Towards a More Perfect (Fiscal) Union

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

Jacob Funk Kirkegaard
Senior Fellow
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

- War of 1812: 1812-1815
- Mexican-American War: 1846-1848
- U.S. Civil War: 1861-1865
- Spanish-American War: 1898
- World War I: 1917-1918
- World War II: 1941-1945

EU Budget in 2014 = ~1.17% of EU GDP

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

Source: US Treasury; Studenski and Krooss (1952)
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

Source: DG Budget
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

- National Only
- National and Then European
- European and Then National
- European Only
- Don't Know

Answer to the question: In the near future - Do you see yourself as...?
Source: European Commission
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.”


- General Fund Revenue
- Federal Government Grants
- Earmarked State Revenues
- Bond Revenue
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 €5 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