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Building a European Union 'Treasury': Explaining the European Commission's New Approach to Debt Issuance and Management

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Abstract

This article examines how the European Commission went from being an occasional participant in capital markets in the 1970s to an established bond issuer by the 2020s. As a result of these changes, the Commission has moved away from its traditional model of back-to-back lending using a wide array of funding instruments towards the regular issuance of EU bonds and bills in the style of a European treasury. Using a principal–agent approach, we ask whether this shift was driven by member states seeking to reap the benefits of collective borrowing or rather by slippage by the Commission aimed at spurring European integration. Our results show that the Commission's occasional attempts to advance wider political objectives were rebuffed by member states, which, nonetheless, ultimately embraced the idea of a European treasury. Our findings emphasise the logic of delegation over agency slack when it comes to the EU's evolution as a borrower.

Keywords: European Commission; European Union budget; Next Generation EU; public debt management

> We [the Commission] have changed very much our approach to issuance. We have undergone a significant transition process by which we have emerged from … an ad hoc issuer for smaller very confined programmes to what we would call a sovereign-style issuer.[1]

Introduction

The power to borrow has long been one of two elements of the European Union's (EU's) financial autonomy, alongside the Union's own resources (Strasser, 1992, p. 73). For some, such borrowing constitutes the Union's 'second financial arm' (Laffan, 1997, p. 217), and for others, it is akin to a 'shadow budget'.[2] Since 2020, the amount of EU borrowing has increased significantly with the creation of SURE (Support to mitigate Unemployment Risks in an Emergency) and Next Generation EU (NGEU) and its Recovery and Resilience Facility (RRF). In 2023, the European Commission issued €115.9 billion in new debt, about twice as much as the Spanish government (Devere, 2023; European Commission, 2023).

[1]Engelen (2022), 19:50 min; see also European Commission (2022).
[2]We borrow the term 'shadow budget' from the German Bundesrechnungshof (*Schattenhaushalt*) (Rasch, 2022); also Interview 9.

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This increased volume of EU borrowing has gone hand in hand with a new approach to debt issuance and management. Introduced by the Commission in April 2021 and January 2023, respectively, the diversified funding strategy and the unified funding approach replace the traditional model of back-to-back and programme-specific borrowing by creating a central funding pool financed through EU bonds and bills. This pool is used, in turn, to finance loans and grants through the NGEU and other financial instruments such as the macro financial assistance plus (MFA+) for Ukraine. By providing regular syndications and auctions, the diversified funding strategy means that the Commission has become an established issuer on capital markets rather than an occasional one, thus taking an important step towards becoming a European 'treasury'.[3]

This article contributes to the debate on the significance of the EU's new financial instruments. A range of scholars have declared the RRF in particular to be a major unprecedented development and one that may change the EU for good (Fabbrini, 2022; Schelkle, 2021). However, others argue that the RRF is neither unprecedented nor bound to be repeated (Howarth and Quaglia, 2021; Hodson and Howarth, 2023; Rehm, 2022). We show that the Commission became an off-budget agency in the 1970s and ask how it eventually acquired greater discretion over borrowing operations and debt management.

We use a principal–agent approach to study the political processes through which member states created larger financial instruments and delegated more autonomy to the European Commission over borrowing and lending operations. We find that the Commission has sought a greater role for itself in this policy domain but found little room for slippage because of member state principals' tight control of borrowing instruments and the low costs of re-contracting. Member states ultimately chose to turn the Commission into a European treasury, our results indicate, to lower lending costs and improve the efficiency of funding operations when borrowing at scale.

This article draws on various original data sources. We analysed dozens of documents from the German Federal Archives and the Historical Archives of the European Commission until 1993, owing to the 30-year rule; EU legislation; European Court of Auditors (ECA) documentation – (performance) audits and other reports – on various Commission borrowing and lending operations; and European Parliament documentation. For policy developments since the 2000s, this primary documentation was triangulated with information gleaned from 12 semi-structured interviews with topic-relevant EU and national officials.

This article is structured as follows. Section I provides an overview of the political science of debt issuance and management and presents the analytical framework we apply to interpret the Commission's changing role as a borrower. Section II examines the state of play in EU debt issuance and management with the Commission operating as an off-budget agency from the 1970s to the 1990s. Section III presents evidence of re-contracting – legislative changes – that resulted in a gradual shift of the institutional framework of Commission borrowing from the 1990s to 2018. Section IV turns to the reform of the Commission's borrowing operations since 2020. The final section discusses the wider implications of this shift in Commission borrowing from off-budget agency to a European 'treasury''.

[3]We use the term 'treasury' in this contribution with the knowledge that some institutions that are named treasuries do not, in fact, issue debt.

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I. The Political Science of (EU) Debt Issuance and Management

In this article, we ask how the development of the European Commission's role as a borrower, lender and debt manager since the 1970s can be best understood. To answer this question, we draw inspiration from the limited political science and political economy literature on public debt management. From this literature, we detect a number of themes which potentially shed light on the development of the European Commission's role as a borrower.

