

Towards a More Perfect (Fiscal) Union

Lessons for the Euro Area From the Formation of America's Fiscal Union

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Agenda



- I. The Lesson(s) of U.S. Fiscal History**
- II. The Public Goods a Central Budget Could Deliver**
- III. A Path to a Larger and More Politically Sustainable EU Budget**



***America's Fiscal Union will be forged in
crises, and will be the sum of the
solutions adopted for those crises.....***

John Monnet – Fictitious Founding Father

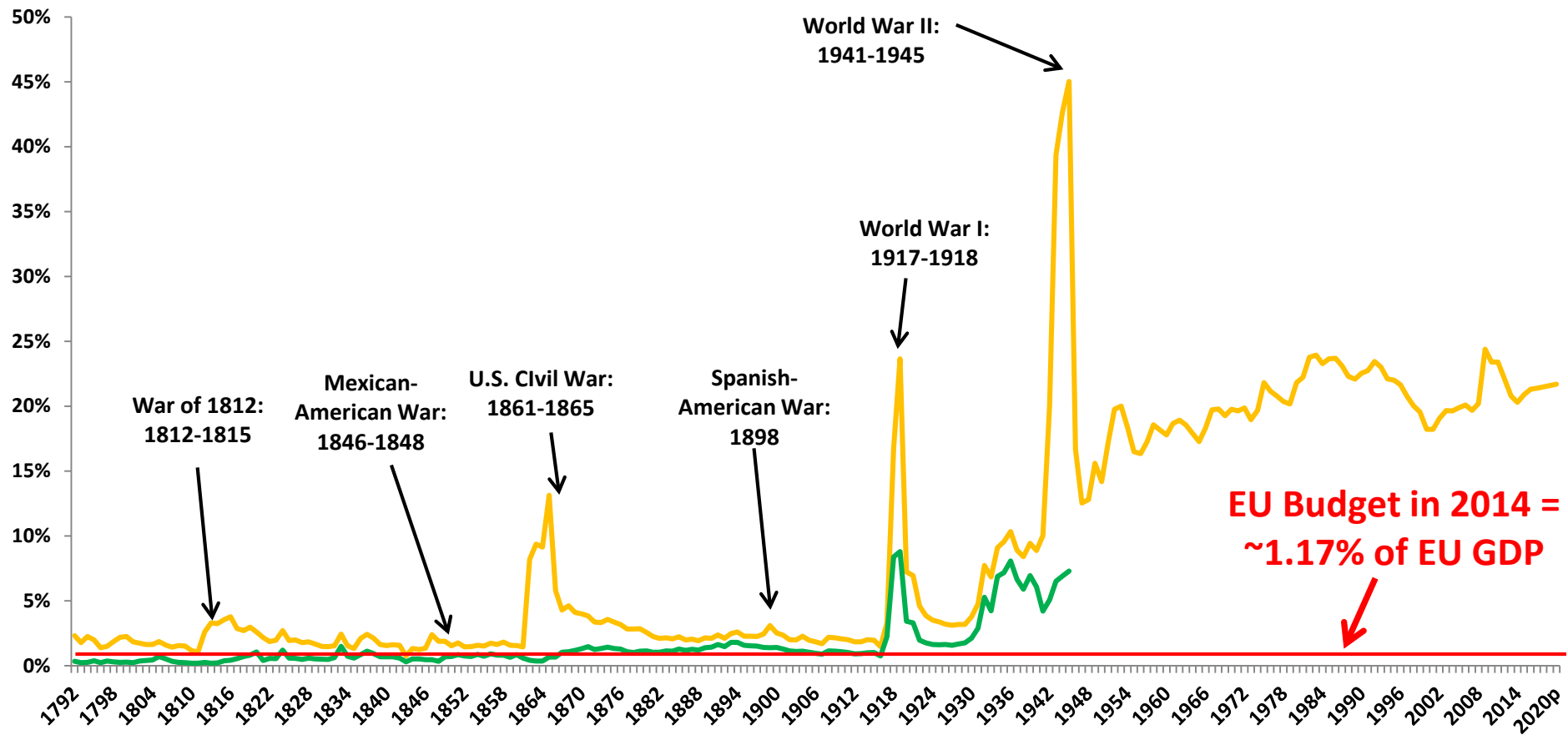
**(psst – its the federal government that
wages war!)**

