The Increased Use and Impact of Enhanced Cooperation in the EU via the Introduction of a Financial Transaction Tax

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Abstract

Member States face continuing challenges in the current economic climate with budget deficits pressurising national treasuries, leading to implementation of austerity measures. This has led to tense recent EU budget negotiations. The current financial crisis does, however present some opportunities for the future. This paper will focus on one of these opportunities and its effect on the future workings of the EU – Adoption of a Financial Transaction Tax (FTT) by the European Commission, viewed as part of a three pronged reform of financing of the EU. The proposal does not face unanimous support and the Enhanced Cooperation mechanism in the treaties has been used. Through assessing the legislative developments for the FTT and two previous instances of Enhanced Cooperation this paper's primary focus will be explaining and assessing the increasing use of Enhanced Cooperation on the European integration project.

There is a belief that the financial sector has been under-taxed and that now it should contribute back to repaying the costs of the current crisis. Many alternatives have been discussed. This paper will explain why the financial sector is in a special position and ripe for reform. Following this the economic background and rationale for adopting such a tax (in brief) and the differences between the terms 'Tobin Tax', 'Robin Hood Tax' and an FTT will be discussed. Therefore the adoption of the Commission's FTT through Enhanced Cooperation acts as a lens to assessing the present and potential future impact of the increasing use of Enhanced Cooperation.

Introduction

The effects of the global financial crisis of 2008 continue to be felt at the time of writing. There has been widespread reporting of the apparent causes and effects of the current crisis with the majority of focus being placed upon the financial sector as a whole, a process of *'bank bashing'*[1]. The full details of the 2008 crisis have been written about in far greater depth elsewhere, yet it is necessary to illustrate the effects for this paper in order to contextualise the actions of politicians and the legislature. There have been many high profile examples of banks failing (e.g. Lehman Bros[2], BNP Paribas[3] and Northern Rock[4]), allegations of criminal activity (e.g. the conduct of Sir Fred Goodwin during his tenure at RBS[5]) and occasions when governments have leapt to the rescue to bail out in one way or another[6] (ranging from facilitating mergers to full scale recapitalisation) failed/failing financial institutions at great cost to the tax payer. Since these bail outs have occurred further evidence of malpractice has come to light, e.g. the LIBOR rate fixing scandal. These

[1] H Lethaby, 'Tax and the City – Financial Transaction Tax' (2011) 1097 Tax Journal 11
[2] N Dorn, 'Lehman – Lemon: "Too Connected to Fail" as a Policy Construct' (2012) 6(4) Law & Financial Markets Review 271
[3] J Goddard, P Molyneux and J Wilson, 'The Financial Crisis in Europe: Evolution, Policy Responses and Lessons for the Future' (2009) 17(4) Journal of Financial Regulation and Compliance 362
[4] D Llewellyn, 'The Northern Rock Crisis: A Multi-Dimensional Problem Waiting to Happen' (2008) 16(1) Journal of Financial Regulation and Compliance 35
[5] For example see D Kirk, 'Criminalising Bad Bankers' (2012) 76(6) Journal of Criminal Law 439
[6] L Dragomir, *European Prudential Banking Regulation and Supervision. The Legal Dimension* (Routledge, 2010 London) 10

allegations were not merely isolated to banks; other financial institutions such as insurance broker firms have also been implicated[7].

The decision to bail out the financial sector was taken by governments at a cost to the taxpayer. Taxpayers also constitute the electorate and therefore there is greater emphasis than ever on justifying to the electorate how their money was spent on an under-regulated sector which (as the *'Occupy LSX'* and *'Occupy Wall Street'* movements show) is perceived as having been offered a *'get out of jail free card*' at the expense of more socially desirable government projects, such as forming part of the health or education budget.

Although the financial crisis was truly global in nature Europe in particular has come under the microscope. Allied with the money spent on bailing out the financial sector are national government debt and the ongoing euro crisis. Although it is arguable that the financial sector in isolation did not cause the crisis it is widely perceived that it at least contributed to the scale. There has been a clear return to austerity governance and hostility against those perceived as cheating the public purse via legally permissible tax avoidance ranging from global corporations (such as Amazon and Google) to high profile celebrities (such as Jimmy Carr)[8]. In the UK pressure has even been put on wealthy pensioners to voluntarily return universal non-means tested benefits such as their Winter Fuel Allowance and free TV Licences provided by the public purse[9].

Austerity however can at times be the catalyst for innovation and solutions are being sought to not only cover the cost of the 2008 crisis but to prevent such an event from ever occurring again (or at least reducing the potential scale). In order for a solution to be truly effective it must be applied across a wide area. The European Union (EU) allows member states (MS) the required platform to address the solution. This paper assesses the controversial measures and developments the European Commission has sought to pursue in attempting to appease the electorate by seeking an effective means of reclaiming the cost of the financial crisis – the Financial Transaction Tax (FTT), its underlying rationale (section I(A)), the legal problem it faces (section I(B)) and the use of Enhanced Cooperation to overcome the problem (in section II(A)). As outlined in the Commission's 2011 Proposal for a Council Decision on the System of Own Resources[10] the FTT forms part of a three pronged approach (along with simplification of MS contributions and the reform of correction mechanisms) to reforming the funding of the EU.

Although this paper is concerned with the adoption of the Commission's FTT Proposal the main purpose is to use this as a lens through which to consider the increasing use of the Enhanced Cooperation procedure in the Treaties. This will require consideration of other uses of Enhanced Cooperation (in section II(B)). This is a procedure which is being used increasingly to overcome legislative stalemates and its impact is the primary quandary of this paper. The conclusion will consider the development of the legislative procedure, how effective the use of this procedure has been thus far and its overall effect on the European integration process if it continues to be used.

<u>i – Commission's FTT Proposal Outline</u>

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[7] B Masters, 'Watchdog Investigates ICAP Over Libor Fixing' *The Financial Times* (London January 24 2013) 1

[8] For example D Bailey, 'A Moral Duty' (2012) 142(Dec) Trusts and Estates Law and Tax Journal 2 See also P Sukhraj, 'At the Sharp End' (2012) 148(1428) Accountancy 18 and T Gregory, 'Tax Avoidance and Morality' (2012) 1129 Tax Journal 8

[9] BBC News, 'Ed Balls: Labour Would Axe Wealthy Pensioners' Fuel Cash' <http://www.bbc.co.uk/news/business-22748914> Accessed 10 June 2013

[10] Commission Proposal for a Council Decision on the system of own resources of the European Union of 29 June 2011 (COM(2011) 510