Rommerskirchen and van der Heide (2022) focus upon debt management as 'quiet politics' – a concept and analytical framework developed by Culpepper (2021) – which allows significant institutional development without the interference of political actors. However, by and large, the politics of debt management is presented as shaped by public and financial market actors. Thus, Fastenrath et al. (2017) point to the reliance on financial markets as a governance mechanism and a number of authors examine the financialisation of sovereign debt management (Dutta, 2018; Lemoine, 2013; Preunkert, 2017). Some studies focus on the interaction of public authorities with individual banks, such as Preunkert's (2023) study of primary dealer networks and Silano's (2022) work on revolving doors in debt management. Trampusch and Gross (2021) examine the limited role of national parliaments in sovereign debt management, arguably a factor contributing to 'quiet politics'.

A contrasting view highlights the bureaucratic politics that underpin changes to national debt management strategies. Trampusch (2015) explains developments in the management of German federal public debt by focusing on institutional innovation and entrepreneurship and specifically institutional change directed by the Ministry of Finance. Similarly, Lemoine (2016) argues that the depoliticisation of debt management in France was a political move by senior officials in the Trésor. No comparable studies have been conducted on the European Commission's public debt management.

Although there is a growing literature on borrowing instruments created during the euro crisis and COVID-19 pandemic, there have been few attempts to explain the EU's evolution as a borrower from a longer term perspective. In the context of NGEU, the question of the EU's fiscal capacity has become more central and thus attracted more academic interest (Howarth and Quaglia, 2021; Schelkle, 2021). Studies of the longer term development of the Commission's financial instruments have largely focused on the politics of their creation – applying, notably, historical institutionalism and the concept of critical juncture (Gocaj and Meunier, 2013; Rehm, 2022; Verdun, 2015, p. 221).

To anchor our institutional analysis of the Commission's borrowing operations, we devise two ideal types (see Table 1; see also ECA, 2023, pp. 8–9; European Commission, 2022). The first outlines a borrowing framework in which the Commission takes the role of an off-budget agency: Its issuance of bonds is authorised ad hoc through legislative acts and the proceeds from each bond issuance are on-lent back-to-back. This framework, which resembles the Commission's borrowing operations during the 1970s, grants the Commission limited discretion over debt management and requires relatively little active monitoring by the Council. By contrast, the second ideal type, labelled 'European treasury', describes a set of borrowing operations wherein the Commission regularly issues debt and engages in active debt management. Bond proceeds are no longer tied to a specific loan but feed a common funding pool. This operational framework entails greater

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Table 1: Ideal Types of Commission Borrowing.

	Off-budget agency	*European treasury*
Authorisation to borrow and spend	Through legislation (basic act)	Through budgetary/own resources appropriation
Financial guarantees	Implicit	Explicit
Accountability and reporting	Limited	Extensive risk controls, parliamentary hearings and audits
Debt management	Back-to-back lending, passive debt management, bonds under different labels	Maturity mismatches, active debt management, single benchmark label
Timing of issuance	Ad hoc issuance	Regular market presence, pre-announced funding calendar and issuance programme
Cash management	Earmarked funds	Cash pool
Disbursement	Different intermediaries	Fiscal/monetary task division

financial risks, which are reflected in more explicit financial guarantees and extensive accountability. The Commission's diversified funding strategy, adopted in 2021, has come to approximate this latter ideal type, even though its borrowing operations remain outside the EU budget.

To understand the Commission's evolution as a borrower, we draw on elements of the principal–agent approach. Specifically, we examine EU member states as a collective principal, the Commission as an agent, and the acts of delegation as new or amended regulation (Delreux and Adriaensen, 2017; Pollack, 2003; Tallberg, 2002). Member states' decision to delegate in this case is driven by a desire to reap the benefits of collective borrowing, which allows the Union to borrow at lower interest rates than many could do alone. For instance, the 19 member states that availed of SURE loans saved an estimated €9 billion by borrowing collectively rather than individually to support short-term work schemes during the Covid-19 pandemic (European Commission, 2023). Such delegation comes at the risk of agency slack, however, either because the Commission fails to conduct bond issuance efficiently or because it is overzealous in its approach to borrowing. The second form of agency slack, which we think of as slippage, is more likely than the first, which we denote as shirking. This is because the Commission – which principal–agent scholars generally assume has more intense preferences for European integration than member states (Pollack, 2003, p. 393) – will favour EU borrowing to advance the scope and range of activities that the EU can undertake. The principal's problem arises in other words, because of the risk that the Commission will use its borrowing powers not simply to deliver lower borrowing costs but to push for deeper integration than member state principals bargained for.

