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Editorial

Comparative Fiscal Federalism and the Post-Covid EU: Between Debt Rules and Borrowing Power

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Abstract
This thematic issue examines two main research questions: What are the features, the determinants, and the implications of fiscal integration in a system of multilevel governance like the EU? And, what can the post-pandemic EU learn from established federations when it comes to fiscal integration? We attempt to conceptualize the patterns of EU fiscal integration. In so doing, we identify eight instruments of fiscal integration in a federal or multilevel polity, equally divided between fiscal capacity and fiscal regulation, depending on the side of the budget and the mode of integration (autonomous or dependent). For instance, as part of the fiscal capacity instrument of integration, we propose to distinguish between revenue and expenditure capacity. Revenue capacity is then further divided into tax capacity, based on EU/federal taxes, and budgetary capacity, based on non-independent sources, for instance, contributions from the member states. Expenditure capacity is divided into autonomous spending capacity, meaning direct spending by the EU, and a dependent transfer capacity, where the EU merely distributes resources (both grants and loans) to the member states.

Keywords
economic governance; EU budget; EU taxes; fiscal capacity; fiscal integration; fiscal solidarity; fiscal union; fiscalization process; Next Generation EU; own resources

Issue
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1. Instruments of Fiscal Integration in the Post-Covid EU

This thematic issue argues that today's EU finds itself in a sort of fiscal limbo. Following the Covid-19 pandemic, the core of the EU's fiscal regulation—the Stability and Growth Pact (SGP)—is currently suspended until 2024. Thanks to an unprecedented recovery programme—Next Generation EU (NGEU)—the EU's fiscal capacity has changed but these changes are limited in time (NGEU expires in 2026) and scope (borrowing power and not fully-fledged taxing power). At the same time, the Russian war against Ukraine forced the EU to put in place ad hoc fiscal solidarity solutions to support common military initiatives and cushion the economic implications of the war on Europe. As a result, we argue that this original combination of rules and resources—the EU's new fiscal policy mix—needs a clear-cut conceptualization. In this editorial, we move beyond Genschel and Jachtenfuchs' (2014) distinction between two instruments of fiscal integration—fiscal capacity and fiscal regulation—and develop it further. Fiscal capacity involves two sides: revenues and expenditures. Fiscal regulation comprises rules regulating the EU's revenues and expenditures. At the same time, it also includes rules regulating the revenues and expenditures of member states (MSs), thus

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constraining national sovereignty over a crucial area of core state powers like fiscal policy (Zgaga et al., in press).

2. EU's Fiscal Patterns

An attempt to conceptualize the patterns of EU fiscal integration is represented by Table 1.

Fiscal capacity and fiscal regulation can be conceived of as autonomous if supranational institutions (the European Commission and the European Parliament) are involved in the decision-making process. On the contrary, the two instruments of fiscal integration are dependent on the MSs if the intergovernmental institutions (the Council and the European Council) are the key decision-makers. Starting from the upper left cell, the autonomous revenue capacity results from the process Woźniakowski (2018) coined "fiscalization" which leads to central tax capacity. Hence, for us, revenue capacity is autonomous if the centre finances itself only or mainly through independent resources in the form of taxes. Second, a dependent revenue capacity leads to what we call budgetary capacity, where the focus is on the size of the budget rather than on the mode of obtaining the revenue. Here, the revenues are based mostly on MSs' contributions rather than on independent resources. Moving down the capacity axis, the lower left cell, autonomous spending capacity, means direct spending by the EU—for instance, to provide common public goods. In this sense, spending capacity resembles a federal budget which is used directly by a government—for instance, for military or welfare expenditures. Spending capacity can involve both independent and non-independent resources and differs from transfer capacity, where the EU distributes independent and non-independent resources in the form of both grants and loans to the MSs, which spend them subject to conditionality. In this sense, transfers resemble grants-in-aid known from the established federations. Such a dependent budgetary capacity and transfer capacity represent the biggest part of the revenues and expenditures of the regular EU budget (the Multiannual Financial Framework) and NGEU.