Following public consultation the Commission's *'Proposal for a Common System of Financial Transaction Tax'* was published 28th September 2011. In short the Commission's FTT is a Proposal for a tax to be levied upon financial transactions to raise revenue for other causes. The Commission's Proposal would apply from 2014 to financial transactions which take place when at least one of the parties is situated in the EU[11] as based on the residence principle. The proposed minimum rates are 0.01% for derivatives and 0.1% for other financial transactions (i.e. acquisition of shares and bonds), although a MS may tax at a higher rate if desired. Some transactions are excluded in the Proposal. These include private household consumer transactions (such as mortgages), transactions on primary markets both for securities (shares and bonds) from taxation so as to not undermine the raising of capital by governments and companies and transactions between National Central Banks and the ECB. The tax would be payable at the moment the transaction takes place (which in the modern day in simple to establish). Revenue is collected by the national tax authority in which the party is based[12]. The treasury can then use the money for other causes, such as reducing national budget deficits or contributing towards the national treasury's EU budget contribution. As an example, suppose a Spanish bank and a Finnish Pension fund enter into a derivative agreement in the City of London. The Finnish pension fund would pay the tax to the Finnish tax authority and the Spanish bank would pay the tax to the Spanish tax authority[13].

The tax has developed from the field of macroeconomics, in particular Keynesian macroeconomics. Macroeconomics is *"The branch of economics that deals with large-scale economic factors; the economics of a national economy as a whole"*[14]. Macroeconomists generally utilise a variety of indicators (GDP, rates of unemployment and price indices) in order to establish the overall functioning of an economy as opposed to microeconomics which focuses on individual aspects of the economy. Macroeconomists have two primary objectives. These are firstly, to explain short term fluctuations in national income both in terms of the cause and effect and secondly to attempt to attain long term, stable economic growth. Although there are different fields of macroeconomic theory, broadly it can be stated that macroeconomists seek to achieve these two particular objectives by proposing theories in order to explain previous recession or growth and to apply these theories within the current economic context. This facilitates forecasting of future economic prospects so that appropriate measures may be taken to achieve these aims. These policies were pursued with great success following the Great Depression of the 1930s but declined in popularity during the 1970s. Many authors (for example Krugman[15]) argue that the economic conditions post 2008 replicate those of the Great Depression and that macroeconomic policies should therefore be revived and pursued by governments.

It is important to note that although they are variations of a form of an FTT the Commission's FTT is not synonymous with the *'Tobin tax'* or the *'Robin Hood Tax'* (as is often reported in the mainstream media[16]) in the same manner in which legally the terms *'state'* and *'country'*

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[11] A Goodall, 'Financial Transaction Tax: A Step Forward or a Blunderbuss?' (2012) 1095 Tax Journal 7
[12] Europa, 'Taxation of the Financial Sector' <http://ec.europa.eu/taxation_customs/taxation/other_taxes/financial_sector/index_en.htm> Accessed 9 May 2013
[13] Per Manfred Bergmann Director for Indirect Taxation and Tax Administration. Europa, 'Taxation of the Financial Sector' <http://ec.europa.eu/taxation_customs/taxation/other_taxes/financial_sector/index_en.htm> Accessed 9 May 2013
[14] Oxford English Dictionary Online, 'Macroeconomics' <http://www.oed.com/view/Entry/111940?redirectedFrom=macroeconomics#footerWrapper> Accessed 17 February 2013
[15] P Krugman, *The Return of Depression Economics and the Crisis of 2008* (Penguin, London 2008)
[16] For example see BBC News, 'Q&A: What is the Tobin Tax on Financial Trading?' <http://www.bbc.co.uk/news/business-15552412> Accessed 10 June 2013

are not synonyms (i.e. at present Wales is a country but not a state. It forms part of the UK, which is a state. The UK therefore enjoys full legal personality in international law but Wales itself does not). This is due to differing degrees of scale, rationale and intention. For example, the *'Tobin tax'* was designed specifically to curb speculative short term conversions in currency transactions. For James Tobin, the proponent of this tax, the rates of taxation and function of revenue levied by the tax were of secondary importance. Subsequently the Tobin tax was politicised and *'hijacked'*[17] by groups (such as *'ATTAC'* in France[18] and the *'Robin Hood Tax Campaign'* in the UK[19]) seeking wide scale taxation on every transaction in order to raise revenue for philanthropic causes (for example providing vaccination programmes in the third world). As will be discussed in the next section the Commission's FTT has a more limited scope than the Robin Hood Tax, but is wider than Tobin's currency conversion tax proposal.

At present the FTT Proposal in its original form has not been introduced. Therefore, in addition this paper will also explain the reasons why the Commission's FTT Proposal is controversial and the subsequent legal problem the Commission's Proposal faces. A partial solution has been found with the use of the Enhanced Cooperation procedures contained in the both the Treaty on the Functioning of the European Union (TFEU) and Treaty on European Union (TEU).

I – Competing Arguments and Legal Basis

One of the interesting aspects about the Commission's Proposal is that there many different methodological approaches that can be taken to explain why it should or should not be introduced. For example, an economist would examine the economic rationale for introducing a tax. A political scientist would look at the political interaction between the Commission, MS and the affected institutions. This paper is predominantly legal in nature as will be illustrated by section I(B), however it is necessary to be aware of and give credence to these other competing interests.

A – Arguments for/against Introduction of the FTT

As has been outlined in the introduction the financial sector is under pressure to reform to prevent future crises. Since reform of the financial sector is such a hot topic the initial question to be asked is why the financial sector is so important? The answer is that the financial sector is *'special'* in nature and therefore requires specific legislation and regulation in the same way in which the medical sector requires specific regulation. Further insight into the financial sector's special nature can be gleaned from two theories.

i – Special Nature of the Financial Sector

The first of these theories is the *'financial intermediation theory'*. This theory explains that in order to attain an efficient and effective financial system five tasks must be fulfilled, namely:

· Enabling and guaranteeing the operation of the payments system.
· Facilitating the allocation and transfer of resources over time between sectors/geographical areas.

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[17] Jubilee (Originally in Der Spiegel 3 September 2001) 'James Tobin : "The Anti-Globalisation Movement has Hijacked my Name"' <http://web.archive.org/web/20050306201839/http://www.jubilee2000uk.org/worldnews/lamerica/james_tobin_030901_english.htm> Accessed 29 December 2012

[18] ATTAC, 'About ATTAC – Overview' <http://www.attac.org/en/overview> Accessed 29 December 2012

[19] The Robin Hood Tax, 'Everything You Need to Know' <http://robinhoodtax.org.uk/how-it-works/everything-you-need-to-know> Accessed 13 January 2013

· Proffering a system of guarantees reducing uncertainty regarding the true value of money.
· Issuing financial products (debt or capital) in order to invest.
· Providing information on the price of financial assets.

