et al. (2017).
proof of local self-interest. As a result, the EU in turn has very little independent room for manoeuvre in its budget.

Responsibility for implementing the EU budget lies with the European Commission (Art. 317 TFEU). However, the bulk of EU expenditure (over 76 per cent\(^1\)) is implemented in cooperation with the Member States under shared management. This means that ultimately the local or national authorities of the Member States – under the Commission's supervision – decide on and manage the use of the funds. Two types of problems arise here. On the one hand, deploying the resources made available often fails on the ground. For example, at the end of 2018, Italy had spent only 23 per cent of the €75 billion EU funds to which it was entitled for the period 2014-2020. On the other hand, the resources made available could be used improperly, as in corruption. This problem is illustrated by a recent New York Times investigation, which reveals that 80 per cent of agricultural funds go to the richest 20 per cent of farms, with sleaze and nepotism often playing a large role.\(^2\) Cohesion policy, too, often has to deal with on-the-ground corruption locally. At times, public (partly "populist") perception of such a corruption can be seen already as an independent burden on European integration that is decoupled from the underlying problem (Batory, 2020).

Co-financing and co-management of EU grant-type expenditure cannot be examined in greater detail here. Our analysis suggests their complications are symptomatic of the current budgetary and policy model.\(^3\) As such, they also reflect the strains that the EU's current expenditure profile, which is barely marked by European common goods, creates for the supranational governance model. The latter, akin to a federal state at its core, should not be inextricably equated with the tasks of today's Union, plagued as they are by juste retour considerations. The supranational governance model, as we argue below, can aim higher.

### B.2. Intergovernmental governance model

By extending policy integration to areas that are strategically relevant when it comes to Member State sovereignty or have high political salience, the Union's decision-making process was placed in a completely different institutional framework than that of the supranational governance model. The policy areas concerned include, among others, the Common Foreign and Security Policy (CFSP), Justice and Home Affairs (JHA), and economic policy for the Eurozone. In the intergovernmental governance model, decisions are generally taken unanimously by the Council of Ministers and the European Council on the basis of voluntary political coordination.\(^4\) The European Commission provides

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\(^1\) See official website on EU-funding: https://europa.eu/european-union/about-eu/funding-grants_en.


\(^3\) An Outlook on the further line of reasoning of the paper: The problems just described, which arise with the joint financing and resource management of existing European tasks, may at first glance resemble the challenges outlined under the catchphrase of "connectivity" in Section E for the realisation of European public goods with and in the Member States. External similarities do not necessarily mean kinship. Nevertheless, the experiences from the current joint policy administration will be able to offer valuable clues as to how to organise more European common goods in a federal EU.

\(^4\) With regard to CFSP, Art. 24 of the EU Treaty explicitly states: "the adoption of legislative acts shall be excluded".
technical support for the operational implementation of intergovernmental decisions. The European Parliament, on the other hand, in the main only needs to be informed; the role of the Court of Justice is also limited.  

Thus, in the intergovernmental governance model, more power lies with the institutions representing the national governments. Albeit with some overlap in the respective areas of competence (“confusion of powers”)18, the European Council has emerged as the main executive body and the Council of Ministers as the main legislative body. This strong political weight of the intergovernmental institutions creates a legitimacy deficit from a European perspective, given that the Council of Ministers and the European Council are not subject to horizontal checks and balances and their members are vertically accountable only to national parliaments.

Moreover, while the concentration of decision-making in the European Council and/or the Council of Ministers has promoted a type of centralisation at European level, at the same time it has blurred the distinction between national and European policy in the areas concerned. Decisions – especially unpopular ones – are not clearly attributable to individual Member States or the EU. Inter alia, this makes it more difficult for citizens to express their (approval or) disapproval of specific policy measures and could favour the success of populist parties in national and European elections.  

Even without such complications, in the intergovernmental system, unanimity and the associated universal veto right inevitably give national interests preponderance in decisions. These are, thus, often characterised by the need to “bring home” a good deal, i.e., by the juste retour logic. As such, they also undermine original European policy and the capacity of European bodies to mediate politically.

Furthermore, the unanimity rule is problematic in view of the growing heterogeneity of Member States, as it allows a minority of national actors to slow down or even block the pan-European agenda. The paralysis of the decision-making process occurs primarily in the case of solutions to crises that come with strong redistributive effects – so interventions of the European Council and the Council of Ministers often arrive too late or are too feeble. The intergovernmental governance model is thus structurally weak at the level of the EU-27 when it comes to further deepening European integration in politically sensitive areas and to setting up and maintaining the Community administrative and financing structures needed for this purpose. Even more flexible integration models under the existing EU treaties – such as the Permanent Structured Cooperation (PESCO) in the Common Security and Defence Policy (CSDP), activated in 2017 – are not automatically more successful in advancing far-reaching and ambitious initiatives.  

In order to avoid the deadlock resulting from the unanimity rule, coalitions of Member States have increasingly concluded inter-se agreements (i.e. agreements between two or more parties) outside the EU legal order with ad hoc rules on their entry into force.

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17 Even where the ordinary legislative procedure applies – as in the case of the Six Pack and Two Pack – the European Parliament plays only a minor role (Bressanelli and Chelotti, 2018).
18 For example, the ECOFIN Council and the Eurogroup are legislative institutions, which nonetheless also perform executive functions (Fabbrini, 2019).
19 Fabbrini (2019) even outlines the extreme case where this could lead to the formation of an anti-EU majority in the European Council.
20 For an overview of the PESCO projects see Blockmans and Crosson (2019).
This happened in particular when it came to managing the euro crisis, as with the Fiscal Compact. For it to enter into force, ratification by only twelve euro countries was required (Art. 14 of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union, in short TSCG). Similarly, the entry into force of the treaty establishing the European Stability Mechanism (ESM) was subject to ratification, approval or acceptance by signatory countries representing “just” 90 per cent of the total capital subscriptions (Art. 48 ESM Treaty).

However, circumventing the ponderous nature of the intergovernmental system of the EU-27 by acting through sub-groups outside the EU treaties has its own limits. This became clear during the fight against the sovereign debt crisis from 2011 onwards. The Lisbon Treaty provides for a “no bail-out clause” for the EU (Art. 125 TFEU). Moreover, the United Kingdom made it immediately and unequivocally clear that it would not take part in any measure to save the common currency. Accordingly, the explicit view was taken that the fiscal rescue of the then crisis states, imperative given the threat of Euro-zone collapse, would have to take place outside the treaties. The aid in support of the economies of highly indebted states had to come indirectly from the economically more stable lender countries under the guise of a collective instrument. Hardly surprisingly then, the legal link between the Fiscal Compact and the ESM has meant that states could not choose to sign up to the compact on a fully voluntary basis: financial support from the European Stability Mechanism was only granted to countries that had simultaneously ratified the Fiscal Compact (preamble ESM Treaty). From a creditor point of view, this might appear to be a standard financial market conditionality for securing loans. From the point of view of the countries in financial difficulties, this was in fact external pressure to sign up to an additional intergovernmental treaty. Such a constellation ran counter to the spirit of intergovernmentalism as a way of organising “coalitions of the willing”. Moreover, by highlighting the distinction between lenders and borrowers among the Member States this exacerbated the sense of dominance (by some) and resentment (by all).

The emergency and recovery measures initiated in 2020 during the coronavirus crisis are in many respects not comparable to those of the ESM period. Nevertheless, a lesson has obviously been learned: without the experience of the euro rescue – including the numerous political distortions between the Member States – the decision of early summer 2020 to rely directly on Community debt in the fight against the pandemic would not have been taken so quickly, if at all.

The euro rescue via ESM and Fiscal Compact has exposed the limits of intergovernmentalism outside the EU treaties in another respect: enforcement is not possible without the supranational institutions. The need to ensure compliance with the agreed rules by a coalition of Member States has prompted the organisations set up by the Fiscal Compact Treaty and the Treaty on the European Stability Mechanism to resort, after all, to the supranational institutions of the Lisbon Treaty: Commission and Court of Justice. The fact that intergovernmentalism in the EU ultimately still relies upon the supranational system is a very good sign in view of the “federal paradox” discussed in Section C below.
C. First analogy: Does the EU as a co-existence of federal state and confederation of states give rise to a “federal paradox”?