US Federal Government Expenditures 1792-2020p, % GDP



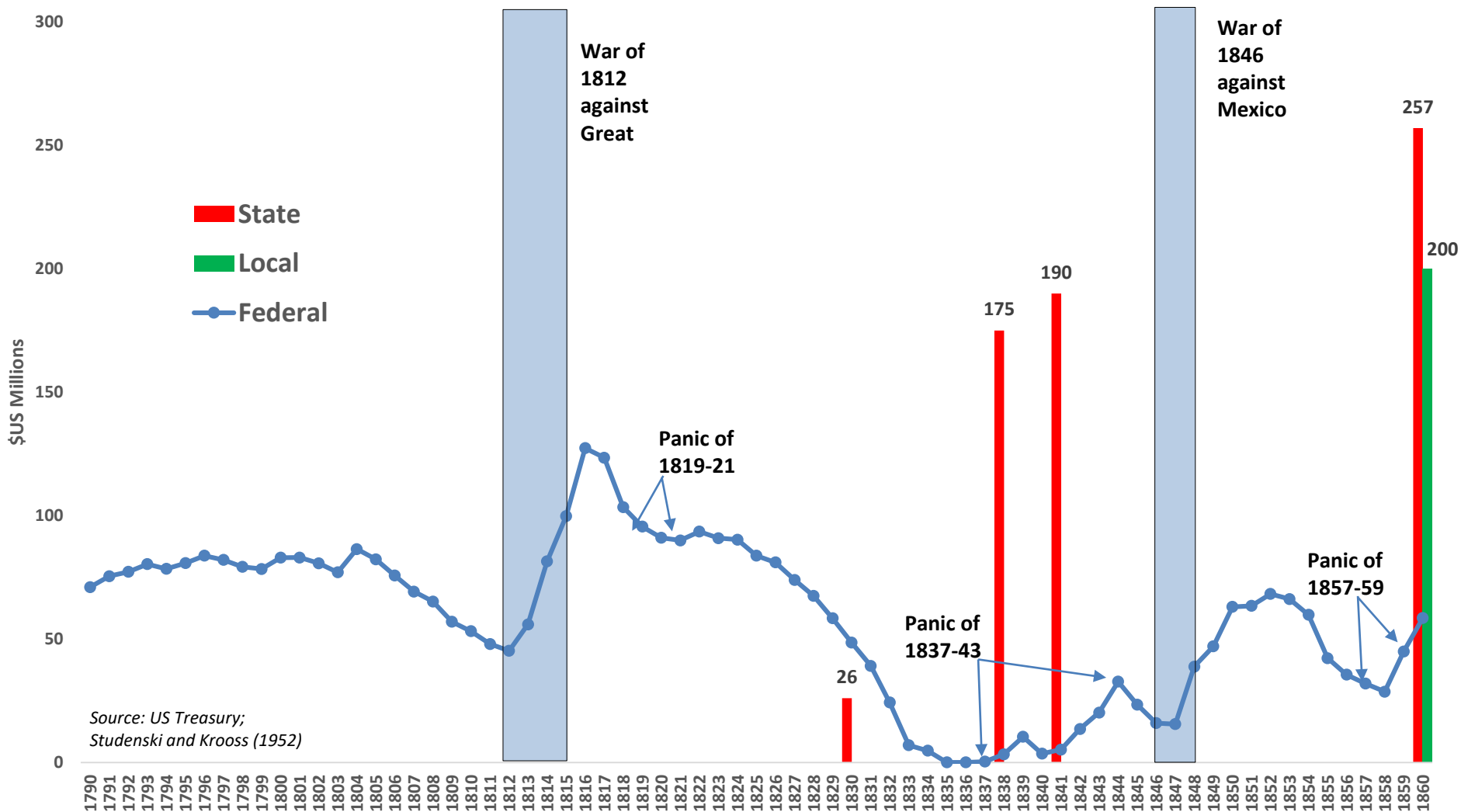
— Total Federal Government Expenditure 1792-2020p

— Total Federal Government Expenditure, Excl. War Department, Naval Department and Interest on the National Debt 1792-1945