Financial institutions collectively work to ensure these five tasks are met. In addition the theory advocates that financial institutions act as intermediaries, ensuring one particular financial asset is transformed and becomes another financial asset. The theory can be sub-divided into an *'institutional approach'* (favouring evaluation of the institutions that form financial markets) or a *'functional approach'* (which focuses on the ensuing functions that wider society expects from both the financial system but also financial intermediaries).

A second theoretical approach is economic theory. This theory focuses on banks in particular (as opposed to the financial sector as a whole) and has developed over time. Pre-1980 theories *"assume the existence of banks in the economy and apply standard micro-economic theory to explain the transformation and consolidation of risks, as well as the broker function performed by banks"*[20] whereas post-1980 theories focus on how market imperfections have caused banks to exist and the resulting functions. The consequences of these imperfections provide three reasons as to why the financial sector, banks in particular, should be considered special.

Firstly, financial institutions are privy to masses of private information through their customer dealings, putting them at a competitive advantage but at a cost of keeping the information confidential. Effectively the profitability of financial institutions depends upon how effectively this information is utilised. Secondly, banks take deposits and lend. Dragomir states that *"The distinctive feature of banks stems primarily from their role in transforming liquid short-term liabilities (deposits that can be easily withdrawn) into illiquid long-term assets (commercial loans for which traditionally there is no market for liquid assets."*[21] If deposits can be easily withdrawn this can hinder a bank's ability to convert deposits into assets, leading to a run on the bank. The final reason given is that banks incur special risks, these risks being different from other financial intermediaries, in particular *'contagion'* – that systemic problems in one bank may spread to another in the same system whether founded in reality (the *'real channel'*) or founded in rumour (the '*information channel'*).

ii – Proponents' and Detractors' Arguments

There is genuine concern that the Commission has made an error in pursuing their proposed FTT. The primary concern is the Commission's admission in the Proposal itself that in spite of mitigating factors the EU would face a minimum of a 0.5% shrink in GDP, making it as a collective less competitive relative to other established and developing markets at a time when the priority should be increasing competitiveness. This 0.5% decrease is teamed with real fear of an exodus of financial services. Whilst commercial high street banking activities may remain within the EU the investment arm of financial services may relocate since the combination of both the volume and the value of transactions means that although the proposed rates seem small relocation to a developing market, such as Dubai is preferable to reduce costs. As a consequence of relocation jobs in the European financial sector will be lost which could place a higher burden on the welfare budget which in turn could be detrimental to the national treasury.

The case often cited by detractors is the experience of Sweden in the 1980s. Sweden introduced a variant of an FTT which had differing characteristics relative to the

[20] L Dragomir, *European Prudential Banking Regulation and Supervision. The Legal Dimension* (Routledge, 2010 London 15
[21] L Dragomir, *European Prudential Banking Regulation and Supervision. The Legal Dimension* (Routledge, 2010 London 18

Commission's proposed FTT, however the tax was repealed following the exodus of financial services. Nowhere is this argument more hotly contested than in the UK in the City of London, the financial powerhouse of the EU (although it must be noted that the other major EU financial sector, Frankfurt is in favour of the FTT). According to the British Bankers Association four in every five transactions which occur in the EU takes place in the City of London[22]. Furthermore it is the UK's single biggest export earner[23]. Therefore, this has been described by some as a tax on the City of London[24].

However, not every party opposed to the Commission's FTT Proposal is opposed to taxation of the financial sector in some manner. There are other potential methods which have positives relative to the Commission's FTT. These include the Financial Activity Tax (FAT) (which is a tax on wealth rather than individual transactions) and the Financial Crisis Responsibility Fee, a punitive levy of a fixed sum placed directly onto financial institutions (as opposed to the FTT and FAT which are proportional based on a financial institution's activities). The issue was discussed in June 2010 at the G-20 meeting in Toronto. The resultant leaders' declaration stated that:

"We agreed the financial sector should make a fair and substantial contribution towards paying for any burdens associated with government interventions, where they occur, to repair the financial system or fund resolution, and reduce risks from the financial system. We recognized that there are a range of policy approaches to this end. Some countries are pursuing a financial levy. Other countries are pursuing different approaches."[25]

The institutions of the EU have been staunch advocates of an FTT. Prior to the G-20 Toronto meeting the Belgian Presidency of the European Council indicated the EU would pursue taxation of the financial sector, advocating that the EU should effectively act as trendsetters:

"[T]he EU should lead efforts to set a global approach for introducing systems for levies and taxes on financial institutions with a view to maintaining a world-wide level playing field and will strongly defend this position with its G-20 partners. The introduction of a global financial transaction tax should be explored and developed further in that context.[26]*"*

However, since then the rhetoric from the EU has gone far greater. In a speech to the European Parliament on the same day that the Commission's FTT Proposal was published the President of the European Commission, José Manuel Barroso stated that *"In the last three years, Member States - I should say taxpayers - have granted aid and provided guarantees of € 4.6 trillion to the financial sector. It is time for the financial sector to make a contribution back to society."*[27] This echoes the sentiment expressed in the introduction that the financial sector should not have a *'get out of jail free card*'.

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[22] A Goodall, 'Financial Transaction Tax: A Step Forward or a Blunderbuss?' (2012) 1095 Tax Journal 7
[23] BBC News, 'Financial Transaction Tax 'Would Kill City of London'' <http://www.bbc.co.uk/news/business-16990025> Accessed 1 March 2012
[24] Ibid
[25] Available to download in Microsoft Word format from G-20, 'Official Materials' <http://www.g20.org/documents/> Accessed 20 February 2013. Also available to view at The White House, 'G-20 Toronto Summit Declaration' <http://www.whitehouse.gov/the-press-office/g-20-toronto-summit-declaration> Accessed 20 February 2013
[26] Europa, 'Conseil Européen – Bruxelles 17 Juin 2010 Conclusions de la Présidence' <http://europa.eu/rapid/press-release_DOC-10-2_en.htm> Accessed 20 February 2013
[27] Europa, '*José Manuel Durão Barroso President of the European Commission European Renewal – State of the Union Address 2011 European Parliament Strasbourg, 28 September 2011'* <http://europa.eu/rapid/press-release_SPEECH-11-607_en.htm> Accessed 19 February 2013. See also A Goodall, 'Financial Transaction Tax: A Step Forward or a Blunderbuss?' (2012) 1095 Tax Journal 7

The argument is that the Commission's proposed FTT would contribute directly to the public purse. Assessing the design of the collection of the tax the FTT is payable to the national treasury, not directly to Brussels. This means that the MS in question can use the money levied by the tax for the purposes for which it sees fit, for example contributing to the EU budget or repayment of national budget deficits. Therefore there is an argument that the greater number of transactions which take place within a particular MS (i.e. the UK), the more that MS could in fact benefit from the tax. This can be contrasted with the collection method for the *'fiscal federalism'* model in Germany[28] whereby tax is collected within the different regions and passed on to central government who reallocate the tax evenly. This system works well for the redevelopment of the regions of the formerly named East Germany, but in effect means that regions with larger populations, generating a larger amount in effect lose out overall and subsidise the redevelopment.