The EU is often described as a federal entity sui generis – no longer a confederation of states, but not yet a federal state either. The German Federal Constitutional Court (1993) even coined its own term for the EU by speaking of a Staatenverband. This neologism may aptly describe the intermediate space between Bundesstaat (federal state) and Staatenbund (confederation of states). It is also suitable as a compromise formula for all those who shy away from definitive terms – as well as from the implications of "no longer a confederation of states" and, especially, of "not yet a federal state" – as being too sensitive. What's more, in terms of federal taxonomy, it is probably entirely appropriate to honour the EU's singular nature with a specific definition. Nevertheless, we do not.

Indeed, the focus on the uniqueness of the EU makes it more difficult to learn from other, roughly comparable federal constellations. So as to do so, we deliberately take a somewhat blurred look at the federal unicum EU. First, we simplify matters at hand by characterising the Union's federal structure as a co-existence of the supranational governance model and the intergovernmental governance model. In the first analogy, we then equate the supranational governance model with that of federal state and the intergovernmental governance model with that of confederation of states. If one leaves out institutional subtleties and existing overlaps, this constellation reflects the side-by-side co-existence of federal state and confederation of states.

In a federal state, several constituent parts join together to form a sovereign state. The latter has a government and decides on all issues that are essential for the unity and existence of the whole, while the constituent parts retain their statehood and join in forming the federation's will.

To what extent does this characterisation apply to the EU's supranational governance model? In the EU, the Member States remain the "masters of the treaties", i.e. the Union formally has no sovereignty of its own, and its fiscal power remains very limited. On the other hand, the EU has been given extensive competences in policies linked to the internal market, and in this context supranational institutions – the European Commission, the European Parliament and the European Court of Justice – also play a major role. Furthermore, the supranational governance model of the EU features the federal-state typical division of the legislature into two chambers (bicameral system), the European Parliament and the Council of Ministers, which represent the citizens of the Union and the member states respectively (dual representation). Voting in the Council of Ministers is here increasingly based on the principle of (qualified) majority voting, and European laws take precedence over national law.

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21 However, it might be difficult to render this fine conceptual differentiation in all the languages of the Union.

22 In a way, the analogy between supranational governance model and federal state also allows for identifying fields of action for future developments. This becomes evident for example with the bicameral principle and dual representation. Here, we are confronted with a historically readily understandable, but nevertheless peculiar criss-cross asymmetry: On the one hand, the principle of qualified majority voting implies that large Member States are less likely to be outvoted than in the case where all constituent parts enjoy exactly equal weight (as e.g. in the US Senate). On the other hand, the elections to the European Parliament are far from realising the basic democratic principle of equality of votes. Not only do the partly very different rules on electoral lists, election periods and
A confederation of states, on the other hand, is a loose association of sovereign states under international law set up to achieve selected common goals. To this end, common institutions are established which exercise state power only outwardly. Internally, their decisions always require implementation by the constituent states.

To what extent does this characterisation apply to the EU’s intergovernmental governance model? As a subject of international law with its own legal personality, the EU is undoubtedly more than a conventional confederation of states. On the other hand, the supranational institutions play only a subordinate role in any policy areas that are politically sensitive for Member States. Here, will formation and decision-making are mainly the responsibility of the Council of Ministers and the European Council, both of which represent Member State governments. Decisions are taken by unanimity, as is customary in international organisations. Moreover, within the intergovernmental system, the EU is dependent on the capacities of the Member States; this limits its ability to act. For individual tasks, however, different groups of Member States may also come together to conclude inter se agreements outside the EU treaties, which allows for more flexibility in establishing new policy areas.

From the above it becomes evident that neither the analogy between the supranational governance system and the model of the federal state nor the analogy between the intergovernmental governance system and the model of the confederation of states are to be understood as exact matches. Despite their inexactitudes, the analogies are nevertheless very helpful in illustrating the strengths and weaknesses of both systems for the introduction and provision of European common goods.

The supranational governance model offers better conditions for the provision of EPGs: its institutional structure – with a bicameral legislature, voting according to majority principles and an executive largely independent of the Member States – meets European democratic standards, and the well-established EU budget ensures the financing of the tasks agreed upon. However, the introduction of new EPGs beyond the competences laid down in the existing EU treaties presupposes – with the exception of enhanced cooperation pursuant to Art. 20 TEU23 – an amendment of these treaties. This requires threshold clauses in the 27 Member States stand in the way of this. Above all, the principle of “regressive proportionality” results in small Member States being allocated significantly more seats in the European Parliament than large Member States. The voting rules of both chambers do not fit the federal state ideal implied by the analogy. To a certain extent – and of course only approximately – they compensate each other crosswise. Whether and how a prospective federal state “normalisation” of the supranational system should also develop from here cannot be foreseen today. For the further deepening of the Union through more European public goods, however, there is hardly any way around adapting the underlying democratic rules of the game – especially in the case of differentiated integration based on club solutions. Whether, e.g. by establishing special voting rights for the enhanced cooperation pursuant to Art. 20 TEU23 – an amendment of these treaties. This requires

23 Taking up an impulse from the Tindemans Report (1976), the Treaty of Amsterdam (1997) introduced enhanced cooperation (EC) for the first time in order to enable, as a last resort, differentiated cooperation between groups of nine or more Member States where a step towards the general deepening of the community (within the competences of the treaties) had previously failed. The EC can only take place if the European Parliament, the Council (unanimously) and, in de facto terms, the Commission have given their consent (cf. Fischer-Lescano and Kommer, 2011). Once this hurdle of “benevolent disinterest” (Wessels, 1998, 205) of the non-participating Member States has been cleared, an EC group internally can switch from the consensus to the qualified majority principle by using the special passerelle clause of Art 333 TFEU, if this was not already provided for in the legal area in question. Enhanced cooperation always takes place by way of “borrowed administration” (Organiefeh); separate institutions cannot be set up. Calliess (2020, 59f.) regards the DC as a starting point for a flexible “Europe of pioneer groups” that can also contribute to the achievement of more European public goods. Within the framework of the purely intergovernmental system, it is conceivable that some progress in the field of public goods can also be made within the existing treaties. However, with a view to the broader goal of strengthening Europe through (substantial) common goods and making it more “European”, it is also important to keep the limits of
a unanimous decision of the European Council as well as ratification in all 27 Member States (Art. 48 TEU). This restriction, in a sense, protrudes from the intergovernmental system into the supranational system, as no regular federal state sets the quorum needed for a constitutional amendment at 100 per cent. As a result, treaty amendments are today treated as virtually impossible in practical EU policy; even talking about it is quickly considered naïve.

On closer inspection, this seemingly pragmatic attitude towards treaty amendments exhibits, rather, signs of despondency and is, above all, unhistorical. Indeed, there have been treaty amendments and it is likely that there will be treaty amendments again. Nevertheless, the need to bring about unanimous treaty amendments in the supranational system for introducing new European common goods is indisputably a major obstacle to this form of deeper integration. Even if the latter hurdle did not exist, the second "relic" from the intergovernmental system would set up another high barrier here: the unanimous decision that all Member States must take when it comes to the MFF constrains EU budgets and virtually depoliticises them over the seven-year period of validity. The introduction of new European common goods with a distinct financial profile proves to be quite difficult in the supranational system, even without a treaty amendment – all the more so when no major crisis is there to serve as an (un-wished-for) catalyst for European cohesion.

In the case of the intergovernmental system, it is exactly the other way round. Here the conditions for the provision of EPGs are much less favourable. The dominant role of government representatives from the Member States, both at the executive and legislative level, weakens democratic legitimacy. Moreover, different financing instruments must be used for each project. Finally, as illustrated by the examples of the ESM and the Fiscal Compact (Section B.2), the intergovernmental system can hardly operate without the institutions of the supranational system when it comes to enforcing European decisions. On the other hand, the introduction of new European common goods proves to be much easier in the intergovernmental system. As pointed out above, this does not primarily apply to new European common goods within the European treaties (with the – albeit limited – exception of enhanced cooperation). Yet, in the intergovernmental system, it is also possible to conclude inter se agreements outside the existing EU treaties. Here, the possibility of forming pioneering groups as "coalitions of the willing" may facilitate the introduction of new EPGs or even make it possible in the first place. This greater flexibility can also be decisive for EPGs that may well be joined by all members of the EU-27 in the medium-term. Indeed, EU states that are not convinced of a new

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Unanimity as a double relic in the supranational system

The intergovernmental system, on the other hand, is better suited for the introduction of EPGs

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EC in mind: Member States in the EC do not have access to the EU budget for their projects. But they are also not allowed to establish their own institutions (which could finance and implement the EPGs). The general democratic deficit of the intergovernmental system should also be mentioned here; after the initial approval of EC, the European Parliament is no longer actually involved. In this respect, EC is more likely to provide integration impulses where it is a matter of differentiated deepening of common guidelines and other framework laws, less so in the case of spending-effective collective public services by a pioneering EPG group.