There are echoes of integration theory in this principal–agent relationship, which casts the Commission as a supranational entrepreneur and member states as being driven by national interests and a rationalist conception of institutional choice (Moravcsik, 1998, pp. 8–20). However, for reasons of parsimony, we employ a dynamic conception of agency theory, which allows for not only slippage but the possibility that member state principals may choose to re-contract with the Commission by means of new legislation or guidance on debt issuance or management. Following Hawkins et al. (2006), we see re-contracting

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as a way for principals to improve the monitoring, management and completion of a contract, especially where the original contract fails to anticipate problems in advance, as well as to de-delegate, where principals decide to withdraw authority from an errant agent. Re-contracting is a feature of national debt management, as evidenced by the decision of several OECD countries in the 1980s to reassign key functions in this domain from finance ministries to independent agencies because of concern over efficiency and portfolio management (Currie et al., 2013). Faced with similar concerns, we would expect the Council to revisit the Commission's approach to raising funds on financial markets.

Heterogenous preferences are a common reason why states do not delegate to international organisations (Hawkins et al., 2006). It follows that changing preferences within the collective principal may lead to re-contracting on the Commission's borrowing instruments. Decisions on new borrowing instruments in the EU are taken by unanimity or qualified majority vote, depending on which treaty provision applies, although consensus is the norm.[4] This gives the most reluctant member states leverage over delegation and re-contracting (Garrett and Tsebelis, 1996) yet encourages member states to work through their differences (Puetter, 2014). This focus on principals' preferences is, however, not to deny the possibility of agency slack, as agents either minimise their effort on behalf of principals or pursue objectives of their own (Kiewiet and McCubbins, 1991). Slack may not be widespread in EU policy-making, but it is possible where member states interpret the Commission's mandate differently (see Da Conceição, 2010). Whilst EU budgetary power is subject to strict control mechanisms, we see greater scope for agency loss in EU debt issuance and management given member states' consistent refusal to incorporate borrowing into the Union's budget. One consequence of this decision is that the European Parliament and European Court of Auditors have been constrained in their ability to play the same police patrol role in relation to borrowing as they have for EU expenditure and revenue (Kiewiet and McCubbins, 1991; McCubbins and Schwartz, 1984).

II. Commission Borrowing as an Off-Budget Agency: The Community Loan Mechanisms, 1975–1988

In 1975, the Council agreed that the European Economic Community could borrow to finance loans to member states facing balance of payments difficulties caused by rising petroleum prices (Regulation (EEC) No 397/75). Commonly considered the first Commission borrowing instrument (Horn et al., 2020), the Community Loan Mechanism initially conferred no explicit borrowing powers on the Commission, which assumed this role de facto. When member states formally authorised the Commission to contract Community Loans in 1981, this act of delegation was subject to strict ex-ante controls (Council Regulation (EEC) No 682/81). Borrowing and lending operations, the Council agreed, would be 'carried out using the same value date and on the same terms with respect to repayment of the principal and payment of interest' (Council Regulation (EEC) No 682/81, Art. 4). The Commission thus began its involvement in this policy domain

[4]The New Community Instrument, for example, was underpinned by Article 235 of the Treaty Establishing the European Economic Community (TEEC) and thus required the unanimous approval of member states. The Balance of Payments Assistance Facility, in contrast, is granted under Article 143 of the Treaty on the Functioning of the European Union (TFEU) on the basis of a qualified majority vote.

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as an off-budget agency with little or no discretion over how it raised funds on behalf of member state principals.

Under the Treaty of Rome, the Community's budget had to be 'in balance', raising the possibility that the Commission might use off-budget borrowing to secure greater resources (Treaty Establishing the European Community, Art. 199). The Council guarded against the risk of such slippage by stipulating that Community Loans must be administered by the European Monetary Cooperation Fund – a body governed by European Community national central bank governors – with the Bank for International Settlements appointed as the financial agent. Thus, funds borrowed under this instrument never went through the Commission's accounts (ECA, 1982).

The Commission's vision at this time of borrowing as a vehicle for deeper integration can be seen in its backing for the 1977 MacDougall Report, a high-level study that had called for the Community Loan Mechanism to be expanded to meet 'short-term cash management needs' and facilitate fiscal stabilisation under EMU (European Commission, 1977, p. 58). Interestingly, the MacDougall Report also proposed a European treasury in all but name when it called for a common organisation to undertake financial intermediation and manage borrowing and lending operations. The high-level study was endorsed by the Commission (Jenkins, 1977), but it went too far for member states, which imposed strict borrowing limits on the Community Loan Mechanism and, its successor, the Balance of Payments (BoP) Assistance Facility. The regulation underpinning the latter reaffirmed member state preferences for an off-budget agency by prohibiting the Commission from involving the Community 'in the transformation of maturities, in any exchange or interest-rate risk, or in any other commercial risk' (Council Regulation (EEC) No 1969/88).