A further argument in favour of such a tax is that it is overdue. ATTAC (a group based in France which advocates wholesale reform of the financial sector) were formed in 1998 and have been lobbying for the introduction of a variation of an FTT (albeit in a much wider form than the Commission's FTT). But in addition the transactions of the majority of the financial sector have not been subject to VAT. This is because in the EU most income is margin based, making VAT calculations for the financial sector extremely difficult.

Of course perhaps the best manner by which to establish the Commission's rationale is to examine the Proposal itself. The Proposal states that an FTT at Union level is necessary in order:

"– to avoid fragmentation in the internal market for financial services, bearing in mind the increasing number of uncoordinated national tax measures being put in place;
– to ensure that financial institutions make a fair contribution to covering the costs of the recent crisis and to ensure a level playing field with other sectors from a taxation point of view;
– to create appropriate disincentives for transactions that do not enhance the efficiency of financial markets thereby complementing regulatory measures aimed at avoiding future crises."[29]

Therefore in addition to echoing the sentiments of President Barroso the Proposal seeks to ensure the *'efficiency'* of transactions in the long term. This is an idea not present in either the '*Tobin Tax'* or the '*Robin Hood Tax'*. The Proposal also seeks to allay fears with regards to relocation, stating that the combination of exemptions and the proposed rates of 0.1% and 0.01% for derivatives (since the instances in which a derivative agreement is liable to pay the tax are more numerous) are correct to mitigate relocation of financial services. Finally one of the benefits of an FTT relative to other methods is that it supports the *'polluter pays'* principle, i.e. the institutions which complete the most transactions will therefore contribute the most back.

There is also a more neutral position which is the introduction of an FTT subject to further conditions. For example, one of the constant criticisms of any form of FTT even dating back to the '*Tobin tax'* is that in order to be truly effective it must be applicable globally otherwise it is easy to avoid. In the composition of the G-20 only four EU MS (France, Germany, Italy and the UK) are members in their own right. The remaining 23 EU MS are represented by the EU being the 20th member of the G-20. This leaves a great scope for the other 15 MS of

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[28] K Albrecht, 'An Economic Analysis of the Fiscal Policy Framework in the EMU' 1(2) (2012) UCL Journal of Law and Jurisprudence 80 See Also P De Grauwe, *Economics of Monetary Union* (OUP, Oxford 2009)
[29] Proposal for a Council Directive on a Common System of Financial Transaction Tax and Amending Directive 2008/7/EC Com (2011 594 Final) of the 28th September 2011

the G-20 to exploit their dominant position. Technically the UK government's official approach is neutral, however this is debateable.

B – Subsequent Legal Problem

Looking beyond the economic merits as to whether or not the Commission's FTT is viable the Proposal faces a particular problem – the appropriate legal basis for introduction. There have been previous instances in which a measure has been challenged either by a MS (as shown by the *Tobacco Advertising*[30] cases) or by private actors[31]. Using the *lex generalis* measures in the TFEU, Article 114 TFEU allows for Qualified Majority Voting (QMV) to adopt legislation. However, Article 114(2) TFEU expressly excludes fiscal matters, making this article null and void in the context of the FTT. Article 115 TFEU requires unanimity for other measures of Treaty competence. This in theory could work, however at present unanimity cannot be achieved. Article 352 TFEU allows for measures not previously included within the Treaty competence to be adopted but by unanimity.

Article 352 TFEU is also inapplicable in this scenario since there is a provision already in the treaties, namely Article 113 TFEU. This is a *lex specialis* provision for the introduction of *'indirect taxation'*. The classic example of an indirect tax is VAT[32]. However, again this requires unanimity. Article 113 TFEU states:

*"The Council shall, acting **unanimously** in accordance with a special legislative procedure and after consulting the European Parliament and the Economic and Social Committee, adopt provisions for the harmonisation of legislation concerning turnover taxes, excise duties and other forms of indirect taxation to the extent that such harmonisation is necessary to ensure the establishment and the functioning of the internal market and to avoid distortion of competition."*

Some MS have taken steps to show their support for introducing an FTT. Former French President Nicolas Sarkozy and German Chancellor Angela Merkel actively supported a union-wide FTT with President Sarkozy stating that:

«Les ministres des Finances allemand et français déposeront sur la table des instances européennes une proposition commune, dès le mois de septembre prochain, de taxe sur les transactions financières»[33]

"The German and French finance ministers will present to the European Institutions a joint proposal for a tax on financial transactions from next September."

President Sarkozy adopted a variation of an FTT, imposing a tax on share transactions akin to Stamp Duty in the UK prior to the 2012 election[34] in order to come into effect on the 1st

[30] Case C-376/98 *Germany v Parliament and Council* [2000] ECR I-8419, Case C-380/03 *Germany v Parliament and Council* [2006] ECR I-11573
[31] Case C-58/08 *R (on the application of Vodaphone) v Secretary of State for BERR* (Judgment 8 June 2010), Case C-66/04 *United Kingdom v Parliament and Council (Smoke Flavouring')* [2005] ECR I-10553
[32] For example see D Butler, 'Case Comment – VAT as a Tax on Consumption: Some Thoughts on the Recent Judgment in Parker Hale Ltd v Customs and Excise Commissioners' (2000) British Tax Review 545
[33] As Reported in Le Figaro, *'Sarkozy et Merkel Veulent un Gouvernement Pour L'Europe'* <http://www.lefigaro.fr/conjoncture/2011/08/16/04016-20110816ARTFIG00420-sarkozy-et-merkel-veulent-un-gouvernement-pour-l-europe.php> Accessed 28 January 2013
[34] S Shaheen, 'Comment: France's Decision To Unilaterally Tax Financial Transactions Is a Risk But One Worth Taking' <http://www.internationaltaxreview.com/Article/2969713/COMMENT-Frances-decision-to-unilaterally-tax-financial-transactions-is-a-risk-but-one-worth-taking.html> Accessed 1 March 2012 see also BBC News, 'Business Bites: Sarkozy Confirms Financial Transaction Tax' <http://www.bbc.co.uk/news/business-16795369> Accessed 1 March 2012

August 2012[35]. The rhetoric from President Sarkozy was to *“provoquer un choc, montrer l’exemple”*[36] (*“to provoke a shock, to set an example”*[37]), echoing the Union’s approach from the Toronto G-20 preparations. However, conversely some MS are fundamentally opposed. In order to garner an understanding of the overall support of MS the following map illustrates the level of MS support calculated in January 2012 by KPMG with those fundamentally opposed (Bulgaria, Czech Republic and Sweden) in red, more neutral states in orange/yellow and those MS firmly in favour in green.