24 The fact that the negotiation of a new MFF is itself highly politicised cannot be seen here as a kind of compensation. True, many of the issues that would otherwise have to be resolved in the context of annual budget negotiations are also addressed with regard to these large package solutions. But for a period of seven years into the future, it is obviously impossible to predict the current need for action at the European level.

25 Cf. footnote 23 above.
Community task from the outset can first assess how it is being realised in practice among the members of the corresponding "EPG-club" before making their final decision. Crucially, there can be no veto players in these more flexible constellations.

Are additional European public goods thus faced with their own "federal paradox"? Indeed, it is not the right way to go about things by introducing new EPGs where an adequate democratic and fiscal framework for their provision is lacking. At the same time, it makes little sense to plan the provision of new EPGs where the prospects for introducing them are low.

However, just as the first analogy cannot be understood as an exact match, so the federal paradox is not logically compelling. It does describe relevant obstacles; nevertheless, its resolution is not unthinkable. On the one hand, major treaty amendments are considered very difficult, but they are not impossible. No constitution can remain permanently unchanged in a changing world – especially not the European one. On the other hand, new European common goods introduced within the intergovernmental system can still be transferred to the supranational system at a later stage. Here, the supranational system, in which the new EPGs are provided, need not be – and this is likely to become decisive – exactly the same as that of the full EU-27. The experience with the ESM has made it clear that common goods which have been introduced in the intergovernmental realm will ultimately also depend on supranational institutions such as the Court of Justice and the Commission. In this perspective, it will therefore be necessary to examine how the democratic building blocks of the supranational system can be geared towards being able to co-represent and co-decide on such common goods that have been launched by a “coalition of the willing” (initially) only for the members of this club.

Any discussion on the democratic institutionalisation of EPG clubs goes far beyond the scope of this paper and requires careful and differentiated consideration. Nevertheless, by taking a closer look below at the practical provision of European common goods in a federal Europe, we also provide pointers for their successful introduction. After all, a well-thought-out concept for the provision of EPGs will – we are convinced – in turn help to significantly lower the hurdles for the introduction of new EPGs.

D. Second analogy: the EU as administrative federalism

The considerations so far suggest that the EU differs fundamentally from the system of dual federalism, which provides for a clear division of tasks between federal levels of government equipped with parallel and largely autonomous bodies (legislative, executive and judicial). Rather, the EU has features of a cooperative federalism or “administrative federalism”, which envisages close vertical cooperation between the central European level and the “decentralised” Member State level. In what follows – our second analogy – we compare the EU’s federal structure with German- and Austrian-style cooperative federalism. This comparison highlights some of the design issues that need to be answered in connection with the concrete provision of European public
goods. At the centre of the analogy is the German model of vertical cooperation, not because it is preferable, but simply because we are more familiar with it.

German federalism has undergone numerous changes throughout its long history. Relevant for our analysis is the experience gained over the past seventy years with the joint fulfilment of public tasks by the Federation, the federal states (Länder) and the municipalities. After World War II, the Western Allies insisted on the reorganisation of Germany in a federal sense so as to limit the power of the central state. The federal structure was enshrined in the German constitution under the principle of the federal state (Art. 20 (1) and Art. 79 (3) of the Basic Law), according to which the Länder retain own state character vis-à-vis the Federation. Both the Federation and the Länder have independent bodies and institutions (in the legislative, executive and judicial branch) with which they can exercise their own state authority.

A defining feature of German federalism is the Bundesrat model. The Bundesrat is a federal constitutional body that helps shape legislation (Art. 50 of the Basic Law) – by initiating bills, submitting opinions on draft government bills, convening the mediation committee, objecting to or approving legislative decisions – and consists of representatives of the Land governments (Art. 51 (1) of the Basic Law). Similar to the EU, the central legislature in Germany also has a second chamber, whose members are not directly elected by the people and perform a dual function, being at the same time members of the Länder governments.

Pursuing the interest of uniform or – as of 1994 – equivalent living conditions, the Federation has greatly expanded its influence over the years, both in terms of exclusive legislation (Art. 73 of the Basic Law) and of concurrent legislation (Art. 74 of the Basic Law), so that today – despite the principle of subsidiarity (Art. 30 of the Basic Law) – most of the legislative competences lie with the Federation. In return for the loss of legislative autonomy, the Länder (through their representatives in the Bundesrat) have been granted participation rights in the form of approval in more and more areas of federal legislation.26 The result is often close political interweaving (Politikverflechtung), which allows for a cooperative centralisation of decisions on matters of general interest, even though this renders the decision-making procedures more complex and less transparent (Scharpf, 2009; Kropp, 2010).

Despite the increasing integration of the German Länder in the central legislative process, their influence is weaker than that of the governments of the Member States in the EU. Indeed, the Bundesrat is subordinate to the Bundestag: it can only react – albeit in different forms (objection or approval) – to laws passed by the Bundestag. In addition, the Bundesrat has no executive powers and there is no other supreme executive body in Germany besides the federal government. On the other hand, the EU’s Council of Ministers is under the legislative control of the European Parliament in policies related to the internal market (supranational governance model). Here, however, the European Council can perform some executive functions alongside the Commission (dual executive). Moreover, in politically sensitive policy areas (intergovernmental governance

26 It is estimated that ahead of the federalism reform of 2006 more than 60 per cent of federal laws required approval by the Bundesrat (Sturm, 2013).
In sum, the institutional structure of German federalism displays important similarities with the supranational governance model of the EU. The institutional structure of the intergovernmental governance model, on the other hand, is nowhere to be seen in Germany – nor in comparable federal states. As already discussed in Section C, given the legitimacy problems associated with the intergovernmental governance model, it would be desirable to provide European public goods under the supranational governance model. For this to happen, there are undoubtedly major hurdles still to be overcome; nevertheless, the following considerations point in that direction.

With regard to the practical implementation of federal tasks, a defining feature of German federalism is so-called administrative federalism. For the execution of its laws, the Federation is usually dependent on the authorities of the Länder, which act either in their own right (Art. 83 of the Basic Law) or on federal commission (Art. 85 of the Basic Law). Only in a few areas falling within the competence of the Federation can the federal government execute its laws via its own administrative authorities (Art. 87 of the Basic Law). The German Basic Law, thus, provides for a separation between legislative competence and administrative competence. This separation is based on purportedly counterbalancing the centralised power of the Federation in legislation with administrative decentralisation within the Länder. The result is the emergence of a vertical political interweaving, in which one level of government cannot work without the other.

This separation of legislative and administrative competences raises the issue of control over proper compliance with decisions taken at central level. To ensure that German laws are executed effectively and in conformity with legal requirements, the Basic Law grants the federal government the possibility to exert a certain degree of influence on
the administration of the Länder: within the framework of enactment under federal oversight, it is entitled to legal supervision (Art. 84 of the Basic Law); within the framework of enactment on federal commission, it is entitled to both legal and technical supervision (Art. 85 of the Basic Law). These so-called rights of intervention enable a uniform interpretation and implementation of federal laws but may limit Länder administrative autonomy. At the same time, they intensify vertical political entanglement.

Another key issue arising from the separation of legislative and administrative competences is that of the responsibility for financing. If the central legislator establishes new common goods or substantially changes existing public tasks, which are carried out at the decentralised level by the Länder or their municipalities, the question as to which government level finances them must be clarified. This fundamental question for the financial constitution is answered in Germany with reference to the so-called principle of connectivity (Konnektivitätsprinzip). Under this heading, two – quite opposing – postulates are formulated, the "execution connectivity" and the "causal connectivity". Along the lines of the first postulate, Article 104a of the Basic Law stipulates that: "[...] the Federation and the Länder shall separately finance the expenditures resulting from the discharge of their respective responsibilities insofar as this Basic Law does not otherwise provide [...]". In other words, the level must bear the costs relative to any task it must carry out. Because of the link between administrative execution and expenditure burden, one also speaks here of "administrative causality" or "execution connectivity". This idea is more easily captured by the phrase "who executes, pays".

The execution connectivity constitutes the traditional foundation of German administrative federalism. The Länder bear the expenses for public services that are largely regulated by federal law, such as the financial and tax authorities, most of the judicial and the penal system. Moreover, the municipalities used to bear the costs for the bulk of local social services, which are regulated by the federal government and, in part, by the Länder. From an administrative economy perspective, a simple incentive consideration speaks in favour of execution connectivity: if the government level that discharges a task also finances the related expenditures, this provides the best incentive for an economic and efficient use of funds. The standard assumption is that one tends to manage one's own money better than someone else's.