There were occasional tensions in this period between the Council's desire to avail of lower borrowing costs and their determination to keep the Commission's borrowing powers in check. In keeping with our dynamic conception of agency relationships, member state principals showed a willingness to re-contract. In 1977, the Council agreed to change the terms of Community Loans to Ireland and Italy from a variable interest rate to a more favourable fixed one (77/414/EEC: Council Decision). In 1981, the Council also allowed for the early redemption of Community Loans (Council Regulation (EEC) No 682/81). When the Community Loan Mechanism was incorporated into the BoP Assistance Facility in 1988, the Commission was also authorised to refinance balance of payments loans and pass on interest cost savings (Council Regulation (EEC) No 1969/88, Art 6.2). However, despite the various borrowing and lending instruments that the Commission managed in the 1980s, it did not run a discernible debt management strategy to the frustration of the European Court of Auditors (ECA, 1989, pp. 174–178).

The Euratom Loan Facility, which was established in 1977 to finance loans for investment in nuclear power stations, relied on the same back-to-back operations as the Community Loan Mechanism (77/270/Euratom: Council Decision of 29 March 1977). The New Community Instrument, which was established a year later to support investment projects related to industrial adjustment and competitiveness, took a small but significant step away from the off-budget agency model. The Commission, member state principals agreed, would be allowed to contract loans 'in the best interests of the Community having regard to the conditions on capital markets and in accordance with the constraints imposed by the duration and other financial aspects of the loans to be granted' (Council

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Decision 78/870/EEC, Art. 4). This authorised the Commission to engage in active debt management, although member states ensured that any funds raised but not yet lent would be deposited with the European Investment Bank (Council Decision 77/27/Euratom and Council Decision 78/870/EEC).

Initially, the Commission borrowed back to back under the New Community Instrument, but this approach ran into problems in 1983 when the Council reconfigured this instrument to allow loans to small and medium-sized businesses (Council Decision 83/200/EEC). This change led to a sharp increase in the number of New Community Instrument loans provided, leaving the Commission with a choice between undertaking a multitude of small borrowing and lending operations or borrowing at scale to cover multiple loans. The European Court of Auditors (1983) raised immediate concerns about this new 'reserve financing system', which it noted had left the New Community Instrument facing a deficit for the first time because of lengthy time lags between borrowing and lending operations. Member states were less concerned about the potential for agency slack under the New Community Instrument, perhaps because the European Investment Bank's role in such borrowing and lending operations served as an intergovernmental check on the Commission's powers. West Germany, which remained sceptical about the New Community Instrument, had been especially keen for the European Investment Bank to play this role.[5]

In 1988, the Commission engaged in a clear-cut act of slippage when it raised ECU 500 million under, what it called, the 'Jean Monnet issue' (European Commission, 1989, p. 47). Unlike previous operations, this loan went not towards new projects but the refinancing of earlier, more costly loans. As noted above, slippage occurs when the Commission substitutes its preferences as an agent for those of member state principals. In this case, the Commission justified the 'Jean Monnet' issue as an attempt to establish a '"benchmark" for all borrowers in the ECU' (European Commission, 1989, p. 47). Hinting at further issuances, the Commission argued that the Community's presence in financial markets must be 'regular and continuous if the benchmark is not to become out of date' (European Commission, 1989, p. 47).

Member state principals had authorised the Commission to depart from back-to-back borrowing when they created the New Community Instrument and tacitly accepted the risks involved, but they drew the line at the 'Jean Monnet' issue. By 1988, the Council had raised the maximum lending volume of the time-limited instrument on three occasions, but only after the previous ceiling had been reached (European Commission, 1986). Each time, likely recipients, including France, were in favour of additional borrowing, with West Germany, and the United Kingdom opposed and ultimately agreeing only for 'higher-order reasons'.[6] A Commission proposal to turn the New Community Instrument into a 'revolving fund' – which would have allowed the supranational institution to

[5]Bundesarchiv (Thereafter B) 102/316889 'Entwurf für einen Beschluβ, mit dem die Kommission im Hinblick auf einen Beitrag der Gemeinschaft zur Finanzierung von Kernkraftwerken zur Aufnahme von Euratomanleihen ermächtigt wird', 19 September 1975. B 136.30941 '457./459. Tagung des EG-Rates – Investitionen und Anleihe in der Gemeinschaft' 13 June 1977.

[6]Service des archives économiques et financières (thereafter SAEF) B-0083216 'Conseil économie et finances 07/02/1983', 1982–1983. Telegramme 'Conseil des Ministres de l'économie et des finances, 7 février 1983', 9 February 1983. B 102/433766 'ECOFIN-Rat (Wirtschafts- und Finanzminister) vol. 12, 06/1986-12/1986', 9 October 1986.

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borrow and re-lend up to a maximum agreed amount and thus exercise unprecedented discretion over borrowing operations – failed to win member state backing (EC, 1988).