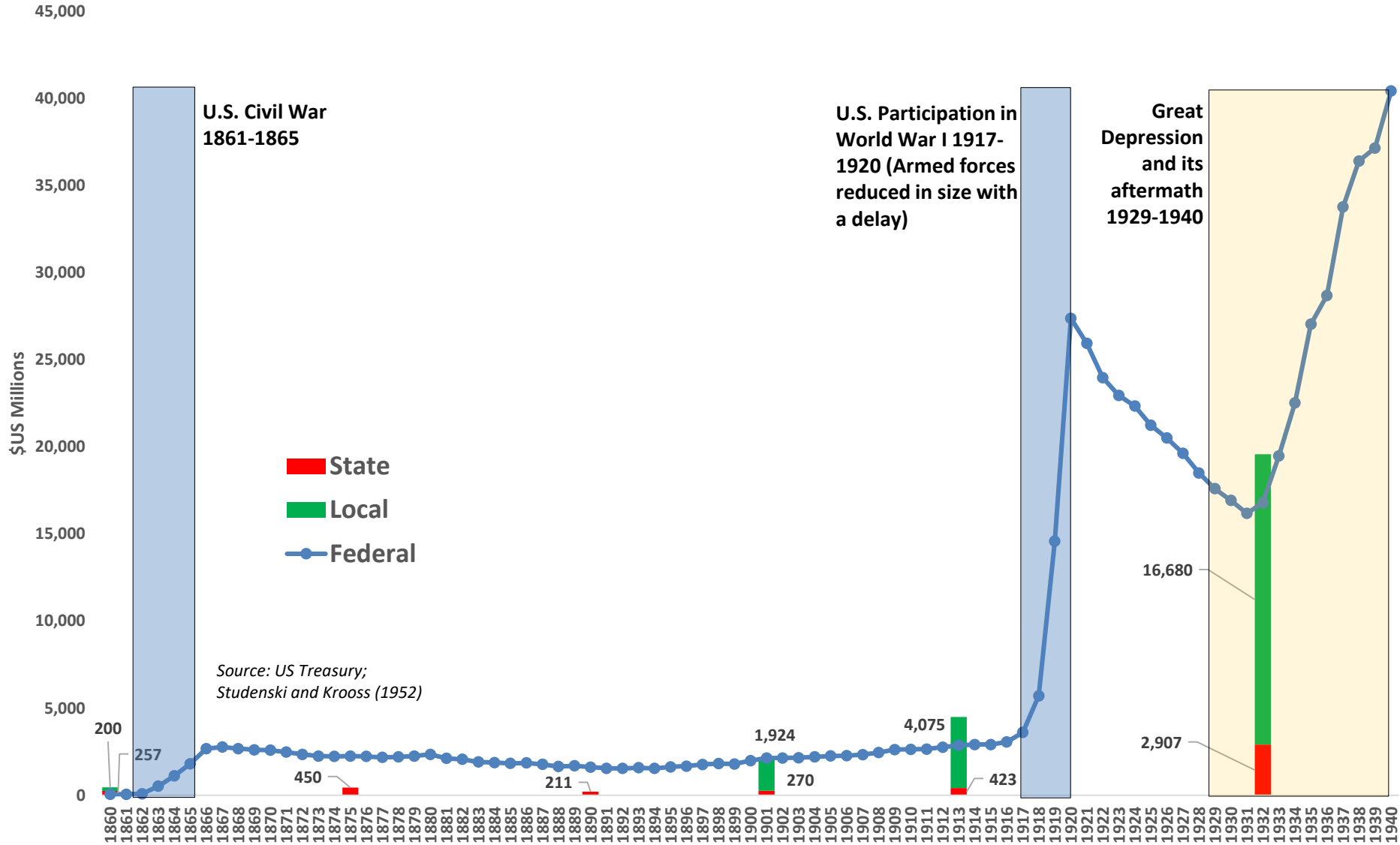


Source: Williamson (2014). Expenditure data from 1792-1945 from US Census (1949); data from 1945-2020p OMB (2015).

U.S. Federal, State and Local Governments' Gross Debt, By Level of Government 1790-1860, \$USmn



U.S. Federal, State and Local Government Gross Debt, By Level of Government 1860-1940, \$US Million



Public Goods a Central Budget Could Deliver



I. “Economic Convergence”

- Hard if not impossible to deliver
- Required budget size politically impossible to (ever) achieve

II. “Counter-Cyclical Buffer”

- Not easy to do through regular EU budget items (automatic stabilizers are MS)
- Banking Union is not part of the EU budget
- Best done by “debt financing” (but Eurobonds are for the future)
- Possible to give the ESM/EMF a banking license and do it conditionally
- Supplementary “European level” catastrophic level unemployment insurance

III. “Best Solved at Regional Level (Subsidiarity)”

- EU powers determined by where “EU-level value-added” exist
- Subsidiarity is a “living concept” that evolves over time
- How to best finance the regional solution of policy challenges?