Nevertheless, the vertical financial relations between the government levels in Germany are nowadays increasingly organised according to a contrary understanding of the principle of connectivity. From "legislative causality" follows "causal connectivity": "who orders, pays". This paradigm shift did not take place in the fifteen years or so after 1992 in order to thwart the incentive for efficient execution of tasks outlined above. Rather, experience had taught that another, politico-economic incentive dominated vertical financial relations: conventional execution connectivity enables a central legislator to expand locally supplied public services without having to pay for the additional costs or raise taxes. This, instead, is laid at the door of the decentralised layers of government; they have to bear the financial consequences of the central government level "doing good" for the electorate.

This "legislation at the expense of others" was supported for decades, albeit often grudgingly, by the Länder and above all their municipalities. The old consensus broke down
when the federal government failed to offer the municipalities any financial compensation for the additional costs of over 15 billion DM expected as a result of the newly created legal entitlement to kindergarten places.  

Today, after several rulings by the Federal Constitutional Court and amendments to Länder constitutions, the federal government can no longer transfer new tasks to the Länder without financial compensation. Nor may the Länder impose higher or new standards of performance on their municipalities without providing them with connectivity-compatible funding. However, the “old” problem of the incentive to manage someone else’s money less efficiently has not disappeared. When the “who orders, pays” principle of causal connectivity is implemented, the next step is to find a mode for this central financing that preserves as much efficiency incentive as possible – the characteristic of execution connectivity. This issue may also play an important role in the provision and financing of new European common goods, as we show later.

As in Germany, the central level of the EU generally relies on the decentralised administrative structures of the Member States to execute its norms. The competence of EU states in the execution of Community law can even go further than that of the Länder as regards enacting federal law. In the case of directives and of intergovernmental agreements under international law, it embraces the transposition of jointly agreed norms into national law, prior to their implementation and enforcement.

In Europe, however, the Community institutions have less influence on the administration of the Member States than the federal government has on the administration of the Länder in Germany. EU countries must take certain legal requirements into account when realising EU norms. But the effectiveness of these legal requirements may prove limited, given the heterogeneous administrative structures in the different Member States and the frequently inadequate possibilities for control. As a result, the execution of EU norms increasingly involves various forms of co-administration or shared administration – both horizontally (among Member State authorities) and vertically (between Member State authorities and EU in its administrative capacity).

In summary, this brings us to our second analogy: Both in the supranational and in the intergovernmental governance models, the EU is characterised by a clear separation of central legislative competence and decentralised administrative competence. The comparison with German cooperative federalism seems obvious here. Germany is considered – for better or worse – a prime example of cooperative, vertically interwoven administrative federalism. Much can be learned from this counterpart to US-American-style dual federalism for the governance of European common goods. Even so, the second analogy can lay claim to a “role model function” or something similar rather less than the first analogy. The fact that the allocation of competences between Bund and Länder in Germany has developed in a roughly similar way to that between Union and Member States in Europe has specific historical reasons in both cases. Nevertheless:

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28 Since the paradigm shift from execution to causal connectivity was only implemented for new or substantially changed provisions (otherwise the German financial constitution would have had to be completely revised), it must be very clearly identified in German practice whether the claim for connectivity-compatible financing of tasks executed decentrally possibly also applies to “old laws”.

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Causal connectivity as a modern response to “legislation at the expense of others”

Similarities and differences with EU administrative federalism

Second analogy as an approach to learn from the experiences and mistakes of German administrative federalism for more EPGs
since Germany – if one follows the analogy – is more advanced in its federal development than the EU, important lessons for EPGs can be drawn from German experiences, even from bad ones. The EU is, in this perspective, a federal state in the making. Compared to German administrative federalism, many aspects of the provision of new European common goods remain unresolved. Therefore, the issue of the appropriate vertical organisation of the provision of EPGs is of central importance. We will address this issue in the next section.

E. Options for the division of competences in the case of European public goods

As emerges from the previous section, the provision of European public goods – both under the supranational and intergovernmental governance models – raises the fundamental question of how it should be organised within the European multi-level system in terms of legislation, administration and financing. The traditional theory of fiscal federalism describes as ideal full fiscal equivalence (Olson, 1969), according to which the circle of those who use a public good should coincide with the circle of those who decide on and finance it.

The implementation of this “correspondence principle” would mean that the central level – here the EU or a “club” of Member States – should take responsibility for all three competences itself. Such fiscal equivalence, which is prototypical for "dual federalism", can from today’s perspective only be achieved for a fraction of the possible EPGs.

The provision of most European common goods will require the participation of both levels of government, the EU and the Member States. In other words: without vertically cooperative European federalism, only a few additional EPGs can be envisaged. More and better EPGs, however, are – that’s the premise of our project – an important key to a strong and sovereign Europe. Therefore, finding a suitable and, for the parties involved, acceptable solution to all the challenges associated with connectivity is paramount.

E.1. Taxonomy: Criteria for the allocation of the three main competences

Before outlining possible practical scenarios for the provision of European public goods, it may be useful to develop criteria for allocating individual competences to the central or decentralised government level.

The EU is based on the idea of a community of law. After all, the development of common policies within a group of very heterogeneous states is hard to imagine without laying down uniform rules of the game. In the case of a European public good, it therefore seems obvious to place the ultimate legislative competence at central government level.
The legislative competence should be transferred to the central government level if the policy of a Member State causes significant (positive or negative) cross-border spillover effects, i.e. entails benefit or harm to others. Typically, such externalities are not taken into account by the lower level of government that triggers them. The resulting undesirable development can be counteracted by shifting the legislative competence to a higher level of government. The correct level of government for a specific policy in a multi-level system is found, when no further cross-border spillover effects occur.29

When taking over legislative competence, the central government level does not always have to regulate the achievement of objectives down to the final detail. Depending on the extent to which preferences differ among Member States, it may simply establish a (more or less broad) general uniform legal framework for these and this can then be filled in taking into account citizens’ wishes.

The best possible allocation of administrative competence is assessed rather on the basis of administrative economy – to a certain extent “business management” – criteria. The execution of European legal acts at the central EU-level is justified whenever significant economies of scale can thereby be achieved. Economies of scale resulting from better utilisation of infrastructures arise, for example, where national execution leads to unnecessary duplication of administrative structures, projects aimed at attaining European objectives and related expenditures. Very large projects, which smaller and medium-sized Member States would not even seriously consider due to technical or organisational indivisibility, can only be realised under joint administration. There are also symbolic European common goods for which implementation by the EU alone can be expected to create the desired European esprit de corps. This may apply analogously to public services that serve at home (and possibly overseas) as objects the European Union is identified with.

On the other hand, the execution of European legal acts by Member State authorities is appropriate whenever existing administrative structures can be readily used and the regional framework conditions (e.g. institutional, geographical, socio-economic) are very heterogeneous. The latter circumstance also encompasses the phenomenon of negative economies of scale in the form of different wage levels and other cost structures. Decentralised administration preserves more of the national sovereignty of the Member States and, thus, enables a differentiated distribution of power between federal levels. In addition, in the context of decentralised administration, it may be easier to establish closeness to citizens. This, however, is not a matter of course; the upper authorities of the Member States are by no means automatically designed to be participatory and close to the people.

Besides, uncoordinated parallel administrative procedures in the various Member States may jeopardise the uniform execution of European legal acts. Sometimes, administrative action in one country can also have cross-border effects. In order to guarantee the correct and effective execution of its legal acts, the Community is dependent upon the

29 In the case of global public goods, such as climate protection, the legislative competence should lie – in the absence of an assertive world legislator – with the next highest assertive level of government, which should address the remaining spillovers, inter alia, via international treaties such as the Paris Agreement.
cooperation of the Member State authorities among themselves and/or with the central administration. This cooperation can take various forms:

- information, notification and reporting obligations of Member States authorities;
- control, coordination and support by Union institutions;
- mutual involvement in decisions;
- regular exchanges in joint committees or bodies;
- bundling of administrative competences in a single Member State.

The financing competence, understood as the obligation upon a public budget to bear the costs for the provision of a common good, should be allocated according to the principle of connectivity. This is simple in the case of fiscal equivalence: if the above criteria suggest that the legislative competence and the administrative competence should be assigned to the same level of government, then the financing competence also resides here. In the event – probably frequent for European common goods – that the first two competences do not go hand in hand, it is worth looking at experiences from the German federal model (Section D). Here, administrative economy arguments in favour of decentralisation compete with political economy arguments in favour of centralisation.