In November 1988, the Commission put forward a proposal to renew the New Community Instrument once again, but it failed to win support from member states. An amended proposal presented 10 months later, suffered the same fate. Member states always had varying degrees of enthusiasm about empowering the Commission as a borrower in this domain, but the French, German and British came to the view that the EIB should lead on the provision of loans to SMEs. West Germany had long feared that its grip on the Community budget could be loosened by Commission borrowing and so favoured a bigger role for the EIB.[7] Having originally pushed for the New Community Instrument to support SMEs, France saw EU budget guarantees for the EIB, as a way for the Luxembourg-based lender to do the same.[8] In the United Kingdom, Prime Minister Margaret Thatcher became increasingly critical of the Commission after her Bruges speech in September 1988. The EIB avoided such animus, perhaps because of its low profile in the United Kingdom (Coppolaro, 2023, p. 2). When EC finance ministers agreed to double the EIB's capital in June 1990, the New Community Instrument's fate was sealed. The Commission's act of slippage was thus brought to an abrupt end by the Council's ability to re-contract and, in this case, de-delegate.

III. 'Disengagement' and Incremental Reform, 1990–2008

Far from being pushed into greater borrowing by the Commission, member state principals exercised their right to re-contract during the 1990s by significantly decreasing the amounts of new borrowing operations. The Council's decision not to authorise the refinancing of NCI and Euratom loans in 1990 brought borrowing for these instruments to a 'virtual standstill' (European Commission, 1991, p. 2). Although the Council authorised the Commission to provide macro financial assistance to third countries, starting with Hungary in 1990, the funds raised for this purpose were offset by the end of New Community loans, the winding down of European Coal and Steel Community loans and the moratorium on Euratom loans after the Chernobyl disaster. Following so-called 'disengagement guidelines laid down by the Council' (European Commission, 1998, p. 6), annual borrowing by the Commission shrank drastically and never exceeded ECU/€ 500 million in a single year between 1993 and 2008 (European Commission, 2007). Reflecting this collapse of new borrowing, police patrol-type monitoring efforts were also downgraded. In 1998, the European Court of Auditors stopped publishing a dedicated chapter on the EU's borrowing and lending operations in its Annual Report (see ECA, 1999).

Yet, even in the absence of a major crisis, the Council adopted additional legislation in 2002 with the aim of strengthening the Commission's borrowing powers, albeit in a strictly delimited way, and developing the principles that applied to the Commission's

[7] B 136.30941 Bundesarchiv 457/459. Tagung des EG-Rates, 13 June 1977.

[8] B 102/433766 'Vorschlag für einen Beschluss des Rates der Ermächtigung der Kommission, im Rahmen des neuen Gemeinschaftsinstruments (NGI) Anleihen zur Investitionsförderung in der Gemeinschaft aufzunhmen - NGI IV: 1,5 Mrd ECU für 2 Jahre -', 9 October 1986. Telegramme 'Conseil des Ministres de l'économie et des finances, 7 février 1983', 9 février 1983.

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borrowing operations. The revised BoP Assistance Facility regulation of 2002 was the last piece of legislation in which member states mandated strict back-to-back financing, but it already included some provisions that delegated to the Commission more flexibility for managing loans (Council Regulation (EC) 332/2002).[9] Specifically, the Council strengthened the Commission's position in negotiating loan agreements, allowing it to reject proposed disbursement schedules in light of market conditions (Council Regulation (EC) 332/2002, Art 7.1). The Council also acknowledged the Commission's practice of refinancing loans, by mandating it to pass on savings from loan refinancing Council Regulation (EC) 332/2002, Art. 7.2).

In 1994, the Commission created two separate Euro Medium Term Notes (EMTN) programmes of ECU 1 billion each: one to fund the BoP Assistance Facility, NCI and Euratom loans and the other for the final ECSC loans (European Commission, 1994). From then on, the Commission had a single fiscal agent, the European Central Bank, and it could draw on a framework contract for loans and issue debt under a programme. Whilst this might appear at first glance as an instance of slippage, the Council expressly allowed the Commission to update the EMTN programmes several times, raising the volume to €2 billion in 1999 and to €4 billion in the context of the Council-mandated review of the BoP Assistance Facility in 2005 (European Commission, 2005). The 2005 review also updated the EMTN's terms – including the insertion of a collective action clause and allowing the Commission to issue bonds with maturities of between 3 months and 30 years. Thus, the infrastructure for large-scale issuance under a programme was well established at the behest of member state principals prior to the euro crisis and the COVID-19 pandemic.

In 1989, the Commission spelt out for the first time how Commission borrowings were guaranteed against the budget headroom and how these guarantees were to be drawn. The Council's 1989 Own Resources Decision (ORD) allowed for debt service to be decoupled from budgetary allocations. The Commission was authorised to draw down its account with national finance ministries above existing budgetary appropriations and up to the own resources ceiling in the 'sole case of default under a loan contracted pursuant to Council Regulations and Decisions' to service outstanding debt (Council Regulation (EEC, Euratom) No 1552/89, Art 12.2 and 12.3). All EU loans to member states have since then been guaranteed in this way.

The Council also moved to clarify guarantees on Commission borrowing for loans to third countries, which were secured through explicit budgetary appropriations. Starting in 1990, the EU began providing medium-term financial assistance to third countries, which entailed significantly riskier loans than assistance to member states.[10] Reflecting these concerns, the Council decided in 1994 to establish a dedicated guarantee fund for external action, which would remove the need to reallocate funds from other budget entries in case of a default and reduce the likelihood of reaching the own resources ceiling (Council Regulation (EC Euratom) 2728/94).