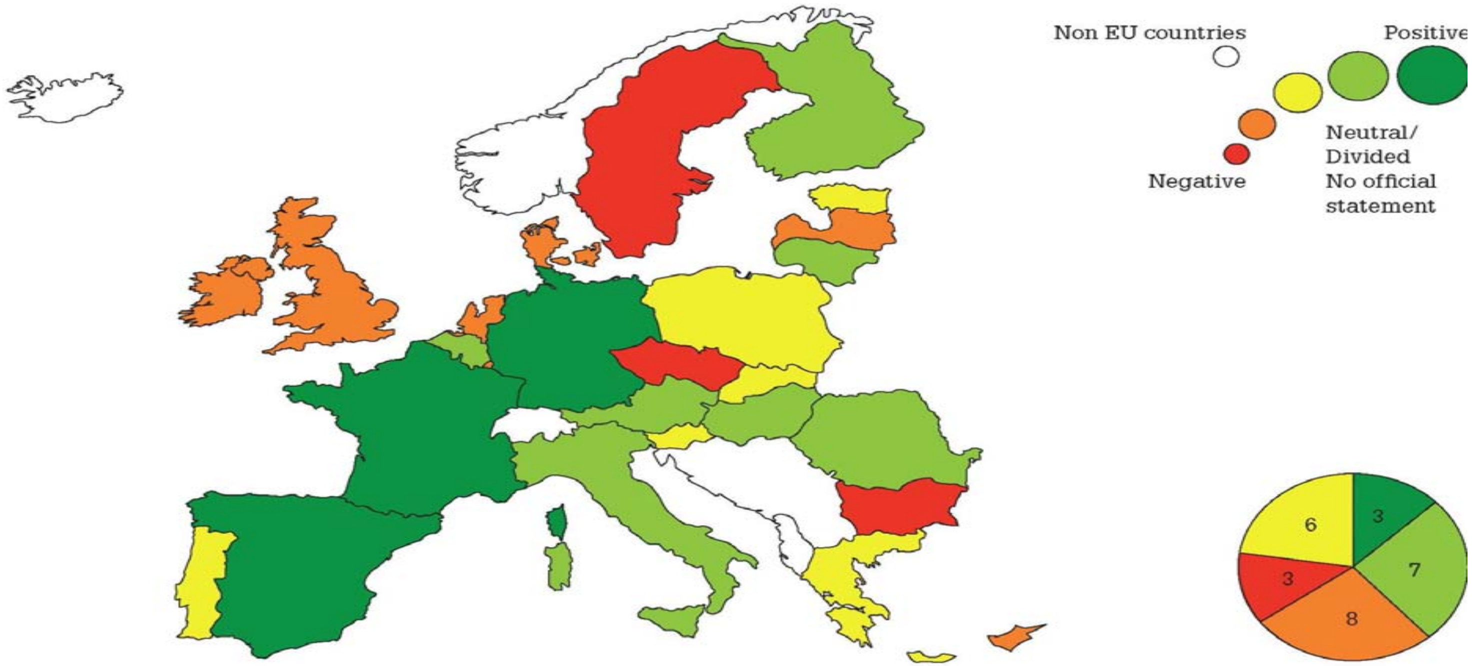
[35] Cyrille Lachèvre, *‘Une Taxe sur les Transactions Financières dès le 1er Août’* <http://www.lefigaro.fr/conjoncture/2012/01/30/20002-20120130ARTFIG00354-une-taxe-sur-les-transactions-financieres-des-le-1er-aout.php> Accessed 28 January 2013

[36] As Reported in C Lachèvre, *‘Une Taxe sur les Transactions Financières dès le 1er Août’* <http://www.lefigaro.fr/conjoncture/2012/01/30/20002-20120130ARTFIG00354-une-taxe-sur-les-transactions-financieres-des-le-1er-aout.php> Accessed 28 January 2013

[37] S Shaheen, ‘Comment: France’s Decision To Unilaterally Tax Financial Transactions Is a Risk But One Worth Taking’ <http://www.internationaltaxreview.com/Article/2969713/COMMENT-Frances-decision-to-unilaterally-tax-financial-transactions-is-a-risk-but-one-worth-taking.html> Accessed 1 March 2012

The Financial Transaction Tax 'thermometer'

The following 'map' shows the position of the 27 Member States



Level of support	EU Member State
In support	France, Germany & Spain
Supporting subject to conditions such as global or EU introduction, and are overall more positive	Austria, Belgium, Finland, Hungary, Italy, Lithuania and Romania
Neutral, divided or have not yet expressed an opinion	Estonia, Greece, Poland, Portugal, Slovakia and Slovenia
Supporting if certain conditions are satisfied, such as global or EU introduction, but are overall less positive	Cyprus, Denmark, Ireland, Latvia, Luxembourg, Malta the Netherlands and the UK
Against	Bulgaria, the Czech Republic and Sweden

Figure 1 S Lane, 'Reviewing Member State Support For The FTT' (2012) 1111 Tax Journal 16

II – Enhanced Cooperation – The Chosen Solution

Stagnation within the EU is not a new phenomenon. A high profile early example is that of the *'empty chair crisis'* in the 1960s[38]. French President Charles de Gaulle refused to take his seat in protest at the accession of the UK to the EU (perceived as a Trojan horse for America) and the proposed increase of Qualified Majority Voting (QMV) in the EU decision making process. Over time EU institutions have sought to counter the preservation of the status quo approach by adopting more flexible solutions in order to encourage the integration process. This includes the extension of QMV practice via Treaty amendments so that as a general rule of thumb adoption of proposals under Article 114 TFEU is the norm as opposed to Article 115 TFEU, particularly following the ratification of the Lisbon Treaty.

As has been illustrated above problems arise when the required legal basis for the Treaties is unanimity. Some areas of policy are ripe for reform from the legislature, whereas other areas are off limit. Following the combined effect of the CJEU's decisions in *Van Gend en Loos*[39] and *Costa*[40] (introducing the concepts of direct effect and supremacy not envisioned in the Treaties) there have been many examples of a genuine fear of a *'competence creep'* highlighted in particular by the German Constitutional Court in the *Solange* cases and the reaction in the UK to the *Factortame*[41] cases.