One argument in favour of decentralised financing by the Member States – pursuant to execution connectivity – is that these have a cost effectiveness incentive when they also bear the costs for public services regulated by the EU. These incentives to perform the delegated tasks efficiently and economically result here from the budgetary self-interest of the executing Member State, which would have to burden its own taxpayers with tax increases or benefit cuts in the event of inefficiently high expenditure. Another argument in favour of decentralised financing is greater flexibility and co-responsibility – especially if the Member State enjoys leeway when it comes to implementing centrally regulated services. This aspect plays a very important role in the context of European framework legislation via directives yet to be transposed into national law. It also becomes clear here that such a constellation may be a “standard model” of federal distribution of competences in Europe across many policy fields today.

Furthermore, an argument in favour of decentralised financing lies with administrative unity: if public bodies in the Member States fulfil their own subject-related tasks in addition to the European ones, then integrated decentralised financing also prevents demarcation problems, does not encourage hidden cross-subsidisation or the like, and thus strengthens budget transparency.

In contrast, the arguments in favour of centralised financing of locally discharged Community tasks – pursuant to causal connectivity – are rather more concerned with political governance. Decades of experience with German administrative federalism teach that central legislative competence unaccompanied by the obligation to finance the regulated matter allows for a largely “generous” policy to the detriment of other public budgets. The obligation to finance self-regulated services from one’s own budget thus becomes an important tool for assuming political responsibility. In Germany, the very extensively used opportunity for conducting central policy at the expense of decentralised finances has ultimately forced a paradigm shift towards causal connectivity. To finance common goods that are regulated centrally also with funds from the central level paves the way for locally executed services in a harmonised quality. The quality of the common good
is decoupled from the differing fiscal strength of the respective Member State. Accordingly, central financing also fits better to solidary burden-sharing whenever European goals weigh very unevenly on the individual Member States. The same is true for Member States that are exposed to asymmetric risks.

Table 1 summarises, in the form of a condensed taxonomy, the criteria for the allocation of the three main competences when it comes to providing European public goods. Even though the focus in this "federal state view" is on the supranational system, the criteria can also be applied to the intergovernmental governance model.

<table>
<thead>
<tr>
<th>Table 1: Criteria for the allocation of the three competences in the case of the provision of European public goods</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Legislative competence</strong></td>
</tr>
<tr>
<td>• Cross-border spillover effects</td>
</tr>
<tr>
<td>• Homogeneous preferences for the public good</td>
</tr>
<tr>
<td>• No spillover effects</td>
</tr>
<tr>
<td>• Heterogeneous preferences for the public good</td>
</tr>
<tr>
<td><strong>Administrative competence</strong></td>
</tr>
<tr>
<td>• Positive economies of scale</td>
</tr>
<tr>
<td>• Indivisibility</td>
</tr>
<tr>
<td>• European identification</td>
</tr>
<tr>
<td>• Supervision and coordination of decentralised administration</td>
</tr>
<tr>
<td>• Use of existing administrative structures</td>
</tr>
<tr>
<td>• Negative economies of scale</td>
</tr>
<tr>
<td>• Further specification in the Member States</td>
</tr>
<tr>
<td><strong>Financing competence</strong></td>
</tr>
<tr>
<td>• Political incentive for legislation under own responsibility</td>
</tr>
<tr>
<td>• Solidarity-based burden-sharing or burden-sharing according to economic performance</td>
</tr>
<tr>
<td>• Administrative economy incentive for efficient (decentralised) administration</td>
</tr>
<tr>
<td>• Flexibility in the scope of (decentralised) administration</td>
</tr>
<tr>
<td>• Individual, subject or politically differentiated contributions (in the case of central administration)</td>
</tr>
</tbody>
</table>

The criteria within the taxonomy show that the vertical allocation of competences – at least beyond the simple case of full fiscal equivalence (notably rare in Europe) – can only seldom occur unambiguously and without weighing up strong pro- and con- arguments. Decisions will have to be made on a case-by-case basis that recognises the empirical framework conditions. In Section E.3, we briefly outline exemplary scenarios of different constellations of centralised/decentralised competence allocation. Before that, in Section E.2, we take a more in-depth look at causal connectivity in the context of advancing Europeanisation, as this important option still needs to be further fleshed out.
E.2. How can central financing be realised?

The execution of European legal acts is deemed to be financed by the central level of government when the European Union – or a club of Member States – collects non-earmarked revenues in a central budget and grants the individual Member States funding adequate for the task in hand from it. As with carrying out any task via a public budget, two fiscal design questions must, in principle, be answered here. First, how are the funds raised? And, second, how are the funds from the European budget transferred to the Member States or their bodies?

However, the first question – as important as it may be for the general chances of introducing additional European common goods – can be answered as regards the fiscal-federal implementation of specific EPGs by the so-called principle of non-affectation or principle of budget unity: all public revenues held at any level of government serve to finance all its tasks without distinction. Behind this budgetary rule is the principle of democratic equivalence of state objectives. New services must be justified vis-à-vis existing ones only by virtue of their purpose and be able to persist in this respect. Yet, new public services should not be hampered within the democratic order by the fact that they have to “bring along their own money”. Nor should traditional services be privileged by having certain budgetary components reserved for them.

In view of the above-mentioned problems with the juste retour logic, the rigidity of the multi-annual financial framework, especially in the proportion of traditional to new EU-tasks, and the outlined innovations on the revenue side with regard to debt and new tax-like own resources, it is obvious that the EU must still pass through several stages of reform before it can meet the objectives of budget unity. This is a big task – but a different task. Whether it is worth tackling such a big task in order to strengthen the Union via more European common goods depends not least on how precisely to provide for them within the fiscal-federal context. For the latter question, it is of secondary importance whether the required central funds flowed into the budget – hidden behind the veil of the principle of budget unity – in the form of traditional EU own resources, in the form of other contributions, in the form of new EU taxes or even in the form of EU debt. The focus here is on alternative ways of transferring funds from the central budget to the Member States.\(^\text{30}\)

If we now briefly look at the different designs of central task financing, we see that elements of mixed financing are also quite common. In mixed financing the centralised and decentralised government levels each raise part of the financial resources for implementation (purely decentralised). In the practice of financing current European measures (as in the framework of cohesion policy), national co-financing shares and interest quotas play an important role. What's more, when it comes to the centralised financing of European common goods, mixed models fall within the spectrum of legitimate and – depending on the EPG – likely solutions. Nevertheless, we will not examine them in depth here. On the one hand, because mixed financing reveals the advantages and

\(^{30}\) In principle, the same also applies to EPGs that are not provided for the full EU 27, but only for some of the Member States within the framework of club solutions. Notwithstanding this, the consideration made above that clubs would probably be best financed by contributions from the participating Member States still holds (see footnote 6).
disadvantages of its components "proportionately" – and is thus implicitly taken into account. On the other hand, mixed financing can bring its own problems, so that in most cases it should, at best, be considered a second or third choice.

In particular, mixed financing adds an extra twist to the – in vertical cooperation unavoidable – policy entanglement: co-financing – not least a fair and equal split – impairs sense of responsibility, so-called ownership. Political accountability for programmes conducted "jointly" due to mixed financing is often spread over all parties involved, not properly allocated to any of them. If one level of government no longer has to bear the full costs alone, the willingness to undertake controversial corrections of undesirable courses decreases radically. Indeed: the political costs of such conflicts are usually borne by the level of government that raised the issue in dispute; the financial returns from a consequent correction of costly undesirable developments are, however, reaped by all interested parties. Conversely, in the case of positive developments, success proverbially has "many fathers and mothers". Since bringing political measures to fruition does not generally come without effort and political costs for the initiators, the incentives for good governance under shared ownership are weakened here as well. That's precisely why, in German federalism, the co-financed and shared tasks of the Federation and the Länder set out in Article 91a of the Basic Law were regarded very early on as a prime example of the crippling aspects of policy entanglement.³¹

Against this background, three basic mechanisms for the transfer of European funds to the Member States or their bodies can be identified: tax share, grant allocated according to some key or reimbursement of expenses.