Moving right the axis of the instruments of fiscal integration, to fiscal regulation, the upper left cell, which indicates the regulation affecting EU revenues, is called the revenue regulation of the centre. This includes rules on the EU budget. The second cell, which points to the regulation affecting MSs' decisions on taxes and debts, is called the revenue regulation of the units. Such rules involve tax harmonization and rules on borrowing, such as those of the SGP, the Six Pack, and the Two Pack. The third cell is the expenditure regulation of the centre. This concerns restraints on policy areas of EU spending, for example, the Common Agricultural Policy and cohesion policy, but also the lack of EU welfare benefits. The fourth cell indicates the expenditure regulation of the units and refers to the impact of the EU on the spending policies of the MSs, as exemplified by various *Country Specific Recommendations of the European Semester*, the annual framework for EU economic regulation.

It is not yet clear how the post-pandemic EU is going to combine fiscal regulation and fiscal capacity. As Zgaga (2023a, p. 2) notes, this implies that "the future division of fiscal sovereignty between the EU and the MSs has not yet been clarified." Can the EU learn something from established federations and, if so, what exactly?

3. Comparative Fiscal Federalism

This thematic issue discusses the fiscal trajectory of the EU from the perspective of comparative federalism, according to which the EU is not a sui generis political system, but can be better understood if compared to established federations (Fossum & Jachtenfuchs, 2017; S. Fabbrini, 2019). Specifically, this thematic issue adopts comparative fiscal federalism to interpret EU fiscal developments in light of the experience of consolidated federations with different borrowing, taxing, spending,

Table 1. Instruments and modes of EU fiscal integration.

		Instruments of fiscal integration			
		Fiscal capacity		Fiscal regulation	
Mode of fiscal integration (autonomous or dependent)		Autonomous: Supranational institutions involved	Dependent: Intergovernmental institutions only	Regulation of the centre (autonomous or dependent)	Regulation of the units (autonomous or dependent)
Side of the budget	Revenue capacity	Tax capacity based on independent resources (fiscalization)	Budgetary capacity based on non-independent resources	Revenue regulation of the centre	Revenue regulation of the units
	Expenditure capacity	Spending capacity of independent or non-independent resources	Transfer capacity of independent and non-independent resources	Expenditure regulation of the centre	Expenditure regulation of the units

and regulatory powers, and identify insights from them. We consider both decentralized federations (federal unions, like the US and Switzerland) and centralized federations (federal states, like Germany and Canada; S. Fabbrini, 2017; Kelemen & McNamara, 2022).

Comparative federalism shows that developing fiscal autonomy requires "fiscalization" which is defined as "a process through which a certain level of government (supranational/federal/central) expands its power to raise its own sources of revenue, and in so doing it decreases the level of vertical fiscal imbalance" (Woźniakowski, 2022, p. 10), namely the dependency on national transfers. Fiscalization comes about as a result of an existenstial internal threat and stresses that what matters for fiscal autonomy is not only the resources' size (revenue endowment) but also the resources' source (revenue diversification). A crucial lesson from comparative fiscal federalism is that multilevel governance systems managed to develop an autonomous fiscal capacity at the central level only once they developed a significant tax capacity, i.e., access to taxes that produce large revenues, such as an income tax and a value-added tax. On the one hand, such fiscalization process leading to the emergence of a federal fiscal union with taxing powers (Woźniakowski, 2022) would imply that significant fiscal powers are transferred to the centre which, thus, would no longer depend on national transfers. On the other hand, in federations, the empowerment of the centre does not significantly impair the spending power of the constituent units, but rather the fiscal sovereignty of the centre coexists with the fiscal sovereignty of the units (Zgaga, 2023a).

4. Overview of Contributions

By combining the contributions from the disciplines of political science, political economy, and law, this thematic issue aims to locate the post-Covid EU in the context of the literature on comparative fiscal federalism. The first set of contributions focuses on the nature of the EU's revenue capacity. Groenendijk (2023) analyses the EU's revenue capacity to show that the EU's own resources, to a large extent, constitute de facto taxing power, that the EU significantly uses off-budget borrowing capacity, and that it has a variety of schemes that offer revenue capacity to the centre, through the pooling of resources (transfers, guarantees) by its MSs and third countries. García Antón (2023), on the other hand, argues that the EU has the power to tax, embedded in the narrative of the internal market, provided that the chosen resources in the basket match its objectives and policies, but the MSs are still the "masters" to unanimously decide the level of resources.