One of the solutions available in the Treaties themselves is the Enhanced Cooperation procedure contained in Articles 326 – 334 TFEU and Article 20 TEU. This concept was first introduced as *'Closer Cooperation'* in the Treaty of Amsterdam (1997) and has since been refined and developed as a means of integration on a limited scale. The process was renamed and reformed at the ratification of the Treaty of Nice (2000) due to misgivings about the feasibility of the process (for example the *'emergency brake'* procedure whereby any MS could block the process was removed). The Treaty Articles themselves do not exclude any measures from the procedures (although there are some different procedures for measures affecting the Common Foreign and Security Policy[42]).

In spite of its availability Enhanced Cooperation has been used sparingly since its introduction. It has been used only three times, most recently for the Commission's Proposal for a Common System of Financial Transaction Tax. In this section these instances will be outlined in brief in order to ascertain if there are any common themes. However prior to this it is necessary to include a brief summary of exactly what the Enhanced Cooperation procedure is and what its requirements are.

Enhanced Cooperation is described in Article 20 TEU as the "*last resort*". It means that if a section of MS wishes to press ahead with positive harmonisation they may be able to do so provided that:

i – They express their intention to the Commission once it has been established over a period of time that progress cannot be made.
ii – The Commission submits a proposal to the Council on their behalf.
iii – The Council approves the measure by QMV.

However, there are some provisos. There must be at least 9 MS which wish to pursue the legislation. The Commission may choose not to submit a proposal within the designated

[38] L Van Middelaar, 'Spanning the River: The Constitutional Crisis of 1965-1966 as the Genesis of Europe's Political Order' (2008) 4(1) European Constitutional Law Review 98
[39] Case C-26/62 Van Gend en Loos v. Nederlandse Administratie der Belastingen, 1963 E.C.R. 1
[40] Case 6/64 Flaminio Costa v. ENEL [1964] ECR 585
[41] Case C-221/89 R v Secretary of State for Transport ex parte Factortame Ltd and Others [1991] ECR I-3905
[42] See Article 329(2) TFEU

timeline. If not, it must explain to the MS why. Thirdly, whilst all MS may debate the issue only members of the Council which pursue Enhanced Cooperation may vote (except for Foreign Affairs and Security Policy proposals). Finally, the legislation wouldn't form part of the *aquis communautaire* therefore new MS which accede to the EU (such as Croatia) wouldn't be forced to accept the provisions.

A – Enhanced Cooperation and the FTT

The first usage of Enhanced Cooperation to consider is the most recent use, for the Commission's FTT. The origins of the Commission's FTT lie in 2010. Certain MS had taken action against the financial sector by introducing various forms of legislation. The issue was debated in the European Parliament and momentum was gained in 2010 following a European Parliament Resolution asking the Council and Commission the question of implementing an FTT to finance development cooperation. As has been illustrated in the previous section the issue was discussed at the G-20 summit in Toronto in June 2010. This was followed on the 7th October 2010 by the publication of a European Commission Communication entitled '*Taxation of the Financial Sector*[43]' in which two proposals were considered – an FTT and an FAT. At this stage it appeared that the FAT was the Commission's preferred method, but a public consultation was launched. The result of the consultation was that key players, such as trade unions, were opposed to an FAT. This led to the publication on 28th September 2011 of the Proposal for a Council Directive on a Common System of Financial Transaction Tax[44].

It quickly became apparent, notably at the June and July ECOFIN meetings of 2012 that a stalemate had been reached and the Proposal in its current form would not be adopted. Therefore on the 22nd September 2012 11 MS requested to pursue Enhanced Cooperation (Austria, Belgium, Estonia, France, Germany, Greece, Italy, Portugal, Slovakia, Slovenia and Spain). On the 25th October 2012 the European Commission published its *'Proposal for a Council Decision Authorising Enhanced Cooperation in the area of Financial Transaction Tax'*[45]. This was followed by the consent of the European Parliament (22nd December 2012) and Council (22nd January 2013) to authorise Enhanced Cooperation. On the 14th February 2013 the European Commission adopted a Proposal for a Council Directive implementing Enhanced Cooperation[46].

The final hurdle in theory is a unanimous vote of the 11 MS involved. However, the UK government on the 18th April 2013 launched a legal challenge to the CJEU opposing the introduction of the tax[47] upon the basis that under the Proposed tax system the UK would be required to collect revenue raised in the City of London and be forced to forward the amount levied to Brussels, for example if a British firm completes a transaction with a French bank based in the UK[48]. However, it must be noted that in spite of this potential delay the timeline between the initial Proposal, the debate and the decision to use Enhanced Cooperation has been, at least compared to the previous two instances, relatively swift. In the next section the

[43] Communication from the Commission to the European Parliament, The Council, The European Economic and Social Committee and the Committee of the Regions – Taxation of the Financial Sector Com(2010)549 Final 7th October 2009

[44] Proposal for a Council Directive on a Common System of Financial Transaction Tax and Amending Directive 2008/7/EC Com (2011 594 Final)

[45] Proposal for a Council Decision Authorising Enhanced Cooperation in the Area of Financial Transaction Tax Com(2012)631 Final/2 25th October 2012

[46] BBC News, 'Financial Transaction Tax Tabled By European Commission' <http://www.bbc.co.uk/news/business-21457562> Accessed 10 June 2013

[47] Case C-209/13 – United Kingdom v Council (currently unreported).

[48] BBC News, 'Financial Transactions Tax: UK Launches Legal Challenge' <http://www.bbc.co.uk/news/business-22227019> Accessed 28 May 2013

first two instances of Enhanced Cooperation being used (in divorce laws and patenting laws) will be outlined.

B – Enhanced Cooperation in Other Areas

In this section a brief summary of the issues regarding the introduction of divorce laws and patenting laws will be outlined. There is a common thread between the three occasions when Enhanced Cooperation has been used but it is important to note that each occurrence is a case study which has its own specific quirks.

i – Divorce Laws

Enhanced Cooperation was used for the first time in 2010 regarding the introduction of divorce laws, known as the *'Rome III Regulations'* within the EU. The roots of divorce law within the EU lie in 1998 with the *'Brussels II Convention'* which regulated the jurisdiction for divorce, not the laws itself, which Rome III covers. Following the acquisition of competence in the area after the entry into force of the Amsterdam Treaty, Brussels II was later replaced by an EC Regulation, referred to as the '*Brussels II* Regulation'. In 2005 a Green Paper was published in which the complexities of combining the rules contained in Brussels II and Brussels IIa with domestic laws were established. By way of response in 2006 the Commission proposed a Regulation to amend Brussels II.