A tax share would allow Member States to retain a certain proportion of the European taxes levied by them or on their territory for refinancing the European common goods they administer.³²

To date, the EU has no significant tax revenues of its own. It is only entitled to so-called "traditional own resources" (customs duties and sugar levies) and "VAT-based own resources", which are collected by the Member States and have stagnated or declined over the last decade. Thus, as long as the EU financing system remains unreformed, the tax share mechanism is not an option for transferring funds to Member States. Yet, as briefly mentioned in Section B.1, the own resources system is supposedly extended towards EU taxes as such over the coming years, as a means of paying off grants made from the Coronavirus Recovery Fund.³³

Anyway, for the time being, Member States' shares of EU taxes should not be envisaged. It would not be conducive to establishing a European tax system, however limited in scope, if parts of the new own levies remained in the direct hands of the Member

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³¹ See Scharpf et al. (1976). This mechanism can also be detected on the revenue side. For example, Thöne (2012) explains notoriously strong resilience against any changes in fiscal spending proven to be ineffective within German joint taxes through their character as hidden joint tasks.

³² In exceptional cases, the spatial reference to the respective Member State could also be dispensed with if an alternative allocation key related to the taxable item were used. In this case, one would speak of apportionment of the Member State's share of the tax.

³³ Own EU taxes would be an important financing instrument for those European common goods that are administered by the Union itself. EU taxes can also help increase the revenues of the EU budget so as to finance with them new EPGs, which are administered by the Member States in the spirit of causal connectivity. This, however, is a different question from the one of interest here, namely the central financing of decentralised Member State administration.
States. Moreover, matching Member States costs to be financed in line with connectivity and the tax bases of potential EU levies to be apportioned according to an undetermined-as-yet formula would rarely succeed.\textsuperscript{34} Accordingly, shares of European taxes should be considered only in exceptional cases for central financing of EPGs that is compatible with the connectivity principle. Given the minor role of tax shares envisaged here, grants and repayments obviously become more important when it comes to realising causal connectivity.

Grants are financial transfers to national public authorities, which can be either earmarked or non-earmarked. Non-earmarked grants are transfer payments that are granted to the recipients without conditions, i.e., the funds are freely available to them. Earmarked grants, on the other hand, are transfer payments whose use is tied to a more or less narrowly defined purpose. In enacting the recipient’s budget, this distinction is often not quite so strict, if earmarked grants disbursed by central government (partially) replace spending effected at the level of government performing the service, thus giving rise to substitution effects within the decentralised budget, which gains more leeway elsewhere as well. However, even when earmarked grants do not automatically meet the targeted purpose 100 per cent, earmarking naturally creates a right of control over how the public service is executed. In the case of non-earmarked grants, central information and control rights are in place from the outset but must be expressly agreed upon.

Grants can also be subjected to a co-financing obligation, i.e. the national public authorities receive the transfer only on condition that they raise a proportion of the monies themselves. This can be made to be a way of strengthening self-interest in efficient execution. But large co-financing shares quickly result in mixed financing; the reservations expressed above on such models – as well as on the execution connectivity – would apply again here, especially with regard to EPGs.

The size and distribution of grants can be determined in various ways. In principle, there is great flexibility here in either using rough and ready indicators or assessing financial needs with differentiated sets of indicators that better approximate task fulfilment by the individual Member States. The difference can be illustrated using the fictitious example of the EPG “European army”. Here, e.g., the number of inhabitants of a Member State could serve as a rough “umbrella indicator” covering the financial needs in a very general way. A more differentiated set of indicators would additionally take into account, say, land area, border length, coastline, geographical location and distribution of military tasks. A likewise differentiated form of grant is case-based lump sums for European projects that have direct “end customers”, such as students.

Depending on the degree to which such indicator sets or case-based lump sums are differentiated, the transition to expenditure reimbursement does not seem far off. Expenditure reimbursement allows one to pay for specific Member States services in the interest of or on behalf of the EU. In this context, only costs truly incurred are taken into

\textsuperscript{34} Most likely, an approximate match between execution costs and tax share would be achieved if the EPG delegated to the Member States for administration and the, in return, apportioned EU tax were factually related. This would be conceivable, for example, in the context of climate protection – with local climate protection investments that would be refinanced through participation in an EU energy tax. However, such factual correspondences between task and tax are likely to occur only very rarely with most of the still eligible European common goods and potential EU levies.
account. If the motive for expenditure reimbursement persists over a longer period of time, the amount automatically adjusts to the changed needs and cost structures. Even so, cost reimbursement is associated with a high bureaucratic effort into determining, transmitting and controlling the exact billing. As they leave no cost risk with the executing government levels, reimbursement solutions are generally easy to agree upon politically. At the same time, however, they embody the problems of “managing someone else’s money” outlined in Section D almost in pure form: the inefficient use of funds in the case of expenditure reimbursement can be counteracted only with great effort and even then normally only to a limited extent.

Table 2 below summarises for Europe in a condensed form the strengths and weaknesses of the various financing instruments in the relations between higher and lower government levels. Following Thöne (2019), it draws on the broad field of experience that German administrative federalism offers: in addition to the federation-Länder context, the rich experiences from Land-municipalities relations in the thirteen territorial states (Flächenländer) can also be considered, especially for this question.

<table>
<thead>
<tr>
<th>Criteria</th>
<th>Tax share</th>
<th>Grant</th>
<th>Reimbursement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Appropriateness initial size</td>
<td>+</td>
<td>+</td>
<td>+</td>
</tr>
<tr>
<td>Appropriateness initial allocation</td>
<td>-</td>
<td>-</td>
<td>+</td>
</tr>
<tr>
<td>Dynamization of overall size</td>
<td>-</td>
<td>-</td>
<td>+</td>
</tr>
<tr>
<td>Dynamization of allocation</td>
<td>-</td>
<td>-</td>
<td>+</td>
</tr>
<tr>
<td>Central management and control</td>
<td>-</td>
<td>-</td>
<td>+</td>
</tr>
<tr>
<td>Decentral cost effectiveness</td>
<td>+ (1)</td>
<td>+ (1)</td>
<td>+ (2)</td>
</tr>
<tr>
<td>Resilience w.r.t. strategic behaviour</td>
<td>+</td>
<td>+</td>
<td>-</td>
</tr>
<tr>
<td>Political feasibility</td>
<td>-</td>
<td>-</td>
<td>+</td>
</tr>
<tr>
<td>Bureaucratic burden</td>
<td>+</td>
<td>+</td>
<td>-</td>
</tr>
</tbody>
</table>

(1) The incentive for cost effectiveness works exclusively to the advantage of the decentralised level, as the latter creates leeway for itself.
(2) Positive assessment when centralised and decentralised incentives are linked in such a way that efficiency gains are shared.

Source: Own representation following Thöne (2019).

With no space here to derive partial evaluations for all instruments in detail, assessment criteria are characterised in the form of key points:

- **Appropriateness of initial size**: Can, at the outset of vertical financing, a total amount be determined that is necessary to adequately cover the financial needs associated with the task?
Public goods in a federal Europe

- **Appropriateness of initial allocation**: How well can it be established at the outset of vertical financing how the initial amount should be distributed among the individual decentralised units so as to adequately cover the decentralised financial needs associated with the task?
- **Dynamization of overall size**: Can the chosen instrument automatically or relatively easily take into account changes in the overall financial needs over time?
- **Dynamization of allocation**: Can the chosen instrument automatically or relatively easily take into account changes in the decentralised distribution of financial needs over time?
- **Central management and control**: Does the instrument provide a transparent and easily accessible incentive for the central level to manage and control size, allocation and other instrument parameters in accordance with the principles of economic efficiency?
- **Local cost effectiveness**: Does the instrument provide a clear incentive for the decentralised level to execute the vertically financed public good efficiently and economically?
- **Resilience with respect to strategic behaviour**: Is the instrument resilient to strategic behaviour by the decentralised government level?
- **Political feasibility**: Is the instrument politically easy to introduce, given the stakeholders to be involved?
- **How great is the expected bureaucratic burden?**

Summing up, it’s clear that there are many ways in which European tasks carried out by the Member States can be financed at EU level. In the overall picture, the design options of different types of grants stand out. Nevertheless, since no instrument appears to be preferable in all cases, the choice must always be made in the concrete case of a given EPG, depending on the strengths/weaknesses profile of the different ways of transferring funds.

In this regard, the "price for the diligence" of making differentiated design decisions on the financing side of European common goods as well should be kept in view: the planned use of the experience gained from vertically cooperative administrative federalism opens up more and better ways of advancing and deepening European integration via EPGs. In pursuit of this goal, it is worth the effort dealing with the supposedly technical but often eminently political details of various financing methods and giving robust answers to the questions that arise in each individual case.