Today's EU Budget



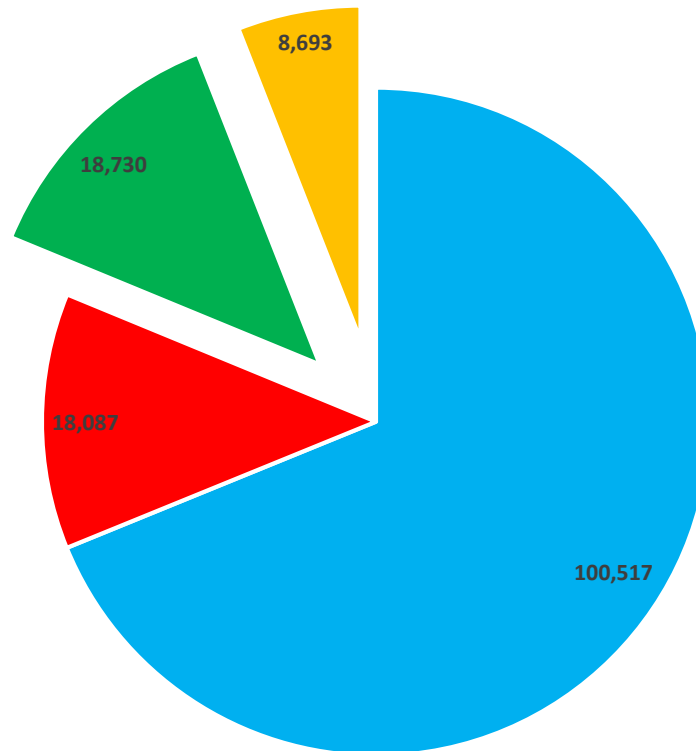
~\$165bn/year and
80% is direct
GNI/VAT-based
transfers

Focus on “national
net contributions”
similar to US pre-
XIV Amendment
federal budget

Lesson From U.S.
fiscal history –
Direct centralized
taxation requires
changes to
Constitution/Treaty

EU Budget Resources by Category, Euro Billion, 2015

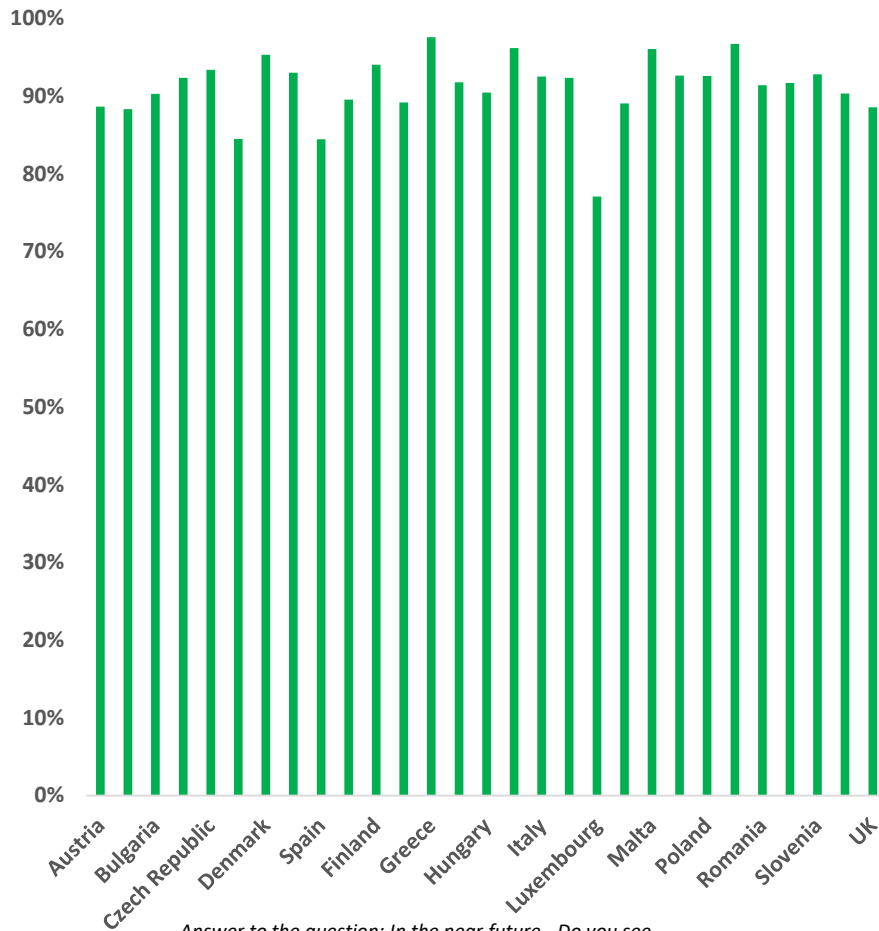
- GNI-based Own Resource
- VAT-based Own Resource
- Traditional Own Resources (TOR)
- Other Revenue