[9]The Council blocked the Commission's proposal to be able to conduct debt and interest swaps on its borrowings (see Article 7.1, EC, 2001).
[10]Monetary Committee 1992. The treatment of medium-term loans in the Community budget, 30 January 1992. BAC 228-2012 No-738-1. European Commission Historical Archives, Brussels, Belgium.

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IV. Scaling Up, 2009–2018

The Council responded to the Global Financial Crisis and euro crisis by quadrupling the volume of the BoP Assistance Facility to €50 billion and creating the European Financial Stabilisation Mechanism (EFSM), a temporary instrument of up to €60 billion aimed at euro area members. With the EFSM, the Council allowed the Commission to raise the EMTN ceiling to €80 billion whilst noting the possibility of raising the ceiling further to €110 billion if necessary (European Commission, 2010, p. 4). To be able to raise these volumes at favourable terms, member state principals delegated a greater margin of manoeuvre to the Commission as an agent, subject as always to strict ex ante controls (Council Regulation (EU) 407/2010). Specifically, the Council set out a new objective for the Commission's debt management, which was 'to optimise the cost of funding and preserve its reputation as the Union's issuer in the markets' (Council Regulation (EU) 407/2010, Art. 63). For this purpose, the Commission could raise funds separately from the disbursement schedule and invest these funds temporarily in a reserve account, which could be used for the sole purpose of providing financial assistance under the EFSM.

The agreement on the EFSM once again reflects the importance of intergovernmental divisions between member state principals. The instrument was created in May 2010 to supplement the European Financial Stability Facility, the first euro area financial assistance fund. However, the German government – concerned with greater Commission power, the problematic legal basis of the EFSM and its potential implications for the national budget – insisted upon a temporary and limited mechanism (European Stability Mechanism [ESM], 2019: pp. 48–52). Moreover, the United Kingdom was extremely reluctant to take on liabilities for a borrowing instrument limited to euro area members and abstained from the vote (Thompson, 2011). When, in 2015, the Commission used the EFSM once more to provide a bridge loan to Greece, the United Kingdom insisted that the loan be guaranteed only by euro area member states and the EFSM Regulation was amended to that effect (Council Regulation (EU) 2015/1360; Mason, 2015).

The Commission resumed efforts to gain more autonomy over financial instruments in 2011. It proposed a framework regulation under which the Commission would assume responsibility for the implementation, management and disbursement of Macro-Financial Assistance (MFA) to certain third countries (European Commission, 2011). However, the Council and the European Parliament (which was co-legislator for the MFA since the Lisbon Treaty) pre-empted any potential for agency slippage by insisting that MFA programmes be subject to the ordinary legislative procedure on a case-by-case basis. The Commission withdrew its proposal in 2013, and the Council and Parliament instead inserted their agreed principles in a joint declaration appended to the 2013 Georgia MFA (Ritleng, 2016).

With Commission borrowing back on the table, the Council moved to clarify budgetary principles. The 2012 Financial Regulation stated that the EU 'may not raise loans within the framework of the budget', which left the possibility of additional borrowing operations so long as they remained outside the budget (Regulation (EU, Euratom) No 966/2012, Art 17.1; Vitsentzatos, 2014). It was not until 2018 – after the euro crisis had abated – that a revision of the Financial Regulation established guidelines for new financial instruments (Regulation (EU, Euratom) 2018/1046). The updated regulation acknowledged member states' authority to delegate borrowing powers to the Commission

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for the purpose of providing financial assistance, whilst reaffirming the Commission's status as an off-budget agency. A new article applied the principles of no maturity transformation, the earmarking of funds, direct implementation of assistance by the Commission and the protection of the EU's financial interests to all Commission lending instruments (Regulation (EU, Euratom) 2018/1046, Art. 220). The Council also moved to reinforce the monitoring controls on these operations with the necessary inclusion of explicit authorisation in all new Commission loan agreements and for the European Court of Auditors and the European Anti-Fraud Office (OLAF) to conduct checks and audits (Regulation (EU, Euratom) 2018/1046, Art. 220.5(d)). The Council, lastly, required the Commission to report annually on all financial instruments, budgetary guarantees, financial assistance and contingent liabilities (Regulation (EU, Euratom) 2018/1046, Art. 250).

V. Becoming a European Treasury, 2020–2023

The introduction of SURE and NGEU in response to the COVID-19 pandemic was critically enabled by two shifts in the preferences of member state principals. First, the United Kingdom, the main opponent of joint borrowing through the EFSM, had left the EU in January 2020. Second, Germany switched sides to support large-scale joint borrowing and, together with France, pushed the creation of a recovery fund guaranteed through the EU budget (Smeets and Beach, 2023). This new consensus in favour of large-scale borrowing had transformative implications for the Commission's borrowing operations.