Interestingly the Rome III regulations fell within Title IV of the Institutional framework, from which 3 MS have negotiated opt-outs. Denmark has a complete opt-out from Title IV, whereas the UK and Ireland have to declare if they wish to opt-in (which they declined to do so in this instance), meaning that potentially 24 MS were subject to Rome III. The required legal basis for family law specifies unanimity. However, it quickly became clear that unanimity simply was not possible due to vast differences in domestic attitudes and legislation regarding divorce. For example, at one end of the scale were states such as Poland and Malta, with a strong Catholic background in which obtaining a divorce is only possible under strict circumstances. At the other end of the scale were the Scandinavian states which have an extremely liberal approach to divorce. Any middle ground would be unsatisfactory for Scandinavians since the applicable rules would be stricter than their own domestic laws, and for strongly Catholic states too liberal to accept in line with their domestic laws. By June 2008 it was clear that following the proposed amendments from 2006 unanimity simply was not possible. However, most states were willing and able to agree to some of the text.

Therefore in late June 2008 Austria, Greece, Hungary, Italy, Luxembourg, Romania, Slovenia and Spain requested to use the Enhanced Cooperation procedure. They were later joined by Bulgaria and France. The request initially was delayed due to the formation of the second Barroso Commission. Later, Greece elected to withdraw their request, however following a request for further participation Belgium, Germany, Latvia, Malta and Portugal elected to participate in the procedure. After having obtained the necessary consents the final outcome came on the 12th July 2010 with the publication by the Council of the European Union of Decision 2010/405 Authorising Enhanced Cooperation in the area of the law Applicable to Divorce and Legal Separation. At present this has not faced legal challenge from a non-participating MS.

ii – Patenting Law

The second case in which the Enhanced Cooperation provisions were used was for the establishment of a common European system for patenting regulations. This is an area which has been problematic for the EU since the 1950s/1960s. Progress was reached to a degree in 1973 with the signing and ratification of the European Patent Convention (EPC).

This is an inter-governmental agreement between 38 European states (including all 27 EU MS) but not the EU itself so did not form part of the EU's legal order (akin to the status of the European Convention of Human Rights). On the 8th March 2011 the CJEU blocked the EU acceding to the EPC, holding it would be inapplicable with EU law[49].

However any patent issued by the EPC is national in nature since it only applies in the state for which it is granted. In 1989 an amendment granting power to a national judge to rule that a Community patent was invalid across the Community was agreed but not ratified. In 1997 a Green Paper was published, seeking to revive the issue. It argued that following CJEU case law confirming competence to harmonise patenting law and establish uniform IP rights the patent was able to be established by means of a Regulation adopted pursuant to EU law. Harmonising patenting law was able to be adopted in line with the EU's internal market powers but the establishment of uniform IP rights required the use of residual powers in order to adopt legislation where necessary to attain one of the EU's common market objectives, requiring unanimity.

A Proposal was drafted in 2000[50] which sought to introduce a common European patenting system. The key features of the proposal included amendments to the EPC rules regarding translation of applications, litigation and creation of a central court with jurisdiction over the patent (although the Treaties would need to be amended to make formation of such a court possible). The required Treaty amendments were made at the Treaty of Nice, however the proposal faced problems with regards to the translation issues – the argument being that altering the existing system of three working languages was cost ineffective. Following the entry into force of the Lisbon Treaty Article 118 TFEU provides legislative competence to *'establish measures for the creation of European intellectual property rights to provide uniform protection of intellectual property rights throughout the Union and for the setting up of centralised Union-wide authorisation, co-ordination and supervision arrangements.'*[51] However, Article 118(2) TFEU states that in order to *'establish language arrangements for the European intellectual property rights'*[52] the special legislative procedure must be followed i.e. unanimity is required. Following further proposed and amended Proposals it became clear that unanimity regarding the translation issues again would not be possible due in part to Spanish and Italian concerns about the status of their language in spite of strong support from the Belgian Presidency in 2010.

Again the Enhanced Cooperation procedure was pursued and authorisation from the Council was provided on 10th March 2011 via the publication of 'Decision 2011/167 on Enhanced Cooperation in the area of the Creation of Unitary Patent Protection'. With 25 of the 27 MS agreeing to Enhanced Cooperation the European patent has obtained far greater support from MS than both the divorce laws (14/24 MS with 3 opt-outs) and the FTT (11/27 MS). Yet in spite of the mass support there remain problems. The CJEU's decision to block accession to the EPC is detrimental. In addition like the FTT Proposal the Patenting Proposal faces legal challenge from two non-participants – Spain and Italy[53]. This highlights the effect that a single state can have on Proposals requiring unanimity.

On the occasions in which Enhanced Cooperation has been used so far it can be ascertained that it has been used once for a non-contentious practicality issue (divorce laws) and twice for highly controversial technical issues). Furthermore it can be established that is not a panacea and that the process is still open to legal challenge. In the next section the

[49] *Opinion 1/09*, judgment of 8 March 2011, not yet reported.
[50] COM(2000)412, 1 Aug. 2000.
[51] Article 118 TFEU
[52] Article 118(2) TFEU
[53] Cases C-274/11 *Spain* v. *Council* and C-295/11 *Italy* v. *Council*

practicalities of the Enhanced Cooperation process will be assessed to establish its success as a concept, its potential impact and its potential cost.

Conclusion – Progression or Pragmatism at a Cost?

The Commission's FTT, marriage and patenting proposals noted above are interesting in their own right but are specific case studies. For the purposes of this paper they act as lenses by which to assess the adoption of legislation within the EU through Enhanced Cooperation. European integration is a balancing act between two forms of harmonisation – positive harmonisation (adoption of proposals to create new links between MS) and negative harmonisation (removal of measures to facilitate links between MS). In the instances in which it has been used so far Enhanced Cooperation seeks to facilitate positive harmonisation. Although it may take some time to be fully able to evaluate the success or failure of Enhanced Cooperation it is clear from the above information that the concept has taken its time to hit its stride.

However, MS are clearly now more willing to accept it as a means of adopting legislation when unanimity is not possible, utilising it as a tie break concept. One particularly interesting indicator of increased MS recognition and willingness to use Enhanced Cooperation is Article 10 of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (2012), the Treaty which famously the UK decided to veto. Article 10 states that in line with the founding Treaties the contracting parties to the Stability Treaty agree to *"make active use, whenever appropriate and necessary, of measures specific to those Member States whose currency is the euro...and of enhanced cooperation, as provided for in Article 20 of the Treaty on European Union and in Articles 326 to 334 of the Treaty on the Functioning of the European Union on matters that are essential for the proper functioning of the euro area, without undermining the internal market"*[54]. The vast majority of EU MS were contracting parties to the Treaty, a clear indication that Enhanced Cooperation will be used more often, particularly in light of the ongoing financial crisis. Although it must be noted potential future usage of Enhanced Cooperation is not limited to taxation and economic matters, for example there has been consideration of using Enhanced Cooperation to introduce regulations for online gambling within the EU[55].