The second set of contributions deals with the evolution of the EU's fiscal capacity and the use of off-budget financial instruments. Breuer (2023) compares the introduction of NGEU with the public goods budget of the European Coal and Steel Community (ECSC). Revisiting the ECSC budget system allows her to understand the fiscal federal appearance of the NGEU funds, which is limited through the institutional structure of the EU's transfer budget. Capati (2023), in turn, explains the change in the EU's financial assistance regime between the euro crisis and the Covid-19 pandemic. The author finds that financial assistance in the EU moved from "intergovernmental coordination" with the European Stability Mechanism to a form of "limited supranational delegation" with the NGEU' s Recovery and Resilience Facility and argues that such a change is due to a collective policy-learning process. F. Fabbrini (2023) examines the two key tools deployed by the EU to fund Ukraine in its war against Russia, namely the European Peace Facility and the Macro-Financial Assistance Instrument. The author argues that while the war in Ukraine quickly prompted the EU to replicate some of the novelties it used to respond to the Covid-19 pandemic, structural fiscal and governance weaknesses still limit the ability of the EU to mobilize resources and leverage power on the international stage. In turn, Serowaniec (2023) focuses on the phenomenon of "debudgetization" of public finances in Poland after Covid-19 and the Russian invasion of Ukraine to show that using off-budget instruments in cases of emergency limits the transparency, legitimacy, and parliamentary oversight of state public finances.

The third set of contributions compares the EU with established federations. Woźniakowski (2023) compares the mode of financing the NGEU with the American central budget, under the Articles of Confederation when Robert Morris was in charge of the United States' finances. The author shows that both are based on borrowing, without significant tax capacity, which could be used to pay off this central/federal debt. He points to the risk of disconnecting borrowing from taxing, which may result in fiscal chaos and even social unrest, when the central debt is paid by the MSs, rather than from the central tax revenues. In turn, Georgiou (2023) focuses on the historical development of fiscal regulation and federal fiscal capacity in the US and fiscal relations between the EU and the states. He outlines that the NGEU, with its borrowing at the central level and the bulk of spending at the state level, resembles the American system of grants-in-aid and "intergovernmental relations." Successively, Donnelly (2023) examines four mechanisms for establishing federal spending programs in the EU, Canada, and the US despite veto players' resistance. He shows that three of these mechanisms were used to overcome the opposition against the NGEU: clocks (temporary), caps (limited amount of borrowing), and compartments (limited range of public policy expenditure). In turn, Zgaga (2023b) operationalizes the fiscal sovereignties—the fiscal sovereignty of the centre (here, the EU) and the fiscal sovereignty of the units (here, the MSs)—and specifies the conditions under which the two can coexist. He shows how a federal union like Switzerland organizes the coexistence of fiscal

sovereignties and identifies insights for the EU. Finally, Buti and S. Fabbrini (2023) outline the political and institutional conditions for the convergence towards a new fiscal equilibrium, combining central (although limited) fiscal capacity with binding (although simplified) rules on MSs' fiscal policies. They propose a "Triple-T model" composed of existential threats to the EU, trust among the units, and a time horizon—all three elements must come together for central fiscal capacity to emerge.

5. Conclusions

In conclusion, this thematic issue aims to contribute to an original strategy of fiscal governance for the EU, based on the combination of rules and resources in the form of a new fiscal policy mix. Overalll, our contributions show that the EU mainly uses transfer capacity, and very little spending capacity, while its revenue capacity is still mainly budgetary capacity, with a very limited tax capacity. This budgetary capacity—unable to address the various crises-related challenges via the regular EU budget—involves financial instruments which are often ad-hoc, temporary, off-budget, conditional, borrowing-based, transfer-oriented, intergovernmental, and with limited parliamentary accountability. The historical experience of the established federations shows that the central budget is mainly used to finance common goods at the federal level (via spending capacity) and less so as grants-in-aid or transfers to the MSs (via transfer capacity). If the EU wants to become resilient to future threats, it may have to follow this path of fiscalization, through creating a central fiscal capacity consisting of a tax capacity, which could be used to finance European public goods.

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Conflict of Interests

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