When the Commission unveiled its diversified funding strategy in April 2021, it did so not as an act of slippage, but because member state principals had decided once again that borrowing at scale required a different approach to debt management. Although the Council mandated that loans under SURE formally remained back-to-back operations, the provision of loans to 19 member states under this instrument tested the limits of this approach (European Commission, 2022a, p. 7). Through the legislation establishing the borrowing operations for NGEU, the Council authorised the Commission to derogate from the back-to-back principle and the prohibition on maturity transformation laid down in Article 220 of the Financial Regulation (Council Decision (EU, Euratom) 2020/2053; Council Regulation (EU) 2020/2094; Regulation (EU) 2021/241, Art 15.2 (b)). The Council's 2020 ORD included further provisions concerning the Commission's debt management under the Recovery Instrument. (Council Decision (EU, Euratom) 2020/2053). The decision stated that the Commission should implement a diversified funding strategy to ensure the most advantageous repayment conditions (Council Decision (EU, Euratom) 2020/2053).

We find no evidence that the Commission persuaded member states that deeper integration was required in this domain at this time. Rather, member state principals supported this new funding approach as a rational response to the demands of large-scale bond issuance. Germany, which had played a crucial role in the RRF's creation, saw the diversified funding strategy as justified by, but also limited to, the exigencies of borrowing at scale under this temporary borrowing instrument. This logic is visible, for example, in the German Federal Constitutional Court's December 2022 judgment on a constitutional challenge against the ORD underpinning NGEU. Although it rejected the challenge, the Court accepted that the 'unprecedented nature of [the Recovery and Resilience Facility] and the exceptional amount of the funds to be borrowed' necessitated 'the

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implementation of a diversified borrowing strategy'.[11] Without EU treaty change, the Court concluded, borrowing could never be recognised as a 'permanent source of financing' for the Union.[12]

To raise the large amount required for NGEU, the member states agreed to allow the Commission to introduce the use of auctions alongside syndication, as is common amongst national debt management agencies (Blommestein, 2009). The Commission began operating both funding techniques in parallel: in the second half of 2022, it raised €15 billion through auctions and €35 billion through syndication. Moreover, the Commission moved to increase its reliance on short-term bills for cash management and issued a wider range of securities. SURE was funded through a newly developed social bond framework and a third of the financial means for NGEU were to be raised through NGEU Green Bonds (Hodson and Howarth, 2023; Spielberger 2024). Prodded by the Council, the Commission expanded its primary dealer network to 37 banks, put in place a set of eligibility criteria to determine participation, and announced its borrowing intentions in semi-annual funding plans (Commission Decision (EU, Euratom) 2021/625).

With greater budgetary powers, the Council imposed increased monitoring: the Commission was to report annually on the assets and liabilities under the Recovery Instrument and was to 'regularly and comprehensively inform the European Parliament and the Council about all aspects of its debt management'(Interinstitutional Agreement, Recital 16; Council Decision (EU, Euratom) 2020/2053). In January 2023, the Parliament's Budget Committee held its first hearing with the Commission's newly installed chief risk officer (CRO) (European Parliament, 2023). From 2020, the European Court of Auditors covered the Commission's borrowing operations in its Annual Report and published reports about SURE (ECA, 2022) and NGEU debt management (ECA, 2023), amongst other work on NGEU (ECA Officials, Interviews 1, 3 and 8).

It fell on DG BUDGET (2021) to develop new staff capacities and internal policies to cope with the requirements of large-scale borrowing. After its borrowing and lending unit had been downsized to four staff in 2009 (ECA, 2015), the Commission now built up a formidable borrowing unit (ECA, 2023). Amongst the new staff recruited for NGEU were several former or seconded ESM staff, who helped model the Commission's new debt management operations on the ESM's approach (Interviews 10 and 11). The Commission appointed a CRO to oversee the Borrowing and Lending Unit, a Chief Compliance Officer for NGEU debt management, and it instituted a High-Level Risk and Compliance Policy (DG BUDGET, 2022, p. 5; Interviews 5 and 6). Member states nevertheless continued to monitor Commission borrowing closely. The Council required the Commission to establish a structured dialogue with national debt management offices about its issuance and repayment schedules, as mandated under the ORD (Council Decision 2020/2053, Art. 9.5).

Whilst all these changes were linked specifically to the requirements of NGEU, the Council re-contracted the rules of Commission borrowing yet again in late 2022. When the EU agreed to provide up to €18 billion in macro financial assistance + to Ukraine, following Russia's invasion, the Council moved to revise Article 220 of the Financial Regulation to allow the Commission to fund several instruments through the same bonds

[11]BVerfG, Judgment of the Second Senate of 6 December 2022 – 2 BvR 547/21 –, para. 3.
[12]BVerfG, Judgment of the Second Senate of 6 December 2022 – 2 BvR 547/21 –, para. 152.

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and determine flexibly the timing of its issuance (Interviews 2, 4, 5, and 7). The provisions that banned maturity transformation and the cross-allocation of funds were deleted. Instead, the new Article 220a of the Financial Regulation states that

> [… t]he diversified funding strategy shall be implemented through all necessary transactions aiming at a regular capital market presence, shall be based on pooling of funding instruments and shall make use of a common liquidity pool. (Regulation (EU, Euratom) 2022/2434, Art 1(2)).