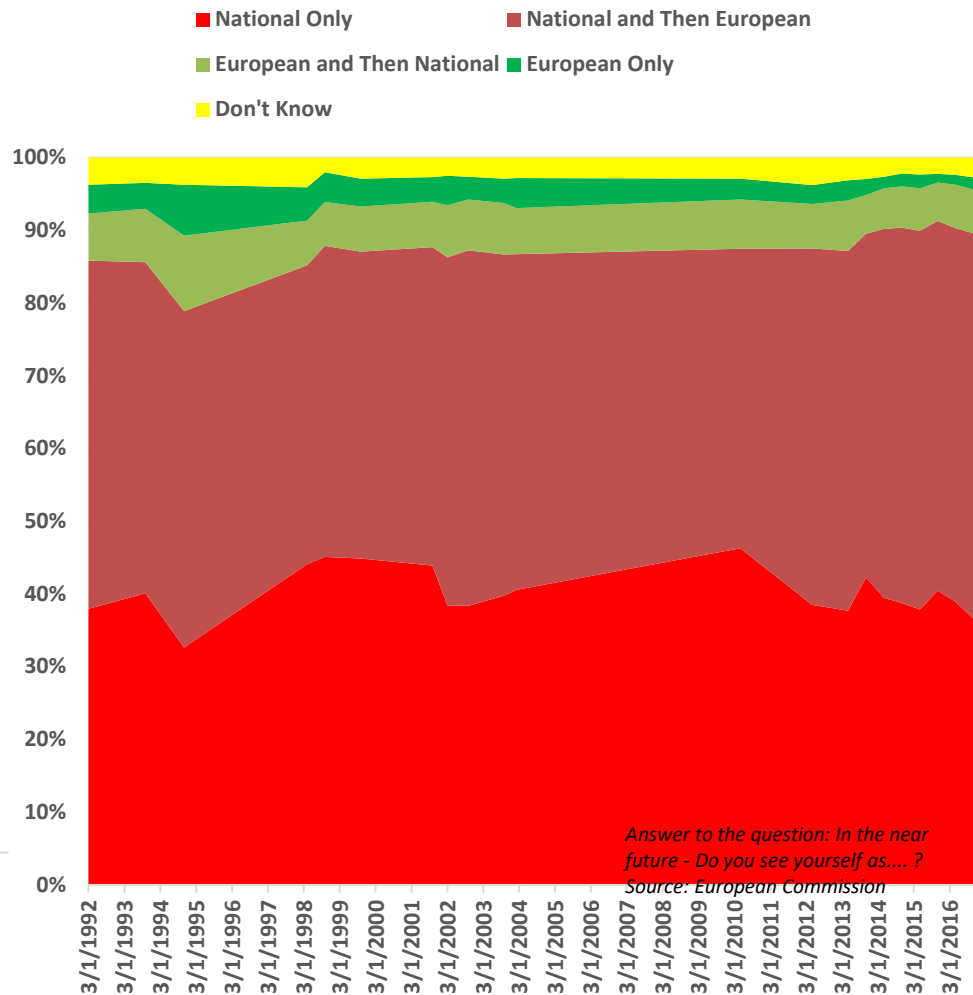
Direct Tax Financing Not Happening



Share of Residents Feeling National Only or Predominantly National, Fall 2016



Feelings of Self-Identity, Share of EU Residents 1992-2016



Earmarked Revenue Widely Used in U.S.