It is debateable as to whether or not MS were previously reluctant to use Enhanced Cooperation or not but the question remains – why are MS beginning to find the prospect of using Enhanced Cooperation so appealing? This could be for various reasons. The first of these reasons is the rapid expansion of the EU. It has previously been stated that the origins of Enhanced Cooperation lie in the *'closer cooperation'* concept introduced via the Treaty of Amsterdam (1997). At the time the Treaty was ratified the EU was composed of 15 MS. In the space of 10 years a mass expansion occurred leading to today's total of 27 EU MS. The increased use of Enhanced Cooperation is explained by simple mathematics and probability – the instances in which the notion of a measure that works for one does not necessarily work for another greatly increases. This means that the *'tie break'* situation occurs far more often.

Another potential explanation for increased usage is increased familiarity with the procedure. Although explained in great detail in the Treaties it can be argued that the process was uncertain and MS were wary – a fear of the unknown. It is highly unlikely that MS were unaware of the procedure; therefore there may have been a lack in confidence in the institutions of the EU to adapt accordingly. Alternatively the MS may have wished to use Enhanced Cooperation but the EU institutions (i.e. the first Barroso Commission) were

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[54] Article 10 Ibid

[55] V Paeno, 'Online Gambling in Europe: Enhanced Cooperation' (2012), 11(7), World Online Gambling Law Report, 3

reluctant to do so. Following the first occasion of Enhanced Cooperation being adopted familiarity with the process both for MS and the EU institutions would have increased and a willingness to utilise Enhanced Cooperation would also have increased.

There are alternatives to Enhanced Cooperation, notably the presence of opt-outs. However, it could be argued that another reason for its increased practice is that at its core is a positive ideology relative to other methods of limited adoption of legislation. In the language of the treaties it is clear that it is envisioned as an inclusive process. Many references are made towards non-participating MS being able to join the process at any time. In particular Article 328(1) TFEU allows MS which have not agreed to the original establishment of Enhanced Cooperation to adopt the measure at a later stage. It states that Enhanced Cooperation is available to MS "*at any other time, subject to compliance with the acts already adopted within that framework, in addition to those conditions.*"[56] There are also obligations upon the European Commission and MS to ensure that as many MS as possible agree to pursue Enhanced Cooperation within that particular field.

Also a possibility is Article 136 TFEU, an Article which was also recognised in Article 10 of the Stability Treaty. Article 136 TFEU allows MS whose currency is the euro to adopt measures specific to them via QMV in order:

"(a) to strengthen the coordination and surveillance of their budgetary discipline;
(b) to set out economic policy guidelines for them, while ensuring that they are compatible with those adopted for the whole of the Union and are kept under surveillance."[57]

This means at present 17 MS would be bound by any decisions adopted via QMV, far greater than the minimum of 9 (and in the case of the FTT 11 MS) consenting to adopt legislation via Enhanced Cooperation. However the measures which are able to be adopted are limited in their scope relative to Enhanced Cooperation. Although this is positive in the sense that it promotes integration between the 17 Eurozone MS there is also an exclusive element present since 10 MS are excluded (however it must be noted that some MS are content to be excluded from the euro). Although Article 136 TFEU may have a more limited scope than Enhanced Cooperation in light of the financial crisis and the determination to make the euro currency workable it is safe to argue that Article 136 TFEU should not be overlooked. This too, like Enhanced Cooperation will be used increasingly often and gaps will appear in the EU integration project between Eurozone MS and non-Eurozone MS.

The positive obligations of inclusion of Enhanced Cooperation can be contrasted with the concept of an *'opt-out'* in line with the *'à la carte'* model of integration. Utilising this method ensures that at least one MS expressly excludes itself from proceedings via negotiation with other MS. At present there are in total 11 legislatively recognised opt-outs (for Denmark, Ireland, Poland and the UK), 1 *de facto* opt-out (Sweden) and 1 opt-out for the Czech Republic to be recognised during the ratification of the next Treaty. It is arguable that the Enhanced Cooperation procedure is a much quicker method of adopting proposals relative to the opt-out procedure due to this negotiation process.

At first glance the Enhanced Cooperation procedure therefore appears to be a wholly positive concept. It is a legislative means of facilitating integration in a limited form and can be considered as progress. The EU offers a global platform for legislation to be adopted. In line with the famous adage that *'too many cooks spoil the broth'* legislation can be adopted in its original form across a variety of MS with little need for a watered down compromise. Furthermore it may provide a means by which to introduce dormant proposals, proposals which had merit at the time and which may be applicable today, but which faced the

[56] Article 328(1) TFEU
[57] Article 136 TFEU

obstacles that the FTT proposal, marriage legislation and patenting proposal have faced. The MS which agree to Enhanced Cooperation can be satisfied that the measure is being introduced. The MS which decline Enhanced Cooperation can be satisfied that the measure is not applicable to them and that their sovereignty is not infringed. Both camps would argue that their position in the matter puts them at a competitive advantage either socially or economically.

However, it is equally arguable that Enhanced Cooperation is a negative. The treaties themselves refer to the process as a *'last resort'*. Yet negative within this context has a different meaning from everyday vernacular. The use of negative here does not mean that the process itself should not exist. In fact the existence of the Enhanced Cooperation procedure should be applauded. Rather, it means that in pursuing integration the focus has shifted towards finding *pragmatic* solutions. Although the procedure allows proposals to be adopted with relatively little compromise from its original form the Enhanced Cooperation procedure itself is a compromise. EU expansion has its positives and negatives.

Of course, simply because a Treaty power is available for MS to use does not necessarily mean that it has to be used. The Enhanced Cooperation procedure relies on proposals of a high quality to be produced by the legislature (i.e. the Commission) in order to be effective, otherwise legitimate concerns about the quality of the draftsmanship may be misconstrued as fundamental opposition to the original underlying concept. Looking back to the FTT map there are many states which have been classed as being in favour of an FTT subject to certain conditions. It is arguable that their concerns are justified.

For a Europhile at least any measures which facilitate integration in any form are preferable to stagnation. If the EU integration project is considered as a car on a journey the Enhanced Cooperation process can be considered as an anti-stall mechanism preventing the car from grinding to a halt. It is encouraging to see that it is beginning to be used more frequently and Enhanced Cooperation should be used, however caution must be exercised. Percentage wise the number of measures adopted via Enhanced Cooperation of all the EU measures adopted is minute. However, each instance of its use creates a series of blocks of MS. Although the language of the treaties indicates that the procedure is inclusive in nature if it is used too often, particularly for contentious issues then certain MS may risk being ostracised within Europe. This is fundamentally the opposite of the aims of the Union set out in the Schuman Declaration, the pursuance of a united Europe. Therefore Enhanced Cooperation can be considered as this – a pragmatic solution but with a potentially irreversible cost to the EU integration project.

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