From 2023, the Commission could thus issue bonds under a single EU label and conduct a range of active debt management operations (Commission Implementing Decision (EU, Euratom) 2022/2544). Member states supported this re-contracting to increase the depth and liquidity of the secondary market for the EU's debt, helping to reduce the Commission's borrowing costs (Interviews 2, 5 and 12).

When the Commission undertook the ECU 500 million 'Jean Monnet' issue in 1988, it sought to use its discretion under the New Community Instrument to establish a regular and continuous presence as a borrower on financial markets. A similar political ambition was suggested 35 years later when the Commission argued that its diversified funding strategy could 'consolidate its market presence and further advance its transformation towards a sovereign-style issuer' (European Commission, 2023). Such drive was discernible too in September 2024 when reports emerged that Commission officials were exploring ways to roll over RRF debt in light of the Draghi Report, a high-level study that called for a common safe asset to fund joint investment projects (Draghi, 2024, pp. 290; Tamma and Foy 2024). As in the late 1980s, however, there was no room for slippage. Just as the New Community Instrument was discontinued, there is no guarantee that member states will replace the RRF once it stops funding projects in 2026. That the Commission is capable of borrowing at scale does not mean that it will be entrusted to do so in perpetuity by the Council.

Conclusion

This article has sought to explain how the European Commission's borrowing, lending and debt management operations have been transformed over the last half-century. When the Commission was entrusted with responsibility for the Community Loan Mechanism in 1975, its authority was closely circumscribed: loans were issued back to back and earmarked for specific purposes, and they involved neither financial risks nor maturity transformation. Today, the Commission has moved away from this off-budget model to an approach that possesses many of the characteristics of a European treasury (see Table). Although EU borrowing is still not recorded in the Union's budget, which remains subject to the requirement that expenditure and revenue be in balance, instruments such as the RRF and macro financial assistance are explicitly backed by the EU budget and subject to risk controls. Back-to-back lending has been replaced by active debt management under which the Commission issues single brand EU bonds and uses the funds raised to finance multiple policy programmes.

We explain the Commission's evolution as a borrower using a dynamic principal–agent approach. The shift from the off-budget model to a European treasury was not the result of slippage by the Commission as an agent in pursuit of its own goals, we find,

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but successive rounds of re-contracting by member state principals. Member states granted the Commission greater discretion, we find, because back-to-back lending suffered from serious inefficiencies when the EU borrowed at scale. Although the Commission tried to use this leeway to establish a permanent presence in financial markets, it was blocked from doing so by ex-ante and ex-post controls and, above all, by the ease with which member states could re-contract. Discretion thus served member states' interests without allowing the Commission to pursue its own aims.

The Commission's increased role in debt issuance and management may, paradoxically, come to limit its margin of manoeuvre as an agent. The Commission's ability to implement a competent borrowing strategy is now scrutinised closely in the context of the mid-term revision of the Multiannual Financial Framework (Foy, 2023). The Commission's bonds still underperform on markets, and its debt service costs have increased due to rising interest rates (Johnston and McDougall, 2023). Even if the Council's revision to the Financial Regulation in 2022 has allowed the Commission to put in place a robust borrowing architecture, it remains likely that the Commission will have to scale down its market presence unless new financial instruments are created after 2026. The financial autonomy the Commission has gained in its approximation of an EU treasury may yet be taken away by the member states in future instances of re-contracting.

Given the limited scholarly attention to the Commission's borrowing and lending operations to date, this article leaves no shortage of questions for further research. One is what role crises played in the construction of a European treasury. Whilst historical institutionalism points towards the importance of economic crises as critical junctures, as noted above, many of the key decisions over borrowing and lending operations have taken place after the acute phase of economic crises has passed. Another avenue for future research is to draw out the integration dynamics, which underpin our principal–agent approach. An important question in this regard is how member states reconciled their growing reluctance to delegate new powers to the Commission in the 1990s with their willingness to establish a European treasury. A final issue for consideration is whether ex post controls are sufficient to address concerns that EU borrowing suffers from an accountability gap. The President of the European Court of Auditors, Tony Murphy, has warned that limited control is unavoidable so long as EU borrowing is not fully embedded in the EU budget (Moller-Nielsen, 2024). Accountability to member state principals, in other words, is not the same as accountability to citizen-principals.

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List of Interviewees

1. ECA officials, 30 March 2023
2. National official, 24 May 2023
3. ECA officials, 12 July, 2023
4. National official, 17 July 2023
5. National official, 4 August 2023
6. National official, 12 September 2023
7. National official, 28 September 2023
8. Commission official, 5 October 2023
9. National official, 20 October 2023
10. European official, 3 November 2023
11. Klaus Regling, former ESM Managing Director, 28 November and 1 December 2023
12. National official, 22 January 2024

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