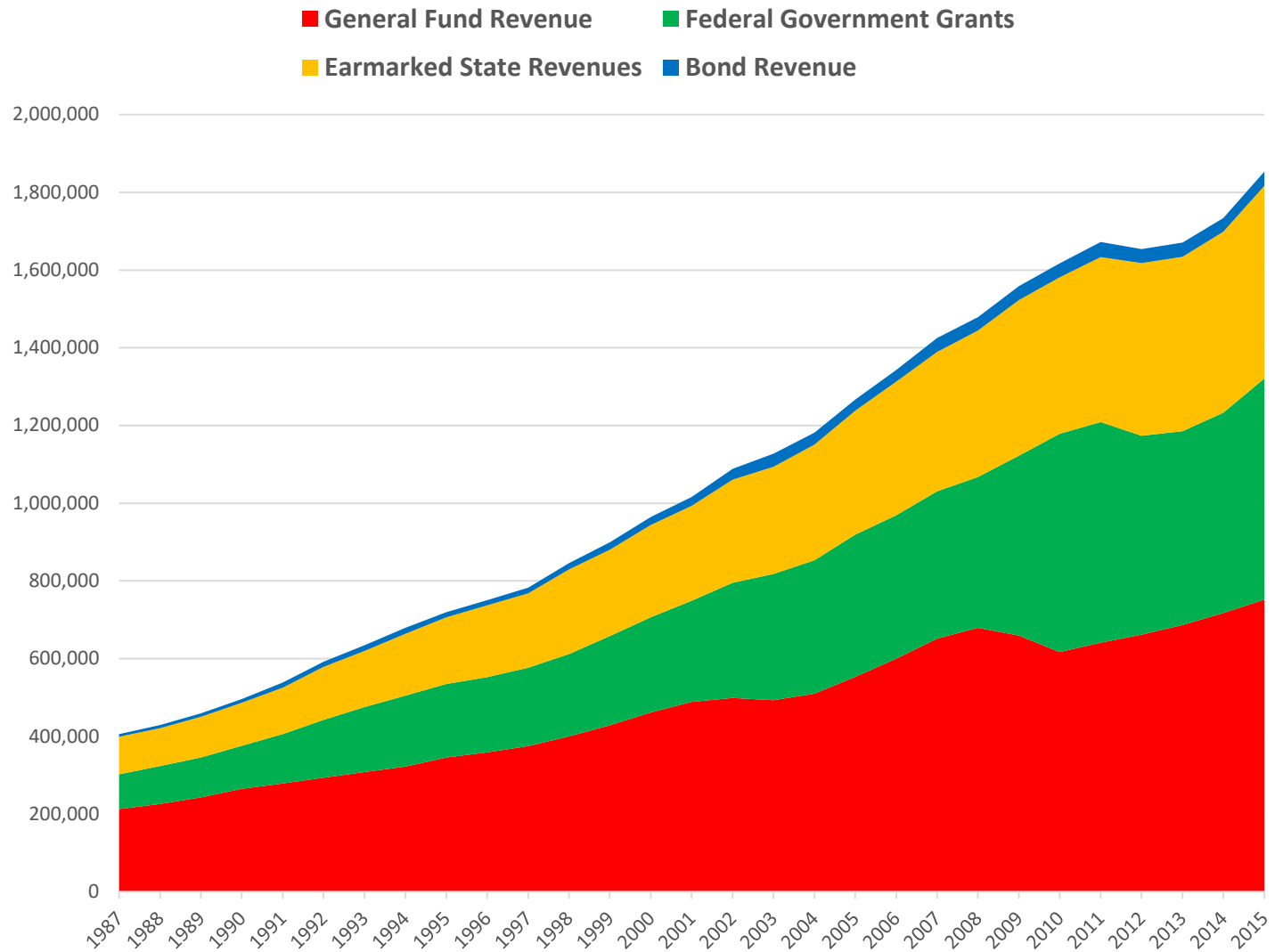


U.S. states derive a minority of revenue from general taxes with full discretion over use

Earmarked U.S. state revenue over 25% of total revenues

35% of U.S. federal budget is earmarked “trust fund revenue”

U.S. State Revenues, By Source, \$USmn 1987-2015



Earmarked Revenues = Bigger EU Budget?



- With voters' self-identity/allegiance at member state level, *single tax for single public service* may be EU's only avenue to raise indirect tax/fee revenue
- Simpler and therefore democratically more legitimate than current complex budget process
- Some applications:
 - Explicit user fees; polluter pays principle or € ETIAS fees
 - Fees on related use items; Highway TF structures that for instance finances infrastructure through gas taxes, climate mitigation through ETS (EU Carbon Dividend?) revenue
 - Broad taxes earmarked for specific EU budget items; finance a CAP through a 2% VAT on food?

Concluding Remarks



- **Lessons from U.S. fiscal history – fiscal unions takes a long time to construct and you really do need crises to do it**
- **Being a “Project of Peace” sets the EU back in the process of “state/fiscal union building”**
- **EU budget should focus on funding solutions to regional challenges**
- **Financing the EU budget through an increasing use of earmarked revenue from targeted indirect taxes/fees best available path for now to more direct European revenue**
- **Earmarked revenue probably best path to a larger and politically sustainable EU budget**