**E.3. Scenarios for the federal provision of European public goods**

What do the different constellations of federal provision of common goods in the Union look like, if one takes into account the lessons from the theory of fiscal federalism, from the first and second analogy of the present paper and, with that, from experience with vertically cooperative public tasks in a federally organised Member State such as Germany?
To answer this question, we in conclusion present four scenarios of how the EU can provide EPGs in the multi-level system and discuss them in the light of the criteria developed earlier. We illustrate each scenario in a forward-looking way, using a service that would be a good European common good in itself but is not yet or insufficiently provided as such today. In all scenarios, we start from the premise that the central government level will be responsible for the formative political design (legislating for) of all European public goods. Looking further forward, four main scenarios can be imagined, characterised by different allocations of competences (Table 3).

**Table 3: Scenarios for the federal provision of European public goods**

<table>
<thead>
<tr>
<th>Scenarios</th>
<th>Legislation</th>
<th>Administration</th>
<th>Financing</th>
</tr>
</thead>
<tbody>
<tr>
<td>1: Dual Federalism</td>
<td>Central</td>
<td>Central</td>
<td>Central</td>
</tr>
<tr>
<td>2: Central &amp; financed by contributions</td>
<td>Central</td>
<td>Central</td>
<td>Decentralised</td>
</tr>
<tr>
<td>3: Execution connectivity</td>
<td>Central</td>
<td>Decentralised</td>
<td>Decentralised</td>
</tr>
<tr>
<td>4: Causal connectivity</td>
<td>Central</td>
<td>Decentralised</td>
<td>Central</td>
</tr>
</tbody>
</table>

Note: central: EU or a group of Member States; decentralised: Member State.

Source: Own representation.

1. **Dual federalism**: The first scenario assumes that the EU sets up its own administration with which it executes Community law and also finances the resulting expenses. It thus corresponds to the provision of central public services in the US-American-style model of “dual federalism”. According to the basic criteria for allocation of the three competences (see Table 1), this scenario of complete centralisation is conceivable when cross-border spillover effects of legislation go hand in hand with positive economies of scale in administration. Added to this comes the demand for a financing system that reflects solidarity-based burden sharing and is intended to leave the juste retour problem behind.

EU asylum policy can be taken as an example (Berger and Heinemann, 2016). Here, there are clear spatial spillover effects: in view of the EU’s humanitarian obligations towards refugees (Art. 78 TFEU) and the chances for stabilising the situation in crisis-ridden regions, all Member States benefit from the reception of asylum seekers in individual countries that are over-burdened due to their geographical location and current migration flows. This justifies central rules on burden sharing.

Responsibility for asylum procedures is still regulated by the Dublin Regulation, according to which the first Member State an asylum seeker enters is responsible for processing his or her asylum claim. In the face of temporarily large-scale inflows of migrants, some Member States have been overwhelmed with this task. Since they receive comparatively little support from the EU and have to meet only minimum standards when executing the procedures (the Asylum Procedures Directive, the Reception Conditions Directive, the Qualification Directive), from country to country refugees are often treated very differently.

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On this see Gnath et al. (2020), Thöne and Kreuter (2020b) and Callies (2021) [all with further references].
Should administration of the common asylum policy remain in the hands of the Member States? The establishment of a European Asylum Agency (replacing or building on the European Asylum Support Office, EASO), which takes responsibility for the reception of refugees and for enacting asylum procedures in the country of arrival according to uniform standards, would make the fulfillment of European objectives more effective and probably less costly. In addition, European administration would prevent the – otherwise almost unstoppable – unstated race to the bottom in asylum standards across Europe and thus better ensure respect for international human rights standards. To avoid one-sided financial burdens on individual Member States, direct financing by the EU is appropriate.

2. Central & financed by contributions: The second scenario assumes that, besides legislation, the administration of European tasks is taken on by the central government level, while financing lies with the Member States. In the jargon of fiscal federal theory, regionally homogeneous preferences go here hand in hand with positive economies of scale (see Table 1). Decentralised financing via national contributions makes this, otherwise centralised, scenario seem unusual at first glance, and will seldom be compelling in real terms. However, decentralised contributions can have clear advantages where, for issue-driven or political reasons, national financing shares that may well be unequal across Member States help pave the way for EPGs. Moreover, with contribution-based financing, it is easiest to involve non-EU countries in Community tasks and/or to provide public services only for a group of Member States (“EPG-clubs”). In these cases, the central regulation and execution of the tasks would generally take place within a separate European organisation. Finally, contribution-based financing offers a pragmatic interim solution for those public services, where European legislation as well as central administration could well get underway but could precede the own resources system before it has achieved its full efficiency and flexibility. In such cases, scenario 2 is a preliminary stage of scenario 1.

A good example for the second scenario is the promotion of a common defence capability. In the face of conventional and unconventional threats in a latently tense geopolitical landscape, European states have an interest in up-to-date military equipment that’s fit for the future at the same time. A joint project for research and development of innovative military technologies within a European organisation can make it easier for each Member State to maintain their armed forces at a mutually beneficial level. In this way, positive economies of scale can be realised and parallel expenditures avoided while procurement becomes more efficient. As a result, the European pillar in NATO can be strengthened.

Financing via Member State budgets offers possibilities for flexibility. In view of the different strategic interests and threat perceptions of the individual countries, not all of them have to participate in the joint project and participants could, moreover, be given the choice between mandatory and optional elements. Moreover, the contribution-based financing of the joint organisation or some of its projects has opened up an easy way to involve European NATO members outwith the EU. This issue has been particularly salient since Brexit but already relevant as regards Norway, Iceland and certain Balkan states in NATO.
The EU defence initiative PESCO, established in 2017 and comprising by now 46 projects, corresponds to this scenario in many elements. From the perspective of the EPG discussion, these defence initiatives are proper, albeit cautious, steps towards the great common good of an integrated European army (together with navy and air force) in NATO.

3. Execution connectivity: The third scenario envisages the central EU level setting the legal norms for a common good and obliges the Member States to supply adequate administration and financing. The basic criteria suggest this scenario should come into play when regionally homogeneous preferences or cross-border spillover effects go hand in hand with relevant residual differences in one-the-ground conditions in the Member States. Decentralised financing in accordance with execution connectivity links national responsibility for administration with incentives for efficient use of funds.

Preventing future epidemics can serve as a potential example here. The coronavirus pandemic has made this task a priority. As an area with open borders and a vibrant exchange of people and goods, the EU is vulnerable to the rapid spread of infectious diseases and the emergence of pandemics. Uniform standards are therefore needed for the early detection of risks, for the capacity of health care systems (material, equipment and personnel), for logistical structures and for binding action plans in the event of an outbreak.

The health care system in Europe today is organised in complex national structures, which differ greatly one from the other and draw on decades of varied experience. From this, it follows that European norms for pandemic prevention are probably best executed nationally. Funding, which can be made available directly by the respective Member State or indirectly by its citizens or their insurance companies, should remain decentralised, given that Member State health care systems are built around very different organisational and cost structures.

4. Causal connectivity: In the final scenario, the central government level enacts legal norms, delegates (or leaves) their administration to the Member States but assumes the financial burdens associated with decentralised administration. According to the basic criteria (see Table 1), this scenario is conceivable when spillover effects or Europe-wide homogeneous preferences go hand in hand with different conditions for legal implementation within the Member States. Such a constellation corresponds to the third scenario; however, financing by the central European level in accordance with causal connectivity places a clear emphasis on solidarity-based burden sharing in the EU. By financing EPGs from the EU budget, the commitment to make Europe stronger and, in essence, more "European" through genuine European common goods becomes more evident.

The fourth scenario can be exemplified by a European programme to finance short-time working in the event of large exogenous shocks. Such a programme would help to maintain production capacities in the affected countries, alleviate the burden on national unemployment insurance schemes and buttress the incomes of private households. This would mitigate any downturn in individual economies, which would inevitably have negative effects on other countries within the European single market. The central regulation
of financial support for short-time work as part of collective crisis management therefore meets the interest of each Member State in macroeconomic stability.\footnote{The macroeconomic argument reflects the proposals for a European unemployment (re-)insurance scheme. See e.g. European Commission (2013); Dolls (2018).}

The need to lodge and manage claims locally, as well as the wide range of existing national organisational forms, argue for the decentralised execution of such a programme. Since each country could be hit by exogenous shocks and may be unable to cope with the ensuing burdens on its own, mutual protection through solidarity-based financing by the Community is appropriate. For this purpose, in addition to payments from the current EU budget, joint debt instruments can also be considered, especially in prolonged, far-reaching crises.

Along these lines, on 2 April 2020, the EU Commission launched a temporary initiative to protect jobs and workers in times of coronavirus – the “Support Mitigating Unemployment Risks in Emergency” (SURE). In view of the unpredictable crises that Member States may always be confronted with, setting up a system that works permanently and is financially secured on a broader basis acquires a greater salience.

The four scenarios outlined above represent prototypical constellations. They cover a broad spectrum of federally organised European public goods. However, the criteria for centralised or decentralised allocation of legislative, administrative and financing competences in the provision of EPGs (Section E.1), as well as ways we have discussed to design central financing (section E.2), will not always provide clear-cut, undisputed indications. Therefore, scenarios cannot be ruled out in which overlaps arise in the form of framework legislation, co-administration or mixed financing. Mixed solutions within partial competences are never without problems, because such intensive policy entanglements can quickly lead to an organised loss of responsibility – the proverbial “too many cooks spoil the broth”.

Nevertheless, even in such constellations, the advantages and disadvantages, the opportunities and risks, of the possible options for allocating competences will have to be assessed in the specific case of each planned European common good. Often enough, the effort of fine-tuning the federal design will pay off, because European integration can thus be advanced with the individually best-suited organisational form for a Community public good. But there will also be cases where it becomes clear that the hoped-for European added value of a common good cannot be realised in the federal praxis of the EU. In these cases the criteria outlined above and experiences gained from the fulfilment of tasks in the federal state will be of help. After all, they apply equally to centralised and decentralised public goods.
F. Conclusion

Our analysis "Public goods in a federal Europe" started by purporting to look at the current EU as a federal state – where the Union assumes the role of the central government and the 27 Member States the role of its constituent parts. We are not saying that the EU is a federal state. It is not. Whether it ever will be is another story.

There are good reasons to strengthen the EU of the 21st century internally and externally and to expand its sovereignty. The path to this goal requires the EU to take on more of the tasks to which it can lay claim by virtue of its size and function. Europe should become stronger and more sovereign through the provision of more and better European public goods. Europe should become more European. This can hardly succeed without further developing the Union in the direction of a federal state with a central level of governance given the means to act.

European strength and sovereignty, European common goods and European federalism are thus closely intertwined. With this in mind, the present paper examines the federal dimensions of Europe and its potential strengthening through more EPGs, by shedding light on different aspects of the European multi-level system. We look at some elements of European federalism from a greater distance in order to better identify its basic structures. Other aspects, on the other hand, which are particularly salient from a fiscal-federal perspective or in need of innovative treatment, are closely scrutinised. They are examined in detail to find out how they work and where things go wrong.

We have structured this interplay of bird’s-eye and frog’s-eye perspectives using two central analogies, both formulated with some distance. On the basis of the two analogies, we put forward the thesis that the undoubtedly unique European Union is confronted in its further development with problems and tasks that are anything but singular. In contrast, peering too closely, the expert's view of the federal unicum EU alone, obstructs such perspectives.

In the first analogy, we view the Union, its intergovernmental and supranational governance models, as a co-existence of confederation and federal state. In the second analogy, we place the multi-level system of the EU beside a federal state following the example of German cooperative federalism. Germany is not a role model here, but rather a reservoir of federal problems and solutions. With both analogies, our interest always lies in the question of how and with which instruments European integration can be deepened – primarily through European public goods. But the options for further development of the EU via the fiscal side that are emerging with NextGenerationEU are also considered.

The conclusion cannot and should not summarise the study. Instead, it draws together and highlights the insights that seem important to us at the end – regardless of whether they are central findings of the reflections or observations along the way:

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37 This distance is motivated not least by the perspective and experience of the authors after (for one of them) a quarter of a century of research and policy advice on fiscal federal issues at all levels – from individual municipalities, through regions and federated states, to nation states and supranational bodies, such as the EU and the WTO.
• A strong and sovereign Europe must be able to act more decisively and in a more European manner. In addition to taking on the right tasks – among others, EPGs – this requires also an appropriate governance structure. In many policy areas (but not all), deepening integration will come up against the limits of the European treaties. Even the fundamentally federal onward development of the EU, for which the instruments have been outlined here, can by and large be consistently progressed by treaty amendments alone. Politically, treaty amendments are often considered a big taboo. But as gruelling as they may be, sooner or later the EU will revise its treaties. Better sooner – there is much to be gained.

• However, public goods in a federal Europe should not necessarily have to wait for treaty changes, because European citizens and firms cannot wait for enhanced performance in a dynamic and multipolar world. Thus, where treaty hurdles and/or veto players block timely progress under the unanimity rule, the possibilities for “EPG clubs” in or outside the treaties should be aggressively developed, so that the (more often than not extended) coalitions of the willing can readily move forward.

• The criteria for the federal allocation of competences presented in this paper can be best applied in their entirety to the full EU-27 with the European Parliament and using the EU budget. Nevertheless, most of the criteria are equally applicable to selective integration in the form of club solutions inter alia.

• The characterisation of the supranational system as a federal state and of the intergovernmental system as a confederation of states makes it clear that new European common goods, by their nature, fit better into the supranational system, but can be introduced more realistically – precisely as club solutions – in the intergovernmental system. This “federal paradox” is not insurmountable but must always be borne in mind in the process of further European integration.

• In the transition of new European common goods to the “federal-state-like” supranational system, the particular challenge of a suitable democratic governance for selective integration arises.

• The consideration of vertical cooperation and related connectivity issues will lead to the conclusion for many EPGs that the primary legislative and financing competences should lie with the EU, while administrative competence should rest with the Member States. Except for the financing competence, this pattern is quite similar to the division of competences that already characterises the provision of many European public goods by the EU today. The central financing of EPGs executed locally in accordance with causal connectivity is still quite new within federal practice and in this respect innovative. From the outset, it avoids the misguided incentives to pursue a policy at the expense of the Member States, incentives that arise with decentralised financing in the traditional (German) model of administrative federalism.

• With respect to the central European financing of such EPGs, which the Member States administer locally, we have developed a criteria-based grid of different models for the transfer of funds. Surprisingly at first glance, but very plausibly on closer
inspection, traditional grants often turn out to be the most suitable instrument for innovative central funding.

- Central financing requires more and possibly new revenues at European level. This would actually be a "different issue", as the optimal raising of funds follows different criteria than the fiscal issues on the expenditure side of EU finances that are central to our analysis. The innovations in terms of EU taxes and EU debt launched by the NextGenerationEU package – albeit still to be concretised – open up additional possibilities here that would hardly have arisen without the great coronavirus crisis as an un-wished-for catalyst for European progress.

- In view of this resurgent debate on the future financing of the EU, we discuss – as part of the description of the supranational governance model – the long-standing and contentious issue of juste retour, i.e. the Member States’ attitude of always attempting to claw back in receipts/rebates as many of their contributions as possible. Far from being a special problem of fiscal policy, juste retour symbolically and at the same time factually embodies one of the central hurdles that still distinguishes the supranational system of the EU from the "normal" upper level of a federal state. Ultimately, juste retour is so relevant because it occurs on both the expenditure and revenue sides. It will therefore only be solved consistently if key revenue instruments politically assigned to the EU are used to finance services with a visible European added value – i.e., genuine European common goods.

- Finally, we outline four different scenarios for the federal provision of EPGs in Europe. These scenarios represent prototypical constellations. They cover a broad spectrum of federally organised European common goods. In this way, our study’s approach of viewing Europe as a federal state actually contributes to strengthening the EU through more and better EPGs, insofar as "dual federal" solutions of complete centralisation alone are no longer considered. The reservation on European common goods, according to which it would hardly ever be possible in practice to centralise everything of a public task at European level, is – as the whole paper has shown – very often true. But this reservation is not a defensive argument. On the contrary, it is a design mandate.

The responsibility for this design mandate does not lie with science alone. The coronavirus pandemic has postponed, but not cancelled, the start of the Conference on the Future of Europe. An upcoming conference on that theme will look very different from the one originally planned. It will reflect the experience of the coronavirus pandemic. It will take into account the shameful failure of European solidarity at the beginning of the pandemic as well as the –unexpected for some – strength and unity in the further course of the crisis (and in the parallel conclusion of the Brexit negotiations). From both sets of experience, good and bad, the lesson for Europe is that its future is crucially linked to its strength and its unity.

Such unity is easy to demand, but difficult to achieve. In Europe, whose diversity is its main strength and also its pride, there is only one path to unity: a strong, fair and, moreover, efficient European federalism. The present paper attempts to contribute to mapping this.
References


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